Chinese Economy Reels from Shock Of Global Financial Catastrophe

by Mary Burdman

The collapse of the world financial system hit the enormous Chinese economy like a shock wave in October. On Nov. 6, a senior official of the State Council, the national cabinet, told the *China Daily* that the nation must take "comprehensive and radical measures." The wake-up call for him, the official said, was the rapid contraction of electricity usage, where the rate is now negative. Over 70% of China's electricity is used by industry, especially heavy industry such as steel. The official said that the electricity supply growth rate collapsed from 5.1% in August to 3.6% in September; but he was most "shocked by the October growth rate, which is below zero, which means more closures, bankruptcies and job cuts.... We have entered into a hard time," he said. "Without radical remedies, it will become even harder."

In fact, this was an understatement. Without a new world monetary system as Lyndon LaRouche has proposed, China is facing destruction of genocidal proportions. Many industries are being hurt, the official, said. He was not named, but *China Daily* reported that he is "close to the nation's highest decision-makers." "Major economic gauges indicate that we have entered into an excessive economic slowdown and need a radical stimulus package right now," the official said. Only three to four months ago, the Chinese government was most concerned about economic "overheating"; now, the danger is the opposite. He reported that in China's steel and iron industry, at least 30% of firms have already *stopped production*, and this is hitting other industries.

The government is putting together a program for massive investment in railways, ports, and energy infrastructure, and increasing treasury bonds to finance them, for the annual Central Economic Working Conference in late November. But, if LaRouche's proposals—bankruptcy reorganization of the whole system, breaking the control of the "globalized" Anglo-Dutch financial empire, and restoring national sovereignty over national economies—are not carried out, China will not be able to make the urgent strategic shift away from its dangerous dependence upon processing and exporting low-cost consumer goods, and toward building a national economy which can meet the present and future needs of its 1.3 billion people.

Underpricing Kills

President Hu Jintao emphasized that China wants to make this economic shift, when he spoke to government leaders from Asia and Europe, in Beijing Oct. 24 at the Asia-Europe Meeting summit. "The global financial crisis has clearly increased the uncertainties and unstable factors in the Chinese economy's development," Hu said. With its 1.3 billion population, "China's sound economic growth is, in itself, a major contribution to global financial stability and economic growth. That is why we must first and foremost run our own affairs well."

The greatest problem, as LaRouche has repeatedly said in discussions with Chinese policymakers, is that the export sector has actually been *an enormous cost* to the Chinese economy. "Chinese" exports are, in reality, hardly Chinese: Foreign-invested companies produced almost 60% of China's exports last year, and almost 90% of high-tech exports. As leading Chinese economists know, these operations use up Chinese transport infrastructure, energy, water, and other resources—all at the costs of China's own industries. But the greatest cost, as LaRouche emphasizes, is that China's workforce is producing at prices far *below* what is needed to meet the population's needs—now, or in the future.

This year is the 30th anniversary of the inauguration of China's reform and opening up policy. Despite the enormous changes in China since 1978, this policy has ultimately only worsened the gap between China's urban, industrial economy and the huge rural sector—where 700 million people live. A special report just issued by the State Council in September, showed that although rural incomes rose last year by the highest percentage in two decades, the gap between the urban and rural economy was at its greatest since 1978. The most serious gulf between what are, in fact, two separate economies, is not so much in incomes, as in the education, medical care, and welfare available to the people.

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Millions of migrant workers in China have seen their jobs vanish, as industrial and agricultural production shuts down; these two unemployed men wait for handouts in Yantai, Shandong province.

The crisis hitting the export sector will make the situation much worse. Millions of migrant laborers from the countryside work in these factories, and send funds back to their families.

China's other vulnerability is its foreign-exchange reserves, the biggest in the world, which hit a record $1.91 trillion by end-September, up almost 33% over a year. These huge reserves are the result of its trade surplus with the U.S. and other Western nations, and the notion, prevalent among Asian nations since 1997-98, that monetary reserves could offer protection to national currencies from speculators and currency flight. The problem is that the dollar is now the currency of the Anglo-Dutch financial empire, and is being shredded by the mega-bailout operation. While China's banking system is, to some degree, protected, because it never abandoned currency and foreign exchange controls, only LaRouche's policy, to restore U.S. national sovereignty over the dollar, can prevent the hyperinflationary evaporation of China's huge dollar holdings.

