

China and stagflation. What if they now infect us with this?

At the beginning of the summer we saw the world reborn. The vaccines had instilled in us an unequalled optimism, nothing gave sign that it was not over. After a virus that came from the East, but not like the Three Wise Men, although we coincide at the time of year, and a storm with a comic book name that had not been able to kill us, came end of summer floods like every year and all accompanied by a volcano eruption. What else could happen? We were not sufficiently aware that China would once again leave our problems in the background. After COVID, China and its communist regime may give us a terrible inflationary problem, who the only guilty (and we should recognize it) for it are Westerners for having consented to being Chinese-dependent. A Tsunami caused by the bursting of a real estate bubble that accounts for 18% of their GDP, creating a financial crisis: one, bad Chinese gas planning generating a disproportionate rise in electricity prices in Europe and two, a communist intervention of the market generating an export deficit. What can this all bring us?



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We are seeing news these days that are difficult to understand as we were in a world that seemed to be clearly expanding and emerging from a deep crisis caused by the COVID pandemic.

It is no longer that electricity is expensive in Europe, it is that we constantly read news about blackouts in China and unintentionally, we link them together, but the situation is so different in both places that it seems impossible that it will have similar consequences. But this is not going to end everything, the withdrawals of monetary stimuli by the central banks, something apparently unrelated to all this, forms the perfect triumvirate for the red dragon with the cursed name to appear: *stagflation*.

"In the mid-1960s an English minister coined one of the cursed terms in economics, stagflation: inflation without growth."

China is experiencing constant blackouts, both in its homes and in its factories, in two-thirds of the country, and unfortunately in the 2/3 most populous. Almost all of the South, Central and Eastern China. If we divided the map of China with parallel oblique lines, only the western third would be spared.

To understand this situation, it is necessary to know that, despite the decarbonization policies promoted in China by President Xi Jinping, dependence on coal to manufacture electricity still exceeds 60%. But in China, the price of

electricity is controlled by the Chinese Communist Party (CCP), that is, it cannot be higher than a certain price. Same as what some parties want to impose in Spain.

"A government can impose the sale price of a good or service, but unfortunately, it cannot impose the purchase prices of supplies."

In a regulated market, such as electricity, you can force yourself not to sell above a certain price, but unfortunately you can't force yourself to produce cheaply. Coal shortages due to Australia's low imports - given their poor relations because of tensions in the China Sea - results in high supply prices.

High purchase prices and regulated sales prices produce losses, which the PCC does not want to socialize, that is, it does not want the State to pay for them, for which producers respond in the only possible way, not producing, which leads to the electricity shortage that is occurring.

Allow me a subsection. It would not hurt for those brilliant minds that demand to regulate the maximum price of electricity in Spain, to turn their heads towards the country from which they want to copy ways and policies.

"The PCC's growth model is based on an exaggerated and sustained domestic consumption growth."

On the other hand, the expansionary policy in monetary terms promoted by the Chinese government and the growth model based on domestic consumption (to keep the population calm) has led to an ever-growing consumption of electric power.

It doesn't take a Nobel Prize winner to realize that the situation is explosive: growing demand offset by shrinking supply.

Well, the PCC has had the occurrence none other than (since it refuses to liberate the price of electricity) to demand that companies and families reduce their energy consumption. In a word: blackouts. And the blackouts are and will be both voluntary and enforced, something inappropriate for the second largest economy in the world.

"The lack of energy will inexorably translate into a lack of production."

These blackouts will inexorably produce a reduction in productivity, although the PCC does not want to account for it on their forecasts, that will be reflected in its growth. And this is going to affect us in a reduction in the number of imports from China. And we already saw just before the pandemic how Chinese-dependent we Westerners are to manufacture.

In the middle of this, the gas crisis is adding to the mix. Here the problem is due to poor planning, fundamentally also from the Chinese. 61% of the consumption of liquefied natural gas (LNG) in the world is used as fuel in factories, with the rest being mostly used by commercial establishments and families.

The consumption of gas for transportation of any kind is residual, which is not the case with oil, where almost 60% is used for this purpose. This is why both fossil fuels have their market prices so unrelated.

The main world exporters of LNG are the USA, Russia and Qatar, although the largest reserves on the planet are counted by the Russians in Siberia.

China is mainly supplied by Qatari and Russian gas, but they have had a terrible forecast and have not stored enough gas during the spring and summer, so they are going *en masse* to the "spot market" to buy, causing the rise in the prices that we see reflected indirectly in our electricity bill.

"Let no one expect much help from the Russians if their winter is colder than usual. Putin is clear about who he must protect."

Winter is approaching and the Russians, Europe's main suppliers, have to fill their reserves, which is why exports are further restricted. This lack of supply is causing many Chinese factories to see their production restricted as they are unable to transmit cost to price.

Well, the lack of gas to produce and the blackouts due to the low production of electricity are the perfect mix to suddenly weaken an economy, at the same time that the prices of the products that are manufactured become more expensive. Perfect example of stagflation, whose term was coined by the English Conservative Minister, Ian MacLeod, back in the mid-1960s. Perhaps the worst nightmare of any economy: price growth in a poorly performing (i.e. low growth) economy and rising unemployment.

As my mother said, I "have already made a suit" for the Chinese, against whom I personally have nothing against, but I must admit that they have fed up after COVID, then the real estate crisis and now this.

But how is this going to affect us? Well, badly. The fact that the second largest economy in the world has these problems, accompanied by a potential financial crisis derived from an expansionary model without control in the real estate world, cannot necessarily be very good for us.

Can we get it? Well, it seems so, now we will see to what extent. No one doubts the Western industry's dependence on Chinese supplies. We lived through it before the pandemic when its confinement paralyzed Chinese factories, de-supplying ours. We live it now because of the shortage in the production of chips, where, without going any further, many car factories like Renault have had to stop their lines several times, crushing the stock on the stock market. And we are going to live it because of their energy crisis, which incidentally creates ours.

"Unfortunately for our interests, the more than likely Chinese stagflation is going to affect us, or more precisely, is already beginning to affect us, according to German data."

Referring to Europe, much higher energy costs and lack of supplies from China are going to cause, well, they are already causing an explosive rise in prices, but in economies like Spain, which are still very weak. Here, very contrary to what the government tell us, we are unlikely going to grow 6.5% this year, and probably lucky if we reach 5%.

In the middle of the pandemic I predicted a full recovery in Spain towards the end of '22. Then I was forced to delay that data to early '23. Nothing substantial has changed since then, only that the vaccination is three months ahead of my estimate. I believed that we would be at this level of vaccination by Christmas, but surprisingly for me, vaccine manufacturers have been able to

manufacture three times the doses of vaccines that they produced before the pandemic. Incredible, and they certainly deserve my recognition.

Meanwhile the western central banks begin their retreat, which will exacerbate these problems. I do not know if it will happen like in March 2020, when Powell had to roll back all his actions from three months prior, and not only reduce intervention rates but also reopen the hand of monetary expansion.

My advice to anyone who has taken the champagne out of the fridge is to put it back for the time being, for drinking it now in celebration may choke you as this unravels.

