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Why Chinese, European Stimulus Won't Be A 'Big Bang'

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Rumblings about monetary easing from China and Europe are expected to have, at best, a modest economic impact both there and in the U.S., which has been strengthening while other top economies are weakening.

In a surprise move, China's central bank cut lending rates Friday for the first time in two years, slicing its one-year benchmark rate by 40 basis points to 5.6% and its one-year deposit rate by 25 basis points to 2.75%.

Meanwhile, European Central Bank President Mario Draghi signaled policymakers are prepared to expand a stimulus program of asset purchases should Europe's dangerously weak inflation fail to rebound quickly.

The news followed another burst of easing from Japan's central bank late last month.

Stocks rallied worldwide. The S&P 500 rose to a new high, led by commodity-related groups.

China's move to cut interest rates is a sign that Beijing views the nation's economic slowdown with growing alarm, said **Bernard Baumohl, chief global economist at the Economic Outlook Group**. But he added that more needs to be done, such as further interest-rate cuts

"I don't think we ought to rush to any kind of optimistic conclusion that the cut in the interest rates in China will spur growth sufficiently to satisfy Chinese leaders," he said.

While China's economy grew 7.3% last quarter, an enviable pace elsewhere, it fell short of the government's 7.5% target.

Storm clouds on the horizon also include a slowdown in its once-heated real estate market and mild inflation.

In Europe, Draghi indicated Friday that further ECB stimulus could include purchases of sovereign European bonds, adding to the covered bank bonds and securities backed by assets like mortgages and other loans that the ECB is already buying.

But Draghi has to deal with more than a dozen sovereign states, each looking out for its own interests and pulling him in different directions. As a result, his talk has been bold, but his actions haven't caught up.

"They're not about ... to launch a massive further stimulus program, and therefore markets shouldn't expect a big bang at the upcoming December meeting a few weeks from now," said Jacob Funk Kirkegaard, a senior fellow at the Peterson Institute for International Economics.

Other problems include the Ukraine-Russia crisis and related Western sanctions, causing the already wobbly Russian economy even more problems that could spill over into Germany, which flirted with recession earlier this year.

Still, while talk is cheap and interest rate cuts won't jolt the world economy, it's not entirely insignificant either, said Bill Adams, a senior international economist at PNC Financial. "This is collectively a larger chunk of the global economy that's moving toward an expansionary monetary policy.

By comparison, the U.S. economy — though not charging ahead like a bullet train — is perhaps more like the Not-So-Little Engine That Could, with the jobless rate falling to 5.8% in October and GDP growth clocking in at a good, but not great, rate of 3.5% in Q3.

Falling gasoline prices will provide a net stimulus for U.S. consumers, and despite the Fed ending quantitative easing last month, other central banks pushing down harder on the gas should further aid growth.

"So far, the strengthening of the domestic U.S. economy is offsetting the weakness of what we're seeing abroad," said **Baumohl**.

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