WHERE DOES ONE GO TO FIND HONEY ?

Just 12 days ago (September 6), The **P**eople's **B**ank of **C**hina (**PBC**) (), the Central Bank of the People's Republic of China (PRC), lowered by 0.50 percentage points, the deposit-reserve requirement ratio of financial institutions with regard to the renminbi, loan-interest rate.

The reason for this move was, in the words of The People's Bank of China:

> *'… to maintain adequate liquidity in the banking system and guide the stable and reasonable growth of money and credit. Meanwhile, in order to enhance the capacity of financial institutions to support the agricultural sector, rural area and the farmers, and the small and micro-enterprises, the deposit reserve requirement ratio will be cut by an additional 0.5 percentage points for the county-level rural commercial banks, rural cooperative banks, rural credit cooperatives, and township and village banks; the deposit reserve requirement ratio of financial leasing companies and auto finance companies will be cut by an additional 3 percentage points to support its role in boosting consumption.'*

It was only 22 days ago, on August 25, that The People's Bank of China announced:

> *'The PBC has decided to cut RMB benchmark loan and deposit interest rates for financial institutions as of August 26, 2015 to further reduce the financing cost of the corporate sector. The one-year RMB benchmark loan interest rate and deposit interest rate will both be lowered by 0.25 percentage points, to 4.6 percent and 1.75 percent, respectively. Adjustments are made correspondingly to benchmark interest rates on deposits and loans of other maturities, and to deposit and loan interest rates on personal housing provident fund. Furthermore, the upper limit of the floating range of the interest rate of time deposit with a maturity of more than one year is lifted while the upper limit of the floating range of the interest rate of time deposit with a maturity of less than one year and that of demand deposit remain unchanged.'*

In spite of these moves by The People's Bank of China and many others by various branches of the Government of the PRC, the key indices of the PRC's two equity markets have continued to fall and, last Monday, some of these indices fell rather dramatically.

The key index of The Shenzhen Stock Exchange, known as The Component Index, shed about 6.55 percent, falling to 9,778.23 points, last Monday, while, on The Shanghai Stock Exchange, its key index, The Shanghai Composite Index, gave up 2.67 percent of its value, ending the trading day at 3,114.80 points.

With regard to The Shanghai Composite Index, it has lost the best part of 40 percent of its value since the middle of June, this year.

As for The Shenzhen Component Index, in the month of August, it fell about 22.73 percent from its highest level, during the month.

According to unconfirmed reports, investors of the PRC are deeply concerned that they have not been told the entire truth about the fundamentals of the second-largest economy of the world.

Further, many investors do not fully understand the reason that the key indices of their equity markets have been going at full speed in reverse gear since June: The indices, investors had been led to believe, should be reaching for higher and ever-higher ground, many investors surmised as the norm for PRC equity markets.

Chinese investors, today, however, are indicating their discontent as to their lot in various ways, dumping stocks and shares on the PRC's two equity markets – while there are, still, buyers, they claim – being just one way.

According to data, recently compiled by the statistically division of The People's Bank of China:

> *'As of April 22, 2015, a total of 2,020 listed companies (those that just went public in 2015 were excluded) released their annual reports, accounting for 77.3 percent of all public companies. Among them, 147 listed companies suffered losses, representing 7.3 percent of the companies that had already released their annual reports. To be specific, 125 went into losses for the first time, while the remaining 22 reported continued losses. The loss-generating firms were mainly from the chemical raw material and chemical manufacturing industry, the computer, communication and other electronic equipment manufacturing industry, the electric machinery and equipment manufacturing industry and the real estate sector. The first two industries were also the ones in which many enterprises reported losses in 2013.*
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> *'In 2014, affected by the overlapping of growth slowdown, structural adjustments, and the economy digesting legacy impact of the previous stimulus policies, the overall profitability of listed companies weakened to some extent, while operations in some sectors were under rather big pressure. As the structural adjustments of the Chinese economy gradually deepens, the performances of a few listed companies will likely further deteriorate. Therefore, attention should be paid to their delisting risk.'*

Thus, it is clear that The People's Bank of China, for some time, had more than an inkling that things were not all beer and skittles in the PRC.

On The Tokyo Stock Exchange, last Monday, its Nikkei-225 Index lost about 1.60 percent of its value, ending the day at 17,965.70 points.

On The Stock Exchange of Hongkong Ltd, its key index, The Hang Seng Index, ended the trading day at 26,512.63 points, a gain of 0.352 of a point, compared with the previous Friday's closing level.

And so it went on, the key indices of one equity market after another, losing traction as investors ran for cover, mostly out of fear of the unknown.

