Is China's $23 Trillion Credit Bubble Ready to Pop?

Is the "mother of all bubbles" about to implode? Many analysts have been predicting that China could have its "Lehman Brothers moment" today, on January 31, 2014. Its colossal $23 trillion ($24 trillion by some accounts) in private domestic debt is, say some economists, but a pin-prick away from a devastating banking collapse that would send shock waves across Asian (and then global) financial markets.

Why was/is January 31, which marks the start of the Chinese New Year (the "Year of the Horse"), considered D-Day for the Chinese economy? As Gordon G. Chang explained in a January 19 op-ed for *Forbes* ("Mega Default in China Scheduled for January 31") that is the maturity date of a massively oversold, risky investment product called "Credit Equals Gold #1." Packaged by China Credit Trust, it promised investors a 10-percent annual rate of return — almost three times the market rate. Credit Equals Gold turned out not to be as good as gold, and China Credit Trust turned out to be (surprise!) not trustworthy. China Credit Trust reportedly had dumped most of the funds from its Credit Equals Gold sales into a coal mining operation, Shanxi Zhenfu Energy Group, which has since gone bankrupt. On January 17, Chinese state media reported that China Credit Trust (CCT) may not repay investors when the January 31 maturity date arrives. Making matters worse, the Industrial and Commercial Bank of China (ICBC), by assets the world's largest bank, had also marketed the Credit Equals Gold bonds and was also refusing to compensate investors.

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On January 28, the CCT/ICBC default on Credit Equals Gold appeared to have been averted. The financial pages of news services were reporting that some type of arrangement had been reached by CCT and ICBC to indemnify investors, though the details remain murky. *International Business Times* reported on January 28:

> China Credit Trust has reached a last-minute deal to repay investors in the 3bn yuan ($500m, £296.2m, €361.1m) high-yield product, avoiding the first high-profile default in the country's trust industry….
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> In a statement, the trust asked the investors to contact their wealth managers at Industrial and Commercial Bank of China (ICBC), which marketed the product, to arrange for payment….
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> Previously ICBC had said it was not responsible for investors in the scheme.

So, does that mean that the global financial apocalypse is called off for today? Maybe. But if it doesn't happen today and if it isn't Credit Equals Gold-CCT/ICBC, there are plenty of other Lehman Brothers and Bear Sterns tipping points waiting to implode/explode in the world's second largest economy. It's a matter of when, not if; the precise "when" is always iffy, but the "if" is certain. China's so-called "economic miracle" that has so dazzled onlookers and investors for the past two decades, is a central-planning monstrosity that has mega-debacle-waiting-to-happen written all over it. Beneath the gleaming, instantly-created Potemkin super-cities such as Shenzhen, and the planet-sized mega-malls, are crumbling infrastructure, vast corruption, and oceans of red ink. So, again, if January 31 passes without a resounding, world-shaking bubble puncture, it simply means a deferment of the day of reckoning.

"The truth is," wrote Michael Snyder, on The Economic Collapse blog on January 20, "that what has been going on in the global financial system is completely and totally unsustainable, and it is inevitable that it is all going to come horribly crashing down at some point during the next few years. It is just a matter of time."

"Since Lehman Brothers collapsed in 2008," noted Snyder, "the level of private domestic credit in China has risen from $9 trillion to an astounding $23 trillion. That is an increase of $14 trillion in just a little bit more than 5 years. Much of that 'hot money' has flowed into stocks, bonds and real estate in the United States. So what do you think is going to happen when that bubble collapses?" He continued:

> The bubble of private debt that we have seen inflate in China since the Lehman crisis is unlike anything that the world has ever seen. Never before has so much private debt been accumulated in such a short period of time. All of this debt has helped fuel tremendous economic growth in China, but now a whole bunch of Chinese companies are realizing that they have gotten in way, way over their heads. In fact, it is being projected that Chinese companies will pay out the equivalent of approximately a trillion dollars in interest payments this year alone. That is more than twice the amount that the U.S. government will pay in interest in 2014.

"Over the past several years," Snyder noted, "the U.S. Federal Reserve, the European Central Bank, the Bank of Japan and the Bank of England have all been criticized for creating too much money. But the truth is that what has been happening in China surpasses all of their efforts combined."

Tyler Durdin at ZeroHedge.com has produced a bar graph that dramatically illustrates the immensity of the increase in Chinese bank assets over the past five years, completely dwarfing the combined QE (quantitative easing) money creation of the Federal Reserve, Bank of England, European Central Bank, and Bank of Japan combined. ZeroHedge has been in the forefront of exposing this danger of China's "shadow banking system" for years (see here, here, and here) while most of the financial commentariat in the MSM choir have continued to praise China's economic model of "capitalism": central planning by the Communist Party and the dominance of giant SOEs (State-owned Enterprises). Even many of the so-called private Chinese corporations are little different from SOEs in that they are run by party members and "princelings" and their actual balance sheets, ownership, and other financial information are not publicly available.

And, as we have reported, the Communist Party, recognizing the out-of-hand corruption that is endemic in their faux "capitalist" system, have embarked on an anti-corruption drive that has resulted in many former billionaire princeling peacocks being turned into featherdusters; many are in prison, some have been executed (officially or otherwise). The MSM choir see this as a hopeful sign; the same commentators would, undoubtedly, greet an "anti-corruption" campaign within the Mafia with equal credulity and enthusiasm. As with the Mafia or any other organized criminal cartel, the Beijing Mafia (Chinese Communist Party, CCP) that runs China cannot tolerate lower-level criminals cheating on the bosses. But a minor cleanup among thieves should not be mistaken for real systemic reform. The Beijing bosses are continuing on the same unsustainable path, which means the day of reckoning will come and that, as Snyder put it, "it is all going to come horribly crashing down at some point."

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