Globalization Backfires

China is going to see worse to come, Prime Minister Wen Jiabao wrote. The nation "must be aware that this year would be the worst in recent times for our economic development," Wen wrote in an article published Nov. 1 in *Qiushi* [*Seeking Truth*], the leading theoretical journal of the Communist Party of China. "Against the current international financial and economic turmoil, we must give even greater priority to maintaining our country's steady, and relatively fast economic development," which will be hard, because of the "unfavorable changes" in the international economy. Wen warned that "it is very difficult to maintain high growth and a low inflation rate in the long run.... The [global economic] situation is worsening," and the negative impact of the volatile international market on the Chinese economy will become more obvious as the days go by. "We must be crystal-clear that without a certain pace of economic growth, there will be difficulties with employment, fiscal revenues, and social development ... and factors damaging social stability will grow." Inflation is another threat—one taken seriously in China, which was hit by uncontrollable hyperinflation in the last years before the Chiang Kai-shek government collapsed in 1947.

At this point, globalization is backfiring, *China*

Daily acknowledged in a commentary published Oct. 6. International freight costs have shot up over 30% already, and rising materials costs are eliminating whatever "advantages" there had been for producers to use cheap labor and infrastructure in China and other nations. The globalizers will have no choice but to return "international manufacturing industries to the developed countries and their neighbors"—if they keep manufacturing at all.

While many Chinese reports focus on the growth rate of exports to the U.S. and Europe—already down by 5-6% to around 10% this year—that is not the real story. The 6% rise of the Chinese yuan this year alone means that half the reported growth in export value—reported in dollars—is due only to the currency rates. The actual volume of U.S.-China bilateral trade fell 3.1% outright in the first eight months of the year, the *International Herald Tribune* reported Oct. 15.

The crunch in textile and other low-cost export industries began early in 2008; now, hundreds of toy and textile firms are closing down every week. The National Development Commission reports that more than 10,000 textile firms have collapsed so far this year, and two-thirds have had to restructure, such as by shifting from cotton to cheaper synthetic fibers. One result is that, at the beginning of November, half the Autumn harvest of China's largest cotton-growing region in Xinjiang, which produces about one-third of China's cotton, was left unsold. From August to October, the cotton price crashed from 13,700 yuan to just 2,000 yuan a ton. Not only the regular farmers, but impoverished migrant workers, are hurt—millions of them find seasonal jobs picking cotton in Xinjiang, and as production shrinks, those jobs will vanish.

The growth rate of textile exports to the U.S. and the EU was already down by almost 20% in September, from a year earlier, the General Administration of Customs reported. In August, when exports are usually highest, they actually fell outright by 0.95%. Investment growth is also shrinking. Chinese textile producers operate on very thin profit margins, and cannot survive a shrinking market. Already, several hundred shoe producers have shut down just in the city of Dongguan, Guangdong, a center of the export industry, as orders fell by 30-40%, and production costs soared by over 20%. Last year, China exported 73% of the world's shoes. Thousands of workers are being locked out of bankrupt factories.

On Oct. 13, the Customs reported that half of China's toy exporters have shut down this year. These were mostly smaller producers, who produced less than $100,000 worth a year. Export growth rate was just barely over 1%, which is 22% lower than a year ago.

Crisis in Steel

"More than 60%" of China's steel producers "are in the red, and many small steelmakers are facing closure," China Iron and Steel Association (CISA) vice-chairman Luo Bingsheng announced at a national meeting in Beijing on Oct. 31. The situation has deteriorated very fast. Prices for steel products have crashed by up to 60%, according to steel industry sources, *China Daily* reported, while exports are dropping. In the first nine months of this year, exports were 390 million tons, down by 11.6%. "Exports may be halved in October and the sharp decline will continue until March, as the global financial crisis worsens," Luo Bingsheng warned.

