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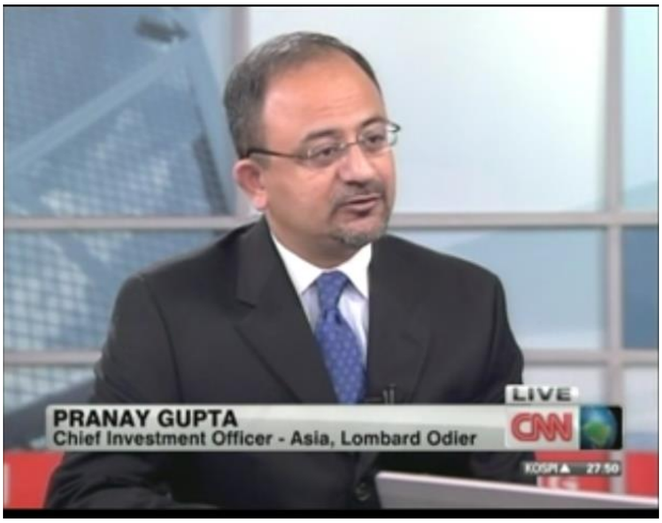
Slowdown in China



Q: China reported GDP numbers of a 7.6% growth. I think, despite what the pro-China analyst will say, this is a significant slowdown. Some would actually question whether these data are reliable. Is it an accurate reflection of what is actually happening in China?

China is a single propeller economy. It is purely based on government investment. So when the government pushes the pedal the numbers goes up. But this really masks the structural weakness that is inside China. Premier Wen has been preparing the world and his people for a much slower China over the coming years. So, I think we should be prepared that over the next 2 to 5 years the growth rate in China can potentially be 6% not 8%.

Q: So you think it is worse?

Definitely. Government investment is slowing down not over the short term but over the longer term, the rebalancing from investment to domestic demand is going to take a lot longer time.

Q: As the world's second largest economy and as the engine room, what are the global ramifications of this over the next 2 to 5 years?

Huge. China has been a source of two things: cheap exports to the western world, and imports from the rest of Asia. China is the biggest trading partner of most of the Asian countries, so when China slows down the rest of Asia slows down. It has huge implications in terms of commodity prices because China imports a lot of commodities and has implication for global growth in general.

Q: Quite fascinating and also a very different view from what some people out there will try and spin.

Indeed.

Q: Let's turn to the LIBOR scandal which has obviously engulfed Barclays Bank. But as we know the US Justice Department is extending their investigation and building cases against several banks and several individuals. How far reaching will this scandal be and I guess, do you see it really rocking the banking world?

LIBOR is a survey base rate as supposed to a transaction base rate. Any survey is prone to manipulation, and to that extent LIBOR has been one of the prime candidates for a cartel type manipulation. This is much more widespread than just Barclays. It is a survey of thirteen odd banks so probably the scandal will progress for a long period of time. Some more heads will roll. There will be more penalties. It is across major banks, across the world. LIBOR is used to price mortgages, lending, derivatives, and is at the back all the financial instruments across world. Everyone has been impacted by this. This is not the end of the LIBOR scandal.

Q: The US - we have not been seeing the growth that many had hoped for. Within the US Government, as they face the election come November, this will be a key issue. Are you expecting the US to see the growth problems that they experienced in the second half of 2011 and 2010?

We are in a much more fragile world today than we were in 2009, the global economy is much weaker. Having said that, there are a few key differences today compared to 2010 and 2011. The US housing market has stabilized for the first time. Credit growth has picked up. There is a slowdown, but it is not a structural weakness

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Q: What is happening in the US is happening in China and the Euro zone crises. What impact is this going to have on the Asian economies that have been growing?

Asian economies have two parts: Korea and Taiwan which are huge in exporting to the US. They are going to be impacted by a China slowdown as we discussed. And there is India and Indonesia, which are relatively insulated but are mired in their own specific problems. At the end of the day, all economies across the world are going to slow down over the medium term. The economies which are more reliant on domestic demand like the Indian and Indonesian have the potential to grow faster. Anyone who has an export led growth model is going to have some problems. Anyone where the cost of labor has been the main driver of growth is also going to be vulnerable. Whenever China decides to invest in something, we know that they are going to invest in creating a very large capacity and in the next 5 year plan it is in semi-conductors and technology. Korea and Taiwan are prime candidates both from an export perspective as well as a comparative perspective to lose out in this scenario.