3 Alarming Facts About China's Economy

Description

Concerns over the health of China's economy continue to mount as people fear that an ever-expanding debt bubble could be sufficient to trigger an economic hard landing that would have global consequences. Recent data from China indicates that the risk of an economic crisis is escalating rapidly with three indicators highlighting that the debt situation may be more dire than initially believed.

Now what?

Firstly, China's debt has ballooned to 250% of GDP.

In layman terms, this means its economy is up to its eyeballs in debt, which is threatening the sustainability of that growth. There are some economists who believe such an excessive volume of debt could be fatal for China's economy, eventually triggering an economic hard landing.

Billionaire investor George Soros has weighed in on the debate, claiming that China's debt-laden economy resembles that which existed in the U.S. leading up to the 2007 financial meltdown.

Secondly, China's debt is growing at a phenomenal rate.

According to research from the International Bank of Settlements, China's debt load is growing at a rate of 30% per annum. This incredible rate of growth has alarmed many economists.

Typically, economists become worried if debt grows at about 10% annually.

Of even greater concern is that China's debt is being directed to unproductive parts of the economy and is being used to prop up unprofitable state-owned businesses that would normally be closed down. This rapid growth in non-productive debt points to China's economic growth becoming increasingly unsustainable.

Finally, bad debts are rising at a rapid pace and are thought to be 10 times higher than what is reported.

International financial information agency Fitch Ratings recently reported that non-performing loans could be as high as 15-21% of all loans–roughly 10 times greater than the 1.8% reported by Beijing.

More worrying is that those bad debts could rise to be a third of GDP by 2018, placing considerable pressure on an already stretched financial system where Beijing continues to use debt as a lever to achieve targeted economic growth.

So what?

It is easy to see why there are mounting concerns over the health and sustainability of China's economy. What is more worrying is that China has become a systemically important economy for global growth, and any hard landing would create considerable fallout for a number of economies.

Among the hardest hit would those that are highly dependent on the extraction and export of commodities. China is the single largest market for the majority of commodities with the exception of crude.

This wouldn't be good news for miners such as **Teck Resources Ltd.** (TSX:TCK.B)(NYSE:TCK) or **First Quantum Minerals Ltd.** (TSX:FM). Both have enjoyed monster rallies and are up by 379% and 106%, respectively, for the year to date**,** and these rallies are predicated on the expectation of higher commodity prices in the future.

This certainly won't occur should China's economy falter.

It could also have a sharp impact on Canada's financial system; the fallout from a hard landing is one of the external shocks that could affect Canada's heavily indebted households. Canada's economic growth would slow further, causing unemployment to rise and household income to stagnate, placing pressure on the ability of households to meet their financial obligations. The end result would be an increase in non-performing loans with credit cards and consumer finance being the most vulnerable.

Of the major banks**, Bank of Nova Scotia** (TSX:BNS)(NYSE:BNS) would be among the most vulnerable because of its aggressive expansion into unsecured consumer lending in recent years. This would be magnified by its exposure to the commodity-dependent economies of Latin America.

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Author
mattdsmith