Financial Turbulence: New Downturn in the Global Economy

By Nick Beams
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There are increasing signs that the global economy is about to enter a new period of financial turbulence, coupled with deepening recession in a growing number of countries.

In the immediate aftermath of the global economic breakdown that began in 2008, set off by the collapse of the US investment bank Lehman Brothers, governments around the world took on increased debt as they made available trillions of dollars to prevent a complete collapse of the financial system. Meetings of the Group of 20 were dominated by pledges there would be no return to the conditions of the 1930s and assurances that the lessons of history had been learned.

The writings of John Maynard Keynes, the British economist of the 1930s who advocated increased government spending to counter depressions, were suddenly back in vogue. But a sharp turn came in June 2010, when a meeting of the G20 initiated a turn to austerity, emphasising the necessity to impose "fiscal consolidation." The essence of this program was to claw back the money given to the banks through massive cutbacks to government spending, especially on social services.

However, this program brought a contraction in economic growth leading to decreased profit opportunities for major corporations. Faced with this situation, the US Federal Reserve initiated a policy of "quantitative easing"—the provision of unlimited supplies of money to banks and financial institutions. Central banks around the world cut interest rates to record lows and followed that up with their own versions of quantitative easing (QE). Under conditions of a stagnant real economy, these measures were aimed at boosting the value of financial assets, thereby providing a new avenue for finance houses to realise speculative profits.

While the QE program and its equivalents have been touted as a means of preventing a slide into global recession—US Fed Chairman Ben Bernanke claimed the recently enacted QE3 program was motivated by continuing high unemployment—they have done virtually nothing to boost the real economy. Their only significant impact has been to increase profits through financial manipulation, with the ultra-cheap money provided by the central banks.

But now there are signs that a new stage in the global breakdown is underway, marked by growing recessionary trends, as the impact of the central bankers' program wanes.

Share prices in the US, which had been lifted by the QE program, have started to fall as companies report a downturn in sales and profits amid announcements of further job cuts. This week American companies pointed to weakening global demand and the fears generated by the continuing financial crisis in Europe.

Dow Chemical announced it would axe 2,400 jobs, 5 percent of its global workforce. It also said it would shut 20 plants and cut capital spending by $500 million, citing a “slow-growth environment in the near term.” DuPont, the largest US chemical group, announced 1,500 layoffs and a loss for the third quarter. It pointed to a sharp drop in sales to the Asia-Pacific region, where volumes were down 10 percent compared to a year ago, dealing a blow to claims that so-called “emerging markets” would provide an alternative source of global demand.

Overall, US corporate profits and earnings are expected to fall for the first time since 2009. The latest data on the US economy show that gross domestic product (GDP) grew at an annual rate of only 2 percent in the third quarter, well below that required to maintain employment levels. Were it not for the effect of an increase in defence spending, the figure would have been significantly under market expectations.

The most significant feature of the US GDP data was investment spending. Its continuing decline reduced the overall growth figure by 0.1 percentage points for the quarter, while imports and exports both fell, taking off 0.2 percentage points.

While the central bankers will continue to pump money into financial markets, these measures will do nothing to turn the situation around. This week, in a major speech, the governor of the Bank of England, Mervyn King, noted that every increase in the money supply had a declining impact on the real economy.

His warnings are confirmed by historical trends. Writing in the *Financial Times*, financial analyst Satyajit Das pointed out that between 2001 and 2008, borrowing against the rising value of houses contributed about half the growth in the US. “But ever increasing borrowings are needed to sustain growth. By 2008, $4 to $5 of debt was required to create $1 of US growth, up from $1 to $2 in the 1950s. China now needs $6 to $8 of credit to generate $1 of growth, an increase from around $1 to $2 15-20 years ago.”

At the meetings of the G20 in 2009, government leaders insisted there would be no return to the protectionist measures of the 1930s which had such a devastating impact on world trade. But the QE program is producing a twenty-first century version of the beggar-thy-neighbour policies of the Great Depression. The flood of money from the US Federal Reserve has pushed down the value of the US dollar, hitting the export markets of its competitors and leading to the development of “currency wars” as they try to maintain their position.

Furthermore, the boosting of financial assets under conditions of slowing economic growth threatens to replicate the conditions that sparked the 2008 collapse on an even broader scale. This is because, unlike the situation four years ago, the central banks themselves are now heavily involved in financial markets and stand to lose massive amounts in a market collapse.

The central bankers and capitalist politicians claim that while their actions may not have promoted growth, they have at least averted a return to the conditions of the 1930s. These claims are belied by the conditions in Spain and Greece, where unemployment is already at 1930s levels.

Moreover, when viewed from an historical perspective, their self-congratulations are somewhat premature. The Great Depression came after a decade of financial and economic turbulence set off by the breakdown of global capitalism that began with the outbreak of World War I in 1914.

This time around, the capitalist breakdown began with a financial crisis that has now set in motion a deepening contraction in world economy.

Like their counterparts in an earlier period, the ruling elites have no response to the historic crisis of the profit system other than a social counterrevolution against the working class, militarism, and the imposition of dictatorial forms of rule.

Far from ending, the global economic crisis is only just beginning. The working class must respond by developing its own independent program based on an intransigent political struggle for the overthrow of the bankrupt capitalist profit system and the bringing of the banks and major corporations under public ownership in order to establish a planned world socialist economy.

Nick Beams