The World Economy in Decline*

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The European Central Bank last month pushed its benchmark interest rate to minus 0.5 per cent, which means that if it gives a loan of 100 euros then it would be paid back only 99.5 euros at the expiry of the loan. This has started a new trend: in countries like Germany, Spain, Italy, Czech Republic and even Greece, the yields on government bonds have been pushed into the negative region. Lenders to these governments in other words are willing to pay for holding government bonds. Longer term bonds typically have higher yields than shorter-term ones, but in Germany now even the 30-year government bond is offering negative yields.

Since the idea behind the European Central Bank's policy is to have a low interest rate regime, which, it is hoped, would cause a larger amount of investment to be undertaken, so that the level of aggregate demand and hence output and employment increases, the interest rate offered to depositors too will have to be lowered.

This would entail, on the whole, a regressive distribution of income, since, taking society as a whole, whatever net lending occurs across classes is from the working and middle classes (including the contributors to pension funds) towards the corporate sector; and this is irrespective of whether any productive investment occurs or not. A reduction in the interest rates therefore entails a net shift in income distribution from the working and middle classes (the creditors) towards the corporate sector (the debtors).

The lowering of interest rates has now gone to a point where even nominal rates have entered the negative region, a phenomenon that is quite unprecedented in the history of capitalism. It is obvious that in a cash-using economy there are limits to the extent to which the interest rates can be pushed down (unless cash holdings themselves begin to get taxed); this is because if people can hold cash which has a zero interest rate, then they will never hold deposits with banks or with any other financial intermediaries at less than zero rates. And if depositors have to be offered a non-negative rate, then the extent to which rates to lenders can be pushed down by banks is also limited. But it a sign of the desperation in the advanced capitalist economies that interest rates are being pushed down even to negative regions in a bid to revive economic activity.

The need for such negative interest rates would not arise if governments could adopt fiscal measures for stimulating activity, but since international finance capital is opposed to fiscal deficits (the countries of the EU have a fiscal deficit limit of 3 per cent of GDP), and does not naturally approve of taxing capitalists (taxing workers and spending the proceeds would not help in expanding aggregate demand), fiscal measures are ruled out. Hence monetary policy remains the only instrument for stimulating aggregate demand.

This helplessness and desperation is evident in India too where there have been five rounds of interest rate cuts by the Reserve Bank of India till now, but to no effect; and when the government finally decided to adopt some fiscal measures, all it did was to offer corporate tax concessions, which would actually be counter-productive. To the extent that such concessions are financed by a corresponding enhancement of taxes on the working people (or a reduction of transfers towards them), they would shrink rather than expand aggregate demand.

Ironically, even in Europe and elsewhere, the complete bluntness of the monetary policy instrument is being amply demonstrated. Even The Financial Times (October 14) is now talking of the global economy having entered a period of "synchronized stagnation", "with weak growth in some countries and no growth or a mild contraction in others".

This bluntness of the monetary policy instrument arises from the fact that corporate investment is essentially interest rate-insensitive: net investment occurs in response to the expected growth of the market, and if the market is expected to remain stagnant then no amount of lowering of the interest rate, and hence of the cost of finance for the corporate sector, will bring forth an iota of net investment.

Of course monetary authorities may believe that lower interest rates would help in a different way, via the generation of asset-price bubbles. Such a bubble, to the extent that it makes the holders of the concerned asset feel wealthier (until the bubble collapses), may induce larger expenditure on conspicuous consumption, and thereby stimulate aggregate demand.

But this is a dicey proposition; besides, if at all there is some increase in conspicuous consumption via the wealth effect, it takes time. What is more, after 2008 the asset price bubble route for stimulating the level of activity in the real economy, which in any case is a reprehensible route compared to other ways of stimulating activity such as larger government spending on welfare schemes, has also lost its effectiveness as a stimulant.

It is not surprising in this context that the so-called "headline economic indicators" have now slipped to their lowest levels since the spring of 2006. Considering the fact that in the interim, i.e. between those years and now, the world economy has continued to experience sluggish growth, the current fears of stagnation and recession are symptomatic of a protracted crisis of the system. In fact the IMF's new managing director admitted in a speech last week that "in 2019 we expect slower growth in nearly 90 per cent of the world". What is particularly striking is that even a country like Germany, which appeared to have escaped the crisis until now, is also facing the prospects of a recession now.

Bourgeois commentators adduce specific factors like the trade conflict between the U.S. and China to explain the current slowdown. These according to them have dented the "animal spirits" of the capitalists, adversely affecting their desire to invest in productive assets and hence precipitating the slowdown. The Economic Times report for example talks of the current situation being characterized by "falling economic confidence".

But such explanations which see the crisis essentially as episodic, rather than structural and hence protracted, miss two vital points: first, ever since 2008 the growth rate of the world economy has slowed down quite substantially; in fact what has been happening in the world's largest economy, the U.S., has been aptly described by the analogy of a ball bouncing along the floor. Secondly, the trade tensions between the U.S. and China are themselves a reflection of this protracted crisis of world capitalism. Donald Trump's aggressive protectionism is a means of enlarging the level of activity in the U.S., through an actual reduction in imports into the U.S. as well as through pressurizing other countries into providing greater market access to U.S. goods.

The root of the current crisis lies not in the obstreperousness of a Donald Trump that precipitated the trade war with China and thereby led to "falling economic confidence". It lies in the nature of neo-liberal capitalism itself which has unleashed powerful income-inequalizing tendencies. These tendencies have a contractionary effect on the level of aggregate demand both in the world economy as well as within particular countries. This contractionary effect had been kept in check in the period before 2008 because of a series of powerful asset-price bubbles within the U.S. With their collapse, however, the basic tendency towards an over-production crisis within neo-liberal capitalism, has revealed itself.

Since any such crisis affects high-cost producers first, countries like the U.S. and the Eurozone were its first victims, with countries in East and South Asia, to which outsourcing of activities had occurred from the advanced capitalist world because of the latter's low wages, appearing initially to withstand it. But the very continuance of the crisis, and Trump's "beggar-thy-neighbour" policy, have finally caught up with these Asian countries as well, because of which we are now in the process of moving towards a truly world-wide recession. This would start a whole new era of intense class struggles and powerful social transformations.

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