

World markets expecting further falls

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World stock markets are bracing themselves for further turbulence following the sharp decline on Wall Street last week which saw the Dow Jones index close at its lowest level for the year. The sell-off began on Wednesday and accelerated as the market fell 191.24 points on Friday, the biggest one-day decline for almost two years. For the week, the Dow fell 373.83 points, bringing the total decline for the year to more than 6 percent.

Summing up market sentiment, the *Washington Post* noted that the “bullish mood”, which had been seen at the end of last year, had now disappeared. Instead, there was a sentiment of “intense anxiety in which all news is viewed negatively and not even strong earnings reports... can overcome fears of a slackening economy, a bulging trade deficit, and a worn-out consumer struggling to keep up with higher energy costs.”

The sell-off was sparked by adverse reports from some of America’s biggest companies, coupled with fears that the US economy could be sliding into a recession.

General Motors has stated that its year-end profits could fall to below \$1 billion—a drop of \$3 billion from its estimates as recently as January. Its operations in North America could record a loss of more than \$1 billion in 2005. Shares in the company touched a 12-year low last Thursday amid rumours that it could possibly file for bankruptcy. GM is desperate to cut former employees’ health and other benefits, which are regarded by financial markets as the chief obstacle to the restoration of profitability. Credit rating agencies are on the verge of reducing GM’s debt to junk bond status.

But GM was not the only problem. After reporting a net income of \$1.4 billion—5 percent below the level expected by the market—IBM saw its shares plunge by 8.3 percent on Friday. The fall extended across the range of technology companies, which are most

dependent on an expanding economy. The technology-dominated Nasdaq composite index fell by almost 2 percent, bringing its losses for the year to more than 12 percent.

Reports on the general state of the US economy also contributed to the downturn. On Tuesday it was announced that the US trade deficit had expanded by a further \$2.5 billion in February to reach an all-time high of \$61 billion for the month. No serious commentators any longer believe that even a sharp fall in the dollar and a corresponding rise in East Asian currencies—especially the Chinese yuan—will lead to a significant narrowing of the trade gap. This is because the main factor inhibiting the increase in US exports is the lack of growth in major world economies. Large areas of the eurozone are stagnant—German unemployment has reached 12 percent, close to its highest levels in the post-war period—and the latest surveys from Japan show that business confidence was weaker than expected for the first quarter.

Falling consumer confidence in the face of rising oil prices and fears about the general state of the US economy also contributed to the market downturn. The influential University of Michigan’s consumer sentiment index dropped to 87.7 in mid-April from 92.6 in March, compared with expectations of a drop to about 91.3.

Other figures showed that factory output fell by 0.1 percent last month, the first decline since last September. Production of cars and home electronics fell in March, indicating that consumers are putting off spending plans. Bank of Tokyo-Mitsubishi economist Christopher Rupkey described it as “worrisome situation” because “once confidence takes a hit, consumers go on a buying strike. There has been a sea change in expectations for the economy and the culprit is rising energy prices at the pump.”

The slide on Wall Street formed the backdrop to

meetings of the International Monetary Fund (IMF) and the G7 meeting of finance ministers and central bankers held in Washington over the weekend.

A statement issued by the IMF's International Monetary and Finance Committee (IMFC) forecast that global growth would remain "robust" in 2005 but warned that "widening imbalances across regions and the continued rise in oil prices and oil market volatility have increased risks." There was a potential for sharper-than-expected increases in interest rates and increased exchange rate volatility. The chief imbalance in the world economy was the balance of payments deficit of the United States, now requiring an inflow of \$2 billion per day to sustain it, and absorbing up to 80 percent of the available surplus capital from the rest of the world.

Speaking in his capacity as IMFC chairman, British Chancellor of the Exchequer Gordon Brown outlined the measures needed to ensure "orderly adjustment of global imbalances". The committee had "agreed to call for concrete actions in all continents, fiscal consolidation to increase national savings in the United States, greater exchange rate flexibility as appropriate supported by continuing financial sector reform in Asia, continued structural reforms to boost growth and domestic demand in Europe, and further structural reforms including fiscal consolidation in Japan."

But in the absence of any concrete plans, the IMF prescriptions were virtually meaningless.

That did not stop them being repeated in the G7 communiqué. The only difference was that the G7 added the call for "vigorous action" to meet the desired goals without, however, spelling out what it should comprise.

Speaking to a press conference following the IMFC meeting, the fund's managing director Rodrigo de Rato said the risks to the world economy posed by financial imbalances were increasing. He claimed that the "central scenario" of the world economy was "extremely positive". De Rato emphasised, however, that the IMF was not only advising countries "but calling on countries to take action on those issues of global imbalances, insisting that if policies do not adapt, do not change to react to those imbalances, we run the risk of an abrupt correction by the markets at a moment in which confidence, for different reasons, could evaporate or could be reduced."

The clear signs of desperation in the IMF chief's

remarks are a reflection of the growing contradiction in the present situation. While the "central scenario" of the world economy is "extremely positive", it will nevertheless lead to a major crisis if it continues to be played out in the same direction.

De Rato concluded his remarks by insisting that that the decision to take action was the "responsibility of governments" and that "right now there are important economies in the world that face a special responsibility regarding world imbalances."

But there is no sign that any of the major governments have any real idea of what to do, let alone the capacity to decide on a joint plan of action.



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