ECB chief Draghi is commanding even more influence over global economy than Bernanke

By Associated Press,

WASHINGTON — Move over, Ben Bernanke. This is Mario Draghi’s moment.

The European Central Bank president is overtaking the Federal Reserve chairman — at least for now — as the central banker with the most influence on the global economy and markets. Faced with a growing recession and a possible breakup of the 17-country euro alliance, Draghi has bigger problems than Bernanke, who’s overseeing an economy in recovery.

As head of the ECB, which meets Thursday, Draghi also has more ammunition left than Bernanke does.

The Fed chief still wields considerable power to drive financial markets. That was clear last week, when stocks jumped after Bernanke signaled in a speech in Jackson Hole, Wyo., that the Fed will do more to help the still-weak U.S. economy.

Yet the focus of the global financial world has shifted to Draghi. Some economists expect the ECB to cut its benchmark interest rate Thursday. Many also hope Draghi spells out plans by the ECB to start buying bonds of troubled European governments to ease their borrowing costs and shore up the euro alliance.

“Draghi’s role in averting an implosion of the eurozone puts him in the unfortunate position of being the central banker with the greatest influence on global financial stability in the short term,” says Eswar Prasad, professor of trade policy at Cornell University.

Bernanke’s task isn’t as urgent, “since the U.S. economy is plodding along and does not face an imminent disaster scenario.”

Stock prices have risen in recent weeks, in part because investors expect the Fed and the ECB to reduce lending costs in the United States and Europe. The Standard & Poor’s 500 stock index has risen more than 5 percent since July 25.

Greece, struggling with debts and its fifth year in recession, may have to stop using Europe’s single currency if it doesn’t impose the tough budget cuts being demanded as a condition for its bailout. Many fear that bigger indebted countries — like Spain and Italy — would be forced to follow Greece
out of the eurozone.

The breakup of the alliance could be devastating. Borrowers in countries that left the eurozone would struggle to produce enough money in their weak local currencies to repay old debts denominated in much stronger euros. As debts soured, Europe’s banking system would freeze up. Its economy would likely follow.

“The stakes in Europe are much higher,” says Ethan Harris, co-head of global economic research at Bank of America Merrill Lynch. “Europe is already in a recession. Their banking system is in worse shape than ours. And their fiscal policy process is even more broken ... The survival of the euro is at stake.”

Last month, Draghi vowed to do “whatever it takes” to hold the eurozone together and said that “believe me it will be enough.” Markets rallied on the bold promise. Investors assumed the ECB would intervene in the bond market and buy up Italian and Spanish government debt. They hope its purchases would drive Italy’s and Spain’s borrowing costs down to sustainable levels.

Imminent action by the ECB is considered unlikely. Indebted countries like Spain would first have to apply for aid to the eurozone’s bailout fund. Then they would have to agree to conditions spelling out how they’d shrink their deficits.

And key details have yet to be settled. They include how tough the conditions would be and whether any bond purchases would target a specific interest-rate ceiling.

Theoretically, Draghi has limitless power to print money to pour into bond purchases. But Germany’s conservative Bundesbank opposes the purchase plan. It says governments could become addicted to central bank support — and slack off on cutting their deficits.

Bundesbank head Jens Weidmann, who sits on the ECB’s governing council, is so far alone in opposition to bond purchases by the ECB. But Weidmann could conceivably rally more support for his position if Draghi and the council majority are perceived as going too far.

Chancellor Angela Merkel has indicated she’s open to Draghi’s plans — a key factor fueling market expectations he’ll be able to carry out a strong intervention. Analysts say the effort to save the euro ultimately needs public support in the currency union’s largest country.

Draghi must also navigate past the ECB’s narrow mandate under the basic EU treaty. The treaty forbids the ECB to directly finance governments. But it allows it to buy securities including government bonds on the open market, leaving a gray area that’s been hotly debated.

“Draghi can do a lot, but he’s significantly more constrained by politics,” says Julian Brigden, managing partner of Macro Intelligence 2 Partners, an investment consultancy.

Last week, Draghi urged Germans to support his efforts to rescue the euro. Writing in the German weekly Die Zeit, he said the ECB sometimes must use “exceptional measures” to stabilize the currency alliance.
David Rosenberg, chief economist at Toronto money manager Gluskin Sheff & Associates, says power has shifted from Bernanke to Draghi. During the U.S. recession, Bernanke held the most sway. But now Europe’s woes have taken center stage, and what Draghi says and does can move markets more.

But Draghi may have set expectations too high with his whatever-it-takes pledge, Rosenberg says. Markets won’t accept anything less than an open-ended commitment to buy Spanish, Italian and other European countries’ bonds.

“He better have some form of bazooka, loaded and ready to go,” Rosenberg says.

By contrast, many analysts worry that the Fed has used up its tools to help the U.S. economy’s sluggish recovery. It has pushed short- and long-term interest rates to historic lows. The economy might not get much of a kick even if the Fed proceeds with a third round of bond purchases designed to drive long-term rates even lower — a move the markets are expecting after Bernanke’s speech at Jackson Hole.

“There’s a tremendous amount of hype in the United States surrounding the importance of monetary easing,” says David Levy, chairman of the Jerome Levy Forecasting Center, a consultancy. “But such moves by the Fed seem to have relatively little effect.”

On Friday, the U.S. government will issue the August employment report. Economists’ consensus forecast is that employers added 135,000 jobs and that the unemployment rate remained 8.3 percent. U.S. unemployment has topped 8 percent for 42 straight months.

Cornell’s Prasad says Bernanke could reclaim the No. 1 market mover title if America’s bickering politicians fight once more over the nation’s debt limit or can’t reach a budget deal by the end of the year.

Under rules designed to force a compromise, failure to reach agreement would trigger $600 billion worth of spending cuts and tax hikes. The draconian moves would send the economy over the so-called “fiscal cliff” and possibly into recession. Bernanke might be forced to move aggressively to limit the damage if that happens — or even appears likely to happen.

Both Bernanke and Draghi are already powerful enough to have nicknames worthy of economic superheroes. Bernanke is “Helicopter Ben” because he once referred to the Fed’s ability to rescue the economy with a “helicopter drop” of cash. And Draghi is, perhaps inevitably, “Super Mario.”

For now, Draghi appears to have the most influence over global markets and the world economy. After all, Draghi had to cancel his appearance at the Jackson Hole conference where Bernanke made so many headlines. He was too busy preparing for the ECB’s Sept. 6 meeting and looking for ways to hold Europe together.

Condon reported from New York. AP Business Writer David McHugh in Frankfurt contributed to this report.
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