World stock markets slump as Europe moves into recession

Stefan Steinberg
23 September 2011

World stock markets slumped sharply on Thursday following reports indicating a slide into recession in Europe and the US, together with a rapid slowing of growth in Asian markets.

In the US, stock prices went into free fall, with the Dow Jones Industrial average ending the day down 391.01 points, or 3.51 percent. The S&P 500 fell 3.19 percent, and the NASDAQ composite plunged 3.25 percent. The two-day slump in the Dow Jones average was the steepest since the financial meltdown in 2008.

Commodities also fell sharply, with the S&P GSCI index of 24 commodities plunging 4.9 percent. Oil fell below $80, hitting a six-week low. The fall in share prices for raw materials and energy firms was driven by expectations of a worldwide downturn in demand and particularly by signs that manufacturing in China will shrink for a third month in a row.

Stock markets across Europe lost 4.5-5.5 percent as heavy selling took place in London, Frankfurt and Paris. The latest declines mean that many leading European markets have now lost around 20 percent of their value from their peak two years ago.

According to the Markit Economics group, the key Purchasing Managers' Index (PMI) for euro zone economies fell to 49.2 in September from 50.7 in August. The fall under 50 percent means that business activity in the euro zone has now contracted for the first time since July 2009. "The recovery has finished, we are now contracting," the author of the Markit survey, Chris Williamson, commented.

The same report also indicated that European economies would continue to decline in coming months and noted that new orders for euro zone businesses fell at their steepest rate since July 2009. "Things will deteriorate further in the coming months", Williamson concluded.

The main factor in the slump in the euro zone is the decline in economic activity in its biggest economy, Germany. The "recovery" in economic activity in the euro zone countries during the past two years always disguised huge deviations between individual economies. While a number of euro economies are actually in recession—most notably Greece—others are hovering on the brink—Portugal, Spain and Italy. Levels of economic activity in the euro zone were mainly pulled upwards by the growth in its biggest economy, Germany.

Now Germany is also tilting towards recession. The German PMI index also fell to its lowest level in more than two years (50.89 percent). The slide in the figures for both manufacturing and service industries marks the eighth straight month of slowdown in the German economy. According to Tim Moore from Markit: "September's flash PMI data suggest that the recovery in Germany's private sector economy is teetering on the brink."

The indications of a slide into recession in Europe and the sharp market downturn come on the heels of a series of warnings that other parts of the world were also in the grip of recession or rapidly slowing growth.

On Tuesday the International Monetary Fund declared in its *World Economic Outlook* report that "The global economy is in a dangerous new phase" and warned of a double dip recession in the US and Europe. World Bank President Robert Zoellick said that the global economy is "in a danger zone."

US Federal Reserve chief Ben Bernanke announced on Wednesday that the US economy faced "serious downside risks." The measures announced by Bernanke to increase liquidity to American banks means a continuation of the cheap-dollar policy which has forced up the value of the euro and increased the prices of European exports, thereby contributing to the current reverse in the European economy.

At the same time, markets on both sides of the Atlantic took from the Fed's measures a growing conviction that central banks have run out of instruments to halt a deepening economic downturn.

Back to back columns in the *Financial Times* by Roger Altman, the US deputy treasury secretary under President Bill Clinton, and Mohamed El-Erian, the chief executive of

© World Socialist Web Site

the world's biggest bond investment fund, the Pacific Investment Management Company (PIMCO), underscored the growing sense of doom within the financial elite.

Altman’s column, entitled “America and Europe are on the Verge of Disastrous Recession”, warned: “For the American and western European economies to decline again, when unemployment levels are already so high, would be disastrous. It would shock consumers, businesses and financial markets. Fearful, they would retrench further, causing the economic decline to accelerate. Weak labour markets would worsen as would the already swollen government deficits and debt.” Altman compared the situation to 1937 and the renewed onslaught of the Great Depression.

El-Erian described Europe’s banking system as a “rapidly burning fuse” and warned that “Europe is getting very close to yet another tipping point.” He wrote that all signs point to “an institutional run on French banks” that threatens to see Europe “thrown into a full-blown banking crisis that aggravates the sovereign debt trap, renders certain another economic recession and significantly worsens the outlook for the global economy.”

The slide into recession on both sides of the Atlantic has been accompanied by growing tensions between the traditional postwar partners. The increasingly antagonistic relationship between the two sides was most clearly revealed following the visit by US Treasury Secretary Timothy Geithner to a meeting of European finance ministers in Poland last week.

Geithner received a cool reception from European ministers when he raised the proposal for an economic stimulus plan for Europe. A number of European leaders, including the head of the eurogroup of states, Jean-Claude Juncker, and the German finance minister, Wolfgang Schäuble, promptly rejected Geithner’s plan.

Austrian Finance Minister Maria Fekter was especially blunt in her criticism of the US proposal and Washington’s economic policy as a whole. She told the press: “I found it peculiar that the Americans, although they themselves have significantly worse fundamental data than the euro area, explain to us what we should do, but when we make a proposal ... they say ‘no’ right away.”

US-European frictions have also been exacerbated by the continual pressure from US-based rating agencies on European banks. On Monday, the Standard & Poor’s rating agency cut the credit rating of the Italian economy and then followed on Wednesday with a similar downgrading of seven Italian banks, including Italy’s leading bank, UniCredit.

The agency justified its decision by noting that it had targeted banks with high levels of exposure to the sovereign debt of other European countries. The S&P downgrade also included the Italian branch of the French bank BNP Paribas, thereby increasing pressure from the financial markets on the French banking sector. The French CAC 40 index racked up the biggest losses on Thursday (down 5.25 percent), reflecting fears of a collapse of the French banking sector.

The Italian prime minister reacted to the S&P decision by publicly rebuking the ratings agency whose assessments, Silvio Berlusconi declared, “appear dictated more by newspaper articles than reality and appear to be tainted by political considerations.”

While tensions and chauvinism are rising across the Atlantic, national divisions inside Europe are also intensifying. The move into recession by both the US and Europe is the consequence of the decision by their respective governments to make virtually unlimited sums of capital available to the banks—funds which are then recouped in the form of massive austerity programs directed against the working class.

What began as a debt crisis in a number of peripheral European nations has now quickly spread into the heart of Europe itself. At the same time, leading nations in Europe—first and foremost Germany—are intent on tightening the screws of austerity on the European mainland. Leading members from the parties involved in the German governing coalition welcomed the Italian downgrade and pressure for more austerity. Peter Altmaier, from the Christian Democratic Union, noted earlier this week: “The case of Italy shows that we’re not just talking about Greece.”

The political elite in Germany and across Europe is determined to maintain the policy of austerity which is plunging Europe into a new recession and means unemployment and poverty for millions more European workers.

To contact the WSWS and the Socialist Equality Party visit:

wsws.org/contact

© World Socialist Web Site