Posted on: December 7, 2015

China's Global Impact

Tags: investment planning [1]

The August correction in the Chinese stock market led to a lot of "how terrible" news coverage and speculation as to whether or not this signaled the end of the China growth story and how it would impact the US and global economies.

Calmer voices were more resolute in the midst of the chaos, proclaiming that the Chinese stock market correction was a local event and would not contaminate the rest of the global economy. Case in point, trade from the US to China only accounts for about 15% of US GDP[1] and a slowdown in this trade would hardly be felt within the rest of the U.S. economy.

So what impact does a slowing Chinese economy have for investors and how will this be reflected in client portfolios? The impact for clients will vary for each individual.

Consider the following. Recent events most likely mean the end of China’s economic model of export-led and investment driven growth. As economist Richard Duncan notes, there is no one left to export more to every year and China finds itself with extraordinary excess capacity across every industry. Product prices are falling, companies are unprofitable and bank loans in China are going bad; moreover, China is also buying much less raw materials from the rest of the world. As a result, commodity prices have collapsed. In October, China’s imports fell 20%[2] from same month in the previous year. Thus, China is no longer a driver of global growth as it was coming out of the Great Recession of 2008-09.

Secondly, China would like to devalue their currency, the yuan, against the US Dollar in an effort to boost China’s exports and economic growth. However, China already has a trade surplus with the U.S. last year of $340 billion[3], which means that further exports to the U.S. would see the Yuan appreciate against the Dollar, hurt future Chinese exports and lead to further economic slowdown.

The U.S. worries that further Yuan weakness will hinder the competitiveness of U.S. exporters relative to Chinese exporters. In addition, since the U.S. buys approximately $500 billion worth of goods[4] from China yearly, the declining Yuan would influence export deflation, thereby defeating the U.S. government’s efforts to create inflation of 2% or more per annum[5] as a way to stimulate and grow the U.S. economy and reduce the outstanding U.S. government debt. The above scenario would also include the debt issued as part of the Quantitative Easing, following the 2008 crisis program, to prevent a U.S. collapse into another 1930’s style Depression.

Finally, China does not want the Dollar to strengthen any further relative to the Euro and the Yen. According to Duncan’s notes, the Yuan is tied closely to the US Dollar, so when the USD strengthens against the Euro and the Yen so does the Chinese Yuan. A stronger Yuan hurts exports to Europe and Japan; therefore, China does not want the Federal Reserve to increase interest rates because higher U.S. interest rates would cause the USD and the Yuan to appreciate together and further hurt Chinese economic growth.

The coming months will determine if the Chinese move to further devalue the Yuan and possibly trigger a currency war, of which the impact will be felt globally on all asset classes.

Call us today for a review of your investment strategy in light of these recent developments.

[1] US Census Statistics, [2,3,4] Richard Duncan, Economist (www.richardduncaneconomics.com [2]) [5] US Federal Reserve

Do you have questions about your financial strategies?

[Contact our office today !](https://kevinbrewerfinancial.com/contact-us) **[3]**

Source URL:https://kevinbrewerfinancial.com/e-newsletter/2015/2015-12/article-1.htm

Links
[1] https://kevinbrewerfinancial.com/taxonomy/term/19 [2] http://www.richardduncaneconomics.com [3] https://kevinbrewerfinancial.com/contact-us