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Turbulence Hit World Economy as New Year Opened

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Turbulence hit the world economy as the year 2015 opened. After rising to an all-time closing high of $18,054 on December 26 on the strength of the brisk U.S. economy, the Dow Jones Industrial Average on the New York Stock Exchange entered a downward trend upon the turn of the year and plunged to $17,372 on January 6, inducing a global stock market decline. On the Tokyo Stock Exchange, the 225-issue Nikkei Stock Average slipped below the psychologically important level of Yen 17,000 to Yen 16,883 on January 6, losing 525 points or 3% from the previous day.

The stock market decline came as both Japanese and U.S. markets were expected to rise this year. Among factors behind the unexpected stock drop are (1) rapid crude oil price falls and (2) concerns over the future European economy, including fears of the resurging Greek debt crisis, indicating growing risks involving the whole of the world economy. The growing risks prompted market participants to take risk-averse actions to shift from risky assets to safer assets including bonds, creating stock and crude oil price drops as a synergetic effect.

The rapid crude oil price drops cited above as a factor behind the global stock market plunge included the benchmark West Texas Intermediate futures price's slip below $50 per barrel meeting earlier expectations. The price fell below the level briefly on January 5 and dropped to $47.93 on the next day's close. The price, which had been expected to decline below $50 late last year, actually did so, prompting market players to pay attention to how far the price would decrease.

Crude oil price drops are expected to benefit the world economy on a net basis. But rapid, substantial falls are feared to seriously affect oil producing countries with vulnerable economies depending heavily on oil revenues, spilling credit risks over to the whole of the world economy.

In a typical case, concerns have grown over a Russian financial crisis. Late last year, the Russian ruble's plunge was coupled with a Russian stock market drop and a capital outflow from Russia. As crude oil prices have declined below $50 and are expected to fall further, market players have grown concerned that the Russian economic problems could become serious and trigger credit and monetary fears that could spread to the world economy including the European market. There are other countries with structurally vulnerable economies, including Venezuela, Nigeria and other oil producing countries in severe economic conditions, as well as Indonesia, Brazil, Turkey and other emerging countries affected by "Russia-selling" last month. In this way, crude oil price drops have induced credit and monetary risks and led to risk-averse selling of stocks, becoming a factor to shake the world economy.

The second factor, the European economic problem including fears of the resurging Greek debt crisis, is unignorable. The serious Greek economic problem triggered the euro crisis in late 2009 and had been contained thanks to rescue plans by the European Union and the International Monetary Fund, and Greece's austere budget policy. On December 29, however, the Greek parliament was dissolved due to its failure to elect a president, with a snap election scheduled for January 25. The problem is that a radical leftist party with populist policies of abandoning the austere budget and refusing to repay debt is dominantly expected to win in the coming election. If the expectation comes true, Greece is feared to enter economic turmoil, default on debt repayment, see bank runs and secede from the eurozone in the worst scenario.

While Greece attracts attention as the weakest link with the Greek crisis and fears of its secession from the eurozone resurging, market players are looking to other eurozone countries in vulnerable economic conditions and under strong populist influences. As Greece's secession from the eurozone is expected by some people to have a far greater impact than the Lehman Shock, the European market turmoil has emerged as a major destabilizing factor for the world economy since December 29.

In July 2012, European Central Bank Governor Mario Draghi vowed to do anything to defend the euro, contributing to restoring market stability. The European economy, though remaining stagnant and weak, kept from plunging into any crisis, with the Greek situation remaining in a lull. In the meantime, however, discontent with the austere budget policy might have accumulated with populist forces growing in Greece, leading to the parliamentary election. The development has exposed serious economic and political problems plaguing the European economy anew.

The two grave events of crude oil price drops and Greek crisis fears thus shook the world economy at the outset of 2015. The turbulent opening of the year has made future developments even more uncertain.

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