Japan disaster to intensify global economic contradictions

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In former "normal" times, the Japanese earthquake disaster would not have led to a global economic and financial crisis. But those days are long gone. In the present situation, it could well be the catalyst that sets off a new stage in the global financial breakdown that began with the collapse of Lehman Brothers in September 2008.

A central banker from the Group of Seven major capitalist economies, who declined to be named, told Reuters: "I think the world economy is going to go right down and it has happened at a time when financial markets are still fragile."

Even before the events of last Friday, the global financial system was looking increasingly unstable.

In the US, the two-year rise in US equity markets has been based, not on any upturn in the American economy, but on a massive injection of funds by the Federal Reserve into the financial system. In a recent comment published in the *Financial Times*, business economist David Rosenberg noted that just as the stock market rise of 2003-2007 had been built on a "shaky foundation of unsustainable credit growth and house price appreciation, the current … rally has been built on the even shakier ground of surreal public sector intervention."

The absence of any real recovery in the US economy was underlined by home construction figures released on Wednesday. They showed that last month, construction of single-family and multi-family homes was down 22.5 percent on the level in January, while building permits fell to their lowest level, in seasonally adjusted terms, since the government started recording them in 1960. At the same time, wholesale prices in the US rose by 1.6 percent last month, as a result of higher energy and food costs.

In Europe, it is clear that the banking and currency crisis, which exploded a year ago, has not been resolved as Spain and Portugal come under increasing pressure from financial markets.

And in Asia, it had become apparent that the Japanese economy was about to experience another downturn, while fears were being voiced that the Chinese economic expansion was being produced by an unsustainable real estate and construction boom, fuelled by a massive expansion of credit.

In addition, the rise in oil prices resulting from the turmoil in the Middle East sparked fears of a recession, or at least a significant reduction in economic growth.

Now the earthquake catastrophe has further intensified global instability. One of its immediate effects has been to push up the value of the yen, which yesterday reached a post-World War II record high of 76.25 to the US dollar. This counter-intuitive development arises from the leading role played by Japanese institutions in supplying credit to financial markets around the world.

Notwithstanding its enormous internal public debt, equivalent to more than 220 percent of gross domestic product (GDP), Japan is the world's leading creditor nation, with around $3 trillion in foreign assets. Of this, around $900 billion is invested in US treasury bonds, playing a crucial role in sustaining the American financial system.

In the expectation of insurance and other claims at home, however, Japanese institutions are shifting some of their funds back onshore, thereby lifting the value of the yen. But a rising yen threatens to cut exports and economic growth, and to depress the stock market. This could further undermine the capital position of the banks and insurance companies, forcing them to sell more overseas assets and repatriate funds, creating a negative feedback process. And this under conditions where the total cost to the economy as a result of the earthquake is estimated to be around $200 billion, equivalent to 4 percent of GDP.

With the rise in the yen threatening to further destabilize the global economy, G7 central banks have agreed to sell yen to try to keep down its value. But, at the same time, the US Federal Reserve continues to pump money into the global financial system, through its quantitative easing program, with the aim, among other things, of holding down the value of the US dollar.

It is impossible to predict the exact outcome of these contradictory flows and counter-flows. It is clear, however, that they have the potential to create massive financial turbulence in a situation where none of the problems that led to the 2008 meltdown have been resolved.

Even before the earthquake struck, billionaire hedge fund manager Carl Icahn sent a letter to his clients saying he was returning their money. “While we are not forecasting another market dislocation, this possibility cannot be dismissed,” he wrote. Icahn cited the “rapid market run-up over the past two years” and “ongoing concerns about the economic outlook” as the reason for the decision not to risk “another possible market crisis”.

In a major speech delivered last Friday, prepared before the Japanese events, Bank of England Governor Mervyn King noted that the imbalances in the world economy that had led to the financial crisis in 2008 had not been overcome. “None of the underlying causes of the current crisis have been removed. The problem of ‘too important to fail’ banks is still with us. And even more intractable is the challenge of how to reconcile free trade with a stable international monetary and financial system. Today, the most obvious problem at the global level is that the imbalances are growing again.”

King did not directly refer to Europe, but it is here that the deepening contradictions of the global financial system emerge in some of their sharpest forms. The ongoing crisis of so-called “sovereign debt” is in reality a crisis of the banking system, as well-known American macro-economist Barry Eichengreen noted in a recent interview with *Der Spiegel*.

“The present bailout attempts have never made sense,” he told the magazine. “Essentially, all Germany and France want to achieve with these measures it to protect their own banks from collapsing.... The euro crisis is first and foremost a banking crisis.… European banks are in far greater danger than most people realize.”

The extent of this danger is revealed by the latest figures from the Bank for International Settlements. These show that foreign banks have a total exposure of more than $2.5 trillion to the four most troubled European economies—Greece, Ireland, Portugal and Spain.

The growing threat of a further financial meltdown is emerging in conditions where there is even less possibility of a coordinated international response than there was at the time of the Lehman collapse. In the aftermath of that meltdown, the so-called G20 was invoked as a kind of regulatory and coordinating body for international capitalism.

Two years on, this perspective has been exposed for the illusion it always was. As an article by American economists Ian Bremmer and Nouriel Roubini, published in the latest issue of *Foreign Affairs*, points out, there is not a viable G-20, a G-3 or even a G-2. “We are now living in a G-Zero world, one in which no single country or bloc of countries has the political and economic leverage—or the will—to drive a truly international agenda.” The two economists warned that the consequences will be intensified conflict on the international arena over vitally important issues of macroeconomic policy, trade, finance and climate change. And as the economic and financial shock waves spread out from Japan, these antagonisms will intensify.

The deadly consequences of an economic and political order in which decisions are made to place nuclear facilities in the most earthquake prone region in the world, under the control of privately-owned corporations, can now be clearly seen.

No less deadly, however, are the consequences of a global economic order in which the lives and livelihoods of the world’s people are subject to the blind and destructive operations of the capitalist market and private profit system. They pose the necessity for the international working class to unify around the program of international socialism, to reorganize the global economy to meet social needs.

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