

Oil price slide and ruble plunge shake global markets

Nick Beams

16 December 2014

Sharp falls in European markets and wild swings on Wall Street yesterday, combined with a further plunge of more than 10 percent in the value of the Russian rouble, indicate that the worsening global slump is starting to have a major impact on financial markets.

The day began with a 1.1 percent fall in Asian markets, followed by losses across Europe, indicated by a 2.4 percent decline in the FTSE Eurofirst 300 index. Turbulence on Wall Street recalled the gyrations of mid-October, when a “flash crash” in bond market yields created conditions resembling those following the collapse of Lehman Brothers in September 2008.

New York’s S&P 500 index rose 0.8 percent in the first half hour of trading and then sank by 1 percent in its biggest movement since the events of two months ago. The Dow Jones index traded in a 300-point range on either side of neutral as concerns mounted over the falling price of oil.

Claims that a lower oil price will boost the global economy are being overwhelmed by reality as it becomes apparent that the 45 percent slide since June is indicative of worsening conditions.

The price for West Texas Intermediate crude, widely regarded as a benchmark, has fallen by 15 percent this month alone, following the decision by the OPEC oil producers’ cartel not to reduce production and a move by the International Energy Agency to cut its forecast for oil consumption in 2015.

The oil price fall’s most severe effect is being felt in Russia, where the rouble has lost around half its value against the US dollar so far this year.

In response to yesterday’s precipitous fall and the failure of several market interventions during the day, the Russian central bank announced in the middle of the night that it was lifting its main interest rate from 10.5 percent to 17 percent. “The decision was driven by

the need to limit the risk of devaluation and inflation, both of which have recently significantly increased,” the bank said.

Earlier in the day, the bank warned that the Russian economy could contract by up to 4.7 percent next year if oil prices remain at around \$60 per barrel. The fall could be even larger, because there is no sign the slide is ending. Morgan Stanley has warned that the economy will contract by 6 percent if the price of oil drops to \$50.

The Russian budget, and economic projections for the next year, were framed on the expectation that the oil price would stay around \$100 per barrel, the level at which it remained from 2011 until June.

As the rouble has plunged, so have share markets. The key Micex index has dropped 26 percent since the beginning of December in what could be the biggest fall since October 2008.

Financial market traders and analysts in New York said the Russian central bank move was a “last-ditch” effort to halt the currency’s decline.

While Russia is in the eye of the storm, it extends across all the “emerging market economies.” It has been likened to the 1997-98 Asian financial crisis, but its implications are far more serious because the Asian economies and financial markets are now an integral part of the global financial system.

A report on *Bloomberg* noted: “From Russia to Venezuela, Thailand to Brazil, stock, bonds and currencies across the developing world are plunging.” The two most significant changes since the crisis of 1997-98 are that many of these countries have flexible exchange rates and high currency reserves.

However, there has been a massive inflow of private capital into their financial sectors, which now threatens to depart. Earlier this month, the Bank for International

Settlements reported that cross-border loans to developing economies had risen from \$3 trillion to \$9 trillion in the past decade.

Last week, investors withdrew more than \$2.5 billion from US exchange-traded funds that buy emerging market stocks and bonds. It was the biggest outflow since the beginning of the year, when there were concerns over moves by the US Federal Reserve to wind back its program of asset purchases known as “quantitative easing.”

Many investment strategies have been based on continuing low US interest rates and high commodity prices. Now conditions are rapidly shifting. The US Fed is moving to tighten interest rates, and commodity prices are falling across the board, not only for oil. Any rise in the value of the dollar as a result of Fed tightening immediately increases the debt and interest burden of financial and non-financial corporations that have taken out dollar-denominated loans.

Besides its immediate impact on financial markets, the fall in the oil price has long-term implications. The *Financial Times* reported that, according to a Goldman Sachs analysis, almost \$1 trillion worth of spending on oil projects around the world could be put at risk, because many projects are uneconomic with oil at \$70 per barrel. The cutback could be higher because the study did not include shale oil production in the US.

The worsening economic situation is being exacerbated both by the intensifying geo-political tensions and the absence of any coordinated response by the major economic powers to the crisis. Russia’s position has been considerably worsened by the sanctions imposed by the US and the European Union, which have restricted its access to global financial markets.

The lack of coordination is most apparent in the divergent policies of the major central banks. Having ended its program of asset purchases, the US Fed is moving to tighten interest rates, albeit gradually. The European Central Bank is looking to step up its purchases of financial assets, possibly including sovereign debt.

The Bank of Japan is undertaking an even more aggressive form of quantitative easing, with its purchases of government debt running at the equivalent of 1.4 percent of gross domestic product each month. While the bank insists it is not engaging in the kind of

beggar-thy-neighbour policies that proved so disastrous in the 1930s, the Japanese program is aimed at pushing down the value of the yen, in order to benefit the country’s exporters.

With Tokyo’s policy set to become more aggressive following the Abe government’s return in last Sunday’s election, the global bank HSBC warned that the yen’s decline could become “disorderly and swift” and lead to a global currency storm. It pointed to a scenario involving a collapse in the yen, a slide in the euro and an emerging crisis. The report stressed this was not a forecast, just a “tail risk,” but one that could not be ignored.

Whatever the immediate outcome of the market turmoil, there are unmistakable signs that the extraordinary measures initiated by central banks after 2008 are losing their capacity to hold back the deepening crisis of the global economy.



To contact the WSWS and the
Socialist Equality Party visit:

wsws.org/contact