

ARE WE HEADING FOR A GLOBAL HARD LANDING?

The narrative on Wall Street considers whether or not the world economy will manage a soft landing or a hard landing. Of course the navigators in the spotlight are the central banks of the world. Ah, to be a central banker elevated to god-like status, then blamed for the good times (low interest rates) by the Austrians, then blamed for the bad times (high interest rates) by the Keynesians.

It is not looking good. Hunger stalks the continents as many countries run out of foreign currencies. China is in extended lockdown. The Yen is collapsing. Germany is reeling from the price of energy driving up producer prices by a Weimar 30%. Most stock markets are in bear territory. The bond markets have suffered their sharpest losses for 30 years. Under all the hammer blows, the world economy is beginning to buckle.

The desperate stupidity of capitalism is palpable. Who provokes a war in a world still reeling from a pandemic, in the midst of a restructuring of the global economy, and at a time when society needs to deal urgently with global warming. History's first industrial economy has come to the end of the road. Capitalism promises nothing and threatens everything.

Japan.

Thursday was a crucial day for the Bank of Japan (BOJ). As the exchange rate with the Dollar approached the key level of 130 last crossed 20 years ago, the choice facing the BOJ was to either defend the Yen to help insulate Japan from the wave of inflation, or to maintain easy monetary conditions in Japan. It could not do both. It opted not to raise interest rates to defend the Yen and the result is that the Yen continued to collapse against the dollar which is supported by the FED raising interest rates in the USA.

Graph 1.



Graph 2.

Yen vs US Dollar



The Yen is the third most traded currency globally. It is the currency of choice for the carry trade when investors borrow in Yen to buy higher yielding assets in another country, mainly the USA. Investors pay little interest on their Yen borrowings and hope to reap the difference from higher rates abroad. However, carry trades rely on stable currency exchange rates, otherwise currency losses could overwhelm higher yields. This is happening now as the Yen has lost 13% of its value since March. These trades are a source of liquidity in global markets and their absence will add to the tightening conditions in the USA & Europe.

In addition the fall in the Yen, as in 2015, is putting pressure on the Renminbi due to the deep trading relationship between the two countries. I was going to do a brief report on China but with escalating and ongoing lockdowns, what is happening there is indeterminable.

Germany.

After Ukraine and Russia, the country which will be most damaged by the war in Europe will be Germany. The latest 4.9% monthly jump in the German Producer Price Index was twice the market consensus. It propelled the annual rate to 30.9% the highest rate since modern records began. Within that energy prices rose by 83.8%. Why buy piped gas from Russia when you can pay 7 times more for U.S. LPG gas. And as U.S. gas is priced in dollars, the collapse in the Euro as shown in Graph 3, makes it even more unaffordable.

The word dummkopf comes to mind. The US may have baited and trapped Russia into a war in Ukraine, but the real sacrificial goat in all this has to be Germany. Germany could have become a global powerhouse had it rebuffed the US over the Ukraine. It is about to learn that economic duress and abuse is just as destructive of economic activity as being carpet bombed. Germany will follow the USA into recession, only its recession will be deeper and more protracted. (I intend to do a fuller report on Germany once the rate of profit for the first quarter becomes visible.)

Now imagine if the strong dollar has been a problem for Germany and Japan how overpowering it must be for the poorer nations with dollar debts.

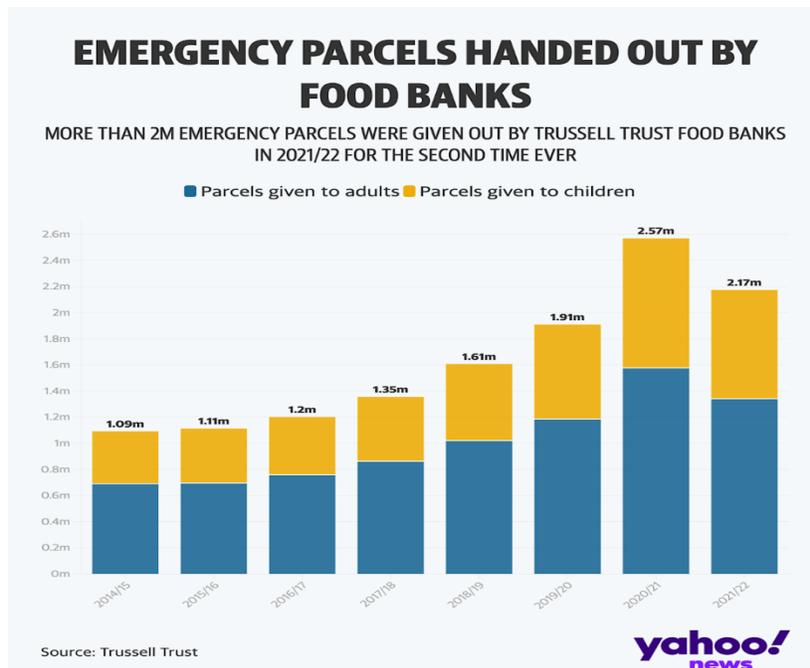
Graph 3.



