

## Economic Views for Investors

by Roger Nightingale

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Lies, damned lies, and economics statistics!

In the last eighteen months, while economics activity in most of the rest of the world has crashed into recession, that in China is reported merely to have moderated. Conditions in North America, Western Europe and Japan are currently desperate – the worst since the early thirties. But, in the PRC, they seem still to be highly satisfactory – growth running in the first quarter of 2009 at 6% per annum!

Are the Chinese still flying? Or do they just want us to believe they are?

Is that figure credible? Not really. The *numbers* add up, but the *logic* doesn't. The proposition, for instance, that domestic demand picked up just as export sales started to fall away is a little hard to swallow. It's rather more likely that workers, newly anxious about job security, would have cut their consumption. And it's probable also that companies, noting the slower throughput and duller profits, would have reduced investment programmes.

Forensic economists are unimpressed

What, moreover, is the economist to make of the imports data? How likely is it that tastes for foreign goods would have been severely depressed when general appetites were reasonably robust? Could the higher personal consumption have been restricted to domestically produced goods? Did the surge in industrial production require no extra raw materials? Hmph.

Too much wishful thinking. Shades of the Met!

Official data are error-prone – sometimes accidentally, sometimes deliberately. If the authorities let it be known that they'd like certain phenomena to be illustrated, it's quite often the case that they are. Britain's crime figures tend magically to conform to official targets. So do school examination results and hospital waiting lists. Perhaps similar pressures manifested themselves in China in relation to economics reports in the last nine months.

How weak might things be genuinely?

Exactly how strange are China's numbers? Not outrageously. But, if developments had conformed to "normal" patterns, if personal and company spending had been "ordinarily" subdued, the effect on GDP would have been quite sizeable. In the first quarter of 2009, it would have grown by just 4% in comparison with the equivalent period of the previous year; and it would have contracted at an annual rate of 3% in comparison with the prior quarter!

Will the truth out?

Might we see some revisions, therefore, in the months that lie ahead? Possibly. It all depends on the behaviour of the world economy. If it should revive strongly, China will soon follow suit and the "errors" relating to early 2009 will be buried forever. But if the global slump should continue, that'll not be possible: the pretence of resilience will not be sustainable.

It depends largely on economies elsewhere

So is there any prospect of near term regeneration? Many commentators seem to think there is. Obama is cautiously optimistic about the US economy and Bernanke not wholly gloomy. Additionally, a number of European Commissioners are said also to have spotted early signs of recovery in their countries. For investors, investment bankers in particular, the most telling development is the rising equity market.

Are there any green shoots?

The story is not particularly convincing, though. There is confusion, some of it deliberate, between conditions that are improving and those that are deteriorating less quickly. And there is comparable ambiguity about asset valuations on the one hand and economics progress on the other. But what worries most economists is the outlook for the labour market. Many fret that, in the remainder of 2009, there will be huge swathes of redundancies—amounting, in some countries, to 5% of the existing workforce. What price then an uptick in personal psychology, and a revival in consumer spending?

Probably not

Corporate profits are likely to carry on rising, though. Margins will soar by up to 5% immediately and possibly continue to expand thereafter. Why? Because, under the impact of higher unemployment, pay settlements will moderate. If the picture were to be similar to that in the thirties, margins would rise so

No time to be an incumbent politician!

Banks will be embarrassingly large winners. Borrowing cheaply and lending extortionately, their profits will be almost uncontainable. Competition will have been suppressed: Governments having been duped into winking at cartels and encouraging exploitation.

The reckoning will be swift and final

But voters will be furious. It'll be maintained that Governments misjudged the situation. They helped the wrong people. It'll be all right perhaps if by then the economy is back on an even keel. But if activity is still depressed, unemployment still high, there'll be no mercy. Rightly so. *Sic semper fatuis.*

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