Divisions widen at Genoa in the face of global economic downturn

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When the first summit of the major capitalist powers was convened in 1975 at Rambouillet, just outside Paris, its stated aim was to co-ordinate economic policies in the face of what was, to that point, the most serious economic crisis in the post-war period.

Little co-operation was obtained then and a quarter of a century on, the divergences between the so-called G-7 nations have widened. (Economic statements are produced by the major capitalist powers of the G-7. The G-8, which discusses political matters, includes Russia.) Faced with what an increasing number of economic commentators are arguing is the most serious downturn in the past decade, and possibly since 1975, a mere 90 minutes was devoted to discussing the world economy, and then only to ratify a statement whose main purpose was to paper over all the differences between the major powers.

The statement began by acknowledging that "the global economy has slowed more than expected over the past year" but then went on to offer the reassurance that "sound economic policies and fundamentals provide a solid foundation for growth."

In fact, an examination of the global economy and its key national components reveals that the problems lie precisely in the fundamental relationships. Take the United States. The downturn is not the result of a tightening monetary policy and higher interest rates, the trigger for previous recessions, but is the outcome of a massive over-capacity in key sections of industry, especially high-tech, combined with sharply falling profits.

Falling consumer demand, which leads to falling investment and capital spending, has generally sparked past recessions. But in this case, consumer spending has remained relatively high and the downturn has been set off by a rapid decline in investment spending. This is the main reason why, unlike previous recessions, cuts in interest rates by the Federal Reserve Board have failed to bring about an upturn.

As Yale economist Jeffrey Garten noted in a comment published in the *New York Times* last Wednesday, "the global economy has come to resemble a balloon rapidly losing air."

"The world's three largest economies—in the United States, the European Union and Japan—are slumping, and the financial and trading connections among them are reinforcing the downward spiral. Emerging markets from Argentina to Turkey to Indonesia have serious financial problems, too, all of which are made worse by the slowing of the world's major economies. Corporate profits everywhere are evaporating, and stock markets are weakening."

In a call for the Bush administration to adopt a more international orientation, Garten warned that while the increased flows of money and information around the world were working to make the economic downturn deeper and more widespread, "few mechanisms" now exist to manage them.

A comment published in the Hong Kong-based *South China Morning Post* under the title "Gathering in Genoa heralds start of global slump" pointed out that the "magic" of interest rate cuts was not working any more and the world was "teetering on the brink of a long, deep recession." It cited warnings from the economics group at the HSBC bank in London that the "US recession will be deeper and longer than the consensus currently predicts" and from the investment bank Bear Stearns which claimed that "despite occasional signs of US economic resilience", the world was "falling into a long recession."

As for the "fundamentals" of the US economy—the main engine for world growth—it is here that the major problems reside. The payments deficit, running at around 4.4 percent of gross domestic product, is at an historic high, the dollar is overvalued and the savings level has moved sharply into negative territory.

Across the Pacific, the Japanese economy, the world's second largest, has been in the grip of recessionary forces for the past decade, despite the application of the largest government spending measures aimed at boosting the economy ever seen in peacetime.

The G-7 economic statement was forced to note that in Japan "economic activity has further weakened, and prices continue to decline." It called for "vigorous" implementation of financial and corporate sector reforms to lay the foundation for stronger growth over the medium term and welcomed "the recently announced reform initiatives which will contribute to this end."

But in fact there is considerable concern both within Japan and internationally over the so-called reforms measures announced by the Koizumi government. Cuts in government spending and the wiping out of bad loans from the banking system by shutting down the companies that depend on them may push the Japanese economy into an even deeper recession.

Furthermore, if the restructuring of the banks and financial system proceeds too rapidly this may lead to the withdrawal of Japanese finances from the rest of the world, above all from the US where they play the key role in financing the burgeoning US foreign debt.

The statement noted that in Europe economic activity had weakened but held out the prospect that tax cuts and "structural reforms" would support non-inflationary growth. Nothing, however, was said about interest rate policy because there are major disagreements, with the European Central Bank (ECB) pointedly refusing to follow the lead of the Federal Reserve Board in bringing down rates.

The ECB for its part claims that it is not possible to reduce interest rates because of inflationary pressures, in part resulting from the fall of the euro against the US dollar. But when this was raised, Bush dismissed the prospect of any concerted action to bring down the value of the US currency saying that the dollar had to float and that the market would determine its value.

The only reference to the signs of growing turbulence in the so-called emerging markets was commendation of the spending cuts in Argentina and Turkey and a call for "the continued implementation of their reform programs in close collaboration with the IMF."

In light of the financial crisis three years ago, described by the then US president Clinton as the most serious in 50 years, it might have been expected that the statement would contain more specific commitments to take action should similar conditions re-emerge. But there is no agreement what can or should be done. The Bush administration is opposed to bailout actions by the IMF, with the Treasury secretary Paul O'Neill casting doubt on whether there is any such thing as "contagion"—the process through which a crisis in one section of the financial markets (such as the Russian default in September 1998) can rapidly threaten the stability of the whole system.

Twenty months ago, the divisions between the major powers were clearly on display in the collapse of the World Trade Organisation ministerial meeting at Seattle. Since then there has been a push to ensure that trade negotiations recommence, lest protectionist and even outright trade war measures start to emerge.

Accordingly, the summit statement insisted that economic growth required a "renewed commitment to free trade", that opening markets globally and strengthening the WTO was an "economic imperative" and even contained a pledge by the G-7 leaders to "engage personally and jointly in the launch of a new ambitious round of global trade negotiations at the Fourth WTO Ministerial Conference in Doha, Qatar this November."

But nothing has happened since Seattle to narrow the divisions among the major capitalist powers—over such issues as agriculture, investment policies and gene technology—or lessen the opposition of poorer countries to the operations of the global trading system. Indeed the differences may be widening, with concerns in Europe that the Bush administration may be orienting more towards the establishment a free trade region of the Americas.

When the economic summits began in 1975, world capitalism was still operating, at least to some extent, within the framework of the mechanisms of post-war economic regulation. But over the course of the next decade and a half, the rapid expansion of the international finance system and the development of global production undermined what remained of them.

Today the forces unleashed by these processes dwarf the resources of any national government or group of governments, placing the course of the world capitalist economy increasingly beyond their control. At the same time the differences between the major powers have widened and are certain to deepen if the downturn in the world economy turns into outright recession.