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Growing Fears about Future World Economy

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From the macro viewpoint, the international political situation and world economy are the two major important factors to influence the international energy market. Since early this year, the destabilization of the Middle East and North Africa, an international political or geopolitical problem, has exerted great influences on the international energy market. In addition, a new energy problem emerged on the Great East Japan Earthquake as an unprecedented disaster in Japan and has shaken the international market. While these developments still underlie the market situation, a new problem is apparently emerging. That is the problem of growing fears about the future world economy.

The problem is still limited to "fears about the future." But we now see factors for fears accumulating in major regions of the world.

In the United States, May's employment situation data included a nonfarm payroll increase at 54,000 that month, slipping far below a consensus market forecast of 150,000. The unemployment rate rose from the previous month to 9.1%. The worse-than-expected employment situation data prompted stock prices to turn downward. On June 10, the 30-issue Dow Jones industrial average on the New York Stock Exchange slipped below 12,000 for the first time in almost three months. In addition to concerns about the future course of the economy as indicated by the above macroeconomic indicators, the planned June 30 termination of the Quantitative Easing 2 monetary policy, which has supported stock prices, might have affected the stock market.

Another factor behind the U.S. stock market decline was Europe's serious sovereign crisis. On June 13, U.S. debt rating agency Standard & Poor's lowered the Greek sovereign rating by three notches from single B to triple C. The agency then indicated a critical view that Greece sharply grew likelier to default. As the Greek debt problem has grown more serious again, Irish and Portuguese government securities trading has declined to record lows. Concerns about the euro area economy have increased considerably. Market participants are very unsettled, fearing that if Greece defaults, it may spill over to the whole of Europe including Ireland and Portugal. European and other countries are considering additional financial support to prevent Greece from defaulting and market participants are closely watching their talks with fears in mind. This is the present situation. The growing fears about the future in Europe have reduced market risk tolerance dramatically, destabilizing the whole of financial markets.

As well as the abovementioned European and U.S. situations, we may have to pay attention to the Chinese economic situation. China took advantage of a 4 trillion yuan economic stimulus package to become the first country in the world to overcome the global financial crisis following the Lehman Shock, boosting its presence as the driver of the world economy. Recently, however, problems facing the Chinese economy have rapidly attracted attention.

The first problem is inflation. The consumer price index for May posted a 5.5% rise from a year earlier, the fastest increase in 34 months. Particularly, rural regions scored a CPI hike of 6.0% exceeding the national average. The inflation problem is attracting attention in China because of wide income gaps and a great number of low-income people (mainly in rural regions and even among a growing number of urban residents). Inflation can exacerbate social strains, becoming a risk factor to boost discontent and fears. Price hikes have been remarkable for foods. The CPI inflation rate for foods is as high as 11.7%, attracting great attention. Stable prices and supply of foods and other necessities are required to stabilize the public's livelihood and sentiment. In this sense, the government has no choice but to enhance anti-inflation measures including monetary tightening. In its annual monetary stability report released on June 14, in fact, the People's Bank of China gave top priority to anti-inflation measures. On the same day, the central bank announced a decision to raise the deposit reserve requirement ratio by 0.5 percentage point on June 20.

Amid the present situation, "economic bubbles" have become a matter of concern in China. Chinese bubbles have been cited frequently along with the inflation problem and the government has so far prevented bubbles from bursting with tightening and other policy measures, as is well known. In this sense, bubble-burst fears could turn out to be unfounded. However, media reports have stated that the number of investment companies controlled by local governments in China increased 25% in two years, with their debt expanding to up to 14 trillion yuan by the end of 2010. In fact, fears of expanding bubbles and their burst are growing again.

Meanwhile, it is quite interesting that Britain's Financial Times has published several reports on fears about the future course of the Chinese economy, including the bubble problem, since May. The newspaper acknowledges the significance of China for the world economy, gives attention to the reality and importance of bubbles as China's domestic problem, and concludes that measures must be taken for a soft landing to prevent bubbles from bursting. It may be needless to say that appropriate and timely monetary and economic policy measures are required to avoid economic overheating and the burst of bubbles. But such policy management must be fine-tuned. Depending on policy mismanagement, a hard landing could come. Therefore, the future Chinese economy and the Chinese government's economic policy management will attract global attention.

In response to growing fears about the future world economy, money is flowing out of many financial markets in the world, with market prices dwindling. On June 15, the benchmark West Texas Intermediate crude oil futures price lost $4.56/barrel from the previous day to $94.81/barrel, slipping below $95/barrel for the first time in about four months, since late February. For the immediate future, the trend and fate of fears about the future world economy will be the most important factor to move the international energy situation unless substantial changes emerge in the influences of other factors (including international politics and geopolitical issues) on the energy market. Therefore, we may have to pay even closer attention to the trend.

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