Bad Year Beginning

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The Caixin/Markit factory PMI fell to 48.2 in November for the tenth consecutive decline. On Monday the CSI 300 declined 5% prompting 15 minutes of silence, then continued to -7% triggering an official shutdown. Meanwhile the US ISM PMI for November also fell to 48.2, lowest since 2009, and that along with a Commerce Department report of a 0.4% decline in construction (biggest drop since June 2014) led to a significant fall in American indexes. The worldwide slump then manifested itself in Brazil where economists polled by its central bank predicted a - 2.95 decline following a projected - 3.71 decline for 2015. Brazil's last back to back recessions were in 1930-31. The expected twin recessions for 2015-16 will be much deeper than their last experience, or any other dating back to 1901 when reliable data began.

Later it was revealed that the Chinese government purchased stock in an effort to halt what amounted to a $590 billion stock value loss (about $280 billion in the US). Following last year's $5 trillion loss the government not only purchased an estimated $238 billion of equities but banned large stockholders from selling stock for 6 months. That was ending on January 8th and the government announced its extension. Other state banks have similar policies. They are supposed to build investor confidence by showing that the state has their back, but at the same time it's a double-edged sword in that an emergency intervention is itself a serious scare. But governments trust in the essential greed of the committed investor. When a child puts a tooth under a pillow, he or she knows that it didn't really come from the Easter bunny. But governments can pull strings in plain sight while maintaining the fiction that it's not them but the growing strength of the real economy that caused a stock surge -- and it works because real money tops the real economy.

Wednesday was a repeat of Monday. The CSI 300 lost 5% the first half hour soon after passing 7% closing the market. The Shanghai Composite produced a close copy and the world markets followed suit. The supposed reason was the government weakening the yuan for the 8th day in a row. Perhaps a report in Caixin magazine contributed -- The total volume of goods transported on the national rail system fell 10.5% from the previous year (3.4 billion tons). Last year it dropped 4.7%. The real economy speaks -- the yuan listens.

Brent crude fell to $35 a barrel -- an 11 year low. Crude overall is down to $32.

According to the WSJ, as of Thursday the nation's markets have experienced the worst new year opening ever. But there is still one day left in the week and strings are quietly being pulled for a better tomorrow. The Chinese government finally figured out that doing mechanical fixes out in the open makes things worse. So it dumped its market circuit breaker program and let things fall where they may. Of course, it just *happened* to raise the value of the yuan today after lowering it the previous eight, and no doubt it's purchasing stock by the handful as an improvisation of demand will also help. If lowering the value of the yuan was done to improve exports and help the overall economy, then raising the value will harm the overall economy while helping middle class speculators make easy money. The Chinese ruling class has built whole cities of expensive apartment buildings and amenities for the middle class because it needs them as a supporting buffer when the working class goes on a rampage.

David Stockman has his own little hedge fund business going. That means doing his best to expose the most excessively valued companies. His big objects of scorn are FANG - Facebook, Amazon, Netflix, Google. Recently he did a job on Amazon, a company that ended the year with a market cap of $325 billion after starting the year at $145 billion. He then lists last twelve month figures: $100 billion sales, $32.6 gross profit, operating expenses like $5 billion for sales and marketing, also some on the operating cash flow went like $7 billion for capital expenses, and finally ending with $2.8 billion free cash flow. That results in PE ratio between free cash flow and market cap of 117X. Last year it was 62X. In 2011 it was 40X. Here we see that its value is rising much faster than freely available cash to do things like pay a dividend (something that Amazon has never done). It's a good example of a bubble stock. Should it run into difficulties it would quickly have to cut spending, borrow, or perhaps sell something off. While Amazon has gotten into other things -- rocketry, cloud computing, Kindle, streaming, other companies are more suited to dominate in those areas. It's mainly a giant online retailer with only that to rely on in the last instance. But Stockman's criticism can just as well be turned into praise. Sure, 25 years is a long time for Amazon to keep working on expansion and market share, but the reason why Japan was able to do so well so fast after WW2 was because they stubbornly stuck with gaining market share while their competitors were too much in a hurry for profit. But the ultimate goal is always the same - profit, and Amazon investors have made huge 'profits' without the company (recall that under capitalism it's just one person) making any. Had investors listened to scaremongers when they began predicting daily crashes years ago. , they would have missed many profitable opportunities. Moreover it is impossible to predict *when* capitalism crashes because it is an irrational system, one can only predict that it *will* crash because it *is* an irrational system. The market economy is the basis for that irrationality -- goods and services are produced for sale with need only being the means to a profitable end. Sales are an undefined abstraction that exist profitably even with nothing to sell. Needs and even wants in a non market economy have a definite point of conclusion either when satisfied or impossible to obtain. When the irrational selling of a market economy reaches the rational conclusion of a real economy, it brings down the system that was foolish enough to allow its dominance.

In an earlier article I reported that an important category in the CPI is what homeowners living in their homes guess they would be paying if they had to rent. No doubt greatly exaggerated to express pride in equity and the solidity of a home. Well, it also adds a surprising amount of 'equity' to the GDP -- all of $1.37 trillion in 2014. The GDP in 2014 was $17.4 trillion. That means this ridiculous concoction is working its way toward 10% of the GDP. Of course, the homes themselves are also in the GDP. Imagine the boost for the economy if they could only teach their pets to calculate what they would have to pay for dog and cat rent.

Even with the usual gigantic (and bogus) jobs report of 292,000 the markets dived for the final day of the week. It's official -- the worst opening week of a new year ever for American markets.

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