The disUnited Kingdom.

Once upon a time the U.K. was an island of shopkeepers. Now it is an island of foodbanks as hunger and poverty stalks the land. [Food Bank](#) use is the second highest ever. To add insult to injury, according to a Bloomberg report, Brexit has raised food prices a further 6%. Seems Brexit voters were Conned into sticking their heads in the guillotine and then told to pull the cord to “get it done”.

Graph 4.



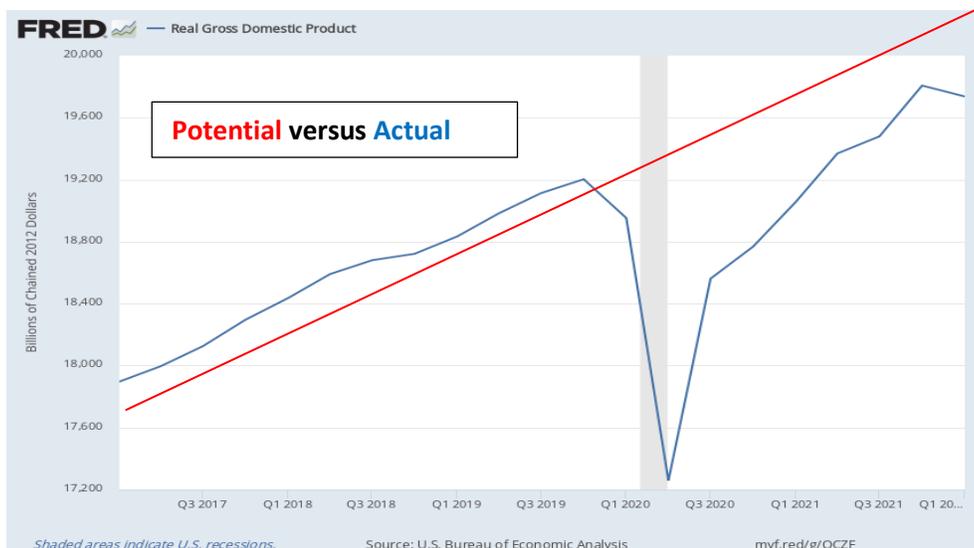
In a report in Thursday's *Financial Times* the wages of public sector workers are analysed. In the year to March median wages for public sector workers rose by only 1.4 percent versus 2.2 percent for workers in the private sector. In the first three months of this year, against the headwind of inflation, private sector pay rose by 6.2 percent vs 1.9 percent for public sector workers. However, in April, the month when half of all wage contracts are concluded, and where bonuses do not distort the figures, the median pay award was just 4% against current (and understated) inflation of 7%. The growing dissatisfaction with these pay cuts is giving way to disaffection, with workers either voting to strike or voting with their feet. Include the cuts to public services which are also part of the basket of consumer goods forming workers' standards of living, and the fall is even greater.

Finally, insolvencies (delinquencies) for the first quarter reported Friday are the highest for 60 years or since records began. Not so much levelling up as sinkhole Britain.

The U.S. economy dives into its first actual recession since 2008.

Only Morgan Stanley and Deutsche Bank predicted a recession later this year. No one, excepting this site, saw it coming sooner. Instead of rising by an expected 1.1%, the economy contracted by 1.4%. How did Wall Street react. According to CNBC, fund managers dismissed the reading as "[noise not a signal](#)". Oh really. What was noise was the previous quarter's growth rate of 6.9% most of which was driven by an inventory build. Marx observed that consciousness lags developments, but for those in self-denial, like the overpaid mediocrity on Wall Street, their consciousness plods behind developments.

Graph 5.



