World economy in danger of being "torn apart"

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On the eve of the International Monetary Fund (IMF) annual spring meeting in Washington next week, its managing director, Christine Lagarde, warned that the international trading system risks destruction because of growing protectionism.

In a speech at the University of Hong Kong on Wednesday, Lagarde said: "The multilateral trade system has transformed our world over the past generation. But that system of rules and shared responsibility is now in danger of being torn apart. This would be an inexcusable, collective policy failure."

Lagarde did not specifically cite the actions of the Trump administration and its plans to impose tariffs on as much as $150 billion of Chinese goods annually but referred to the claim by "some people" that trade imbalances were caused by "unfair" trade practices.

While such practices existed, Lagarde said, bilateral trade imbalances generally were a snapshot of the division of labour across economies, including global value chains.

The first priority for the global economy was for governments to "steer clear of protectionism in all its forms"—a call that has been a regular feature of recent IMF policy pronouncements.

Yet it is a measure of how far and how fast events are moving in the other direction that a year ago such calls were directed to US opposition to having a commitment to "resist protectionism" being included in statements by global economic forums. Today the calls are aimed at actions already initiated by the Trump administration.

The IMF is expected to maintain its upbeat assessment for global economic growth when it issues its *World Economic Outlook* assessment. Growth in 2017 prompted the view that, finally, after nearly a decade, the effects of the 2008 financial crisis were being overcome.

Lagarde said the IMF could still see global momentum and continued to be optimistic. But while the current global picture remained bright, "we can see darker clouds looming,"

The reality was that the momentum expected for 2018 and 2019 would eventually slow, she said. "It will slow because of fading fiscal stimulus, including in the US and China; and because of rising interest rates and tighter financial conditions as major banks normalise monetary policy."

In the longer term, with ageing populations and weak productivity, "you have a challenging medium-term outlook, especially in the advanced world," she said.

There are some indications, however, that even the IMF's predictions for solid growth over the next 18 months may not be met. In an article published April 8 the *Wall Street Journal* noted that "cracks" were forming in the global growth story, with a reassessment of the scenario that growth was "on the verge of blasting out of a long period of weakness."

In the recent period "the global comeback has been in a bit of a rut," the article said. "In the US, gauges of manufacturing and services activity have been pulling back. Retail sales have fallen for three straight months, construction spending decelerated at the start of the year, and auto sales have largely plateaued." On top of this, there was a sharp slowdown in the growth of the US labour market last month.

A recent *Financial Times* article also pointed to slowing growth, posing the question: "Is the global economy starting to splutter?" It stated: "Despite the healthy employment picture, US retail sales unexpectedly fell in January and fell short of forecasts in February. European and Chinese retail sales also came in below economists' expectations in February, and purchasing managers' indices have weakened almost everywhere."

The article cited a Bank of America poll of fund managers last month in which a record 74 percent concluded that the global economy was now in its "late cycle" and pointed to remarks by hedge fund manager Stephen Jen that the present turbulence on stock markets could be the beginning of the end of the bull run.

According the Jen, the "calm the world has enjoyed was the result of Herculean policy efforts that will have negative consequences in the quarters ahead. The calm will probably be followed by a storm."

Jen was referring to the injection of trillions of dollars into the global monetary system by the US Federal Reserve and the other major central banks, which has played the key role in fuelling stock market speculation, above all in the US. But with banks seeking to "normalise" monetary policy by lifting interest rates, this could lead to a collapse of the financial bubble.

Significantly in her Hong Kong speech, Lagarde said that, as a result of easy financial conditions, global debt—public and private—had now reached an all-time high of $164 trillion.

Private debt made up two-thirds of the total, with public debt reaching levels not seen since World War II. Lagarde said if present trends continued, "many low-income countries will face unsustainable debt burdens."

"The bottom line is that high debt burdens have left governments, companies and households more vulnerable to a sudden tightening of financial conditions. This potential shift could prompt market corrections, debt sustainability concerns, and capital flow reversals in emerging markets."

It was necessary to use the current "window of opportunity" to prepare for the challenges ahead by "creating room to act when the next downturn inevitably comes."

Another "downturn," however, will not be a simple fluctuation in the business cycle but a major crisis because none of the underlying contradictions that produced the financial meltdown of 2008 has been resolved. In many ways, as the debt figures show, they have been intensified under conditions where the entire international trading and economic order is, in Lagarde's words, "in danger of being torn apart."