Chinese steel production had more than doubled in the past five years, rising from 180 million tons in 2005 to 489 million tons in 2007, and China shifted from being the world's biggest steel importer to its biggest exporter, exporting about 12.5% of its production in 2007. But, as the chairman of Baosteel, one of China's biggest producers, told a recent steel conference: "We have come to the turning point." The shrinking demand for steel, due to cutbacks in housing construction and car sales in China, forced steel prices down 40-50% just in October. Baosteel Group has already cut production 20% and other producers are cutting 30% or more. It is the smaller, private steel mills which are being hit hardest.

One result is that the production cuts have left a record 89-million-ton stockpile of iron ore at China's big ports. Peter Kraemer, CEO of Marine Services Group, one of Germany"s leading shipping companies, told *Junge Welt* in an interview published Oct. 29, that China, a leading raw material importer, has not imported a single ton of iron ore in the past four weeks.

China's shipbuilding industry—another big steel consumer—is also in trouble, *China Daily* reported Oct. 27. China has some 3,000 shipyards, and has become the second-biggest shipbuilder after South Korea. The China International Capital Corporation Limited recently reported that the number of new ship orders worldwide dropped 66% year-on-year in September, and Chinese yards were hit with a 34% drop in

Edward Burtynsky Manufacturing #6A

The global financial shutdown has closed hundreds of shoe factories in China, which last year exported 73% of the world's shoes. Thousands of workers are now being locked out of bankrupt factories. Shown, a shoe factory in Wenzhou, Zhejiang Province, 2004.

new orders in the first nine months of this year. Guangzhou Shipyard International Company Limited received orders for only five new ships in the first half of 2008, compared with 24 in 2007.

The next question is, what will happen to the ships already ordered? The shipping industry worldwide had ordered 600 million deadweight tons of shipping, to be completed over the next three years. China alone has about 200 million deadweight tons on its order books, and new, smaller private firms will be especially vulnerable to the trade crash.

Auto, power, and other industries are also reporting big production cuts and profit contractions. Chinese auto producers, as opposed to affiliates of foreign producers—will have to be "consolidated" beginning next year, as slower sales and rising costs hit, an official of the National Development and Reform Commission (NDRC) said Oct. 16. "Some weak brands and less competitive players will start to be pushed out next year," Cheng Xiaodong said. The process is already underway. China produces over 50 different cars, most low-cost. There will be pressure on the bigger producers, such as Dongfeng Motor Group Co., to buy the smaller ones out, but that will be a big drain on the Chinese companies. Chery Automobile Co. Ltd., the fourth-largest, and a fully Chinese company, announced Nov. 2 it was planning layoffs of as many as 30% of interns and provisional workers.

The power sector has suffered the most, as coal costs soared. Losses of the country's top five power companies were 21.4 billion yuan ($3.14 billion) in the first nine months, while the profits at China's two biggest power grids plunged 80.9% from a year ago. Even the China Yangtze Power Co. Ltd., which operates the famous Three Gorges hydroelectric dam, had to announce that its net profit was down almost 15% from a year ago. The petrochemical sector saw profits plunge by 81.1% in the same time. The China Petroleum & Chemical Corp. (Sinopec), Asia's biggest oil refiner, reported a 67% fall in net profit so far in 2008, despite government subsidies, because of high crude oil prices.

'Catalyst of Development'

Beijing is already moving to expand development of infrastructure, to attempt to stop the industrial shutdown. In mid-October, the State Council approved 2 trillion yuan ($292 billion) for the construction of a series of railway projects. "Increasing investment in fixed assets has remained a catalyst of China's economic development," *China Daily* wrote Oct. 25. The day before, Ministry of Railways spokesman Wang Yongping said that, "New rail investment will become a shining light in efforts to push forward economic growth."

Senior government policy advisor Zheng Xinli told *China Daily* that, "In 1997, we dealt with the Asian financial crisis by stimulating domestic economic growth by investing in the construction of highways. This time the money will go on improving the rail network."

These programs are urgently needed, but can only work if other nations, especially the U.S., Russia, and India, join in building the international "Land-Bridge" proposed under LaRouche's New Bretton Woods.