Just One More Thing… Central Banks Are Cutting Rates Like There Is No Tomorrow

This year we have apparently seen 23 central banks cutting rates; personally, I have lost count. The question is, why now? How dire are things? And what are these things that are apparently so dire. The US and the UK are the only two majors not cutting rates. Lets exclude the basket cases and currency manipulators from all this. Everyone else either is cutting rates, or will surprise us some Wednesday morning with a jaunty rate cut. Why? The most obvious answer is deflation. Deflation renders real interest rates higher than nominal interest rates and where an economy is struggling and a central bank is aiming for zero real rates, deflation can force a central bank into operating negative nominal rates. It's happening as we speak at the Swiss National Bank and Sveriges Riksbank.

Real interest rates, where we consider core instead of headline inflation has been negative in the US and UK since 2008 and continue to track in negative territory. It is understandable that with the stabilization of growth in these two countries, their central banks are leaning towards raising interest rates. They want to raise interest rates, they just might have complications to deal with such as their currencies and terms of trade. The Eurozone, however, despite zero nominal rates, faces deflation and thus a rising real interest rate which has turned positive since December 2014. Riksbank, which began tightening in 2010, far too early in hindsight, has had to cut rates steadily since 2011. Real krona rates have only just turned negative in October 2014. The Swiss, operating at zero real rates since 2013, recently depressed nominal rates so that real rates are trading at 2008 levels. China's rate cuts were not a response to real rates creeping up but rather to address flagging demand as reforms are implemented. Of the majors only the Eurozone, it appears, has suffered from real rate creep where real rates bottomed at -2% in 2012 and have crept up to +70 basis points in March 2015.

But does the world need negative rates some 7 years from the crisis of 2008? The US economy's health is quite apparent, as is the UK's. Only China is slowing significantly, and by the way causing a slowdown for its vendors in commodities and luxuries. Japan has sunk back into recession but not to worry, inflation is the highest in any major developed country. India is reinvigorating fast under new management. The Eurozone economy recovered in 2010 but slumped in late 2011. It has since bottomed in 2013 and growth appears to be picking up again even as the ECB has embarked on quantitative easing to address deflation.

So let me repeat the question on my mind: Why are central banks around the world cutting rates all at the same time? Do we really need real rates to be so negative 7 years on from the crisis of 2008? What am I missing?