World Bank lowers its growth forecast

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The World Bank has underscored the deepening malaise in the global economy, once again revising downward its estimate for growth in 2015. In its latest Global Economic Prospects report, issued earlier this week, the World Bank cut its forecast for global growth this year to 3 percent, having predicted an increase of 3.4 percent last June.

The growth rate of 2.6 percent for 2014 was also well below the forecast of 3.4 percent as a result of what the report called a "string of disappointing" results in the euro area, Japan, parts of emerging Europe, in particular Russia, and Latin America. The euro area and Japan accounted for half of the downward revisions for global growth in 2014 and one third for the 2015 forecasts.

World Bank chief economist Kaushik Basu said the world economy was "running on a single engine. It is only the US economy that is forging ahead in a global economy with so much uncertainty. We need several engines."

However, the US "engine" is far from functioning with a steady beat. Figures released by the Commerce Department yesterday showed that retail sales fell by 0.9 percent in December from the previous month, compared to a forecast decline of 0.1 percent. The figures were described as a "big surprise" by at least one analyst, as they included a 0.4 percent decline in core sales, including electronics, clothing and sporting goods, but excluding gasoline.

As if to underscore the World Bank's message of a weakening global economy, copper prices fell to their lowest levels in five-and-a-half years yesterday. The price of the metal, which is used extensively in the construction and electrical industries, dropped by as much as 6.6 percent on the London market.

Copper has joined other industrial commodities, most notably iron ore and oil, in falling to price levels not experienced since the immediate aftermath of the global financial crisis of 2008–2009. The Bloomberg Commodity Index is now down to levels last seen in 2002.

There is significant doubt over whether the World Bank's revised prediction of 3 percent for global growth will be met, because risks "remain tilted to the downside." The euro area and Japan could both experience a "prolonged period of stagnation or deflation." There is also a risk of financial volatility as a result of the divergence between the policies of the world's major central banks.

The US Fed is officially moving towards a tightening interest rate regime, while the European Central Bank and the Bank of Japan are expected to step up their programs of quantitative easing. Financial turbulence could also be triggered by increased geopolitical tensions, sharp movements in commodity markets, or financial stress in emerging markets, because a rise in the value of the US dollar could increase the real debt burden of dollar-denominated loans.

Basu warned that "the stalled recovery in some high-income countries and even some middle-income countries may be a symptom of deeper structural malaise."

The report made clear that hopes that growth in lower income countries and emerging markets could provide a boost to the global economy have been well and truly dashed. Growth in middle- and low-income countries had fallen to 4.4 percent in 2014, with "deep structural factors," including a slowdown in productivity, set to dampen growth prospects in the medium term. "Since the post-crisis rebound, output growth in the developing world has settled down at a pace below that of the first decade of the 2000s," the report noted.

Tightening financial conditions, rising geopolitical tensions or repeated growth disappointments could cause investors to reappraise developing country risks and expose "some underlying financial vulnerabilities."

Assigning such an event a "low probability," the report nevertheless warned that the "slowdown in China could turn into a disorderly unwinding of financial vulnerabilities with considerable implications for the global economy."

While the report described the recovery in the United States as "robust," this assessment is not borne out by the figures. The report said growth would be 2.4 percent in 2014, rising to 3.2 percent in 2015, before declining to 2.4 percent in 2017. It noted that while the official level of unemployment had fallen, "labour force participation has declined to levels not seen since the early 1980s."

The bank wrote that investment levels in the US would increase, but remain below the levels reached before the financial crisis. In addition, a strong dollar would dampen net exports, while low oil prices would "negatively affect capital expenditure in the energy sector."

Activity in the euro area had been weaker than expected, especially in France, Germany and Italy—the core economies of the region.

The report identified a potential source of financial turbulence in emerging markets, warning that after "several years of rapid credit growth and record debt issuance on international bond markets, corporations in many developing countries have accumulated significant liabilities and exposure to both global interest rates and exchange rate fluctuations."

One of the most significant indicators of the state of the global economy is the level of world trade. The World Bank noted that since the global financial crisis, world trade growth "has slowed significantly" from the trend of the 1990s and early 2000s. Despite some expected pick-up, global trade growth was not expected to return to the rising path of the years before the crisis.

The bank's forecast of growth of 3 percent has been on the assumption of a strengthening recovery in major economies, a modest rebalancing of demand in China, and a smooth transition of developing countries to tighter financial conditions.

But as the report acknowledged, major consequences would follow if any one of these conditions were not met. Turbulence in financial markets in May–June 2013 and financial volatility in January and October 2014 indicated how rapidly market sentiment could turn.

In Europe, the continuing fall in inflation could signify so-called "secular stagnation," with weak consumption, low investment and falling prices feeding off each other to produce a deflationary spiral. This would have major global ramifications, given that the euro area accounts for a sixth of global gross domestic product and a quarter of global trade and cross-border banking assets.

Likewise if what the bank called "China's carefully managed slowdown" turned disorderly. That would have major consequences for its financial system and the world economy as a whole.

Like other reports on the state of the world economy, including by the International Monetary Fund and the Organisation for Economic Cooperation and Development, the World Bank's Global Prospects study underscores the fact that the crisis of 2008 represented a fundamental breakdown in the functioning of the global capitalist economy—a crisis that is continuing to deepen.