Perplexity and gloom dominate IMF-World Bank meeting

Nick Beams
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A growing sense of gloom and fears of another financial crisis hung over the semi-annual meeting of the International Monetary Fund and the World Bank held in Lima, Peru, over the weekend even as an official communiqué tried to provide an upbeat assessment.

A statement by the International Monetary and Financial Committee began by asserting that the "global recovery continues, but growth remains modest and uneven overall." How the committee could maintain that a "recovery" was underway when the official IMF growth forecast was the lowest since the financial crisis of 2008-2009, it did not explain.

The communiqué said that risks to the global outlook were increasing and, while it claimed emerging market and developing economies were better prepared for a less favourable environment, nevertheless "many emerging market economies are exposed to tighter financial conditions, slowing capital inflow, and currency pressures amid high private sector foreign currency indebtedness."

One of the central features of the past seven years has been the escalation of financial parasitism, marked by the rise of stock markets in the advanced economies as a result of the provision of ultra-cheap money by the world's central banks and the increase of indebtedness in emerging markets as financial capital has scoured the world in the search for ever-higher yields.

In a report issued on the eve of the meeting, the IMF warned that emerging market economies had over-borrowed in the past decade by an estimated $3 trillion, threatening to set off a crisis as a result of falling commodity prices and capital inflows.

It warned that a withdrawal of financial stimulus measures could start a "vicious cycle of fire sales, redemptions and more volatility."

"The global financial outlook is clouded by a triad of policy challenges: emerging market vulnerabilities, legacy issues from the crisis in advanced economies, and weak systemic market liquidity," the report said. The latter refers to a situation where there is a major sell-off in emerging market debt and no buyers are to be found, threatening to spark a crisis in the global financial system as a whole. The IMF has calculated that the over-borrowing accounts for 25 percent of China's gross domestic product (GDP) and 15 percent of the GDP of emerging market economies.

The situation may be even worse than official figures indicate. An article by Carmen Reinhardt, the co-author of a major study on international debt crises, warned that emerging markets may also "be experiencing another common symptom of an impending crisis, one that is much harder to detect and measure: hidden debts." Historical experience had shown, she wrote, that these debts often do not appear on balance sheets and so "often go undetected until it is too late."

Any crisis in emerging markets will have a major impact on the world economy as a whole because they have accounted for around 80 percent of the increase in world output since 2010. But those days are over. According to Colombian central bank governor Joe Uribe, it is time to face facts: "We cannot keep trying to grow at the rates of the past."

The country's finance minister, Mauricio Cardenas, said Latin America and other emerging economies were facing a new situation. "The new world is lower commodity prices which are going to stay low for the foreseeable future. At the same time there is going to be less global liquidity." There was no expectation that these economies will go back to the situation of five or six years ago.

The future is indicated by Brazil. Once touted as an engine of global growth, the Brazilian economy will contract by three percent this year, according to the IMF, and by a further one percent next year. Brazil's credit rating has been downgraded to "junk" by Standard &

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Poor's after enjoying investment grade status for the past seven years.

According to Ilan Goldfajn, the chief economist at Itau Unibanco, Brazil's largest bank, emerging markets face a new reality created by a shift in the terms of trade. "Oil in Colombia, copper in Chile, iron ore in Brazil: all the commodity producers just have to realise it's a different business now," he said.

The "new reality" confronts major advanced commodity-dependent economies such as Canada and Australia.

Economic conditions are rapidly becoming more perilous in the Asia-Pacific region. In a report issued on the sidelines of the Lima meeting, the IMF warned that any significant slowdown in China would have a major impact. While the IMF did not downgrade its growth forecast for China, in contrast to virtually every other region of the world, it warned that "any negative growth shock there would hit the rest of the Asia-Pacific region hard," impacting on trade and financial markets.

Singapore's deputy prime minister Tharman Shanmugaratnam, a former chairman of the IMF's policy committee, said the world economy was marked by "a great sense of unease." "That sense of unease explains why globally, almost everywhere, investment is much weaker that we'd expect," he said.

The fall in investment—in some areas it is 25 percent below levels reached before the global financial crisis of 2008—exposes the total bankruptcy, so far as economic growth is concerned, of the zero interest rate and quantitative easing programs of the world's central banks. Since the collapse of Lehman Brothers in 2008, central banks around the world have cut interest rates more than 600 times—all to no avail. Instead of boosting growth, monetary policy has simply fuelled financial parasitism, which has created the conditions for another crisis.

And there is nothing on the horizon to turn real growth around. According to David Lipton, the special advisor to IMF managing director Christine Lagarde: "If there's going to be strong growth in the global economy, the engine of growth will be emerging markets."

But that fiction has been exposed. As Ilan Goldfajn commented, the golden years of growth are a thing of the past. "You will tell your grandchildren about them," he said.

Having no policy prescriptions to promote real economic growth, the IMF's International Monetary and Financial Committee simply called for advanced economies to "maintain an accommodative monetary stance."

This perspective received the backing of Stanley Fischer, the vice-chairman of the US Fed, who told the conference in Lima that while he shared the view that it would be appropriate to lift interest rates sometime this year, and, while many emerging market financial officials wanted the Fed to "just do it" and end uncertainty, it was necessary to be conscious of the risks ahead.

Among these risks were that "shifting expectations concerning US interest rates could lead to more volatility in financial markets and the value of the dollar, intensifying spill-overs to other countries, including emerging market economies."

He said that the increase in the value of the US dollar—which is up by 15 percent—was impacting on exports which had been a "significant drag on US growth over the past year" and there was a risk that a "slowdown in foreign growth might restrain US economic activity somewhat further."

Bank of England governor Mark Carney warned in a speech that the build-up of emerging market debt was the biggest threat to stability and it was "not the kind of economy in which you can make a mistake."

Last month, the British central bank's chief economist Andy Haldane said the world may be locked into a three-part trilogy: the first part being the crisis of 2008-2009, the second being the euro crisis of 2012 and the third, the emerging market crisis of 2015 and onwards.

The air of gloom and perplexity which marked the IMF-World Bank meeting underscores the systematic character of the economic and financial breakdown that began in 2008 and that seven years on, those in charge of the global economy can present no policies to end it.

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