IT WAS a day of desperate global action, unprecedented in both scale and cost, intended to stymie the international devastation being wrought by the financial crisis.

As the London stock market steeled itself to open again following days of vicious battering, Alistair Darling, the Chancellor, rose to stake the future of the country and the Cabinet on an audacious £500 billion banking bail-out.

And barely had the City begun to digest the hugely complex and unorthodox scheme when it was sent reeling again by an unscheduled interest rate cut – mirrored across the world – by the Monetary Policy Committee. It was the first such co-ordinated approach since the 9/11 terrorist attacks in 2001 – yet another indicator, had one been needed, of the gravity of the situation.

The half percentage point drop was immediately passed on to millions of borrowers, with leading high-street banks cutting their mortgages.

The government's scheme, a three-part plan which takes in short, medium and long-term measures, was welcomed by business leaders and analysts.

David Kern, adviser to the British Chamber of Commerce, said: "The government has taken a radical step, but it is one we welcome."

But there was concern a phenomenal amount of taxpayers' cash was being staked on a last-ditch measure that could fail. The Taxpayers' Alliance accused ministers of failing to address other options first.

Meanwhile, the International Monetary Fund (IMF) issued a fresh warning that Britain was on the brink of recession.

In its latest World Economic Outlook, it predicted the UK economy would contract by 0.1 per cent next year as growth across the developed countries slowed to almost zero.

The downturn will mean lost jobs, with unemployment forecast to rise from 5.4 per cent to 6 per cent, while public finances were said to be "considerably weaker" than in previous slowdowns. However, the IMF said it was expecting Britain to bounce back strongly in 2010.

The £500 billion plan includes the government taking shares of up to £50 billion in leading banks, increasing funds available to banks to £200 billion, and guaranteeing their debts when they lend to one another. The guarantees are likely to cost up to £250 billion.

The Prime Minister called the plans "bold and far-reaching", but admitted they would offer no quick fix.

Eight UK banks and building societies – including Royal Bank of Scotland, Halifax Bank of

Scotland, Barclays, Lloyds TSB and Nationwide – have pledged to increase their capital by £25 billion but the government will pump in the funds if called upon. The Treasury also stands ready to make at least another £25 billion available, if necessary.

The Bank of England – alongside its interest rate cut – is taking emergency action to help ensure banks have enough cash to run their day-to-day activities. It has increased to £200 billion the size of its special liquidity scheme that lets banks swap risky assets for Treasury bonds.

The government is also making the further £250 billion available for banks to guarantee debt, but a fee will be charged.

Mr Brown moved to reassure taxpayers they would have the potential to "earn a proper return" from their investment. There would be "strings attached and conditions to be met" to protect taxpayer interests.

One key concern is whether there will be controls over the bonuses of the "fat cat" bank bosses. Gordon Brown, the Prime Minister, said such issues would be dealt with case by case. Remuneration should be "based on responsibility, hard work, effort and enterprise", he said.

It had been claimed that RBS bosses, chief executive Sir Fred Goodwin and chairman Sir Tom McKillop, had offered to leave under a boardroom clear-out agreed with the government, but this was denied by the bank.

The announcement provided an initial boost to the FTSE 100 index of leading shares, and in particular to banking stocks, but this fell away later in the day. The FTSE closed at a loss of 5 per cent – its lowest close since 2004 – while banks failed to hold on to the huge gains of up to 60 per cent made earlier in the day.

When Mr Brown stood to address the House of Commons on the package, which could well determine how his premiership is judged, he was able to announce the interest rate cut.

Central banks across Europe, the US, Canada and China also reduced interest rates in an emergency move.

The banks hope to encourage nervous consumers and businesses to spend more freely again after widespread housing, credit and financial problems.

The cut – which was immediately passed on to more than five million homeowners – was cautiously welcomed by analysts and business leaders.

Miles Templeman, director-general of the Institute of Directors, said: "Before today's announcement, the financial system was in the deep freeze. After today, it might be in the fridge, but there is no guarantee. Nobody should be under any illusion that the financial system is now fixed. Our concern now is for the real economy and how much it will slow.

"There remains a real risk that the economic downturn under way will further undermine bank capital due to rising repossessions and bad debt."

Howard Archer, an economist, of Global Insight, said: "It's not the magic pill. We have a lot of difficult times ahead. But the first stage is stopping things getting worse, and the hope is this will help to stabilise the economy."

