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‘Mutation’ in the Global Economy?

By Christopher H Lim & Victor R Savage

Synopsis

Since the 2007-2008 Global Finance Crisis (GFC), the global economy has experienced a decade-long “economic stimulus” which can be likened to a steroid in human health. Could this possibly create a highly resistant “economic superbug” which might be impervious to existing economic solutions?

Commentary

AS A collective response to the Global Financial Crisis (GFC) of 2007-2008, the United States Federal Reserve (Fed), the European Central Bank (ECB) and the Bank of Japan have over the past 10 years issued a combined stimulus package of more than US\$13 trillion.

In addition, during this same period, many other central banks had pursued short-term low interest regimes (close to zero or even below zero) as part of the economic global effort to avert the GFC.

Mixed Outcomes

Since the GFC, we have noted the following developments:

- Global stocks were up in [positive](#) territory and even the Junk-rated sovereign debt bonds from the emerging markets were able to rise to [US\\$75 billion](#).
- The bumper harvest at Wall Street, where the borrowing spree by governments and corporate entities reached [\\$6.8 trillion](#) in 2017, has set a record high far exceeding all past annual levels [since 1995](#).
- Observations from the index of US stock market (S&P 500) over US\$ per troy ounce

of gold (stock market when priced in gold) and US homebuilding stocks have both bottomed out in the third quarter of 2011.

- The last US unemployment figure in August 2018 based on the Bureau of US labour Statistics was 3.9% which was at record low since Jan 2008.

Beneath the glowing façade, we observe the worsening global “debt-fever”, marked by a further increase of [\\$30 trillion](#) from end 2016 to a record high total debt of [\\$247 trillion](#) (first quarter 2018) in spite of the strong global economic growth in 2017.

Yet, the real wage percentage change increase for the [US](#) is below the OECD average of 8.4% from 2008 to 2017. Studies of the US Federal Reserve System found that 40% of US adults were [unable to pay](#) emergency expense of even \$400.

Unintended Economic/Fiscal Developments

Following the GFC and quantitative easing (QE) measures, central banks and policymakers had no alternative but to ensure the enhancement of bank capitalisation under their jurisdiction.

Given the active role of governments during the GFC decade, a lot of attention was focused on the debt liability of governments but not on other actors in the global economy.

Total debt continued to climb between 2007 to the first half of 2017 with the incremental debt of [\\$72 trillion](#), of which government debt accounts for 43% of this increase and nonfinancial corporate debt is responsible for 41%.

Between 2007 and mid-2017, as commercial bank lending tightened many corporations particularly from the emerging markets moved to bond financing. This shift pushed the global value of nonfinancial corporate bonds outstanding to US\$1.7 trillion. Such developments indirectly attracted the emergence of many speculative-grade bonds, with their increasing attendant risks.

Withdrawal Symptoms

At the third quarter of 2017, the chair of the Fed indicated the end of US quantitative easing, which means the end of expansionary monetary policy, and the rise in interest rates in 2018. Similarly, ECB intends to taper off its stimulus package within 2018 or by 2019 followed by a gradual increase of interest rates.

The immediate concern is whether the global economy will suffer ‘withdrawal symptoms’, since it has been addicted to a decade of constant and generous supply of ‘stimulus drugs’ (i.e. QEs and low interest rates) – adopted initially by the US, EU and Japanese markets and then quickly spreading beyond. The question is whether the global economy can sustain and grow without additional “stimulus drugs” as a catalyst?

Challenges Ahead

There is a [disconnect](#) between the Wall Street Economy (WSE) and the Main Street Economy (MSE). This stems from differences in basic application. These involve differences when one compares the high-frequency trading in the financial sector where time is measured in nanoseconds or even smaller units, whereas the real economy application is calculated in days, months or even years.

Yet, both the WSE and MSE are using the identical currency for transactions despite their distinct value and concept in wealth creation.

Due to the footloose capital and the “efficient market hypothesis”, at the launch of QE measures over the past decade, huge quantum of funds were channelled to real estate, stock and bond markets in emerging economies and some developed economies that were less affected by the GFC.

Additionally, with the fungibility and velocity of money coupled with the dynamic power and influence of the “money-elite” over the past decade and the short-term memory arbitrage culture of high-frequency traders, governments have been unable to design good policies to filter and deter speculators without discouraging investment. This results in many economies facing “boom and bust” volatilities in their economies within a day.

Without the long-term memory mindset, the daily economic activities in the real economy will grind to a halt, as economic and commercial agreements will not be safeguarded. As evidenced in recent months, the reversal of QE measures has led to funds leaving the emerging economies and triggering an immediate risk of an exchange-rate crisis in national economies.

Indications of Market Failure?

There are strong indications of market failure in the emerging economies as a result of market distortions in prices created by the “money-elite” capitalising on arbitrage policy changes of QE measures.

These developments are leading to a bifurcation phenomenon in three ways:

- Widening of individual wealth distribution – in a single year (2017) alone, the fortunes of billionaires have grown by \$762 billion, that is more than [times](#) of resources to overcome global extreme poverty.
- Uneven corporate wealth distribution – the top 600 global companies control 80% of economic profit and the top 1% grabs 36% of the [pie](#).
- Increasingly, in the US, there is a [geographical bifurcation](#) where 10% counties contribute 90% of the GDP.

Unintended “Economic Superbug”

The long term stimulus (QEs and extreme low interest rates) have inadvertently created a [distorted perception](#) of risk and risk appetite. This has unintentionally

induced structural changes and vulnerabilities in the global economic “DNA” (free market principle).

One wonders if the decade-long QE measures, disruptive business models and technologies plus the bifurcation phenomenon have accelerated mutations in the global economic structure. Has this created an “economic superbug” in our global economy especially without any political and/or regulatory changes in the operating environment?

Finally, will this unintentionally-created “economic superbug” result in an untreatable condition (as in the case of antimicrobial resistance) for following global recessions? This means that the existing “drug protocol” (QEs and low interest rate) administered at the last GFC will no longer be effective. Hence the world urgently needs to develop [new economic tools/theories](#) to tackle future global crises.

Christopher H. Lim is a Senior Fellow in the Office of the Executive Deputy Chairman, S. Rajaratnam School of International Studies (RSIS), Nanyang Technological University (NTU), Singapore. Victor R Savage is a visiting Senior Fellow at RSIS.

Nanyang Technological University

Block S4, Level B3, 50 Nanyang Avenue, Singapore 639798
Tel: +65 6790 6982 | Fax: +65 6794 0617 | www.rsis.edu.sg