Five years after the financial crash, global economy continues to weaken

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In the immediate aftermath of the September 2008 eruption of the global financial crisis, the claim was made that so-called "emerging markets," including China, India and Brazil, would be able to decouple from the major capitalist economies and provide a new foundation for growth in the world economy as a whole.

That piece of economic fiction has been exposed. Not only are the "emerging markets" unable to provide a boost to growth, they are rapidly becoming a new source of global instability.

Last week, the *Wall Street Journal* cited a report from Bridgewater, the world's largest hedge fund, which noted that the major economies, including the US, Europe and Japan, were now adding more to world economic growth than the emerging nations.

That result, however, does not point to a revival in the advanced countries. Rather, it signifies the weakening of the global economy as a whole. Growth rates in all the major economies remain well below the levels attained in 2007-2008, with no prospect of the pre-crisis rates ever being seen again.

A survey of economists released by the Federal Reserve Bank of Philadelphia found that they expected the US economy to grow by only 1.5 percent in 2013, well down from their prediction of 2.0 percent in May. Growth will not pick up in the longer term, according to a report by a leading JPMorgan economist, which found that the potential growth rate for the US economy, which used to be 3.5 percent, had halved.

The situation is even worse elsewhere. Europe continues to stagnate, with the euro zone economies growing by only 0.3 percent in the June quarter, which translates to an annualised rate of 1.1 percent. The return to positive growth, after six consecutive quarters of contraction, by no means signifies that Europe has "turned the corner." The euro zone economy as a whole is still 3 percent smaller than it was in 2008. Most analysts consider that an annual growth rate of at least 2-3 percent over the next three years is needed to start to bring down unemployment, and there is no prospect of that.

The *Wall Street Journal* commented that it was "hard to see how Europe can reach escape velocity." The newspaper continued: "Among the brakes on the recovery: continuing austerity, lack of affordable bank loans, rising unemployment and weak household incomes, and lack of investment by companies that are still operating well below capacity."

The Bank of Japan's program of doubling the money supply appears to have given Japan's economy something of a boost, with growth in the third quarter coming in at an annualised rate of 2.6 percent. But this was well below predictions of a 3.6 percent increase.

The main factor in the weakening contribution of "emerging markets" to global growth is the slowdown in China. The official growth prediction for this year is 7.5 percent, the lowest increase since 1990. But there are warnings that it could be lower.

Falling Chinese growth is having a significant impact on the economies of South East Asia as well as on raw material suppliers such as Brazil and Australia.

Two years ago, Brazil, which exports soya beans and iron ore to China, grew at a rate of 7.6 per cent. This year predicted growth is just 2.3 percent.

Australia, which is a major supplier of iron ore, is being heavily impacted by the winding down of the Chinese investment infrastructure, with official Treasury forecasts pointing to a significant downturn in Australia's terms of trade--the ratio of export to import prices. The Rudd Labor government has stated that the "China boom," which drove major investments in iron

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ore projects, is over.

Lower growth is not the only problem. There are increasing concerns that high debt levels in China--the result of the credit and fiscal stimulus put in place after the global financial crisis of 2008-2009--could set off a financial crisis.

The *Financial Times* reported last week that, according to Fitch Ratings analyst Charlene Chu, a study of China's so-called shadow banking sector had revealed that the country's total debt could be as much as 200 percent of gross domestic product. Chu warned that the banking sector as a whole was more exposed to shadow banking loans than most people realised. She estimates that the assets of the Chinese banking system expanded by $14 trillion between 2008 and 2013, equivalent to the size of the entire US banking system.

Official figures show that non-performing loans held by Chinese banks rose by $2 billion in the second quarter, the seventh quarterly rise in a row.

The growing financial problems of India--another economy that used to be regarded as a potential centre for global growth--could well be a sign of what is to come elsewhere. There are fears that its worsening economic slowdown--with economic growth predicted to come in at only 5 percent this year, half of its level three years ago--could be increasing the debt burden of some of the country's biggest industrial companies.

The Indian financial system is being hit by a capital flight which last week saw the reimposition of capital controls in a bid to try to halt the fall in the value of the rupee.

The Indian economy is being hit by what the *Financial Times* described as a "toxic combination of a falling rupee, a sharp slowdown in growth, swollen current account and budget deficits and persistently high inflation."

India is not the only emerging economy that faces growing financial problems. The expectation that the US Federal Reserve will soon begin to "taper" its purchases of US Treasury bonds, the centrepiece of the program of "quantitative easing," possibly as early as next month, has triggered capital outflows from other regions as well. Besides India, Indonesia, which has also been touted as a new growth centre, is experiencing growing financial problems.

Markets across Asia experienced falls last week amid fear that that Fed "tapering," which will lift interest rates in the US, could see the movement of capital back into American financial assets. The danger is that the present capital outflow could turn into a flood once "tapering" begins.

In 1997-98, the collapse in the value of the Thai baht sparked the collapse of a financial bubble across Asia, the regional economic consequences of which were equivalent to the impact of the Great Depression in the major capitalist economies.

Given the growing dependence of the world economy on "emerging markets" in recent years and the ever closer integration of financial markets, the consequences of another financial crisis will be even more serious.

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