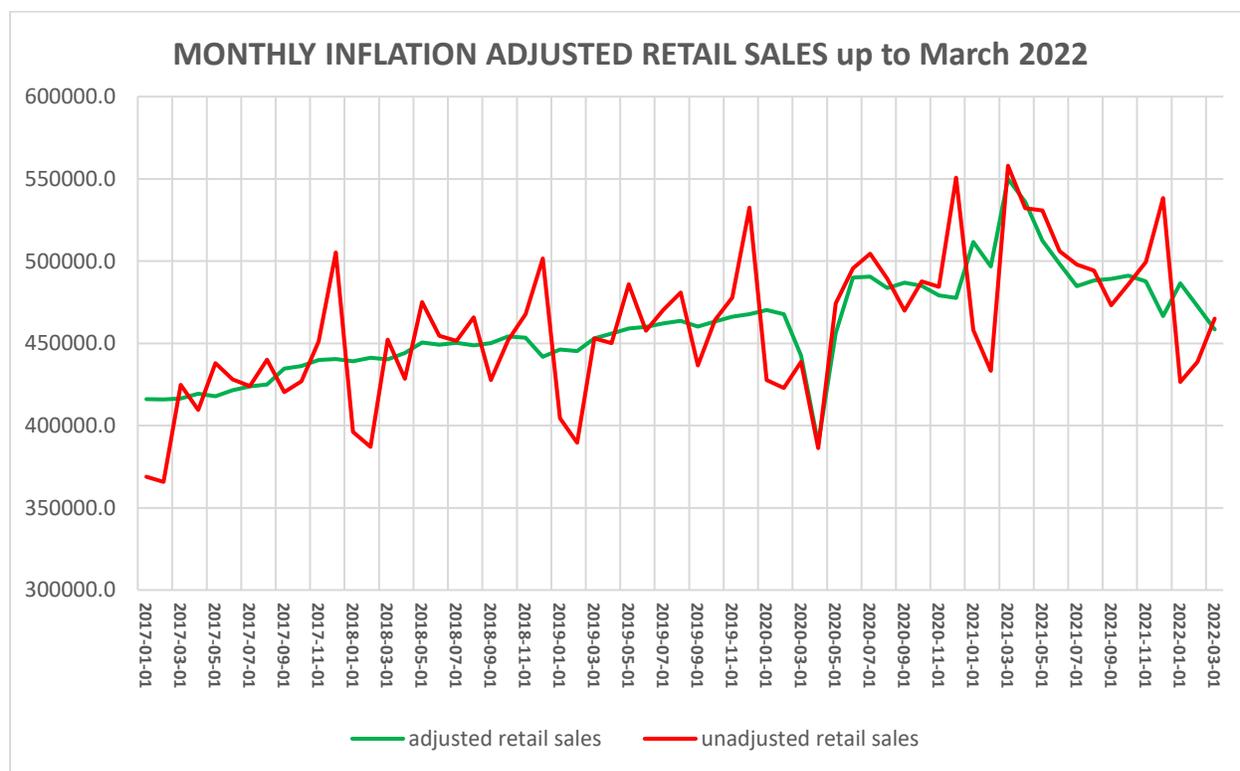
The writing was on the wall or was it the smartphone. [Trucks move 72% of all freight](#) in the USA. Half of all recessions were preceded by freight recessions. Such a freight recession is happening now. A Bank of America survey found that freight demand is down by 23% year on year. Its *Demand Index* fell to 58, a 22-month low. The report also noted that it was likely that inventory levels had climbed to their highest point since May 2020. The [Cass](#) Freight Index, the other authority on freight, has yet to declare a freight recession though their figures for the first quarter of the year shows a volume growth of just 0.4%. Perhaps now they will have to correct their earlier assumption.

“Global fund managers have never been more pessimistic on the outlook for economic growth, a monthly [Bank of America](#) survey found, potentially pointing to a further fall in stock-market holdings. The disconnect between global growth expectations and equity allocation ‘remains staggering,’...” The report published two weeks ago reported that managers now saw a recession, not Russia to be the biggest threat to markets. Someone should have told the markets on Thursday when they dismissed the fall in GDP.

However, the biggest reason for this fall in GDP is the change to the seasonal revisions to consumer spending. According to the Atlanta FED, this adjustment reduced GDP by 0.9%. “The [GDPNow](#) model estimate for real GDP growth (seasonally adjusted annual rate) in the first quarter of 2022 is 0.4 percent on April 26, down from 1.3 percent on April 19. After yesterday’s annual revision to retail sales by the US Census Bureau, the nowcast for first-quarter real personal consumption expenditures growth declined from 3.8 percent to 2.4 percent.” I believe this to be an understatement.

