US stock sell-off in response to Fed policy statement on interest rates

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All three major US stock indexes fell sharply Wednesday in response to the policy statement issued mid-afternoon by the Federal Reserve's interest rate-setting Federal Open Market Committee (FOMC).

The markets had recorded modest gains prior to the release of the FOMC statement, but declined steeply after it became clear that the central bank had failed to signal a possible delay in its plans to begin raising its benchmark federal funds rate as early as June.

The Dow Jones Industrial Average dropped by 195 points, or 1.13 percent, ending the day below 17,200. The Standard & Poor's 500 Index fell 27 points, or 1.35 percent, and the Nasdaq declined by 43 points, or 0.93 percent.

These declines followed a broad sell-off the day before, sparked by poor earnings reports and negative forecasts from a number of major companies across many economic sectors, as well as a dismal report on durable goods orders in December. Over the two days, the Dow lost 486 points.

With the soaring US dollar, slumping global demand and plummeting oil prices beginning to seriously impact the sales and profits of major US firms, the Fed has come under increasing pressure from Wall Street to delay any rate hike until the final months of this year or some time in 2016.

So far this week, Microsoft, Caterpillar, Procter & Gamble, DuPont, United Technologies, Pfizer and a number of other large firms have reported major declines in fourth-quarter earnings and/or sharply reduced forecasts for 2015, attributing the negative results at least in part to the impact of the steady rise in the US currency on their exports and overseas operations.

On Tuesday, Microsoft's stock fell 9 percent, wiping out nearly $35 billion in the company's market value. Caterpillar stock declined 7 percent.

"The rising dollar will not be good for US manufacturing or the US economy," Doug Oberhelman, chief executive of Caterpillar, told analysts on Tuesday.

The consumer goods giant Procter & Gamble said it had been hit by the "most significant fiscal year currency impact" in its 178-year history.

The Fed's plan, announced over a year ago, to begin raising rates from the near-zero level that has prevailed since shortly after the September 2008 financial crash, has been complicated by deflationary tendencies in Japan, Europe and the US itself, and a general slowdown in the world economy. The response of central banks and governments has been to devalue their currencies in an attempt to export the slump to the US.

Last week, the European Central Bank launched a "quantitative easing" plan to purchase 1.1 trillion euros worth of bonds by 2016, diluting the value of the euro against the dollar and other major currencies. On Tuesday, Singapore became the ninth country this month to take action to push down the value of its currency. The others, besides the euro zone, include Denmark, Turkey, India and Canada.

Since June 30, the US dollar has risen 17.7 percent against a basket of international currencies. It has increased by 9 percent over the last three months alone.

Plummeting oil and other commodity prices (oil is down by 57 percent since June), a symptom of stagnating and even negative growth from China and Japan to Europe and much of Latin America, have contributed to extremely low inflation in the US. This is despite headline figures on employment and the gross domestic product that point to relatively solid growth in the US economy.

An index of prices Americans pay for goods and services rose just 0.8 percent during the 12 months ending in December. This is the slowest pace during a period of economic growth in half a century. And on Tuesday, the Commerce Department reported that US durable goods orders fell by 3.4 percent in December, the fourth consecutive monthly decline. The department also reported that US firms broadly cut capital spending in the final three months of 2014.

Under these conditions, the Fed's announced intention to begin raising rates as early as June, while central banks in the rest of the world are lowering rates or printing huge amounts of currency, tends to push the dollar even higher and heighten deflationary tendencies within the US. Already a number of American firms whose exports are being impacted by the rising dollar are preparing to cut costs and shed jobs. On Wednesday, reports emerged that IBM was preparing a massive layoff.

The Fed pioneered the policies of near-zero interest rates and "quantitative easing" to pump virtually free cash into the banking system and rescue the financial elite. Now, it is trying to wean the US banks and hedge funds off of the narcotic of endless central bank subsidies and restore a more normal interest rate regimen. But it is confronting increasing resistance from Wall Street and major US corporations.

In its statement Wednesday, the Fed hailed the "solid pace" of US economic growth and what it called "strong job gains and a lower unemployment rate." It did not mention that most of the new jobs are low-paying and many are part-time or temporary. Nor did it note that much of the fall in the official jobless rate is the result of the exit of millions of long-term unemployed workers from the labor market.

The FOMC made clear that the Fed would not raise interest rates at either of its two meetings prior to June—one in March and one in April. It reiterated previous assurances that its timetable for raising rates would depend on economic conditions, that it was not wedded to a definite date, and that it would increase rates only gradually and keep them abnormally low for "some time."

However, it called the low inflation rate and falling oil prices "transitory" phenomena and said inflation in the US would begin to climb in the mid-term toward the Fed's target rate of 2.0 percent. Wall Street investors and speculators had been hoping for language suggesting that the deflationary trends might cause the bank to hold off on raising US rates.

At last week's World Economic Forum in Davos, Switzerland, the divisions within the American and international bourgeoisie over Fed policy emerged in the open. Former US treasury secretary and Obama administration economic adviser Lawrence Summers warned that an early initiation of monetary tightening by the Fed could trigger a full-scale recession, if not depression, in the US and beyond.

"Deflation and secular stagnation [i.e., indefinite recession] are the threats of our time," Summers, one of the architects of bank deregulation in the US, told a Bloomberg forum.

William White, former chief economist at the Bank for International Settlements, gave vent to his fears over the state of the world economy in an interview with the *Daily Telegraph* on the eve of the Davos gathering. "We are in a world that is dangerously unanchored," he said. "We're seeing true currency wars and everybody is doing it, and I have no idea where this is going to end."

This week's developments show that Fed policy is becoming increasingly entangled in the international net of intractable crisis and economic nationalism fueled by its own parasitic efforts to bail out the American ruling class.