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Global banking crisis deepens, ECB cuts interest rates

Banking giants in Europe and the United States faced fresh questions about their ability to ride out a global financial crisis which prompted European Central Bank interest rate cut on Thursday...

Shares in Bank of America and Citigroup, two of America's biggest banks, tumbled as they faced a new crisis of confidence over whether they have enough capital to cover losses from toxic assets and global recession...

"The large banks in the United States are not lending, and they're desperate to conserve capital," said Dan Alpert at Westwood Capital in New York. "Banks only remain going concerns because the federal government is topping up their equity."

A profit warning from Germany's Deutsche Bank on Wednesday and a prediction HSBC may need fresh capital shook confidence in two major European banks previously credited with dodging the worst of the crisis.

The crisis claimed another big scalp -- Canada's Nortel Networks Corp, North America's biggest telephone equipment maker, filed for bankruptcy.

Citigroup, whose shares dived 23 percent on Wednesday, plans to report quarterly results on Friday and analysts are looking for a fifth straight multibillion-dollar loss.

The bank was also widely expected to provide details of a reorganization of the company designed to ensure its survival. Bank of America is close to receiving billions of dollars of support from the U.S. government, a source familiar with the matter said, as it tries to digest Merrill Lynch, the investment bank it bought on Jan. 1, which has billions in troubled assets ranging from commercial real estate to subprime mortgages.

Citigroup has already taken $45 billion in government funds while Bank of America and Merrill have received $25 billion.

There is no relief in sight, warned Jamie Dimon, chief executive of rival JPMorgan Chase & Co, which reports its own fourth quarter results later on Thursday.

"The worst of the economic situation is not yet behind us. It looks as if it will continue to deteriorate for most of 2009," he told the Financial Times.

ECB CUTS RATE

The European Central Bank cut its benchmark interest rate by 50 basis points to 2.0 percent on Thursday, matching its lowest ever rate as inflation plummets and recession spreads.

The cut, in line with consensus forecasts, marks the fourth cut in just over three months amidst signs the financial crisis is biting hard into the real economy and inflation threatens to fall further below the ECB's 2 percent ceiling.

Data across the developed world pointing to a deepening recession and fears that more public money may be needed to keep banks afloat weighed on financial markets.

European stocks lost ground for a seventh session running, dropping 0.8 percent on escalating fears about the banking sector.

The yen, which tends to gain from its perceived safety in times of market stress, climbed and Tokyo's Nikkei share average slipped close to 5 percent after Japan's core machinery orders fell at a record pace in November.

The financial crisis began in 2007, when bank lending dried up because of huge losses on U.S. home loans. It took a sharp turn for the worse with the collapse of U.S. bank Lehman Brothers last September and has now pushed much of the world into recession.

Euro zone policymakers have been slower than counterparts in the United States, Japan and Britain to lower interest rates.

But news Germany contracted sharply in last year's final quarter and euro zone industrial output plunged in November raised expectations the ECB will cut deeply.

"The data flow does tell a fairly consistent picture, which is unfortunately very downbeat," said Dresdner Kleinwort economist Rainer Guntermann, who sees a 50 basis point cut to 2.0 percent.

Japanese data showed core machinery orders fell a record 16.2 percent in November to a two-decade low, while wholesale inflation hit a four-year low, flagging the risk of deflation.

Deflation -- when price falls and weak demand feed each other in a vicious downward spiral -- would risk turning recession into depression.

The global slowdown has hit Japan, with big firms such as car maker Toyota Motor Corp and electronics firm Sony Corp slashing production and cutting jobs as export orders dry up.

Nissan Motor Co the country's third-largest car maker, is set to post an annual operating loss, a company source said. The company had forecast a profit.

The Japanese numbers followed poor U.S. retail sales data on Wednesday that suggested the year-long recession was deepening and could be the longest since 1981.