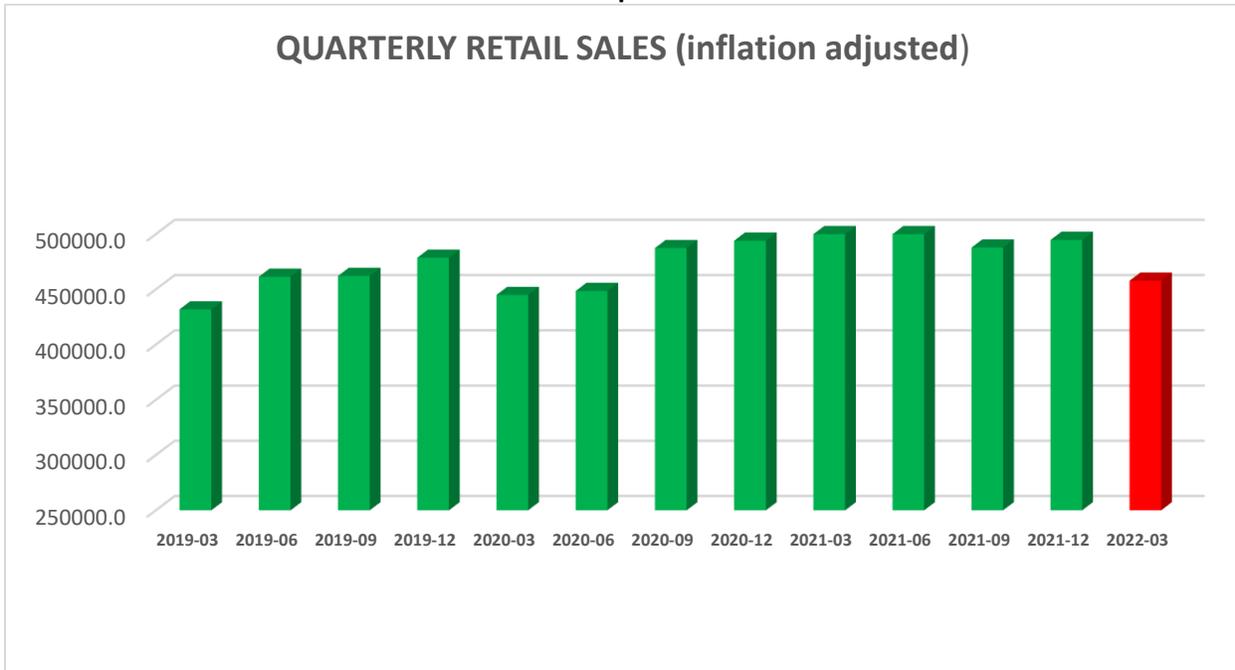
As readers on this site know, I have been banging on about how overstated retail sales have been for a number of years and therefore how overstated GDP growth was. An economy depended on personal consumption is an unhealthy economy. This overstatement is demonstrated by the two graphs below. Each of the graphs has been deflated by the CPI weighted for durable and non-durable goods.

Graph 6.



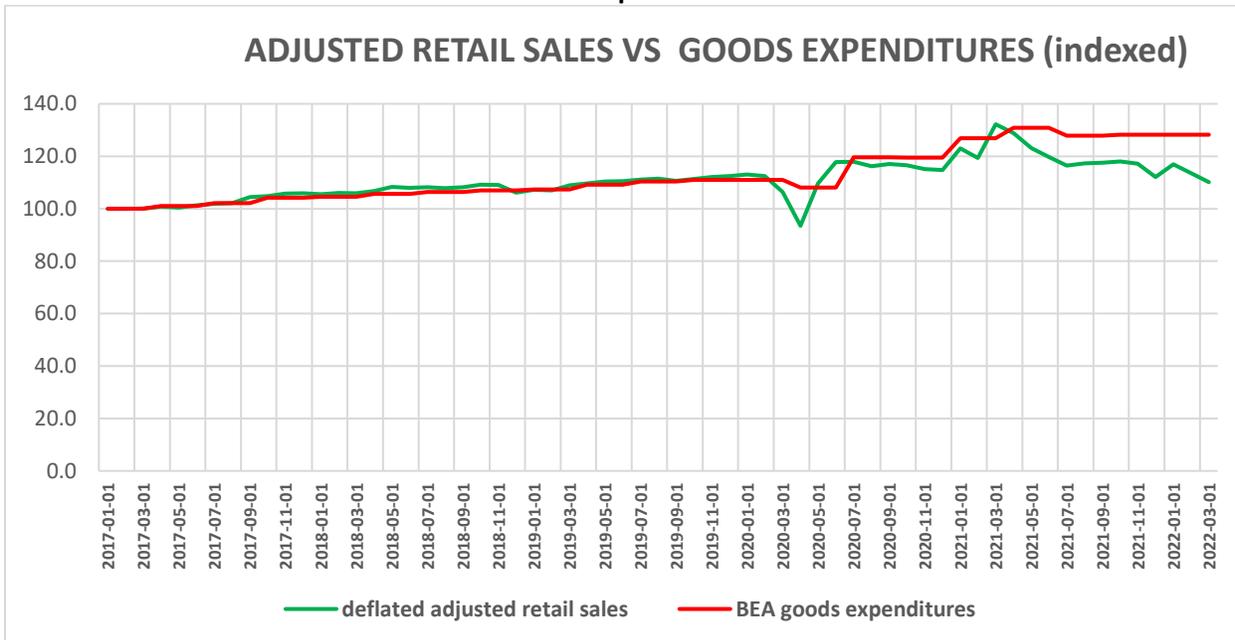
Now admittedly in Thursday’s GDP release, the BEA acknowledged that consumption of goods had fallen by -0.03% quarter on quarter. However, that does not reconcile with Graph 7 below which combines adjusted and unadjusted sales deflated by the goods CPI. (All sources and equations can be found on the accompanying spreadsheet ‘March Retail Sales Analysis’.) Here we find a bigger fall than 0.03%. (In contrast, spending on services rose by 1.86% reducing the fall in GDP.)

