Samso

17:06 10 Jun 2019

Is the commodity market just getting used to a slowing Chinese Panda?

Is the commodity market depressed or is it just not used to the China Panda taking a long time to chew through the bamboo stalks? Whenever the markets get a whacking, the general public is hoping for a quick recovery. This reaction is natural, but seasoned investors will tell you that this never happens.

The recovery is always longer than you expect and usually is more depressing than you wish. Interestingly, this is the same, whether you are talking about property or the equity markets.

Over the last decade, the commodity boom has been primarily being driven by the growth of China. China has come from a farmyard economy to a world juggernaut in just 30 years. I was in China a few years ago and an associate (Chinese migrant with Australian residence for 20 years) was telling us that several years ago when he came home to China, he used to take his relatives and friends out for dinner.

Now it is the other way around, and the return of favour was magnitudes of difference. The wealth creation in China over that time has been tremendous and even surprised those closer to home.

Now that China is undergoing a slowdown and Trump is doubling the misery, the world is confused. Should we buy more? Should we produce more? Should we invest more?

These are the puzzles that are causing heartburn for the rest of the world.

I wonder if all the confusion on the market is just the general commodity market getting used to something new after so many years of the same prosperity.

The Chinese economy

Source: Trading Economics

The Chinese economy advanced 6.4% year-on-year in the March quarter of 2019, the same pace as in the previous quarter but slightly above market expectations of a 6.3% expansion. Industrial output growth accelerated markedly, and consumer demand strengthened amid government's pro-growth policies, which helped stabilise sentiments rattled by the trade dispute with the US.

Share Information

Code:	SAMSO
Listing:	PRIVATE-AU
Sector:	**Investments and investor services**
Website:	**samso.com.au**

Company Synopsis:

Samso provides bespoke research and presentation for clients to engage their customers or investors. Bespoke research is useful for clients who require a two-way flow of communication with their customer/investor base by utilising a social media strategy. Organic content allows audiences to feel a real sense of sincerity when you share your business strategy.

action@proactiveinvestors.com.au

Figure 1: China GDP since 1990. (Source: Trading Economics).

On a quarter-on-quarter basis, the economy grew 1.4% in the first quarter, compared to a 1.5% expansion in the previous period and matching market estimates. It was the weakest quarterly growth rate since the first quarter of 2016. GDP Annual Growth Rate in China averaged 9.52% from 1989 until 2019, reaching an all-time high of 15.40% in the first quarter of 1993 and a record low of 3.80% in the fourth quarter of 1990.

Over inflated GDP figures

In March 2019, I read an article in Bloomberg, which talked about how China had been over-reporting its GDP between 2008 and 2016.

Figure 2: China GDP discrepancy between 2008 and 2016 (source: Bloomberg).

As you can see in Figure 1, the GDP range is much like a roller coaster ride. Over time, there have been numerous reports on this issue, and many debates have argued if this was a conspiracy or an act of jealousy.

According to Bloomberg, one of the significant culprits could be the over inflation of growth by local governments. The provincial government authorities would want to be seen to be achieving economic growth goals to improve their chances of promotion. These are times before President Xi, where brown paper bags and inaccurate reporting were the things to do. Local government authorities had absolute power to approve and influence economic development.

Photo by Chastagner Thierry on Unsplash.

As President Xi started to exert his authority, fear has been brought over the system and 'more accurate' figures are appearing. To the shock of the western economist, these figures started to send shock waves through the market.

What was a reality?

It was around 2015 when I started getting involved with China investments, and that gave me a first-hand look at how private industry do things in China. There was no shortage of money, especially with the younger generation. Ferraris, Lamborghinis and Bentleys were standard features of associates. What else was apparent was over capacity: elaborate factories not fully occupied and the typical industries that were showcased to create a mirage of prosperity. I saw several factories, car parts, shoes, clothing, plastic manufacturing and furniture, to give some examples. The one common feature was the overcapacity.

Photo by Chastagner Thierry on Unsplash.

Many buildings looked like there was nothing in them. And some of the buildings had 25% occupancy. Apart from that, things were just 'normal'.

Friends and associates in China were telling me of a retail downturn, and even the food and beverage sector was not doing well. The tightening of elaborate 'entertaining' killed off 'entertaining' cities. Excessive dining was non-existent practically overnight. My associates in smaller cities in Malaysia were telling me that the Chinese company officers would be too scared even to be associated with these expensive dishes. That was how hard the crackdown was on excessive expenditures by government officials.

Is the commodity price just reacting to World economics?

To blame the fluctuating commodity pricing solely on the China market would be simplistic. In January 2016, almost every commodity was at its lowest, but Crude oil joined the depressed pricing late in 2014. That period was the first time that I can remember where every valuable commodity was at its lowest. During that first quarter of 2016, the markets rebounded, and there was optimism for the next phase for the resource sector.

In our new world of debt, corporations servicing the rapidly growing mountain of debt has proved a great deal more expensive than expected. Corporates have been forced to sell their commodities at increasingly deflated prices (and continue to do so). What many assumed were exceedingly good borrowing terms have proved to be anything but, once the cost of exchange rates are taken into account.

The slowdown in Chinese economic growth is, in no small degree, the result of problems in the banking industry. In 2016, the issues of non-performing loans were rising at no more than 1-2% a year, according to official statistics. During that period, the actual growth rate in non-performing loans is probably more like 5-10%.

