Anatomy of a New Market High

7-03-14

On Tuesday markets hit new record highs reportedly in on a rise in Chinese manufacturing. It climbed all the way up to 51.0 from 50.8. It has been making a slow climb from negative territory for the past several months. This good news means that China is also on track to achieve its planned growth for 2014 of 7.5%. That would be slightly less than the 7.7% growth for 2013, and the worst annual growth rate since 1990. So what we really have here is a gigantic negative development (the worst growth rate in 34 years) being taken out of historical context in order to be transformed into a gigantic stock market positive.

China has had to devote more attention to the home environment once the world economy collapsed. Besides infrastructure improvements, housing development has been heavily supported. This has created a major bubble with prices going through the roof, much like conditions in Japan just before its economy collapsed in 1989. To prevent a repetition in China the state apparatus has attempted to rein in the construction industry - raising bank capital requirements, restraining off-bank financial transactions, etc. It worked only too well. Home sales were down 10.2% the first five months of this year over the same period last year. Price increases have largely stalled or dropped, but so has the economy as a whole. Many firms are on the financial ropes. GDP growth in the first quarter was 7.4%. So now the new Chinese capitalist state must follow the same procedure as other capitalist states by reversing the process to re-stimulate the economy. Loan requirements weakened, bank capital holdings reduced and budgeted infrastructure improvements fast-tracked. There has also been a 54% increase in private bond sales over the last three months to increase available liquidity. Each measure can be visualized as a step on a tightrope, the state being the balancing rod the economy requires in order to keep from falling into the abyss.

Bloomberg provided an interesting side story to Chinese state preparations should the abyss arrive despite all efforts. Chinese parents have been spending up to $16,000 to get their children enrolled in the now miss-named Peoples Liberation Army. Not that long ago new inductees in the PLA received income on the order of $35 a month. Now new recruits receive up to $4000 a month. Quite a jump from the average workers' monthly wage of $656 (Forbes - 2012). Twenty five years ago there was a workers rebellion against harmful conditions created by the new market economy (the earlier student phase posed no threat to party rule and policies). Following the Beijing suppression there were uprisings in over 80 cities over a two month period. At times the reliability of the PLA in suppressing the upheavals was demonstrated by worker-soldiers refusing to subdue people they identified with. Thus the necessity of creating a professional middle class mercenary army that will serve its creators rather than the Chinese people; in short, the same sort of armed forces that exists in the developed West.

Also on Tuesday the Institute of Supply Management reported a slight drop in American manufacturing in June from May. It's worth knowing how little factual material is behind this all-important privately assembled report. The ISM simply asks its members to report on five categories of industrial activity. The most important is orders; some others are inventory and delivery. The reports merely state if they are higher, the same, or worse. No actual figures are provided. The report for orders was 30% saying it was better (for the previous two months is was 35% and 37%). 55% said it was the same (previous two months 51%). 15% said it was worse (up from 14% and 12%). Then they use some formula to come up with 57.5 (down from 60.5 and 62.5). So this most import of the 5 elements seems to have worsened. But after running it through a seasonal adjustment it comes to 58.9 - almost two units higher than the previous month. The point here is that the whole magnificent process is just plain crap.

Recently the Bank of International Settlements warned central banks that they had better think of raising interest rates before the bubble bursts. Recently resigned Federal Reserve governor Jeremy has made similar statements. The mere mentioning of such things scares Yellen of the Fed, so she has had to declare once again that there is nothing to be concerned about. The Fed has been cutting back on bond purchases, but much of that liquidity injection has been replaced by corporations and other financial entities borrowing at low interest rates to buy equities and bonds (including a great deal of junk). Corporations alone have been purchasing their own stock at the rate of about $70 billion a month. Those near zero rates act as the machine that pumps the air into the ever-inflating bubble.

Finally, today the Bureau of Labor Statistics reported a gigantic increase in June jobs of 288,000. It also reported that the number of involuntary part-timers increased by 275,000 over the same period. Enrollment in Affordable Health Care for 2014 closed the end of March. April's jobs number was 304,000 and they have been high the following months. It's been reported that many persons have cut their hours or gone part time to keep their income low enough to qualify for subsidies. Might this figure into the high employment numbers?

http://www.unrealeconomy.org