

IMF meets as war brings greater global economic and financial disruption

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For the second year in a row the International Monetary Fund (IMF) is holding its spring meeting in conditions of global economic and financial turbulence sparked by the actions of the Trump administration in its drive to secure global dominance.

In 2025 the IMF met in the immediate aftermath of the “reciprocal tariffs” launched by Trump against the rest of the world. This year the situation is even more serious as the US intensifies the war against Iran with a naval blockade of the Strait of Hormuz following the inevitable collapse—the US had never intended that they would succeed—of ceasefire talks at the weekend.

In a speech last week, setting the stage for this week’s discussions and reports, IMF chief Kristalina Georgieva made clear there would be a downgrade of the global growth forecast even in the event of an end to the war. In the days since then the dangers have intensified.

Georgieva said that before the war began the IMF had been prepared to lift its forecast because of the impetus provided by artificial intelligence (AI) investment and the prospect of lower interest rates. That prospect has been shattered.

“Even our most hopeful scenario involves a growth downgrade,” she said. “Why? Because of infrastructure damage, supply disruptions, losses of confidence, and other scarring effects.”

She warned policymakers not to make things worse through actions such as export and price controls that could upset global conditions. And she cautioned central banks not to rush in and immediately raise interest rates in response to rising prices.

But if the working class responds to the persistence of inflation with major wages struggles, then central banks should act forcefully, even if this brought about a recession.

“If inflation expectations threaten to break anchor and ignite a costly inflation spiral, then central banks should step in firmly with rate hikes,” she said. “Rate hikes, of course, would further dampen growth—that’s how they work.”

Central bankers around the world and leaders of global financial institutions are all disciples of Paul Volcker, the Federal Reserve chief of the 1980s who used massive interest rate hikes, resulting in a deep recession and economic devastation to crush the wages movement of the working class.

The IMF warnings on growth are being widely echoed.

Even before the talks in Islamabad collapsed with the walkout by the US, the *Financial Times* (FT) reported over the weekend that Wall Street investors have “warned that the conflict in the Middle East will leave ‘scar tissue’ in global markets with commodity prices and bond yields unlikely to quickly return to pre-conflict levels—even if a peace deal is reached.”

The issue now is not whether there will be “scar tissue” but how much deeper will the wounds go.

In a briefing last week, the head of the World Bank, Ajay Banga, said he expected the war to trigger “some degree” of higher inflation and lower growth with countries “directly hit by the conflict” facing a humanitarian crisis.

Bond markets in both Europe and the US are sending out signals that there is going to be no return to the status quo ante. The yield, the interest rate, on the US two-year Treasury bond, which is increasingly the vehicle through which the Treasury is seeking to fund US debt, is 0.4 percentage points higher than it was at the start of the war.

The yields on two-year bonds in the UK, Italy and Germany are 0.5 percentage points higher than they

were at the start of the war.

There are rising concerns about the financial stability of the US as Trump escalates the war and adds hundreds of billions of dollars to the national debt, already at \$39 trillion.

As Andrew Jackson, head of investments at the Swiss financial firm Vontobel told the FT: “International investors are worried about the US because of debt sustainability and the US’s relationship with the rest of the world.... The US dollar curve is probably not the risk-free curve right now.”

The growing instability in financial markets threatens to deliver a blow to so-called emerging markets which have become more vulnerable to the movement of what the IMF has called “flighty capital.”

In a blog post accompanying its report on financial stability, the IMF noted that since the global financial crisis these countries had become more dependent on nonbank sources of finance. Since 2008, portfolio inflows to emerging markets have increased eightfold to reach a cumulative \$4 trillion, much of it in the form of debt with some 80 percent supplied by investment funds, hedge funds, pension funds and insurance firms.

It warned that such investments are “increasingly sensitive to global risk conditions.”

“These risks have come to the fore in the context of the war in the Middle East, as several emerging markets are experiencing a reversal of capital flow from nonresident nonbank investors.”

There are also increasing concerns about the stability of the financial system in the major economies.

In a comment piece in the FT yesterday financial analyst Mohamed El-Erian pointed to the growing problems in the UK bond market.

“The UK sovereign debt market,” he wrote, “has gone from a bedrock of the economy to a temperamental asset class that overreacts at the slightest provocation, both on a standalone basis and relative to other government bond markets.”

He said that for more than a decade the UK had “failed the basic test of debt sustainability” by borrowing too much while the economy grew too little, creating a tinder box waiting for a spark. It came in September 2022 with the Liz Truss budget crisis which “exposed the structural vulnerabilities of the UK’s financial system.”

The same could well be said of the US. Government

debt has now risen to \$39 trillion with the interest bill becoming the largest item in government spending. There are growing concerns over what might trigger a crisis including: whether the AI boom will be a bubble that bursts; the impact of AI on the business models of software firms which have been heavily financed by private capital and hedge funds; and the stability of the private credit market.

The answer of the Trump administration is to shovel more money into the system as it seeks to have more of the \$10 trillion market for 401(k) retirement plans directed into private credit as well as crypto.

The issue was raised as the IMF discussions were getting underway yesterday. Trump’s appointment to the head of the Securities and Exchange Commission, Paul Atkins, promoted private credit at an IMF event, saying those who could not stand the heat should get out of the kitchen and that it was not a “systemic risk.”

The opposite view was outlined in a letter sent yesterday to finance ministers and central bank governors of the G20 countries authored by Bank of England governor Andrew Bailey in his capacity as chair of the Financial Stability Board, a global watchdog.

Pointing to the “substantial shock” to the global economy resulting from the US war against Iran, he wrote: “We have to be particularly alert to this volatility in financial markets and tightening of conditions interacting with other vulnerabilities, including: stretched asset valuations; the build-up in the non-bank sector of high and increasingly concentrated leverage; and liquidity mismatches, opacity and growing complexity in certain markets, notably private credit.”

There was an “increasing likelihood that multiple vulnerabilities could crystallise at the same time, thereby amplifying the threat to financial stability.”



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