Martin Weale, director of the National Institute of Economic and Social Research, said that, for the UK, it was important that the move came alongside the £500 billion package.

He said: "The international banks concluded there is a major international banking crisis. Banks were collapsing in Europe, as well as the United States. I think they rather optimistically concluded a rate cut of this type can restore confidence."

Rate cuts were "a valuable piece on the side", but he added: "The key issue is for affected countries to do what Britain has done and show governments are prepared to inject equity capital into banks that look as though they need it.

"We will only be confident the worst is over when the US adopts a scheme like Britain."

And Louise Cuming, the head of mortgages at moneysupermarket.com, warned: "This is not a magic cure-all, and we won't see either the mortgage or the housing market bouncing back to where it was 18 months ago."

Following the announcements, Mr Brown spoke by phone to the French president, Nicolas Sarkozy, the German chancellor, Angela Merkel, and the Italian prime minister, Silvio Berlusconi, as well as the EC president, José Manuel Barroso.

The government is expected to hold up its plan as a potential model for the rest of Europe. The EU – which is concerned about competition implications of a scheme by Ireland to safeguard its deposits – later said it saw no problem with Britain's move.

Mr Darling is due to fly to Washington today to discuss global action on the crisis.

How clever was it? We offer some marks out of ten

Bill Jamieson,on the wisdom and implications of the British bail-out

IMMEDIATE IMPACT:

5 out of 10. Shares in HBOS and Royal Bank rallied after a faltering start. HBOS closed 24.5 per cent higher and RBS was up 0.8 per cent. UK shares overall continued to plunge, with the FTSE100 down another 5 per cent or 238.53 points at 4366.69. But the reaction in money markets to the package was notably more positive.

TIMING:

1 out of 10. Work has been under way on a bank rescue for weeks. So why the long delay?

RATE CUTS:

9 out of 10. The co-ordinated nature of the move by the world's central banks was particularly impressive. But more will be needed in the coming weeks. The near immediate passing on of the half per cent rate cut to mortgage borrowers is desperately needed good news for home-buyers.

PRESENTATION:

3 out of 10. Not impressive. And negotiations going on till early hours smacked of panic.

CONTENT:

8 out of 10. The package itself broadly went down well in money markets. It is seems well thought out, targeted at the key problems of capital strength and liquidity, is flexible, and does not crush the ordinary shareholders into oblivion.

OVERALL EFFECT:

Jury out.

This is going to take time. And this emergency package for UK banks will be of little use if the fiery panic across the world's markets is not staunched.

It will not stop the recession that is already under way. But what the deal has certainly prevented is a total collapse in confidence in the UK's financial system. It has improved the odds that there will still be a functioning banking system left by the end of the month. Whether that will be true by the time the storm has run its course may depend on further injections of central bank funds – and more rate cuts.

The huge efforts of the US Federal Reserve, the US Treasury, and the British and European governments and central banks have still not turned the tide.

WHAT IS THE TREASURY'S AIM?

It is to staunch the flight of confidence and to revive the inter-bank market – banks lending to other banks. To meet these objectives, it has effectively created a core group of banks of capital strength that will form the heart of the new UK financial system. By doing so the hope is this will end the flight of confidence and stop the run on bank shares.

The government is setting aside a further £25 billion to help other institutions build their capital so that they too will be fit counterparties for the core members. But in reviewing eligibility for

inclusion, the government "will have due regard to an institution's role in the UK banking system and the overall economy".

It is likely a two-tier banking system will develop, similar to the world of 40 years ago when there was a distinction between clearing banks and secondary banks. The government will require a full commitment from participants in its scheme to support lending to small business and to home-buyers.

WILL IT WORK?

No-one can be sure. And certainly nothing is going to work until the firestorm raging across global markets is put out. Overnight Japan's stock market plummeted 9.4 per cent – its biggest one-day drop in 21 years. In Germany the Dax Index opened down 4.8 per cent while trading on the Moscow stock exchange was again halted.

Not even that co-ordinated rate cut by the US Federal Reserve (to 1.5 per cent), the Bank of England (to 4.5 per cent) and the European Central Bank (3.75 per cent) rallied markets as had been expected.

Tumbling share prices are a signal that a severe recession is going to hit whatever governments now do.

The overall aim of government is to reduce the risk that recession turns into depression through the vicious cycle between the worsening economy, deteriorating credit quality, heightened financial strains and reduced credit availability.

The aim is to ensure that there is still a functioning banking system left a) by the end of the month and b) once the recession ends.