In The United States of America, last Monday, investors turned their attention away from the growth (or the lack of acceptable growth) of the economy of the PRC to this Thursday's Open Market Committee Meeting of The Federal Reserve (The Fed, as it is commonly called, being the de facto Central Bank of the US).

In respect of this Thursday's meeting of The Fed, the question to be answered is whether or not interest rates of the largest economy of the world should be permitted to rise.

The Fed is holding all the cards in this regard.

<u>So: How Are Things Shaping Up In the Middle Kingdom?</u>

Motor-vehicle sales in the PRC, proper, being separate and distinct from the Hongkong Special Administrative Region (HKSAR) of the PRC, fell by 5.30 percent in the month of June, Month-On-Month, to 1.80 million, units.

June’s statistic represented the smallest number of motor-vehicle sales since February, this year.

June’s sales of motor vehicles in the PRC were, also, lower by about 2.30 percent, compared with the like month of 2014.

The China Association of Automobile Manufacturers (), as a direct consequence of the above, confirmed vehicle sales for the month of June, has lowered its prediction of motor-vehicle sales for the entire year, from seven percent to three percent, Year-On-Year.

Mr Dong Yang (), Secretary-General of The China Association of Automobile Manufacturers, has gone on record, stating that the falling levels of motor-vehicle sales in the PRC are due, among other things, to the sagging economy and the situation on the country’s equity markets.

Mr Dong Yang is reported to have stated:

> *‘I don’t think the Chinese market has become saturated. Car ownership per 1,000 people in China is still far lower than in developed countries like the US. And, in many smaller cities and towns, motorcycles and electric tricycles are playing the role of cars.’*

For many of the 1.30 billion, human population of the PRC, owning a motor car is a dream, but it is a dream unfulfilled and, as the situation stands today, possibly a rapidly fading dream.

In April, this year, a large number of PRC, motor-vehicle manufacturers as well as distributers of foreign, motor-vehicle imports, offered substantial discounts to prospective customers, throughout the country.

But to no avail: Buyers were as plentiful as hens’ teeth.

Sales of passenger, motor cars in June were about 1.51 million units in June, a fall of about 6.10 percent, Year-On-Year.

As for domestically produced, passenger motor-cars, their numbers fell by about 5.30 percent, Year-On-Year.

Not since December of 2008 had there been such a fall-off of both sales and production of motor cars in the country.

Loans Rise

By July 31, 2015, loans, afforded to bank customers and denominated in renminbi, rose 15.50 percent, Year-On-Year, to 90.27 trillion renminbi.

That was an increase of about 2.10 percent, compared with the June statistic, according to official, PRC Government data.

Outstanding renminbi loans and foreign-currency loans totalled 96 trillion renminbi, up 14.40 percent, Year-On-Year.

Household loans grew by 275.20 billion renminbi, with short-term loans, falling by about 3.60 billion renminbi, whereas medium-and-long-term loans increased by 278.90 billion renminbi.

Of note, it appeared that, in the month of July, foreign-currency deposits fell by $US41.10 billion while renminbi deposits rose by 2.17 trillion renminbi.

The outstanding amounts of renminbi and foreign-currency deposits was 137.92 trillion renminbi, representing an increase, Year-On-Year, of about 12.90 percent.

With renminbi deposits, having increased in the month of July by 2.17 trillion renminbi, it was noted that this was 3.14 trillion renminbi more than the growth of such deposits in the like period of 2014.

Bank loans have continued to rise in the PRC and, with these increases, questions may soon be asked as to how debt-service and capital repayment will be met by borrowers.

Many PRC investors, who had been in the habit of trading in stocks and shares, employing borrowed money to finance their purchases of equities, known in the parlance as '*margin purchases*', today, are quite likely to be in a bit of bind.

When trading was decidedly bullish on PRC equity markets, investors licked their lips at the '*paper*' profits that they were amassing.

But those profits, today, have mostly disappeared and Chinese investors, who employed margin financing in their dealings on PRC equity markets, must, surely, be facing very difficult times.

Many, if not most, PRC stockbroker companies did not, adequately – if at all – confirm many of their customers' ability to meet their financial commitments when trading in stocks and shares.

This was especially true when a stockbroker house accepted buy/sell orders on behalf of customers, the funds for such transactions, often being met from the coffers of the stock broker house – margin financing.

And so, today, many a stockbroker company could well be under threat if a sufficient number of their margin customers default on their financial obligations.

All this does not bode well for the immediate-and-intermediate future of the PRC's two equity markets since it is almost a guarantee that there will be a material influx of scrip for sale on the country's equity markets at '*market*' – because the beneficial holders of that scrip are desperate to raise money in order to meet their obligations to their lenders.

Conclusion

Things are likely to get much worse on the PRC equity markets long before they get better.

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