Japanese stocks plunge amid global financial turmoil

By Andre Damon
14 June 2013

The Japanese stock market plunged 6.4 percent Thursday. The sell-off—part of a 21 percent fall over the past three weeks—was only the most visible sign of the growing volatility in global stock, bond, and currency markets, rooted in fears that any letup in asset purchases by the US Federal Reserve could trigger a global financial collapse.

On May 22, Federal Reserve Chairman Ben Bernanke said in congressional testimony that the US central bank could consider scaling back their $85 billion a month asset purchase program "in the next few meetings" if there is a significant improvement in the economy. This remark added to investors' growing fears of an end to global central banks' unprecedented money-printing operations.

Bernanke's remarks served as a catalyst for a sell-off in bond markets. Last week, research firm EPFR Global said that investors pulled $12.53 billion out of global bonds over the preceding week, the largest bond sell-off on records dating back to 2001. Since the end of April, the interest rate on US 30-year Treasury notes has shot up from 2.8 to 3.37 percent.

Fears that the Federal Reserve would draw down its "quantitative easing" program has also caused emerging market currencies to plunge in value. Over the past three months, the Brazilian real has fallen 8 percent against the dollar, the Indian rupee has fallen 6.8 percent, and the Australian dollar has fallen 7.7 percent.

Credit in emerging markets has likewise tightened significantly. Over the past month, JPMorgan's emerging market EMBI bond index has risen by one percentage point, to 5.5 percent.

The sell-offs in these currencies have been so substantial that governments have moved to stem the process. India's central bank intervened to try to halt the slide in the rupee Tuesday.

That same day, Bank Indonesia announced that it would raise its main interest rate by a quarter of a percentage point, to 6 percent.

The Brazilian government announced that it would eliminate the one percent tax on financial transactions in the country, seeking to halt the slide of the real, which hit its lowest level against the dollar in four years.

These actions come as the world economy continues to deteriorate. China's economy grew at a rate of 7.7 percent last year, the slowest rate in 13 years, and indicators of economic growth are trending downward.

On Thursday the World Bank cut its growth estimate for the Chinese economy in 2013 to 7.7 percent, down from 8.4 percent, and warned of the potential for a "sharp" slowdown of the Chinese economy.

The report noted the "possibility that high investment rates prove unsustainable, provoking a disorderly unwinding and sharp economic slowdown."

Earlier this month, HSBC said that its index of manufacturing activity in China fell to 49.2 in May, the lowest level in eight months, and significantly lower than the reading of 50 that indicates the point between contraction and expansion.

The sell-off in Japan came as investors voiced their dissatisfaction with the Abe government for not attacking working-class living standards aggressively enough. As the *Wall Street Journal* put it, Abe's latest set of economic restructuring proposals "was missing a few key policy items that markets and the business sector were hoping to see, including a reduction in the corporate tax rate and deregulation of employment rules to aid corporate restructuring."

In the global sell-off of bonds there may well be a similar warning to the Federal Reserve: any move to

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restrict the vast quantities of cash flowing into global markets will be met with a calamitous sell-off.

But the element of panic is likely even more pervasive. US stocks have been rising for four years and have more than doubled since their low point in early 2009. Yet since 2010, the US economy has created an average of only 162,000 jobs per month, lower even than the 166,000 average monthly growth rate of the US working-age population.

The only thing sustaining the dizzying rise in stock values, amid a disastrous real economic situation, is the vast infusion of cash into financial markets by central banks, coupled with global austerity programs that have drastically slashed wages and swelled corporate profits.

But there are growing fears that the entire global economic setup created on the basis of the Federal Reserve's asset-purchasing program is on the verge of collapse.

"The tectonic plates of the world economy are shifting," the *Wall Street Journal* noted in an alarmed article on its front page Wednesday. "For the past few years, the global economy, struggling to recover from a financial crisis, has relied on a few constants: The US would print plenty of money and keep interest rates very low. China would provide a lot of demand and vacuum up commodities from around the world."

But the reversal of these trends could be a "harbinger of more volatility in financial markets…that yields an unwelcome increase in market interest rates before the US economy achieves what Fed Chairman Ben Bernanke once called 'escape velocity.'"

The global panic over the prospect of a "tapering" of bond buying by the Federal Reserve is ultimately an expression of the phony character of the economic "recovery." Asset values, having swelled from the vast infusions of Federal Reserve cash, are totally out of proportion with the slowing global economy and threaten to plunge at any moment.

Last month, Gillian Tett wrote in the *Financial Times*, "While the flood of central bank liquidity is enabling the system to absorb small shocks, it is also masking a host of internal contradictions and fragilities that could surface if a shock hits. Or… precisely because central banks are trying to pursue stability at all costs, the potential for a future violent instability is rising apace; 'tail risk,' as statisticians say, is growing."

Put more plainly, Tett is warning that even as the vast expansion of credit by central banks has partially masked the deepening economic contradictions in the global financial system, it has paved the way for a financial collapse on or exceeding the scale of the 2008 crash.

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