Q & A:
WILL CHINA'S SLOWING ECONOMY BE THE TRIGGER EVENT FOR THE NEXT GLOBAL ECONOMIC CRISIS?

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In recent months, fears of China stumbling into an economic crisis have been increasing. Questions about economic volatility, export performance, social tensions, and single-party control are again on the forefront. Could we be witnessing the beginning of a China economic crisis that can cause the next global economic crisis?

It is true that China has entered a period of uncertainty caused by factors mainly connected to the "contradictions" of its economic model, if we wish to recall for a moment Mao's thoughts. Although, overall, the Chinese economy appears resilient, key essentials have begun to feel the pressure. Recent estimates speak of a general economic slowdown, with the Chinese communist government reacting with announced intentions to support domestic demand and increase public investment. There are phenomena that indeed should worry Chinese officials a lot: problems with the Yuan, a sharp decrease in exports, weakening manufacturing industry, a retreat in real estate prices, the failure of a rising number of companies to meet their financial obligations, and evidence that the Chinese economic model remains still immature in comparison to those of China's big competitors. On the other hand though, we need to remember that a Chinese economic crash has been consistently predicted over the last twenty years but has never materialized.

It is true that the Chinese government has been astute in negotiating its economic course. Yet, the question of how long such a political-economic game can survive appears more pertinent today than ever before. Should the Chinese government begin to change tack and, if yes, how can this shift be managed?

I think that this is -- or, at least, should be -- the focal point of current China estimates. Chinese debt is increasing rapidly and, already, many global observers point out that such expansion is dangerous and could trigger a major crisis imminently. Examples from Europe are mentioned in relation to Chinese debt developments and the Chinese government appears to pay attention. Speculative funding is very much at the root of this particular “sub-crisis” and we have already seen what disasters such a model can create on short notice. China may have benefited from the US subprime crisis but appears to have paid insufficient attention to **how** this disaster actually unfolded. The *Financial Times* newspaper recently highlighted, for example, the many Chinese “shadow banking products” which could easily shatter Chinese confidence in a supposedly well regulated system. Most observers today agree that the Chinese government must pay close attention to the mechanics of a developing credit bubble, based on a shadow banking system, whose collapse won’t be pleasant. Seen from the angle of the many bearish analysts, China’s $8.2 trillion economy has the potential to fuel a global meltdown at any moment. It is time, therefore, for the Chinese government to face some difficult decisions.

What are some of these difficult decisions?

The time for the Chinese government to proceed with a thorough re-evaluation of its economic strategy, first launched in the late 1970s, has arrived. We should not forget that half the Chinese population (and that’s **a lot of people** in a country of 1.35 billion) does not partake in the feast fuelled by the super-modern urban class and remains caught in under-development. While consumption has risen to unprecedented levels for the urban classes, half the country has little to show for after thirty years of breakneck growth. Senior Chinese politicians must also address the lurking “monster issue” of a huge government apparatus, with its many compartmentalized fiefdoms, which creates bottlenecks and has a direct -- and not always positive -- impact on the country’s domestic **and** foreign policy. Catching up with methods and ways and means common among the world’s leading powers will be a herculean effort which, however, the Chinese government can ignore only at its own detriment. Such reform, if implemented correctly, will eventually balance the economy between consumption at home and dependence of exports only to the long-term benefit of all Chinese.

It appears then that accurate forecasting of Chinese developments is more complicated than most think. A reasonable expectation, it appears, is that this level of uncertainty may eventually generate its own, independent dynamic of events that the Chinese government won’t be able to control, leading to a “flash fire” crisis with international ramifications.

Indeed, this the current fear among many China observers concerned with individual sectors of Chinese society and economy. The size of China alone, and its rise as a top exporter in the world, makes **any** Chinese development capable of worldwide impact. And we still don’t know details of key aspects of the Chinese economy as, for example, the exact origins of domestic lending and the size of bad loans already in the books, which can destabilize the economy at any moment. Here, the presence of communist tenets in Chinese thinking complicates things beyond a point seen as “manageable” by Western observers. Who can tell today what might be the reaction of the Chinese (communist) government to a “Western-style” credit crunch and the need to impose regulatory steps that will conflict with established bureaucratic enclaves more akin to the defunct Soviet Union? We have been used to seeing quick government reaction to issues of “law and order” but this experience may be misleading in future cases of conflict developing between central government and often powerful regional officials who are experts of skimming and padding their own bank accounts with profits from corruption. It is obvious, therefore, that **any** hard landing in China will push the world onto a road we hate to contemplate -- and vigilance from the West won’t be enough to contain the damage given the West’s existing problems and continuing under-performance between global crises.