World’s two biggest economies show recessionary trends

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Economic developments in the US and China, the world’s number one and two economies respectively, point to recessionary trends in the global economy as a whole.

The latest data from the US released last Friday show a decline in the labour market while price numbers from China on Monday indicate that deflation is starting to become entrenched.

Chinese industrial producer prices fell by 1.8 percent, year on year, in August in the largest decline in four months, largely as a result of falling prices for steel. This compared with a decline of 0.8 percent in July and exceeded expectations of a drop of 1.4 percent.

The consumer price index rose by 0.6 percent year on year, slightly above 0.5 percent in July but below market expectations of a 0.7 percent rise, according to the National Bureau of Statistics.

As far as analysis of the direction of the economy is concerned, the main focus is not consumer price index but the GDP deflator which seeks to measure the growth of the economy after prices changes across the board are taken into account.

It has been negative for the past five quarters, giving rise to concerns that China is entering a deflationary spiral. If it extends into next year, as appears likely, that would amount to the longest period of deflation since data were first collected in 1993.

The deflationary trend has led to further calls for action by the government to stimulate the economy which so far it has been resisting, fearing this will only add to debt problems.

Commenting on the latest numbers, Robin Xing, chief China economist at Morgan Stanley, said: “We are definitely in deflation and probably the second stage of deflation.”

By this he meant that deflationary forces starting in one area of the economy spread more broadly, leading to falling wages and a decline in consumption spending.

“Experience from Japan suggests that the longer deflation drags on the more stimulus China will eventually need to break the debt-deflation challenge,” Xing said.

There is evidence of spreading deflation. Bloomberg reported that even in sectors of the economy which have been supported by the government as part of its drive to develop new “high quality productive forces”—such as electric vehicles and green technology—entry level wages have declined by almost 10 percent from their peak in 2022.

Chinese government officials have sought to prevent discussion of deflation and have told analysts not to use the term. But cracks are opening in the political establishment as the situation becomes more serious.

Speaking at the Bund Summit, an annual economic conference in Shanghai last Friday, the former governor of the People’s Bank of China, Yi Gang, directly addressed the issue.

The state-backed media outlet Caijing reported that he told the conference that policy makers they should loosen monetary policy and support the real economy.

He called for “proactive fiscal policy and accommodative monetary policy” and that officials “should focus on fighting deflationary pressure” with the aim of bringing the GDP deflator back into positive territory.

Apart from the ongoing slide in the housing and property market, which has been a mainstay of the Chinese economy for around a decade and a half, there are many other indicators of the slowdown in the economy.

The steel industry is one of them. Last month, the

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chief executive of one of the largest steel conglomerates warned of a "long winter" for the industry because of overcapacity that has reduced profitability. A recent survey, the results of which were reported in the *Australian Financial Review*, suggested that only 1 percent of Chinese steel mills were operating profitably.

Steel production in China dropped 6 percent in July compared to a year earlier with forecasts that it could fall further.

The price of iron ore, the export of which is crucial for Australia and Brazil in particular, has been falling, reaching $90 a tonne on Monday, its lowest level since November 2022.

The price of copper, regarded as a bellwether for the global industrial economy, has also fallen in recent months.

Another warning signal, reported on by the *Financial Times* (FT) is the fall in demand in office space. It said that offices in some of China's largest cities were emptier than they were during COVID lockdowns. At least a fifth of high-end office space in Shenzhen, a centre of high-tech, was vacant in June.

According to Lucia Leung, a research analyst at the global real estate firm Knight Frank: "The biggest challenge is still the significant reduction in market demand due to the weakening of China's growth expectations."

There is now considerable doubt that the official target for growth of 5 percent will be met with major global banks cutting back their estimates for growth this year and next.

The economic situation in the US presents itself very differently but the same underlying trends are present.

Much attention has been focused on the US labour market in recent days in the search for clues as to the size of the expected cut in interest rates by the US Federal Reserve when it meets later this month.

The labour market report issued last Friday showed that 142,000 jobs were created in August, well below forecasts of 160,000. But in some ways even more significant was the revising down of the July number from 114,000 to 89,000. This followed the downgrading of the number of jobs created in the year to March by 818,000.

It has been noted that such downward revisions most often occur when the economy is starting to move into recession.

Other data showed that the number of US job openings in July fell to its lowest level in more than three years and has been falling steadily since reaching a peak in 2022 and declining by 13 percent over the past year.

There are signs of financial turbulence as well amid speculation about the size of the Fed's interest rate cuts. On Friday, Wall Street closed down after having had its worst week in more than a year, before rising again this week. But the gyrations are signs of a worsening economic outlook. High tech stocks, which have led the market up, have been the hit with the tech-heavy NASDAQ index dropping 5.8 percent last week.

The AI chipmaker Nvidia, which has had led the tech frenzy, lost 14 percent in market value. The decline of $406 billion in market value was the largest weekly drop by a single company ever recorded, according to Dow Jones Market Data.

The FT reported that last week US companies issued a record amount of debt as they sought to bolster their cash holdings to counter economic and financial turbulence.

An official at Bank of America told the newspaper the reason for the high debt issuance was an "effort to de-risk ahead of potential economic risks out there, including upcoming economic data reports, the Fed's decision on interest rates, the election and ongoing geopolitical risk."

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