Stirling Bridge
Wealth Partners, LLC

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A Lehman moment?

The failure of Lehman Brothers in 2008 was the straw that broke the camel's back in an already ailing housing market. Homeowners, lenders, construction workers, savers, and all sorts of others were affected negatively the world over as the repercussions spread along a daisy chain of financial interconnectedness. In many ways we continue to live in the shadows of those events as our federal government became ever-more entangled in the management of economic activity.

A question has been raised of late: are we at risk of another Lehman moment? The short answer is, well, of course we are. We are always at risk if a large financial institution, with lending and borrowing tentacles extending across political boundaries fails to exhibit proper conservatism and liquidity. But more specifically, the question has been directed toward another real estate related area – the Chinese property sector.

Manufacturing and technology in China are well known to have aided the country's economic ascent over the past thirty years. Less well known is the influence levered property development had. Many large corporations and countless individuals borrowed for and invested in massive real estate developments. So much so that the property sector accounted for 30% of the Chinese economy in recent years.

But what happens when economic growth slows? When credit tightens? When the Chinese government layers in more restrictions, stripping out economic and political freedoms? And when a population begins to decline?

The issue. Starting in 2021, one of China's top three property developers, Evergrande, defaulted on its debt. Projects were halted and liquidated. Workers were let go. Government intervention has been ongoing in a slow-motion train wreck that continues to spew out financial debris and repercussions. Sunac China, another huge developer, followed a similar default and shaky government support course soon thereafter.

The latest victim is Country Garden, making it official that all three of the largest developers in China are now in default to the tune of billions. Each would be bankrupt were it not for state life support. Unemployment data in China have risen so dramatically that the government has decided to stop publishing the figures for young workers. Ah, the benefits of being a communist dictatorship – permission to hide and obfuscate truth at every turn.

But back to the initial question. Is this a Lehman moment for the world?

We think not. While no apples-to-apples appraisal with history is precisely possible, we think the closest comparison to the Chinese property debt and sector meltdown might be Japan's lost decade (or decades).

In 1989, Japan was the manufacturing and technology king of the world. Fears abounded of Japanese businesses buying up US assets. Yet, its corporate structures were characterized by an internecine web of borrowing and lending. And its population growth suddenly stalled. What followed was a decades-long stagnation. They remained a wealthy country, but its growth and vibrance was absent.

Today, like Japan in 1989, China's debt is vastly held within its own borders. Good for them from a geopolitical standpoint. Good for the rest of us in that defaults create only small ripples rather than tsunami. <u>There are simply few non-Chinese lenders to Chinese institutions</u>. And on the population front, even the fib-friendly government in Beijing admits its population is in decline today. Though the official numbers are likely rosier than reality.

And so, we think headlines screaming for China's imminent collapse are gross overstatements made only to sell doom to consumers of such content. China has ample dry powder to prop up various sectors and assuage the beleaguered public for a long while. They will remain a force for the foreseeable future. And, unless the US alters its low-growth course, China will still overtake us as the world's largest economy. However, given the current malaise, it will probably take longer than originally thought.

Stirling Bridge Wealth Partners, LLC is fortunate to count many of you as clients. In the good times and bad, we remain committed to providing customized investment solutions and robust financial planning wrapped in a package of exceptional service. We thank each of you for your dedication to us and for your trust.

Sincerely
Jason Born, CFA
President