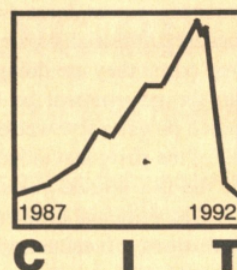


CENTRE FOR INCENTIVE TAXATION ECONOMIC INTELLIGENCE

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BLACK HOLE 1: THE WORLD ECONOMY

BLACK HOLES feature in this issue. The stories are to caution the investors who are fuelling the worldwide boom in the so-called "emerging market funds". Faced with low rates of interest on their money in the bank, punters are throwing their cash at these funds, which are supposed to invest in the high-growth sectors. Last year, US institutions alone poured \$9.7 billion net into emerging markets.

Analysts have now concluded that private investors have put at risk too high a proportion of their wealth. The implications for the global economy are serious: if the emerging markets now submerge, the wipe-out of wealth will further retard recovery in the old industrial economies. What are the prospects?

The world economy continues to consolidate the conditions for a depression that will last for at least another two years. The pathetic beacons of light here and there serve no purpose apart from buoying up the hopes of a few politicians. Reflect on the case of Japan, which had hoped to sell more cars in the booming Chinese market (page 2). It's not happening (for the reason why, see page 3).

THE BLACK HOLES in the numbers appear to preclude effective management of the kind that is supposed to enable policy-makers to plan the economy back to full employment.

◆ Start with the IMF. Despite working parties galore that have been ferreting away for nine years, the Washington, DC-based conscience of the world's financial systems still cannot figure out how Earth could have a deficit with itself. In theory, the current accounts of all countries should sum to zero. Yet according to the accounts, the world's deficit is \$119 billion.

If Earth's financiers cannot add up the statistics in the double-entry books, how can we be sure they even know the nature of the problem facing the world?

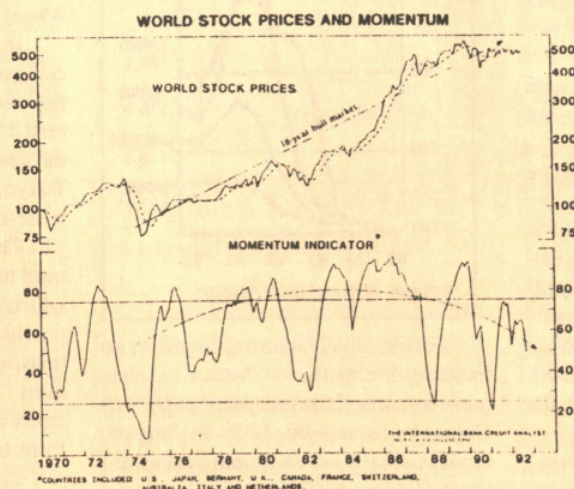
◆ Britain's Treasury has been formulating policy as if it knew where the economy was going - when it didn't. This year, the trade figures have been an unknown quantity. The figures for trade with other EEC countries have not been available because of an administrative change.

If there is no knowing what has been happening to the

country's trade balance, how can the government formulate a coherent strategy for industry?

◆ Then there is the stock market. Analysts declaim on the trends, as a way of whipping up trade. But how reliable are their forecasts? A year ago, the International Bank Credit Analyst (see their graph) warned: "End of an 18-year Bull Market?" Since then, stocks appear to have recovered in markets like the City of London. There have been few voices to warn (like a recent article in the *Financial Times*): "Peril of losing touch with the real world".

The problem, of course, is in not knowing the precise nature of the reality about which we are supposed to be cautious!



WHICH BRINGS US to the Blake Holes in theory. Economists fail to accord the appropriate weight to the signals that matter. Take housing. Economists believe that rising house prices signify recovery; yet such rises may reflect price trends in the land market that could be counterproductive. Japan, again, illustrates the point. For the UK story, see page 4.

Which brings us back to the IMF. Its managing director, Michel Camdessus, wants a uniform approach to policy. He told his 178 members on September 28 that they need "to refocus boldly" their policies. A

diversity of approaches apparently would not be tolerated by the financial markets.

But what if the single policy favoured by the influential IMF proved to be incorrect? That governments do not know what they are doing is authoritatively affirmed by Jean-Claude Paye, secretary general of the Organisation of Economic Cooperation and Development. He has drawn attention to "the apparent failure of the US and European models of economic life in sustaining growth and jobs" (*Financial Times*, October 1).

If all countries follow a single policy - the one favoured by the IMF, of course! - isn't it likely that we would all go down the same pan in a global depression, 1930s style? A dangerously deep hole is being dug, and the policy-makers do not even know it.