



After \$1 trillion European bailout, markets bounce back

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By **David J. Lynch**, USA TODAY



By Martin Oeser, AFP/Getty Images

A trader sits in front of a board displaying the DAX index of leading shares on Monday in Frankfurt. The index gained more than 5%.

Trading screens that were bathed in red for weeks blossomed into green Monday as relieved investors welcomed a nearly \$1 trillion European bailout fund.

The Euro Stoxx 50 blue-chip index soared more than 10% and bond yields in Greece and other troubled continental economies plunged. The yield on two-year Greek debt fell 10.7 percentage points to 7.45%. Portugal's fell 3.05 percentage points to 2.92%.

But after years of looking the other way while governments overspent, Europe faces a long climb back to fiscal prudence. New austerity measures expected not just in Greece, but in larger economies such as Spain, will weigh on an already sluggish continental recovery.

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The International Monetary Fund expected the 16-nation eurozone to grow by less than 1% this year before Sunday's promise of new spending cuts in heavily indebted peripheral countries, due by May 18. "In the best case, Europe won't be a drag on global growth. But it's unlikely to make a significant contribution to global growth," said Eswar Prasad, a former IMF economist who teaches at Cornell University.

Even weaker demand in Europe means the European Central Bank will likely keep interest rates low for an extended period. The euro strengthened Monday but fell back by the close of trading to \$1.28. Analysts at Morgan Stanley and Brown Bros. Harriman expect the single currency to weaken further. And that will make life tougher for U.S. exporters.

"The euro is going to fall," said Marc Chandler, global head of currency strategy for Brown Bros.

After months of failing to keep pace with market pressures, Europe's leaders delivered in a big way Sunday. The nearly \$1 trillion package of loans from the European Union and the IMF was followed by bold steps from the European Central Bank, which said it would buy government and private-sector debt where needed to avert market seizures.

That represented a major turnaround for the bank. "This really shows how spooked they were," said

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Jacob Kirkegaard of the [Peterson Institute](#) for International Economics.

Amid Greek riots over stringent debt-reduction moves, pressure built all week for stronger action. By Friday, Europe's banks, increasingly concerned about the risks of lending even to other banks, had parked nearly \$380 billion in overnight accounts at the ECB — nearly as much as at the time of the September 2008 [Lehman Bros.](#) bankruptcy.

Signs of investor doubt about the health of major banks likewise were appearing. The cost of insuring a nominal \$10 million of [Banco Santander](#) debt topped \$320,000 vs. less than \$125,000 in mid-March.

The "shock-and-awe" EU announcement eliminates the danger that Greece's debt woes will ricochet through Europe's banks, undermining financial stability as the global recovery struggles for momentum. But Greece still may need to restructure its massive debt.

And while the new bailout fund is enormous, it equates to little more than one year of the financing needed for Europe's four potential problem states: Portugal, Spain, Ireland and Italy, former [World Bank](#) economist Uri Dadush said.

The EU package will buy time for troubled economies to tackle their budget and competitiveness problems. "The question is: Will the time be used?" he said.

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