

Take two Prozac before reading this

Written by Barthélemy Barbancourt
Monday, 29 June 2009 15:32 -

I'll start with the ending so people can get a flavor of what I'm seeing financially.

*[If the world's biggest surplus state \(\\$400bn\)](#) is too structurally deformed to help offset the demand shock as Western debtors retrench, **we are trapped in a long deflation slump.***

Now for the facts:

China's banks are veering out of control. The half-reformed economy of the People's Republic cannot absorb the \$1,000bn (£600bn) blitz of new lending issued since December.

"Future losses on stimulus could turn out to be larger than expected, and it is unclear what share the central and/or local governments ultimately will be willing or able to bear."

*Note the phrase "able to bear". Fitch's "macro-prudential risk" indicator for China threatens to jump from category 1 (safe) to category 3 (Iceland, et al). This is a surprise to me but Michael Pettis from Beijing University says **China's public debt may be as high as 50pc-70pc of GDP when "correctly counted"**.*

The regime is so hellbent on meeting its growth target of 8pc that it has given banks an implicit guarantee for what Fitch calls a "massive lending spree".

Bank exposure to corporate debt has reached \$4,200bn. It is rising at a 30pc rate, even as profits contract at a 35pc rate.

China's Banking Regulatory Commission fired a warning shot last week. "The top priority at the moment is to stop explosive lending. Banks should carefully monitor the process of credit approval and allocation, and make sure that loans flow into the real economy," it said.

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Unfortunately, 40pc of the "real economy" consists of exports, mostly to the US and Europe, the consequence of a mercantilist export model that has qcrashed and burned. Chinese exports were down 26pc in May.

So what happens when Obama goes begging for an extra \$2 trillion and China is selling their bonds? The bond rates for the USA rates go up as the risk increases that we will default on our debts. Eventually, no one will be willing to buy our bonds and the BO admin will be forced to both raise taxes (deepening the recession) and cut government spending which will push unemployment into the mid-teens.

Obama's admin is already done, they just don't know it.