IMF-World Bank meeting confronts lowest global growth since 2009

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The semi-annual meeting of the International Monetary Fund and World Bank opens in Lima, Peru on Friday amid the worst economic and financial conditions since the eruption of the global financial crisis in 2008-2009.

The world capitalist economy is being hit by two interconnected and increasingly toxic processes: worsening economic stagnation, lowering growth rates across the board, and the mounting risk of a major financial crisis arising from the consequences of the flood of cheap money pumped out by the world's central banks over the past seven years.

The IMF's *World Economic Outlook* (WEO) published on Wednesday notes that the world economy will expand at its slowest pace this year since the global financial crisis, as growth in China and emerging markets continues to fall. It states that 2015 will mark the fifth year in a row that average growth in emerging markets has declined.

The IMF has downwardly revised its global growth forecast for this year to 3.1 percent from its April estimate of 3.5 percent. It forecasts a gradual recovery in the years ahead, but few people take that prediction seriously, given that the IMF has had to downwardly revise its forecasts every year for the past five years.

In something of an understatement, incoming IMF chief economist Maurice Obstfeld said in introducing the report that the "holy grail of robust and synchronized global expansion remains elusive." The IMF had marked down its predictions "nearly across the board" and indicated the situation could worsen. "[D]ownside risks to the world economy appear more pronounced than they did just a few months ago," he added.

The WEO report is strewn with references to worsening economic conditions. For most emerging markets, it declares, "external conditions are becoming more difficult." In Latin America, "the downturn in Brazil [the country is in recession] was deeper than expected," while momentum in other countries in the region "continues to weaken" because of the decline in commodity prices. Global industrial production remained "weak" in 2014, and then "slowed markedly" over the first half of 2015, reflecting the build-up of inventories and "lower investment growth." World trade volumes slowed in the first half of this year and, according to some measures, have actually contracted.

Pointing to the dangers to its forecasts, the IMF wrote that "financial stability risks" had increased over the past five years in emerging market economies because of lower growth, commodity price declines and increased indebtedness. Over the past decade, the corporate debt of non-financial companies in large emerging markets has more than quadrupled, rising from $4 trillion in 2004 to $18 trillion in 2018. As much of this debt is in dollar-denominated loans, any increase in US interest rates, combined with a rise in the value of the dollar, could set off a financial crisis that would impact not only the corporations immediately involved, but spread to the banks and even to governments.

The increasing instability of the financial system was highlighted in an interview by the IMF's head of financial stability, José Viñals, with the *Financial Times*. He said the world risked sliding into another financial crisis, leading to a recession, if governments and policymakers mishandled the situation. This assessment, he emphasised "does not rely on extreme assumptions at all."

In its *Global Financial Stability* report, published in conjunction with the *World Economic Outlook*, the IMF warned: "Shocks may originate in advanced or emerging markets and, combined with unaddressed system vulnerabilities, could lead to a global asset market disruption and a sudden drying up of market liquidity in many asset classes." In short, the eruption of another financial crisis.

Numerous analysts have pointed to the potential for emerging markets to provide the catalyst for such a crisis as the inflow of capital dries up and reverses. According to a recent report by the Institute of International Finance, falling direct investment and the withdrawal of cash by private investors will result in $540 billion being pulled out of emerging markets this year—the first such outflow since records began at the end of the 1980s.

The head of economics research at Barclays, Christian Keller, told the *Financial Times*: “Capital flows have slowed sharply in recent months and the prospects for an immediate turnaround are dim. This risks creating a negative feedback loop in which capital flows depend on growth, but growth itself depends on the resumption of capital flows.”

In a column published in the same newspaper yesterday, former US Treasury Secretary Lawrence Summers warned that the dangers facing the world economy were more severe than at any time since the collapse of Lehman Brothers in September 2008.

He pointed out that relative to its 2012 forecasts, the IMF had downwardly revised its estimate of gross domestic product for 2020 by 6 percent for the US, 3 percent for Europe, 14 percent for China, 10 percent for emerging markets, and 6 percent for the world economy as a whole. Even these “dismal results” were made on the assumption of no recessions in the industrialised countries and the absence of systemic crises in emerging markets—neither of which could be taken for granted.

According to Summers, the world is in the grip of what he calls secular stagnation—a condition of permanent low growth and deflation. “The idea that slow growth is only a temporary consequence of the 2008 financial crisis is absurd,” he wrote. “The latest data suggest that growth is slowing in the US and it is already slow in Europe and Japan.”

Policymakers “badly underestimate” the risk of a return to recession and lack the tools to respond should it occur, he added.

By one measure, the world economy has already undergone a contraction. According to an analysis by Investec, an asset management firm, global output if calculated in US dollars will show a world economy that sank into recession in 2015, the first since 2009. “In US dollar terms, there is going to be negative global growth this year,” Investec strategist Michael Power told the *Financial Times*. “2009 was a contraction in US dollar GDP growth and we estimate that 2015 will show an even greater contraction.”

Measured in US dollar terms, the fall in GDP of commodity-exporting economies is much more severe than the official data indicate. Brazil’s projected GDP in dollar terms for 2015 is set to show a contraction of 19.1 percent, while Russia’s could fall by as much as 36 percent. Both these economies are part of the so-called BRICS group, which, only a few years ago, was touted as providing a new basis for global expansion.

Anyone still labouring under the illusion that those in charge of global economic affairs gathering in Lima have any policies to meet the rapidly worsening situation need only consult an interview by IMF economist Obstfeld with the *Financial Times* earlier this week.

He told the newspaper that at the top of his list as he began his new job was the task of better understanding the underlying potential for economies to expand and become more prosperous and the linkage of growth to productivity, the size of the labour force and government policies.

“We don’t understand that very well,” he admitted.

It was not the only area of ignorance. Another key issue that was not well understood, he said, was the slow growth of world trade, which is now lagging behind GDP growth in contrast to the situation prior to 2008, when it outpaced it.

Obstfeld did not directly comment on the turmoil in global financial markets. But the situation is no better there, as evidenced by the on-again, off-again gyrations of the US Federal Reserve over whether it should increase its base interest rate by 0.25 percentage points, caused by fears as to what impact this could have on global markets.