Recession Looms? IMF Cuts Growth Forecasts for Major Economies

By Nick Beams

Theme: Global Economy

Global Research, October 05, 2016
World Socialist Web Site 5 October 2016

The International Monetary Fund has revised down its estimates for the US and other advanced economies for this year while maintaining its forecast for global growth as a whole at the low level of 3.1 percent in its latest World Economic Outlook report released yesterday.

It said the major economies would grow by just 1.6 percent this year compared to 2.1 percent in 2015, down from the forecast of 1.8 percent growth made last July. The most significant decline in the US where the IMF cut its July forecast of 2.2 percent growth to just 1.6 percent following what it said was a "disappointing first half caused by weak business investment" and a rundown of inventories.

It said the euro area would expand 1.7 percent this year and 1.5 percent next year compared to 2 percent growth in 2015. Growth in Japan, the world's third largest economy, would be only 0.5 percent this year and 0.6 percent in 2017. Growth in the UK economy is forecast to be 1.8 percent this year, falling to 1.1 percent in 2017, compared to growth to 2.2 percent in 2015.

Growth in the Chinese economy, the world's second largest, is forecast to be 6.6 percent this year, falling to 6.2 percent in 2017, compared to growth of 6.9 percent in 2015.

Falling growth in the major economies is offset to some extent by growth in so-called emerging market and developing economies, which is forecast to rise for the first time in six years to 4.2 percent this year, up from the forecast of 4.1 percent in July, and then increase to 4.6 percent in 2017.

Summarising the outlook, the IMF's economic counsellor Maurice Obstfeld said: "Taken as a whole, the world economy has moved sideways. Without determined policy action to support economic activity over the short and longer terms, sub-par growth at recent levels risks perpetuating itself through the negative economic and political forces it is unleashing."

On the economic front those forces include the emergence of the "deflationary cycle" in which "weak demand and deflation reinforce each other" giving rise to a "deflationary trap" in which interest rates, already close to zero, cannot stimulate the economy," according to the WEO.

An IMF discussion note, co-authored by Obstfeld and released on the eve of the report, warned that downside risks were high, confidence in a sustainable recovery low and, with interest rates at the lower bound, "a deflationary cloud threatens as weak growth looms."

In his remarks on the WEO, Obstfeld pointed to the political impact of slow growth and rising inequality in the eight years since the global financial crisis of 2008. “The slow and incomplete recovery from crisis has been especially damaging in those countries where the distribution of income has been skewed sharply towards the highest earners leaving little room for those with lower incomes to advance,” he said.

The main factor in the growth of income and wealth inequality, above all in the advanced economies, has been the policies of “quantitative easing” by the world’s major central banks. With the full support of the IMF, they have pumped trillions of dollars into the financial system, enabling rampant speculation, parasitism and the accumulation of unprecedented wealth on the heights of society, while living standards and social conditions have been slashed through a combination of lower wages and cuts in social services.

According to Obstfeld, the consequence of this economic development was a “political movement that blames globalisation for all woes and seeks to wall off the economy from global trends rather than engage cooperatively with foreign nations. Brexit is only one example of this.” Protectionist trade measures have been on the rise across the world, he said.

However, to blame the rise of protectionist measures on a movement of resentment and hostility from below over rising social inequality is completely false. The drive toward protectionism is being organised from above as the governments and ruling classes of the major capitalist powers, confronted by a contracting world economy, take action against their rivals.

As the World Trade Organisation and other international trade bodies have noted, protectionist measures have significantly increased over the past two years, mainly as a result of actions initiated by the governments of the major countries. This has taken place despite repeated declarations at the G-20 summit meetings that the lessons of the 1930s, when such beggar-thy neighbour policies helped fuel the drive to war, have been learned.

The conflict over the $14 billion fine imposed by the US Department of Justice against Deutsche Bank was a political initiative aimed at weakening, if not completely crippling, Germany’s only significant international bank. This prompted claims from leading German politicians that the US was waging “economic warfare” against Germany and that the US had a “long tradition” of waging what amounted to trade war “if it benefits their own economy.”

The move on Deutsche Bank followed in the wake of the European Union decision to impose a €13 billion back tax claim on Apple, prompting strident denunciations from US business leaders, and the virtual scuttling of the US-backed Transatlantic Trade and Investment Partnership by Germany and France.

The release of the WEO was preceded by a series of warnings from leading economic commentators about the direction of the global economy and its implications for world politics.

According to the Brookings Institution-Financial Times tracking index, growth rates for the world economy were “sliding back into the morass [they have] been stuck in for some time.”

Brookings Institution economist Eswar Prasad said most of the world could be described as having "weak investment, stagnant productivity and tepid private sector confidence." With little prospect of a spontaneous recovery or any new stimulus " a strong adverse feedback loop has been set in with low growth, fragile business and consumer confidence, low interest rates, trade tensions and political instability feeding into and reinforcing each other."

Writing in the *Financial Times*, Mohamed El-Erian, the chief economic adviser to the financial firm Allianz, warned that the "new normal" of the past seven years was unsustainable. The consequences of low growth went far beyond today's forgone economic opportunities because the longer they persist "the more they eat away at the potential for future growth" as investment plans are shelved.

"The 'new normal'," he concluded, "is coming to an end. The reason is simple: it has lasted for so long that it is now breeding the causes of its own destruction."

Former chairman of Morgan Stanley Asia Stephen Roach, now a lecturer at Yale, took aim at the policies of the central banks. Their approach led to an "insidious connection" between monetary policies, financial markets and asset-dependent economies which had led to the meltdown of 2008-2009 and "could well sow the seeds of another crisis"

"Central bankers desperately want the public to believe they know what they are doing. Nothing could be further from the truth."

The lack of response to zero interest rates was "strikingly reminiscent of the so-called 'liquidity trap' of the 1930s, when central banks were also 'pushing on a string'." But having depleted their traditional arsenal long ago, central bankers remained "myopically focused on devising new tools, rather than owning up to the destructive role their old tools played in sparking the crisis."

The drawing of a parallel between present conditions and those of the 1930s is not misplaced. The stagnation in the world economy and the failure of the ruling elites to devise any measures to turn it around is fuelling the rise of geo-political tensions and conflicts, which, in turn, impact on the world economy. Coupled with the rise of militarism, these processes point inexorably in the direction of war.