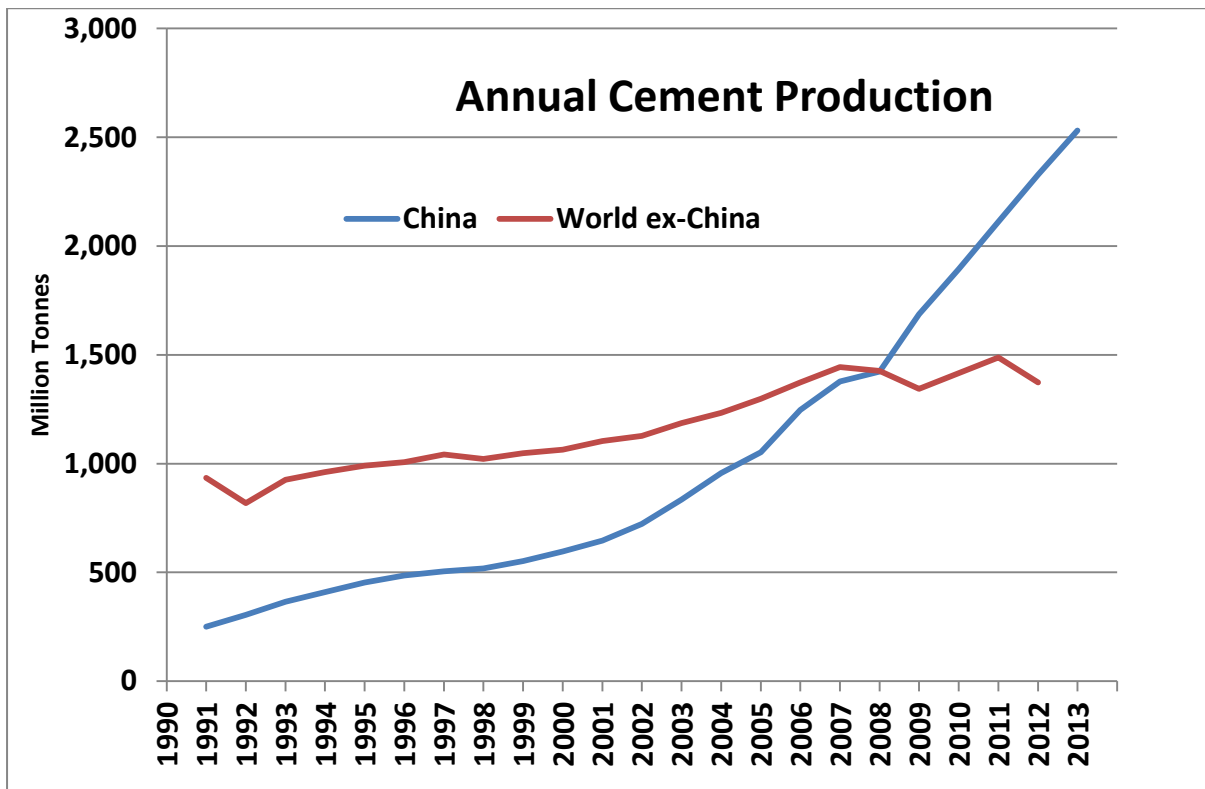


# China's Insanity

The following chart shows China's annual cement production compared with the rest of the world. You can see that China is producing TWICE what the rest of the world produces. The thing is cement is a heavy and low value commodity. As such, it is not economical to export cement from one country to another. Common sense would tell anyone that China doesn't need that much cement.



You can see from the chart that China's cement production went berserk after the 2009 stimulus. In the 5 years after 2008, China's production increase was equal to the increase over 16 years prior to 2008.

