



Capitalism Freezes in Worldwide Winter of Discontent (Update2)

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By James G. Neuger

Jan. 12 (Bloomberg) -- As capitalism staggers through its first globalized economic crisis, the costs won't be measured only in dollars and cents.

From newly rich Russia to eternally impoverished sub-Saharan Africa, social strains are threatening the established political order, putting some countries' very survival at risk.

In the past month, Nigerian rebels threatened renewed warfare against foreign oil producers, Russia sent riot police from Moscow to quell an anti-tax protest in Siberia and China's communist leadership warned of social agitation as the 20th anniversary of the Tiananmen Square massacre looms.

The disillusionment and spillover effects of the global recession "are not only likely to spark existing conflicts in the world and fuel terrorism, but also jeopardize global security in general," says **Louis Michel**, 61, the **European Union's** development aid commissioner in Brussels.

Somewhere in the wreckage may lurk an unexpected test for U.S. President-elect **Barack Obama**, 47, one that upstages his international agenda just as Afghanistan's backwardness and radicalism led to the Sept. 11 attacks that defined the era of **George W. Bush** only eight months into his term.

Among the possible outcomes: instability in Pakistan, a more aggressive if economically stricken Iran, a collapsing Somalia, civil disorder in copper-dependent Zambia, a strengthened, drug-financed insurgency in Colombia and a more warlike North Korea.

Cascading Into a Crisis

The U.S. housing slump that began in 2007 has cascaded into a worldwide crisis that forced central bankers to cut interest rates to near zero to unlock credit markets, pushed governments to bail out their biggest banks amid a \$1 trillion of writedowns, and sent titans like **General Motors Corp.** and **American International Group Inc.** begging for bailouts.

The **World Bank reckons** trade will shrink for the first time in more than 25 years, deepening the economic hole for governments in developing nations, where higher food and fuel prices cost consumers an extra \$680 billion last year and pushed as many as 155 million people into poverty.

Nuclear-armed Pakistan, once touted by Bush as the key U.S. ally in the war on terror, sits at the nexus between economic insecurity and extremism.

"Blood and tears" may be Pakistan's fate, says **Thaksin Shinawatra**, 59, who as prime minister of Thailand fought rural poverty during a stormy five-year tenure until his ouster by a military coup in 2006. "That's where I'm worried, and also about political stability, and the terrorist activities are there," he said in an interview.

IMF Bailout

On Nov. 25, Pakistan clinched a \$7.6 billion **International Monetary Fund** bailout to avert a debt default amid ebbing growth and an **inflation** rate of 23 percent in December that is ruining the

livelihoods of its poor.

A day later, an Islamic terrorist group went on a rampage in Mumbai, India's financial hub, killing 164 people and adding a bloody new chapter to six decades of animosity on the subcontinent. India accused Pakistan of harboring the militants, much as the Taliban uses ungoverned Pakistani tribal regions as a launch pad for attacks on Afghanistan.

Neighboring Iran is among the energy-exporting states afflicted by the 74 percent drop in oil prices from last July's peak of \$147.27. The government, reliant on oil income for more than half the budget, may pare subsidies for utility bills, adding to the pain of October's 30 percent **inflation rate**.

Axis of Evil

Elections in June may determine whether Iran, part of **Bush's "axis of evil,"** presses ahead with its nuclear program -- or may change little regardless of outcome, says **Yousef al- Otaiba**, the United Arab Emirates' ambassador to the U.S. Whether or not President **Mahmoud Ahmadinejad** is re-elected, power will remain with **Ayatollah Ali Khamenei** and religious leaders.

"Whoever comes to office in June is going to be a different face of what I think is the same policy," al-Otaiba said in an interview.

On a global scale, the spiral of economic distress and political radicalism has been at work throughout history, from the bread riots that stoked the French Revolution to the mass unemployment that brought the Nazis to power in Germany. Some dictators, like Hitler and Stalin, turned on their neighbors after disposing of internal enemies. Others, like Mao, walled off their societies, condemning millions to misery.

The increasingly lopsided world economy "provides fertile ground for extremism and violence," French President **Nicolas Sarkozy** said at a conference last week in Paris. With globalization, he said, "we expected competition and abundance, and in the end we got scarcity, debt, speculation and dumping."

Extremism and Violence

Historians say it's too early to declare the end of the intertwining of the global economy, under way at least since the collapse of the Soviet bloc in 1989. For one thing, developed nations still have a huge stake in the system: Even with \$29 trillion wiped off the value of **global equity markets** last year, the **Dow Jones Industrial Average** is back where it was in 2003, hardly a time of privation.

As a result, disturbances in the West -- from Greece's worst riots since the 1970s, to a 31 percent increase in New Year's Eve **car torchings in France**, to a **pickup in shoplifting** at 84 percent of major U.S. retailers -- won't shake the foundations of those societies.

