Finance leaders to address global economic threats

By MARTIN CRUTSINGER, AP Economics Writer – Oct 10, 2012

WASHINGTON (AP) — When global finance ministers meet this week in Tokyo, they'll confront a triple challenge: Economic troubles in three major regions are threatening the world's economy.

And political conflicts are complicating the problem.

Europe is gripped by a debt crisis and stalled growth. A budget standoff in the United States is set to trigger tax increases and spending cuts and perhaps a recession. A weaker Asia is slowing worldwide growth.

Mindful of those threats, the International Monetary Fund has turned gloomier about the global economy. And it's warning that even its dimmer outlook might prove too optimistic if Europe and the United States fail to resolve their crises.

Developed countries are facing a heightened risk of recession, and their troubles threaten China and other emerging economies, the IMF says in its updated World Economic Outlook.

No major solutions are expected to emerge from the Tokyo talks, which begin Thursday when finance ministers and central bank presidents from the seven wealthiest countries meet. They'll be followed Friday by the start of annual meetings of the 188-nation IMF and its sister lending group, the World Bank.

The leaders are expected to downplay any disagreements to avoid jolting financial markets. But they're also likely to warn nations that action is urgently needed to avoid a global disaster.

Their focus will be on Europe, whose financial crisis is entering its fourth year. It poses the gravest risk. European leaders have taken steps to defuse the panic over high government debts and weak banks. Even so, their economies are ailing. Six countries are in recession. More are expected to follow.

Political tensions in European nations over how much to cut spending and debt and how much to promote growth have complicated any solution. The IMF is expected to discuss whether to intensify its oversight of countries that have received IMF aid.

"The European situation is clearly the muddy water coming from upstream," said Sung Won Sohn, an economics professor at the Martin Smith School of Business at California State University. "It is hurting the global economy."

The finance leaders are also sure to warn that if the United States doesn't soon resolve its fiscal crisis, it could derail the fragile U.S. and global economic recoveries.

Here's a look at the threats from Europe, the United States and Asia that will command the attention this week of the Group of Seven wealthy industrial countries, the IMF and the World Bank:

— THE UNITED STATES

The U.S. economy is struggling. It grew at a puny 1.3 percent annual rate in the April-June quarter. The IMF expects it to expand 2.2 percent for all of 2012 and just 2.1 percent next year. The U.S. unemployment rate is a still-high 7.8 percent. Manufacturing remains sluggish. Workers' pay is trailing inflation.

And the U.S. economy remains at risk of dropping off a "fiscal cliff" when 2013 begins. Tax increases and deep spending cuts will take effect unless Congress breaks a budget impasse.

If those measures do take effect, most economists think the U.S. economy would topple into recession next year. The Congressional Budget Office estimates that the U.S. unemployment rate would rise to 9.1 percent by fall. It's now 7.8 percent.

Other nations worry about how a recession in the world's largest economy would ripple around the globe. And surveys of U.S. companies suggest that the fiscal cliff has made some reluctant to hire until the crisis is defused.

Congress will also need to raise the federal debt ceiling early next year. The last debt-ceiling standoff in 2011 was resolved at nearly the last minute, narrowly averting a first-ever default by the U.S. government.

"We will see the rest of the world expressing concerns about the threats if the United States doesn't get its act together and this failure destabilizes financial markets," said Eswar Prasad, an economics professor at Cornell and a former top IMF official.

Many investors appear to assume that Congress will resolve the budget dispute and raise the debt limit once it returns after the November elections for a "lame-duck" session.

In Tokyo, Treasury Secretary Timothy Geithner will likely assure his counterparts that the administration is intent on helping Congress strike a deal to avoid an economic catastrophe.

— EUROPE

As a whole, the alliance of 17 economies that use the euro will shrink 0.4 percent this year and grow just 0.2 percent next year, the IMF predicts.

Europe's economic slide has been deepened by its financial crisis. Countries such as Greece and Spain are suffering from high debts and weak banks. Greece, Ireland and Portugal have already needed bailouts.

Some relief has come from a pledge by the European Central Bank to buy unlimited amounts of government bonds to help lower borrowing costs for the most troubled nations.

Yet political differences are making a solution difficult. Proposals to shore up Europe's financial system — by authorizing the ECB to supervise banks and creating shared bank deposit insurance — have run into obstacles. Germany, for example, wants more time to finalize details before making the ECB the supervisor of banks.

The IMF warns that a failure to bolster Europe's banks and more tightly link its economies would further darken the outlook for the continent.

Spain has begun to unnerve investors by declining so far to ask for financial aid from the rest of the eurozone. That's a condition for receiving help from the ECB. The Spanish government fears the eurozone would force it to make further deep spending cuts. Spain's delay in seeking aid has caused its borrowing costs to creep up.

The most troubled European nations remain gripped by dismal economies. Unemployment in the eurozone as a whole is 11.4 percent. Greece, Spain, Italy, Cyprus, Malta and Portugal are in recession. Unemployment in Greece and Spain is around 25 percent.

— ASIA

China has been a potent economic engine for Asia and the world. But its annual growth fell to a three-year low of 7.6 percent in the quarter that ended in June. The IMF expects China's economy to grow 7.8 percent this year.

That's explosive by Western standards. But as recently as 2010, China's annual economic expansion topped 10 percent. The slowdown has hurt Chinese companies that depend on robust growth. The weakening of its export markets in Europe and the United States will likely delay China's rebound.

Japan's economy, the world's third biggest, is far worse off. The IMF expects the Japanese economy to grow just 2.2 percent this year and 1.2 percent in 2013 as construction related to its recovery from the 2011 earthquake slows. Japan's population is shrinking and aging. And its economy is facing high debts and stagnation.

For developing Asia-Pacific economies as a whole, the World Bank predicts 7.2 percent growth this year. India's cooling economy will grow 4.9 percent, Brazil's just 1.5 percent, the IMF predicts.

Friction between China and Japan over disputed islands in the East China Sea poses another threat to the region's growth. The antagonism and a wave of anti-Japanese riots in China have slashed demand for Japanese-brand cars and cooled a once-booming tourist trade between the two countries.

J.P. Morgan predicts that Japan's auto exports to China will plummet 70 percent during the October-December period. Exports of auto parts will tumble about 40 percent, as will exports of other consumer products such as electronics, J.P. Morgan estimates.

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