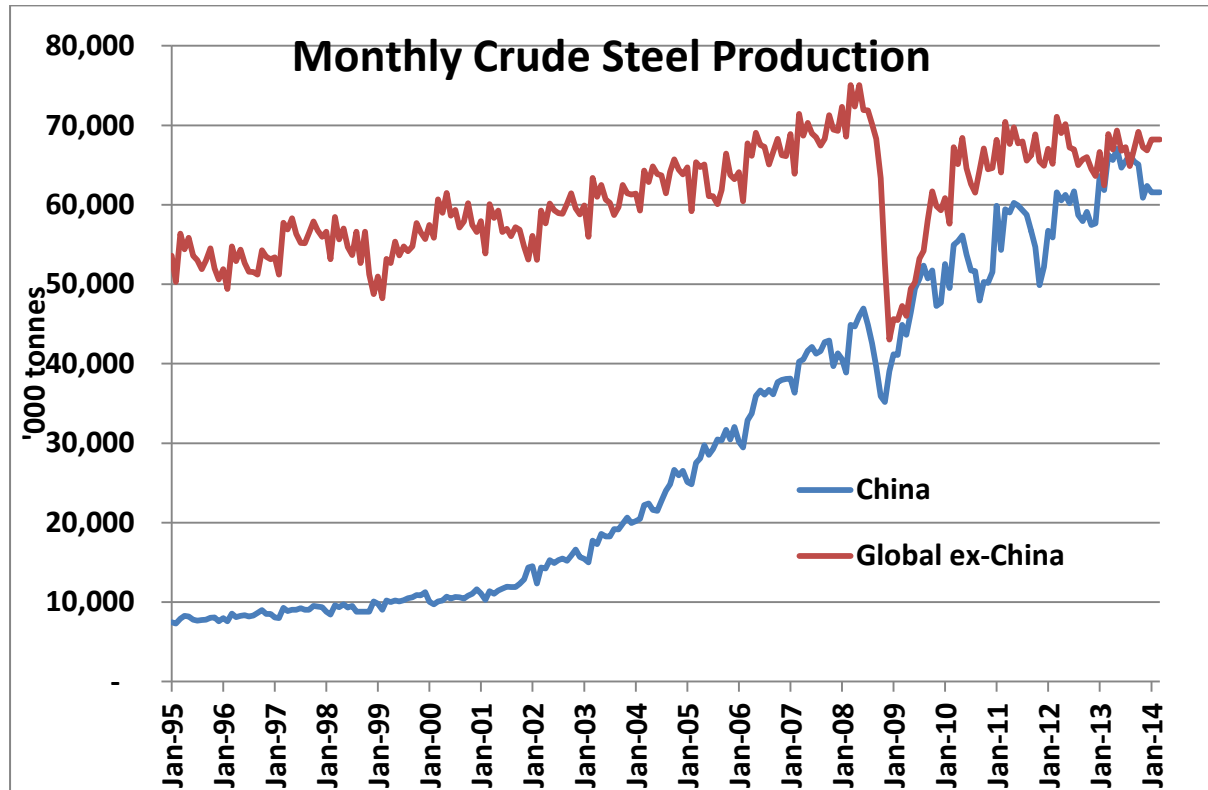
Thailand and China have roughly the same GDP per capita. Thailand has about 40 million tonnes of capacity in a country of 67 million people whereas China with 1,351 million people has 3 billion tonnes of capacity. If it were behaving like Thailand, it would only need 800 million tonnes!

A similar situation exists for steel.

The chart on the next page shows China's steel production compared with the rest of the world. China produces nearly as much steel as the rest of the world put together. Post 2008, monthly production has increased by 20 million tonnes, a 50% increase over 2008 levels.

This is insane. China has to import most of its iron ore and coking coal. It is a net importer of oil and gas. It isn't even an efficient producer of steel - I have seen presentations which illustrate how production cost in the US is now 20-30% cheaper.

Hence, from a competitive advantage standpoint, I cannot see any reason why China, with one sixth of the world's population, should be producing half of the world's steel.



Cement and steel are related as one might expect.

The biggest user of steel in most countries is the construction of commercial buildings. Frequent visitors to China have reported high-rise office blocks in even in very small towns. This wasteful largesse has not only created rising levels of non-performing loans and grossly under-utilized buildings, it has generated a demand for steel (and cement) that has now disappeared, never to return.

One can imagine this story repeated across any number of construction related materials – copper, aluminium, construction timber, ceramic tiles, electrical wiring, etc.

To me, the capacity cuts that need to be taken in China are so enormous, it is hard to understand why everyone seems to believe that a soft landing in China is a given. The ramifications of a billion tonnes of excess cement capacity and 200 million tonnes of excess steel capacity are, in themselves, mind-boggling already!

The sooner they bite the bullet, the better for their economy and environment.