Failed and Failing

It's the failed or failing states that stand to lose the most. "The punch line: Poverty does cause violence," says Raymond Fisman, a professor at Columbia Business School in New York. Researchers led by Edward Miguel of the University of California have even quantified it: a 5 percent drop in national income in African countries increases the risk of civil conflict in the following year to 30 percent.

The frailest nations are those concentrated south of the Sahara desert, plagued by a legacy of despotism, corruption, disease and economic misfortune -- often all at once. The region accounts for seven of the top 10 countries in a ranking of "failed" states compiled by the **Fund for Peace**, a Washington- based research group.

With commodity prices sinking, cutting the **UBS Bloomberg Constant Maturity Commodity Index** by almost half in the past six months, mining companies including Anglo-American Plc, **De Beers**, **Lonmin Plc**, and **Xstrata Plc** are slashing jobs, adding to Africa's economic woes.

Nigeria, holder of Africa's biggest fossil-fuel reserves, is staring into a \$5 billion budget hole due to the oil-price swoon. It also confronts an emboldened guerrilla movement in the southern Niger Delta, the oil-producing region that has attracted the likes of **Royal Dutch Shell Plc** and **Chevron Corp**.

'Not Optimistic'

"The outlook is not optimistic," says **Pauline Baker**, president of the Fund for Peace, which ranks Nigeria 18th on the most-at-risk list. "Unless Nigeria begins to pull itself together, I think with the lowering oil price in particular it is quite vulnerable."

As incomes shrivel in the **poor world**, the economically troubled rich world isn't able to fill the gap. Even when the going was good, the Group of Eight industrial powers were struggling to meet a 2005 commitment to increase annual aid to poor countries by \$50 billion by 2010. Now, official donations are set to fall by as much as 30 percent, the **European Commission** predicts.

The IMF may need another \$150 billion to help reverse the damage to emerging markets, Managing Director **Dominique Strauss-Kahn** says. While "demand may be above what we have," Strauss-Kahn said in an interview that he is convinced the IMF could scrounge up the extra funds.

Putin's Role

Perched between advanced economies and the raw-materials exporters in the southern hemisphere is Russia, which used the eight-fold oil-price surge from 2002 to 2008 to reassert its claim to the great-power status that evaporated along with the Soviet empire.

Under President-turned-Prime Minister **Vladimir Putin**, that newfound clout became manifest in last year's invasion of neighboring Georgia and this month's shutdown of gas shipments to Europe. The tactics deflected domestic attention from the onset of the first recession since Russia's debt default in 1998. The ruble dropped 19 percent against the dollar in 2008, the steepest slide in nine years. Today, it fell to 31.0533 per dollar, the lowest level in almost six years.

Belligerency fueled by sudden wealth is likely to be inflamed by sudden scarcity, says **Harold James**, a history professor at Princeton University.

"Economic difficulties are always a spur to foreign political adventurism," James says. "In Russia, there's already a big devaluation, there's unrest in Siberia and other provincial cities. This is really where the destabilization is going to come from."

China's Course

As Russia clashes with its neighbors, China may be headed toward domestic repression. While **growth of 7.5 percent** as predicted by the **World Bank** will outstrip the industrial economies, the pace will be the **slowest** since 1990, the year after the army put down the Tiananmen pro-democracy uprising.

China's recipe for raising the standard of living has relied on **creating jobs** in coastal boomtowns like Shanghai as a magnet for millions of poor from the vast, rural interior. Now that formula is breaking down. More than 10 million migrant workers lost their jobs in the first 11 months of 2008, an unidentified Labor Ministry official told *Caijing Magazine* last month.

Using Communist Party code for riots and civil disorder, the state-controlled *Outlook Magazine* last week warned that a spike in "mass incidents" will test the government's ability to preserve the social peace.

Dissent Insurance

At stake is the endurance of the Chinese hybrid of an open economy and closed political system. During its two-decade rise that has **increased gross domestic product almost 10 times** to make China the world's fourth-largest economy and engine of global growth, a buoyant economy provided insurance against political dissent.

In a worst-case scenario, U.S. intelligence agencies warn, the communist leadership would roll back China's integration into the world economy.

"Although a protracted slump could pose a serious political threat, the regime would be tempted to deflect public criticism by blaming China's woes on foreign interference, stoking the more virulent and xenophobic forms of Chinese nationalism," the U.S. **National Intelligence Council** concluded in

November.

China has known outbursts of chauvinism in the past and remained intact, thanks to a social hierarchy dating back to the age of Confucius. Poorer countries lacking that political anchor face a bleaker outlook.

The crisis “could undermine the development momentum,” Liberian President **Ellen Johnson Sirleaf** said in an interview. “It would mean joblessness would increase, and that could undermine the stability of nations.”

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