The shadow banking story has been a problem since 2016, and there were reports of the second and third level financial institution not having enough money to repay depositors. The problem in the financial sector has exacerbated domestic slowdown, which will, in turn, create a roll of depressed pricing.

The One Belt and One Road issue

What is a debt financing tool is now slowly biting back with non-repayments and the building of white elephants? Many projects were built on this debt facility all over the world. This was going to be the instrument that would help China get its growth back on track.

However, reports are indicating a lack of real growth and economies are being left with white elephant projects. Ports that are built, but there is no infrastructure to support the development. One of the most significant infrastructure projects in Kazakhstan is now in limbo. China invested over $14 billion in Kazakhstan as the gateway to the new Silk Road. There is a great article titled, Kazakhstan - The Broken Buckle in the Belt and Road, which talked about this particular issue.

On the other hand, projects in Indonesia are booming. Large state-owned enterprises were implementing the One Belt One Road song, and dance and all is happening. Factories and cement plants are popping up everywhere. However, the locals are telling me that they are not performing well, and local employees are being laid off or had wages cut to keep overheads down to show profits.

Conclusion

The slowdown in the world economy is the real blame for the commodity price sentiments. The China story is just part of the equation but I think commodity pricing has just got too comfortable with a rising Chinese economy. The European market is not a happening thing and the US revival is coming to a close.

If you take into account that the China GDP was really not that high and the numbers were not that big, then you would assume that the buoyant pricing had to do with other factors. Now that the pricing is heading south, you would have to apply the same relevance to the other non-China factors.

One can blame the slowdown in the world economy to the instruments of debt funding that has created a circle of death. The same geniuses that created all the tools that blew up Wall Street during the Financial Crises are still doing their magic.

The recent demise of Gascoyne Resources, Dacian Gold and all the Eastern Goldfields companies are most likely to have been driven by the same financial models that were created to justify investments during the Ninja (No Income, No Job, No Asset) Loans period of madness.

The same instruments are hurting corporations and driving the volatility of commodity prices. I am no economist but I am convinced that a combination of these hybrid alternative investment products that are the root cause of the direction of commodity pricing.

One would argue that if investing groups were to make decisions on the factual repayable model, there would be a more stable movement in pricing. This ability would lead to more reliable forecast on pricing movement and future pricing levels.

www.samso.com.au

samso

business development, investment & lifestyle

Samso is primarily a consulting company that delivers digital information to the market in terms of creating organic content.

Samso simplifies your story to customers or investors. **Samso** creates organic content for you to engage your audience and BRAND yourself to them.

Samso provides bespoke research and presentation for clients to engage their customers or investors.

Organic content allows audiences to feel a real sense of sincerity when you share your business strategy, allowing your business to stand out among the sea of social media traffic.

Working with Proactive Investors allows exposing our Insights to over 1.2 million monthly unique views internationally.

Samso has nearly 30 years of experience in developing business ideas and concepts in the Australasian region.

Samso has worked primarily in the mineral resources industry, capital markets and corporate finance. Noel Ong is the founder of **Samso**.

Proactive Investors facilitate the largest global investor network across 4 continents in 4 languages. With a team of analysts journalists & professional investors Proactive produce independent coverage on 1000's of companies across every sector for private investors, private client brokers, fund managers and international investor communities.

Contact us +61 (0)2 9280 0700 action@proactiveinvestors.com.au

No investment advice

The Company is a publisher. You understand and agree that no content published on the Site constitutes a recommendation that any particular security, portfolio of securities, transaction, or investment strategy is suitable or advisable for any specific person. You understand that the Content on the Site is provided for information purposes only, and none of the information contained on the Site constitutes an offer, solicitation or recommendation to buy or sell a security. You understand that the Company receives either monetary or securities compensation for our services. We stand to benefit from any volume which any Content on the Site may generate.

You further understand that none of the information providers or their affiliates will advise you personally concerning the nature, potential, advisability, value, suitability or profitability of any particular security, portfolio of securities, transaction, investment, investment strategy, or other matter.

You understand that the Site may contain opinions from time to time with regard to securities mentioned in other products, including Company-related products, and that those opinions may be different from those obtained by using another product related to the Company. You understand and agree that contributors may write about securities in which they or their firms have a position, and that they may trade such securities for their own account. In cases where the position is held at the time of publication and such position is known to the Company, appropriate disclosure is made. However, you understand and agree that at the time of any transaction that you make, one or more contributors may have a position in the securities written about. You understand that price and other data is supplied by sources believed to be reliable, that the calculations herein are made using such data, and that neither such data nor such calculations are guaranteed by these sources, the Company, the information providers or any other person or entity, and may not be complete or accurate.

From time to time, reference may be made in our marketing materials to prior articles and opinions we have published. These references may be selective, may reference only a portion of an article or recommendation, and are likely not to be current. As markets change continuously, previously published information and data may not be current and should not be relied upon.

The Site does not, and is not intended to, provide investment, tax, accounting, legal or insurance advice, and is not and should not be construed as providing any of the foregoing. You should consult an attorney or other relevant professional regarding your specific legal, tax, investment or other needs as tailored to your specific situation.