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EFFECT W IN THE WORLD ECONOMY?

During the months of June and July, the political events that took place in the United States significantly affected the world economy and shook the international structure of risk benchmarks.

Based on particular positions, political negotiations in the United States involving the budget vote to increase the government's debt limit exposed a lack of consensus and planning in the conduction of the world's largest economy

Along the same lines, the *modus operandi* of the world financial system, weakened by its own mistakes, began acting irrationally again, causing a feeling of panic in the market.

The present moment is not unprecedented in the history of the world economics. Just look back and remember what John Maynard Keynes, one of the most illustrious economists, said in one of the most difficult moments of the world's economic history:

"...the ideas of economists and political philosophers, both when they are right and when they are wrong, are more powerful than is commonly understood. Indeed, the world is ruled by little else. Practical men, who believe themselves to be quite exempt from any intellectual influence, are usually the slaves of some defunct economist".

Practical men. Sticking to this definition from Keynes point of view, to say that this profile of executive, particularly those who work in the financial world, when faced by an economic crisis sustain their arguments on ideas cultivated in academia. In practice, they don't assume their responsibilities.

Other practical men, such as those in risk rating agencies, take into account all sorts of variables in the calculations that result in ratings (also credit scores). However, the models do not entirely express the reality nor do they predict future events; they only infer probabilities of something that may occur.

In view of this paradox, is it fair to lower the United States' rating immediately after a lengthy and tiresome agreement for

President Obama? Furthermore, would these models that lowered the USA's rating be the same that rated the subprime mortgage securities as AAA quality?

Models aside, what needs to be taken into account are the economic interests behind a market bound to economic cycles, which risk rating agencies are responsible for classifying. This "bound" market I just referred to is the current financial market.

Composed of all sorts of speculation, the financial market has also become hostage to itself. In a more illustrative manner: this market is composed of transactions that produce nothing that's real.

Winning cycles and losing cycles in a capitalistic market are natural. What causes concern is the speed at which these cycles are occurring and the size of losses that small and medium sized companies in the real economy are suffering, since they are the weakest link in a capitalist society.

The unnecessary wear from the impasse between Republicans and Democrats in voting the budget and the growing debt of a relative number of European countries was the perfect combination to unleash a speculative process in the world's main stock exchanges.

From close up, the fear in markets hovered over the health of European and American banks after Royal Bank of Scotland (RBS) divulged a net loss of US\$2.34 billion in the first semester of 2011, the origin of which were losses with insurance and Greek securities.

The question raised the most by the market on Friday morning (August 5th) was how deep is the hole of banks? If concerns about bank results were not enough, in the afternoon of this same Friday, after the markets closed, Standard & Poor's lowered the risk rating of U.S. securities!

The event represented a direct shot to U.S. pride and the trigger for a strong drop in stock exchanges on Monday (August 8th), indicating the beginning of an economic adjustment known as: Effect W. But what is this so-called

Effect W? Simply put, I can define Effect W as a negative evolution, generally caused by drops in stock exchanges and GDP after a period of adjustment.

When a recovery period begins, without a defined period and then ends, the market returns to another negative phase and, eventually, to a positive phase. This is what an Effect W looks like: a down and up and down and up period. The signs of economic adjustment worldwide in the first two weeks of August can confirm the second downwards phase of Effect W.

But what are the consequences for Brazil? The greatest danger for the Brazilian market is in a drop in commodity prices, since two-thirds of Brazil's Bovespa exchange is composed of companies that in a certain way operate with some type of commodity. Likewise, the country may also be affected by a drop in international monetary flow, caused by reduced liquidity on the part of large American and European banks due to losses in their operations.

However, the biggest fear comes from the other side of the world, namely China. A recession in the Mandarin country could have a devastating effect on the trade balance, as well as cause commodity prices to plunge. It is also important to bear in mind that today's commodity prices are very close to the levels charged before the 2008/2009 crisis, due to Chinese demand.

Immune or not, Brazil has an arsenal that positions it ahead of the world's main countries considering a potential more intense international adjustment. In a certain way, effects of the shock caused in the first and second weeks of August will be seen during the next quarter, as will its amplitude, outlining a negative phase of, at least, 18 months.

The lessons learned from these latest events could be in the form of what "not to do". Despite its envious position, Brazil should take advantage of its armoring and do its homework in order to make the industrial and other sectors more dynamic and competitive. Now is the time! ■