The measures themselves will not on their own end the financial crisis. This is global in nature and the interlinkages are complex – and potentially highly flammable. So it is unlikely measures by any one country can return financial conditions to normal.

Says Saunders: "We are not yet even halfway through the decline in UK house prices. We are not even close to halfway through the UK recession, with associated job losses, business failures, mortgage arrears and repossessions and debt write- offs. Much pain lies ahead."

TOO LITTLE TOO LATE?

Many fear so. Further bank recapitalisation and liquidity measures may be needed. And there will almost certainly need to be further rate cuts, taking UK rates down to 3 per cent – possibly lower.

Banks move to pass on benefits
LINDSAY MCINTOSH

BORROWERS finally got some good news yesterday when UK banks passed on a shock interest rate cut.

The Bank of England dropped the base rate from 5 to 4.5 per cent at noon, in the surprise move 24 hours ahead of its scheduled decision. Some economists said it might soon plunge much lower.

Yesterday's action was mirrored by the world's major central banks, including the Federal Reserve in the United States and the European Central Bank, in an attempt to prevent a global economic meltdown.

Almost instantly, Britain's high street banks pledged to pass on the cut to customers. HBOS, Barclays and Lloyds TSB – which lends through the Cheltenham & Gloucester – were the first to cut their standard variable rates in line with the Bank of England.

Where the cut is passed on in full, it will knock about £47 off monthly repayments on a typical £150,000 mortgage, reducing repayments to £1,012.81 a month and saving consumers £570 a year, based on a new rate of 6.5 per cent.

Those with loans of £250,000 will benefit even more, saving £79 a month or £950 a year.

The rate reduction was welcomed by the Council of Mortgage Lenders, alongside the other measures taken by the government to help the banking sector.

Michael Coogan, the CML's director-general, said in cutting mortgage rates, the banks had helped to strengthen the rescue package announced by Gordon Brown, the Prime Minister, and Alistair Darling, the Chancellor.

"Not only are the tripartite authorities now pulling together decisively to address domestic confidence, but international central bankers are also collaborating much more effectively on their position," he said. "All this decisive action augurs well for an improving market situation, even though no-one is pretending the tough times are over yet."

The US Federal Reserve reduced rates from 2 per cent to 1.5 per cent and the European Central Bank trimmed its rates from 4.25 per cent to 3.75 per cent. The central banks of Canada, Sweden and Switzerland all took similar action.

The Bank of England said that the drop was justified by likely falls in inflation in the coming months.

Howard Archer, the chief European and UK economist at Global Insight, predicted interest rates could be as low as 4 per cent by the end of the year.

Who thought what of rescue package

"Taken together with the co-ordinated cut in interest rates, today's package represents a

welcome step on the road to normality in financial mar-kets, which is so critical for the wellbeing of the United Kingdom economy."

Keith Skeoch, CEO, Standard Life Investments

- "The government is using taxpayers' money as an easy way out, and haven't fully explored other options that don't put £50 billion of our hard-earned cash on the line." Matthew Elliott, chief executive of the TaxPayers' Alliance
- "At last, the UK Treasury and Bank of England Monetary Policy Committee are wakening up to the scale of the crisis triggered by the credit crunch." Jonathan Fair, chief executive of Homes for Scotland
- "In the wake of the recent financial carnage, the MPC's decision to cut the base rate by 0.5 per cent to 4.5 per cent is welcome news for struggling UK homeowners. This is the first reduction since April, and many borrowers will be breathing a long-awaited sigh of relief." Ann Robinson, director of consumer policy at uSwitch.com
- "It is very welcome that the Bank of England has heeded calls for an interest rate cut to ease lending conditions and provide a stimulus to households and businesses, and brought forward the announcement in conjunction with other central banks. Alex Salmond, First Minister
- "Excessive risk-taking should not be rewarded but punished." Gordon Brown, the Prime Minister

CREDIT CRUNCH N NUMBERS

So what could £500bn buy?

- Four-and-a-half NHS's (based on annual UK health budget)
- Six UK education systems (based on budget for 2008-9)
- 55 UNs (based on its annual budget)
- 20 Beijing Olympics
- 1,250 Scottish Parliaments
- Seven Vietnam wars
- Four-and-a-half Iraq wars
- South Africa, Nigeria, Cameroon, Ghana, Tunisia, the Ivory Coast, Madagascar, the Republic of Congo, Chad and Malawi combined (based on their GDPs)

Source...