IMF to meet amid worsening stagnation and rising geo-economic tensions

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The spring meetings of the International Monetary Fund (IMF) and World Bank will convene in Washington later this week amid reports pointing to deepening stagnation in the world economy and warnings that the negative interest policies of major central banks are worsening the situation.

The latest update from the Brookings Institution-*Financial Times* tracking index said the world economy was characterised by "tepid growth," with world recovery "weak, uneven and in danger of stalling yet again."

"A common theme, from the best performing economies to the worst, is that the growth of physical capital investment is sluggish, industrial production is negative or, at most, weak, and business confidence is falling," it said.

For some time the US economy has been touted as a "bright spot," with continuing employment growth and rising consumer spending. However, the tracking index update said "weak business confidence and minimal increases in investment, despite large corporate profits and stashes of cash, portend a growth pattern that is uneven and of questionable durability."

Evidence of that conclusion has come in the latest forecast from the Atlanta Federal Reserve, which put US growth for the first quarter of this year at just 0.1 percent, compared to a previous estimate of 0.4 percent.

In the euro zone, the update said industrial production and employment were registering "modest growth" but "investment, retail sales and consumer confidence remain weak across the euro zone, raising concerns about the sustainability of the recovery."

In Japan, growth had plateaued at a positive but low level. Industrial production, however, had turned negative and retail sales continued to decline. China's growth had continued to slow but at this point a "hard landing" appeared to have been averted.

In the recent period, India has been hailed as a major source of global growth, possibly even replacing China at some point in the future. But the Brookings Institution-FT report said its headline growth of 7 percent "glosses over many problems beneath the surface." While lower oil prices had been a boon for the Indian economy "investment growth has fallen sharply and industrial production is actually contracting, raising questions about the durability of India's rapid growth."

The report pointed to the deep recessions in Brazil and Russia. In both economies "virtually every indicator of economic activity continues to decline." Other emerging markets were "mostly a picture of gloom. While some had little room to manoeuvre in trying to revive growth, others were trying to deal with both economic and political instability."

In the light of these developments, the IMF is expected to revise down its estimates for global economic growth in its *World Economic Outlook* due to be released later today, continuing a pattern that has marked the last several years.

There are also growing concerns that the negative interest policies being pursued by a number of central banks, including the European Central Bank (ECB) and Bank of Japan (BoJ), instead of providing a stimulus to the world economy may be having the opposite effect.

Pointing to the spread of the negative interest rates regime, the *Financial Times* noted that in less than two years negative interest rates "have gone from being a subject of fireside speculation to a reality for nearly a quarter of the global economy."

A blog posted by key IMF economists on Sunday "tentatively" concluded that while, overall, negative rates may have been helpful in providing monetary

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stimulus and easier financial conditions, "there are limits on how far and for how long negative interest rate policies can go."

They noted that the interest rate margins of banks appear to have been "squeezed by the combination of negative rates and quantitative easing." If low or negative interest rates persisted "they could undermine the viability of life insurers, pensions, and saving vehicles." Low rates made it difficult for insurers to meet guaranteed returns and "this will eventually force losses on life insurance policy holders."

The IMF blog echoed criticisms from key financial interests. In a note to shareholders this week, the chief executive of the giant hedge fund BlackRock, Larry Fink, said instead of boosting the economy, low rates could be leading to a decline in consumer spending as savers were forced to divert money from current expenditure to try to cover the costs of their retirement.

"This reality has profound implications for economic growth: consumers saving for retirement need to reduce spending. A monetary policy intended to spark growth, then, in fact, risks reducing consumer spending," he wrote.

Writing in the *Financial Times* last week, Scott Minerd, the chief investment officer at Guggenheim, said the world was in a "global liquidity trap" for the first time since the Great Depression. This refers to a situation where economic prospects are so poor that lowering interest rates fails to produce any increase in investment in the real economy—a situation sometimes likened to pushing on a piece of string.

Minerd noted that some of the "unintended consequences" of negative interest rates included deflationary headwinds and slower growth—exactly the opposite of what is needed. "But when monetary policy is the only game in town, negative rates are likely to beget even more negative rates, creating a perverse cycle."

The IMF warnings about the limitations of negative interest rates are part of a push to have governments adopt measures to boost spending in a coordinated global response to the worsening economic stagnation. Those proposals have so far fallen on stony ground, however, because of divisions among the major economic powers. The IMF made this call in advance of the recent G-20 meeting but it was not even seriously discussed.

Since then the tensions have grown. Earlier this month, the Japanese government warned it could take action over the rising value of the yen in the face of the quantitative easing and negative interest rate policies of the BoJ, which had been expected to lower the currency's value and provide a boost to Japan's exports.

This was followed by extraordinary comments by German Finance Minister Wolfgang Schäuble, laying some of the blame for the rise of the right-wing Alternative for Germany (AfD) party on the ECB's quantitative easing policies.

In remarks reported by Dow Jones, he told an audience: "I said to Mario Draghi [ECB president] … be very proud: you can attribute 50 percent of the results of a party that seems to be very new and successful in Germany to the design of this policy."

Schäuble said there was a growing understanding that "excess liquidity had become more a cause than a solution to the problem." German Transport Minister Alexander Dobridt said low interest rates were robbing savers of retirement income and the ECB was following a "very risky course."

These conflicts will most likely be carefully "managed" at the IMF meeting but they will not be far underneath the surface of official proceedings.

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