Graph 7.



And this is confirmed by Graph 8. In this novel, but notable graph, inflation adjusted retail sales are contrasted to the real expenditures on goods found in NIPA Table 2.3.3. which informs GDP. (Goods represent the bulk of retail sales.) Until the pandemic, the growth in the two expenditures were aligned, but since the pandemic they have diverged. Currently the gap is >15% which translates into a 4% gap in [GDP](#) itself. If the personal consumption of goods has been overestimated this way, it means that in 2021, on average, the gap has been equal to 3% of GDP. By subtracting this 3% from the official 5.6% growth figure in 2021, actual growth would have fallen to just 2.6%, or less than half the [official](#) figure.

Graph 8.



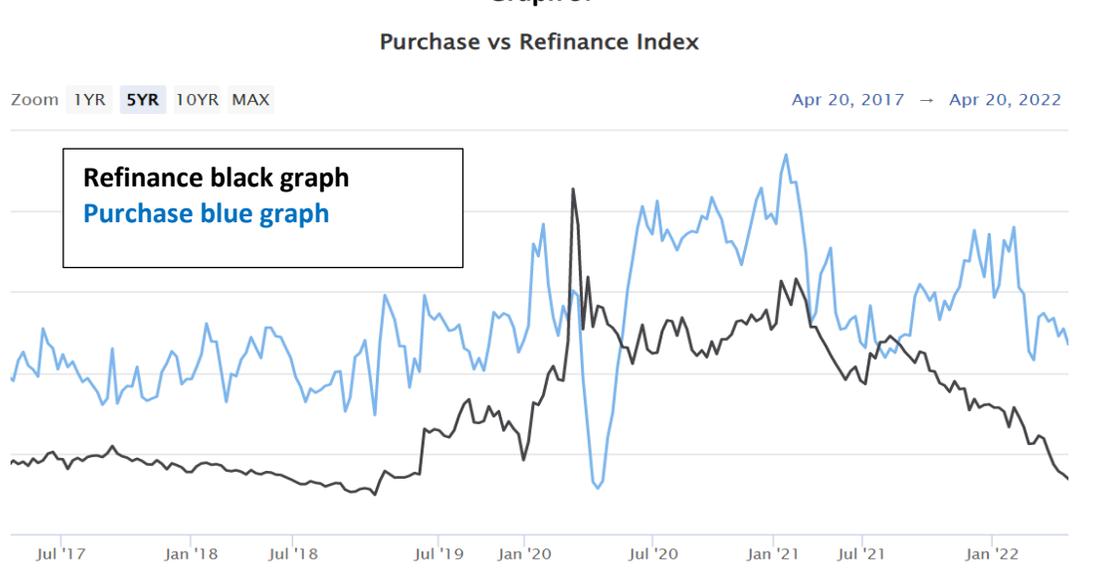
Why has this occurred, why has there been a divergence since early 2020? Two events stand out. Firstly the lockdowns stimulated spending on goods at the expense of services. Secondly, the price of goods suddenly exploded because of this increase in demand coupled to supply chain disruptions. These two events altered the weighting for goods purchases as well as their price distribution. This has not been accounted for in the BEA's deflators. More disturbing, the gap is widening not closing, despite the shift back to service spending.

THE US housing market.

Before proceeding to examine the US housing market it is worth detouring via China to witness the infighting going on within the CCP. As the economic stressors build, which are confined not only to the lockdowns but are more broadly based, the CCP is beginning to factionalize over how best to deal with the property crisis there. On the one side is Liu He, a vice-premier arguing that the government is underestimating the scale of the property crisis and its impact on the property market and should ease up. In this he is supported by local government officials. On the other side are another two vice-premiers, Han Zheng and Hu Chunhau, who are siding with the housing ministry and are supporting current restrictions. Essentially the argument boils down to how much latitude to give developers over the allocation of project revenues. The housing ministry insists that these project revenues (down payments or advanced sales revenues from new customers) should be used exclusively to complete the project. The other side insists these payments can also be used to pare down debt even if this debt is legacy debt unconnected to the project. It is not so much that the housing ministry finds this unethical, which it is, but they resent this latitude because it is the ministry that ends up shouldering the cost of completing the project when the developer defaults. In sum, China is likely facing its most severe economic conditions in 30 years, and it is likely that resentment is building.

