New American

Written by **Bob Adelmann** on October 5, 2015
Published in the October 5, 2015 issue of the New American magazine. Vol. 31, No. 19

Inside Track

Chinese Economy, Stock Market Continue to Crater

News that China has offloaded more than $100 billion of U.S. Treasuries in August to support its currency and its cratering stock market caused many observers to raise concerns about China waging an "economic war" against the United States. It's a threat the Chinese last expressed during the 2012 presidential election, that Beijing would "use its financial weapon to teach the U.S. a lesson" if it insisted on flouting Chinese interests, i.e., by selling arms to Taiwan, for example.

It now appears that the shoe is on the other foot. The Asian tiger is now a pussycat, as its economy continues to crater and the Chinese central bank moves to weaken its currency and shore up its stock markets.

In the days following Beijing's surprise announcement on August 11 that it was devaluing its currency by two percent, the yield on the U.S. 10-year Treasury note jumped 10 percent, from 2.00 percent to 2.20 percent. Since then it has remained quiescent, forcing financial analysts to explain why.

First, the foreign exchange market is huge almost beyond comprehension: Nearly $7 trillion is awash among the world's central banks. A mere $100 billion in that vast ocean is scarcely noticeable, representing a tiny percentage of daily transactions.

Second, Japan is likely to be only too willing to offset China's sales as the country's Prime Minister Shinzō Abe has been, as Bloomberg's William Pesek noted, "as compliant a Japanese partner as Washington has encountered in decades," willingly doing Obama's bidding (such as facilitating the relocation of U.S. military bases and passing secrecy laws). If China's sales are ever perceived to threaten the U.S. Treasury market, a simple phone call from the president to Abe would likely remove it.

In addition, China is not interested in shutting down the economy of its largest trading partner, as a sharp rise in interest rates surely would. Its rickety economy needs every trading partner it has to continue to buy its goods, not preclude them from doing so.

Fourth, the yield on the U.S. 10-year Treasury note is far higher than that of Germany's (at 0.66 percent) or Japan's (at 0.35 percent). Where else would investors seeking safety of principal along with yield go to protect their capital?

Besides, a drop in the value of U.S. Treasuries would impact China as well, which continues to hold more than $1.3 trillion in U.S. debt.

Since Keynesian economists run the Chinese economy, just as they do in the United States — and believe that government money manipulation can enhance the economy — however, there nevertheless is the chance they might just trigger a slowdown that could turn into an avalanche. If the Chinese economy doesn't begin to show signs of recovery soon, more interventions such as forcing brokerages to support the markets further with government monies, guarantees, and promises would require the sale of American dollars in vast amounts.

Further devaluations of the yuan (it is currently still overvalued by 15 percent, according to Sue Trinh, the senior currency strategist for the Royal Bank of Canada) would certainly draw retaliations from other Asian countries, forcing them to devalue their own currencies. As Tyler Durden of ZeroHedge expressed it, something would have to give:

All of these dynamics (i.e., a Fed rate hike, China's massive U. S. Treasury dumping, an emerging market meltdown precipitating foreign exchange reserve drawdowns …) simply cannot coexist for long without something snapping….

In this very unstable [environment], the smallest policy error will reverberate exponentially.

Investors and interested observers could do worse than to watch the yield on the 10-year U.S. Treasury Note here to see if the market remains quiescent. For the time being, China is highly motivated to make only small corrections and keep any threats to teach the United States a lesson to themselves.

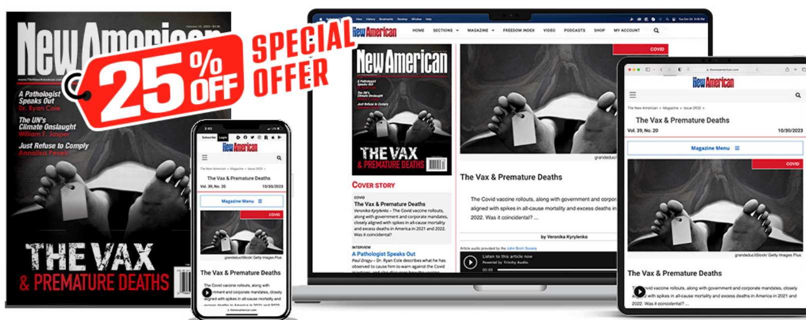
Picture of Beijing, China: ahenobarbus

Subscribe to the New American

Get exclusive digital access to the most informative,
non-partisan truthful news source for patriotic Americans!

Discover a refreshing blend of time-honored values, principles and insightful perspectives within the pages of "The New American" magazine. Delve into a world where tradition is the foundation, and exploration knows no bounds.

From politics and finance to foreign affairs, environment, culture, and technology, we bring you an unparalleled array of topics that matter most.



Subscribe

What's Included?

24 Issues Per Year
Optional Print Edition
Digital Edition Access
Exclusive Subscriber Content
Audio provided for all articles
Unlimited access to past issues
Coming Soon! Ad FREE
60-Day money back guarantee!
Cancel anytime.