A wild week on Wall Street

By Nick Beams
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US stocks fell marginally yesterday, with the Dow down by 76 points after one of the wildest weeks on record left analysts and pundits none the wiser over the future direction of the market. The words “surreal,” “panic” and “shocking” were among those used to describe the situation.

The week began with the worst Christmas Eve in history, as the Dow fell Monday by more than 600 points. The decline was prompted, at least in part, by the report that Treasury Secretary Steven Mnuchin had contacted the major banks, which gave assurances that their liquidity positions were sound. This raised questions as to why he thought it necessary to ask them in the first place.

The markets were closed Tuesday, Christmas Day. On Wednesday, the Dow soared 1,086 points, its largest ever point rise in a single day. The following day the markets opened significantly down before rising at the close. The Dow moved through a range of more than 800 points. After falling by 2.7 percent at one stage it finished the day 1.1 percent higher.

Friday saw a repetition of the pattern of swings, albeit in a somewhat more muted form compared to earlier movements. The market rose on the opening—the Dow was up by 243 points at one stage—but finished the day in the red.

This week registered the first gain for markets in three weeks, but they remain on course for the worst December since 1931, in the depths of the Great Depression. All major indexes are set to record annual losses for the first time since the financial crisis of 2008.

At the beginning of the week, both the Dow and the S&P 500 index were on the brink of entering a bear market, defined as a decline of at least 20 percent from the most recent high. But they pulled back somewhat by end of the week and are now down 14 percent and 15 percent respectively from their peaks.

While any number of events can impact the markets on any given day, the underlying instability is grounded in longer-term economic and political processes.

A key factor is the overall slowdown in the world economy. At the end of 2017, the tone in markets was generally upbeat because global output had experienced its most sustained phase of synchronised growth since the end of the financial crisis. However, it proved to be short-lived, and the year has ended with the Japanese and German economies—number three and number four in the world respectively, after the US and China—on the edge of recession.

At the same time, growth in China is slowing—last quarter it experienced its lowest growth rate since 2008-2009—and US growth is also expected to fall from the level of above 3 percent achieved this year as a result of the stimulus provided by the Trump administration’s tax cuts.

The impact of lower global growth is compounded by fears that the trade war between the US and China is going to escalate. The clock is winding down on the 90-day deadline agreed to on December 1 between US President Trump and Chinese President XI Jinping to reach a deal.

So far the tariff measures introduced by both sides have had relatively little effect. But that could rapidly change because the US has indicated that it will increase a 10 percent tariff imposed on $200 billion worth of Chinese goods to 25 percent if no deal is reached.

While talks between the two sides have taken place, and negotiations will be stepped up in January, there are limited prospects for an agreement because the US is demanding what it calls “structural” changes in the Chinese economy, including to the state subsidies provided to key industries, which Beijing regards as fundamental to its future development.

Moreover, trade tensions have been heightened by the arrest in Canada of Meng Wanzhou, the chief financial officer of the Chinese telecom giant Huawei, and the push by US intelligence and military agencies to have the firm excluded, both in the US and internationally, from the establishment of new networks, above all for 5G mobile phones, on "security" grounds.

Global markets, which have all fallen through this year, are being significantly impacted by the sea change in financial conditions. In the decade since the financial crisis, the Fed and other major central banks have pumped trillions of dollars into the global financial system, providing a major boost to asset values, above all stock prices. But this program of quantitative easing has been replaced by quantitative tightening, as central banks move to reduce their holdings of financial assets.

It is significant that a spark for the US sell-off, following the decision of the Fed earlier this month to raise interest rates 0.25 percentage points, was provided by the comment by Fed Chairman Jerome Powell on the reduction of the central bank's asset holdings.

He indicated that this would proceed at the rate of $50 billion per month and was on "auto pilot." Powell's comment was nothing more than the articulation of what has been Fed policy for more than a year, but it had an impact because it drew attention to the fact that one of the key factors in the market bull run since March 2009 was no longer at work.

In addition to the economic processes, the market turbulence is being fuelled by the ongoing political crisis in the US. Trump has been targeted by key sections of the military and intelligence apparatuses, speaking through the Democratic Party and the *New York Times*, as a threat to the geo-strategic and military interests of the US.

This opposition reached new heights with his announcement of the withdrawal of US troops from Syria and the subsequent resignation of Defense Secretary James Mattis. Now the conclusion is being drawn that Trump may also be a destabilising factor on the economic front and the push for his removal needs to be intensified. This was the essential line of a recent comment published by *New York Times* columnist Thomas Friedman.

Global political upheaval bound up with the growth of the class struggle—the deepening Brexit crisis in the UK, the ongoing opposition to the Macron government in France embodied in the "yellow vest" movement, instability in Italy and uncertainty over the future course of the Merkel government in Germany, to give but a few examples—is also feeding into financial markets. Together with the worsening economic outlook, it means that the market turmoil that has marked the end of this year could be the start of bigger upheavals to come in 2019.