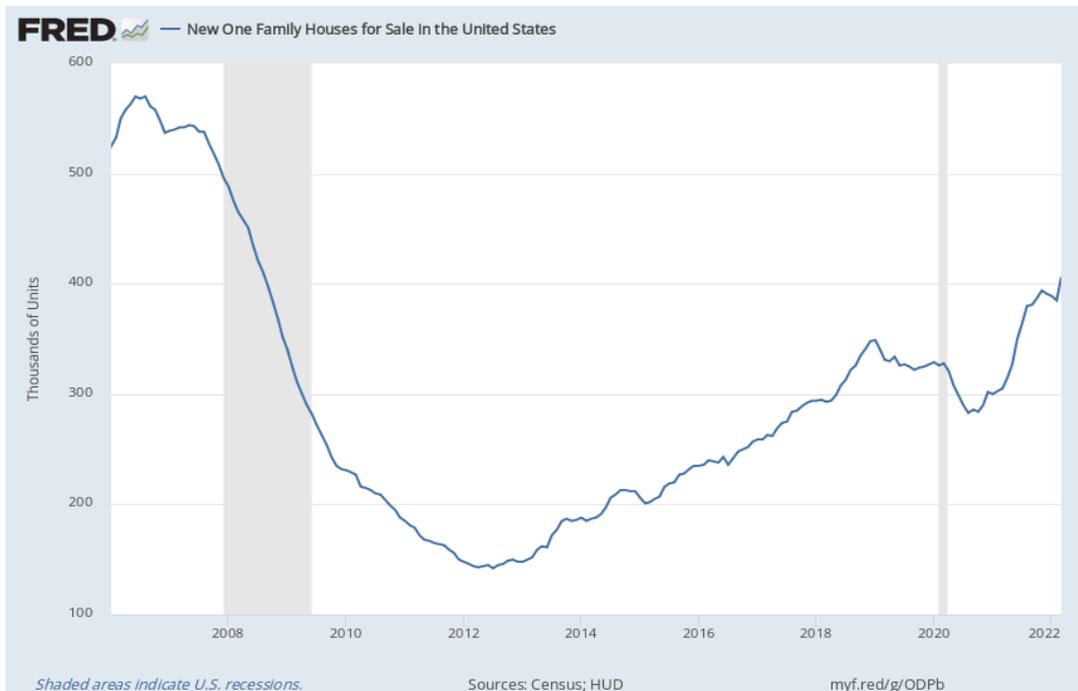
In the USA 30-year mortgage rates have finally popped above 5%. This has had a sobering effect on the housing bubble. According to [CNBC](#) refinancing mortgage applications have fallen by 68%. (No more flipping of homes then.) While mortgages for purchase have fallen 14%. With the exception of building starts, the sale of new and existing homes is falling month on month.

Graph 9.



And the worst is to come. The full effect of the >5% mortgages will only take place in June because many applicants had secured mortgage commitments before the rate rose to 5% and beyond. But the [Black Swan](#) is a-paddling down the Hudson river towards Wall Street, there to shake out its feathers. Once again the Street is in denial, comforted by the myth that falling sales is due to the low stock of available housing for sale. While true in select regions, it is not true nationally. In fact as the data provided by FRED shows, the [stock of housing](#) continues to rise and now stands at 5.7 months. This is confirmed by the graph below which shows new homes for sale are at their highest level since the unwinding of the 2008 crash. Viewed over the longer term the stock of unsold homes is about average.

Graph 10.



There is one confounding factor. Now that the US economy is in recession, the pressure on the FED to lift interest rates will be less severe. Recessions are water to the fire of inflation. However, this is unlikely to occur before the housing bubble bursts.

Wall Street, over-paid and in denial.

Thursday was weird even by Wall Street standards. On the day it was announced that the US had entered recession, both the share market and interest rates went up. It was a relief rally in a depressed economy because a few large corporations did not produce profits as bad as was expected. Below is a table analysing the results of what used to be the **FAMANG** now reduced to **MA** or Microsoft and Apple. Collectively they used to corner ten percent of the global share market cap.

I have also added in Qualcomm and Intel the two big chip producers with their contrasting fortunes. Intel which used to be the world's biggest chip producer continues to struggle with its core market stuck in computers which is growing less quickly than handsets where Qualcomm is a world leader.

