



China raises lending rate causes gold up

By CK Wong 2006.04.27. Last update 2006.04.28

<http://www.ck-wong.ca/China/Money%20Matters/china%20rate%20gold%2020060427.pdf>

Introduction

China has decided to move up the interest rate by 0.27% to 5.85% yesterday, April 26. The immediate effect is to cool off the economic activities. Many economists point out this action will reduce China economic growth. Some even associate the fall of gold price by US\$6 is the result of this change. May be it is the time to look beneath the skin.

Chinese Overheated Areas

The most overheated areas in China are real-estate and the financial market. Any industry and trading are carefully managed by the nation. Nothing could be done beyond the boundary.

The real-estate has been overheated so dramatically that it is going to hurt all the industry because the land for the factory will be sold for development rather for the manufacturing. If the factory is rented, the rent could sky rocketed so high the cost of production could be non-competitive. This tiger has help from the foreign investor to boost it to an uncontrollable level. Farmers have been forced out by all kinds of ways; legal or illegal. Working level could not afford new housing. Old houses which most of the young retirees (about 50) living also suffer the same fate. This created much social unrest. The longer this continues, the more damage costs the foundation of the social stability.

Speculation in the commodity and stock market has been wild. Early in the year, we heard the story of a copper trader short the position and cost country millions to smooth out the position. The continued volatile stock market has created many miseries. The money supply to these marketeers has to be curbed. Otherwise, the wealth will be herd to a small group of people from the public. The social imbalance will slow down the economic growth.

The remedy is to reduce the money supply.

Someone could argue the real-estate could push the whole economy; like the American. When one sector runs too far ahead, it creates chasm between sectors. No sector could survive along. They are all related. A booming country should have all cylinders fired not just one. China needs all sectors move forward not just one to ensure the booming of one sector could benefit others. For example, if copper industry produces too much that the transportation industry could not move the merchandize, it will just suffocated.

The reduction of money supply is not a mean to reduce GDP growth. China has to maintain the growth to feed the population. The reduction of money supply is to reduce sector imbalance.

Gold Price

When Chinese Yuan is strengthen, the American dollar is weaken. This will push the gold price up not down. People has been reverted the cause and consequence. If gold is in unit of Yuan, it will be down.

Gold bull has very long teeth. The market becomes very sensitive to any news and use it to correct gold. This happened this Monday, April 24. On April 25, it is Return of the Jedi.

Many market commentators are paid by article. For those have a salary, just like the academic, produce or die. I wish they read this correctly. They are professional; I am not. In the near future, the Beijing Olympic created tremendous demand on the raw material which still exists. The demand remains. The falling of the commodity price is just another excuse to correct.

Update on 2006.04.28

According to [3], other than slow down the investment mentioned above, the Chinese government would like to increase the saving of the people by raising the interest rate. With higher borrowing cost, this could slow down the spending. This is not good news to American who demands Chinese to spend more. However, this is right way to conserve the capital for future.

Reference

[1] China may take further steps to cool economy after rate rise, Bloomberg, 2006.04.27, http://www.bloomberg.com/apps/news?pid=10001096&sid=aPN27V19e9xg&refer=world_currencies

[2] Gold falls from 25-year high; silver dulls, Market Watch, 2006.04.27, <http://www.marketwatch.com/News/Story/Story.aspx?siteid=mktw&dist=moreover&guid={A05FA358-D79F-45A3-9453-431A43232BCA}>

[3] China raises bank lending rate to slow investment, China Daily, 2006.04.28 http://www.chinadaily.com.cn/china/2006-04/28/content_579345.htm