Fed monetary tightening hits Wall Street

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The move by the US Federal Reserve to lift interest rates and begin reducing its holdings of financial assets because of rising inflation is having a significant impact on Wall Street.

Yesterday, what has been described as an “April rout” continued and the NASDAQ index dropped 4.2 percent, bringing its total loss for the month to 13 percent. It was the worst month since October 2008 amid the global financial crisis, and took its fall for the year to 21 percent.

The *Wall Street Journal* reported that the “broad selloff has erased trillions of dollars in market value from the tech-heavy gauge with investors souring on shares of everything from software and semiconductor companies to social-media giants.”

The *Financial Times* (FT) reported that the fall across the NASDAQ wiped off more than $5 trillion from its market value since the record high of last November.

The so-called FAANG stocks—comprising Meta (the Facebook parent), Apple, Amazon, Netflix and Alphabet (the Google parent)—have together lost $1 trillion in market value. Individual falls are significant. Amazon has recorded a loss of 26 percent for the year and Apple 11 percent. Netflix has dropped by 49 percent in April alone.

There have been sizeable falls in other areas of the market. The S&P 500 index has dropped four weeks in a row with a loss of 8.8 percent for April. Its loss for the year, which began with the index at a record high, is 13 percent.

The Dow fell 4.9 percent in April and has lost 9 percent this year. Both indexes have recorded their worst month since the March 2020 plunge at the start of the COVID-19 pandemic.

The chief reason for the market decline is the inflation surge—the largest in four decades—which is pushing central banks to tighten monetary policy. When inflation was very low, they could pour money into the markets in response to a downturn without the fear this would spark a hike in prices.

These policies led to a 250 percent increase in the MSCI World Growth Index of stock markets over the past decade. But inflation means conditions have changed.

As Barry Norris, chief investment officer at Argonaut Capital told the FT: “Every time there’s been a selloff in markets there’s been a central bank put. Central banks are not going to come to the rescue this time.”

The shift by central banks is intersecting with the continuing problems in global supply chains. These have been caused by the refusal of capitalist governments to take co-ordinated international action to eliminate the pandemic, fearing necessary public health measures would adversely impact the stock markets and the financial system more broadly.

These decisions have now rebounded on the real economy with major effects. Apple alone forecast this week it could take a hit of as much as $8 billion in the current quarter because of supply chain problems.

“Supply constraints caused by COVID-related disruptions and industry-wide silicon shortages are impacting our ability to meet customer demand for our products,” the company’s finance chief, Luca Maestri, told analysts this week.

The type of constraints experienced by Apple stretch across the global economy as a whole—there is virtually no industry that has not been affected—meaning that losses will be of the order of hundreds of billions, if not trillions, of dollars.

Some indication of the continuing and worsening economic effects of COVID was the surprise news earlier this week that the US GDP had contracted at an annualised rate of 1.4 percent in the first quarter, due in part to the effects of the COVID surge at the start of the year.

The Biden administration has dismissed the figure as a “statistical quirk,” but the increasing view is that a significant shift is taking place. There are fears that inflation, already at more than 8 percent, is surging so rapidly that the Fed will need to lift rates to a level that will bring about a recession.

Recessionary trends are becoming ever more apparent in Europe as inflation continues to rise. The rate for the euro zone was 7.5 percent for the year to April and up 7.4 percent in March, led by the surge in energy prices, up 38 percent and unprocessed food prices which jumped 9.2 percent.

The price surge is taking place in conditions of weakening economic growth. GDP in the 19 euro zone countries grew by just 0.2 percent in the first quarter compared to 0.3 percent for the last three months of 2021.

The French economy showed no growth for the first quarter and the Spanish economy contracted as did the Italian. The German economy showed growth of only 0.2 percent over the previous three months.

The chief economics adviser at the Italian banking conglomerate UniCredit, Erik Nielsen, told the FT: “The world is in really bad shape. Particularly in Europe, where we have entered stagflation now.”

He said there was a “double whammy” looming in the euro zone where the European Central Bank was likely to start to lift rates because of inflation under conditions of an economic downturn.

China is also experiencing significant financial turbulence because of the latest outbreak of COVID, which the government is battling to bring under control. The renminbi fell by 4.2 percent against the dollar this month, a record decline, greater than the fall in 2015 which sent a tremor through global markets.

The fall in the currency constricts the ability of the government to take economic stimulus measures. The renminbi selloff accelerated after President Xi Jinping announced increased infrastructure spending to try to mitigate the economic effects of lockdowns in Shanghai and other major cities.

The tightening of monetary policy by the Fed is having major international ramifications because it effectively sets monetary policy for the rest of the world.

One of the effects of a rise in interest rates and a surge in the value of the dollar is to place increasing strains on poorer countries that have dollar-denominated debt.

A recent *New York Times* opinion piece by Georgetown University economic historian Jamie Martin noted: “Conditions are now ripe for the Fed to precipitate another global crisis. Of particular concern are extremely high levels of emerging market debt. The International Monetary Fund estimates that about 60 percent of low-income countries are experiencing debt distress or are close to it.”

Sri Lanka, he wrote, might be just the first domino to fall. But the conditions being experienced there, which have set off mass protests and demonstrations against the government, are only a very sharp expression of the struggles now developing in low-income and advanced economies alike amid a further deepening of the historic crisis of the global capitalist system.