Table 1. (Q1 2022 vs Q1 2021)

corporation	Revenue growth	Gross income growth	Operating income growth
Apple	8.6%	11.8%	5.8%
Alphabet	23.0%	22.2%	-8.3%
Microsoft	18.0%	19.0%	8.0%
Meta	6.6%	-25.0%	-21.4%
Amazon	7.0%	-58.5%	-11.9%
Netflix	9.8%	0.6%	-2.7%
Intel	-7.0%	-14.7%	+3.4%
Qualcomm	41.0%		61%

It is odd that the stock markets had a mini revival when four out of the six high tech corporations had **falls** to their operating incomes which informs their pre-tax profits. In particular Amazon’s margins collapsed from 8.2% down to only 3.2%. Essentially Amazon is a bankrupt corporation sustained by its cloud and advertising business. Its retail arm is a bust and it could be the case that predator investors will be pushing Bezos to divest the retail arm on which Amazon was built. Meta shares rebounded because its profit fall could have been worse. Even Apple, the world’s biggest corporation only managed to eke out a below inflation rise in operating profits because of weakness in its international sales.

It is therefore not coincidental that both Alphabet and Apple announced huge share buy-backs, in the case of Alphabet up to \$70 billion and Apple \$90 billion. No doubt both recognise they have reached the crest of their respective hills and from now on its downhill all the way. Collectively the High-Tech sector, unlike the Energy sector, will not be a positive for year-on-year non-corporate profit growth.

As for the rest of the non-tech multi-nationals, their increase in turnover tended to be below 7% and where they were below the rate of inflation, it tended to squeeze their operating margins. In so far as many raised their outlook for the rest of the year, this was more a function of rising inflation prospects rather than volume, though some on Wall Street interpreted this as positive news. In contrast investors continued to be less confident about the prospects for shares.

Graph 11.



[Global Index](#) on April 27, 2022

It is unlikely that High-Tech overall will make a positive contribution to pre-tax non-financial corporate profits unlike the energy sector. The mass of real non-financial corporate profits peaked in the 1st quarter of 2021. Since then it has fallen every quarter with this quarter likely to add to the fall. In sum, the rate of profit by this quarter will have fallen back to its depressed 2019 levels, or <5%, before falling further.

Globalisation what an irony!

The USA single handedly has set out to wreck globalisation in order to slow down its own decline. And yet it has become more dependent not less dependent on the international division of labour. One of the reasons for the fall in its GDP was the growth in the trade deficit as imported goods overwhelmed the exported goods (see the graph below). Since the outbreak of the pandemic, the deficit has doubled. So much for the hype of reshoring, on-shoring etc. more like the US economy needs shoring up.

Graph 12.



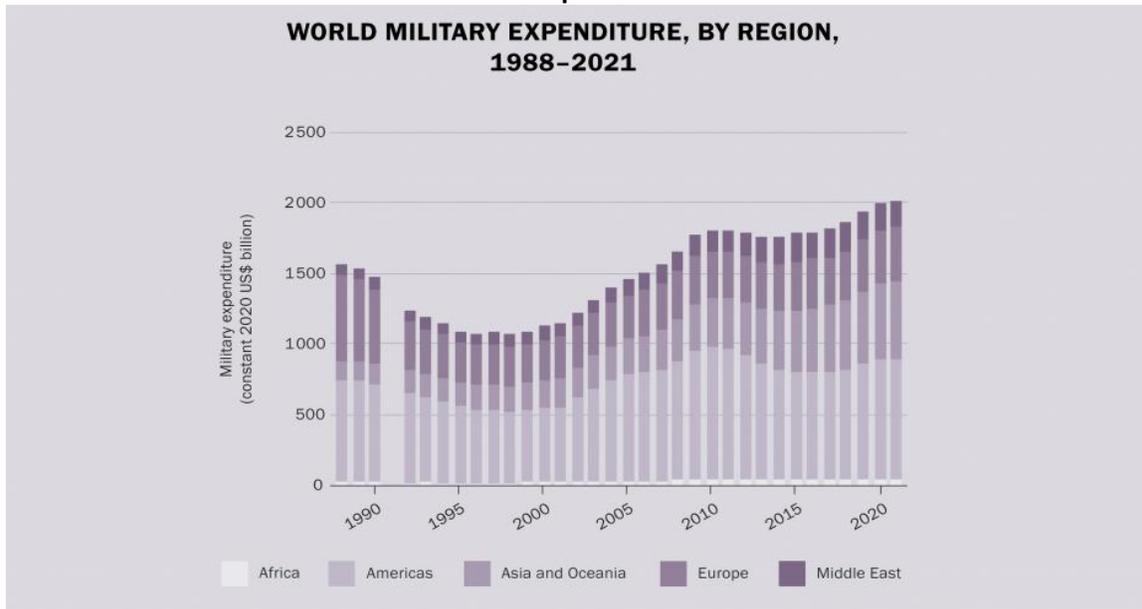
War is big business.

