Concerns grow behind G-7 official optimism

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The meeting of finance ministers from the major capitalist nations, held in Palermo Sicily on Saturday, concluded with an optimistic assessment of the state of the world economy, despite the downturn in the US and the continued stagnation of Japan.

"The basic factors that have supported sustained growth in many of the major industrial economies remain in place," the Group of Seven (G-7) statement issued at the conclusion of the meeting declared.

On the US, the statement said that "economic fundamentals remain strong," while for Japan the G-7 predicted a "modest recovery" but warned that "downside risks remain."

The G-7 assessment of the state of the world economy came in the face of reductions in growth assessments by the International Monetary Fund and further signs of a slowdown in the US.

The IMF has cut its forecast for growth in the US economy for 2001 from 3.2 percent—the prediction it made last September—to just 1.7 percent, while reducing the forecast for world economic growth from 4.2 percent to 3.4 percent.

Figures on the US economy released last Friday show that industrial production fell again in January, the fourth consecutive monthly decline and the longest series of monthly declines since the recession of 1990-91. The rate of capacity use in the manufacturing industry has now dropped to its lowest level since August 1992. At the same time a preliminary report from the University of Michigan showed that its consumer confidence index had fallen for the third month in a row and was now about the same level it was at the start of the last recession in July 1990.

Across the Pacific, the Japanese government downgraded its assessment of the state of the economy on Friday, saying that it expected growth to be "more moderate" as a result of a loss of exports to the US. Revised figures have shown that the Japanese economy contracted by 0.6 percent in the September quarter. If a further decline is recorded for the December quarter then Japan will have officially entered a recession.

While the problems being encountered in the US and Japan were more or less passed over in the official G-7 statement, they are giving rise to concerns. As one unnamed British official told the *Financial Times*: "If you look back to last autumn, we were looking at quite a benign outlook for the world economy. Since then we have had the US figures for the fourth quarter and a downward revision to Japanese growth. These are real changes."

And changes have not only taken place on the economic front.

The coming to power of the Bush administration has created a degree of uncertainty in the ranks of the G-7 nations, and more broadly, over the likely response of the US to a major world financial crisis, along the lines of that in September-October 1998, or a world slump.

These concerns were heightened by an interview with incoming US Treasury Secretary, Paul O'Neill, published in the *Financial Times* last Wednesday. O'Neill's remarks indicated that the new administration favour a more hands-off stance in relation to global financial turbulence.

O'Neill took issue with the view that crises were an inevitable feature of global capitalism, requiring the intervention of financial authorities. Rather than being caused by the market, crises occurred when market mechanisms did not operate freely. "It doesn't have anything to do with the failure of capitalism. It's to do with the absence of capitalism."

According to O'Neill, the market should be able to forestall crises before they happened, and the IMF and the World Bank should never have to intervene. "In an ideal world the fire company never leaves the firehouse ... hopefully they learn how to play chess really well."

As if this were not enough to arouse concerns among his G-7 partners about the future role of the US in financial crisis management, O'Neill cast doubt on the value of the organisation itself.

"Travelling around the world to tell each other about what's going on in the economy doesn't seem to me to be a primary reason for meeting," he told the *Financial Times*. "I can go into my office and look at my machine and find out what's going on right now in London. I don't need to go to Palermo to find out."

In an editorial published on Saturday, under the title "First world fundamentalism," the *Financial Times* drew attention to some of the concerns that are obviously felt in European capitals.

"Over the past eight years no one has had serious cause to question the US commitment to international economic co-operation in the Group of Seven developed countries' forum," it noted. But the comments by O'Neill in the lead up to the G-7 talks "threw the cat among the Sicilian pigeons."

The editorial also noted that Wall Street was worried about the make up of the new regime. "While investors remain convinced that Mr Greenspan will come to the rescue in a market panic, Mr O'Neill is hinting that the next hedge fund or bank collapse will be viewed with a less sympathetic eye in the Treasury than at the Fed."

It went on to point out that even if recent disturbances in the markets proved to be nothing more than transitional upsets associated with the shift from a Democratic to a Republican administration, it was clear that "O'Neill's remarks certainly point in a more unilateralist direction than under the Clinton administration."

Arguing for continued intervention in financial markets, the editorial claimed that "events will in due course force this new US administration into economic co-operation" but until then the world would have to wait to see how the balance was struck between "fundamentalist capitalism and business pragmatism."

And that wait may not be a long one if, in the lead up to the next meeting of the G7, the situation in the world economy changes as fast as it has since last September.