While the world economy heads for a hard economic landing, the hard rain of shells and missiles continues in the Ukraine. By the day it becomes clearer this is not a war in the Ukraine, but a NATO war being fought by Ukrainian soldiers bolstered by mercenaries drawn from the ranks of NATO. In the Ukraine, the US industrial military complex has found the ultimate in profitable outlets. It could be said: “We ship arms to the Ukraine for the Russians to blow up, so that we can send even more arms to be blown up, and all the while the Biden administration pays us with more and more taxpayers’ money.”

In the end of course, as the Japanese learnt in the 1990s, economic recessions do more economic harm than does war.

For the first time, the latest [Stockholm International Peace Research Institute](#) report concludes that total military spending (as opposed to arms spending alone) in 2021 rose above \$2 trillion. At \$801 billion, the US spending on arms represented 38% of the total spend of \$2113 billion a figure representing 2.3% of global GDP.

Graph 13.

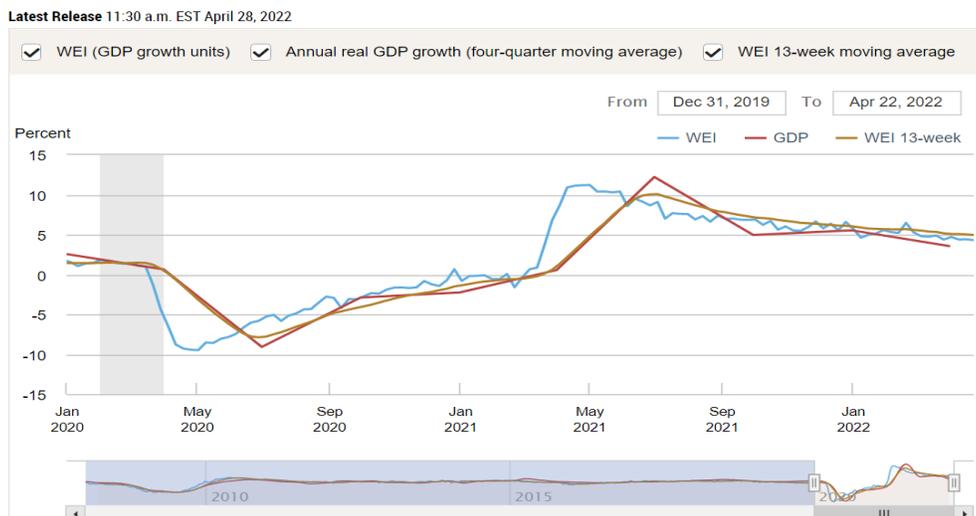


For this to happen at a time when the world’s productive resources should be devoted not to destruction, but to restoring our planet, is the worst possible indictment of this rancid and superfluous capitalist mode of production. It is clear that in pursuit of profit, a few thousand capitalist families are intent on blowing up this planet rather than saving it, and this at a time when the [sun](#) is going to be less kind to our planet.

Conclusion.

The [downward trend](#) in the USA continues despite the Street slobbering over the resilient consumer.

Graph 14.



This has been a year of records, the kind that makes the rich poorer. This April, the 13% fall in the Nasdaq has been the worst since 2008. Overall the U.S. markets have had their fourth biggest first half fall in history according to Bloomberg. The last time the 2-year Treasury Bond rose as steeply as now, was pre-2006. Finally, the employment cost index rose by its fastest rate since 1984 causing the Keynesian Larry Summers to opine that pay rises were now reinforcing price rises.

For months traders were speculating when the next recession was due, the most popular entry in their dairies being mid-2023. They may as well throw away their dairies. The recession is already here. As I have shown, personal consumption is much weaker than official estimates thereby undermining GDP. On the basis of the data presented in Graph 8, US GDP actually fell by over 2% last quarter rather than 1.4%, that's very noisy.

It is likely that when the UK, Germany and Japan report their first quarter data, they too will have entered recession. As the global macro situation deteriorates, no doubt the axis of the debate will switch away from when, to how deep the recession will be, and for how long it will endure. For the investors in first class, it is time to brace, brace, brace. The next stop for the fall in markets could very well be 40%. Capitalism has been living on borrowed time and borrowed money. But as the law of value likes to say, there is always the unavoidable payback time, and it has arrived.

Brian Green, 29th April 2022.