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A Global Downturn Puts the Brakes on China's Industry

By DAVID BARBOZA
MA'ANSHAN, China
- The Ma'anshan Iron and Steel Company recently opened a giant $3 billion steel mill on the outskirts of this city. The mill, which covers one and a half square miles and has its own power plant and shipping port, was built to help meet China's seemingly insatiable appetite for growth.

But during what should have been a peak production period two weeks ago, it was silent. Rolls of coiled steel sat near the end of a long assembly line as a few helmeted workers lounged about, playing with their mobile phones.

Three blast furnaces and a line that produces H-beams for construction were also temporarily shuttered here at Ma'anshan, about an hour west of Nanjing.

"Demand is definitely shrinking," Wang Wei, an investor relations manager, said as he toured one of the brand-new plants. "Everyone is cutting back capacity."

It is happening faster than most anyone predicted: China's economy, long the world's fastest-growing major economy, is slowing down. Economists are forecasting that after growing nearly 12 percent last year, China's economy could slow to 5.5 percent in the fourth quarter of this year - a stunning retreat for a country accustomed to boom times.

Last week, banking regulators began warning about the risk of bad loans accumulating, and labor officials publicly worried about the possibility that mass layoffs would lead to unrest.

"It's the speed of the deceleration that scares people," says Liang Hong, a Goldman Sachs <http://topics.nytimes.com/top/news/business/companies/goldman_sachs_group_inc/index.html?inline=nyt-org> economist who said she recently surveyed companies in China.

The American recession is one big reason China's epic economic growth is imperiled: as Americans buy less, China sells less. And China's own efforts to keep its economy growing, through a stimulus package worth nearly $600 billion, may not replace a falloff in American demand as the United States' recession deepens.

The global downturn is already reaching deep into the heart of the country's once-rapid industrial transformation - its steel, cement and construction companies - stalling dozens of multibillion-dollar investment projects. Plunging housing prices at home combined with a virtual global investment freeze have led to steel orders softening, steel prices plummeting, and inventories and losses piling up.

Coast to interior, China's aggressive building boom is no longer so aggressive.

In Hebei Province, in north China, Capital Steel, one of China's biggest steel makers, is building a $10 billion steel mill complex on an island, even as its profits evaporate.

In the eastern Chinese city of Hangzhou, Vanke - a huge real estate company - is spending more than $1 billion to build what amounts to a new city, with its own schools, a hospital and thousands of town houses at a time when the company is reporting a huge drop in sales.

And in Macao, new construction is grinding to a halt on one of the world's biggest real estate developments - a massive casino and hotel complex whose cost has been estimated at $20 billion - because of huge debt obligations. About 10,000 people could lose their jobs.

Nationally, Chinese officials say their country faces a grim situation. New economic data released over the last weeks is beginning to reveal the extent of the slowdown in China.

This year, housing sales in big cities have plunged by as much as 40 percent from a year ago. Government revenue was down in October. And last month, industrial production registered its weakest growth in seven years.

"Growth is deteriorating fast," says Andrew Driscoll, a China resource analyst at CLSA, the investment bank. "We're not talking about China's growth going backwards. But when supply is geared toward 10 percent growth, and it comes down to 5 percent, you have excess supply."

To cope, Beijing recently approved the biggest economic stimulus effort in China's history: a $586 billion package over two years, aimed at shoring up the very industries that seem to be faltering - steel, cement and companies engaged in building.

The government also approved emergency measures including tax relief, export rebates and housing policies. One Beijing official said the government could spend more than $586 billion.

The government is promising fast approvals for local governments to build subsidized housing, railways and airports, and even nuclear power build subsidized housing, railways and airports, and even nuclear power plants. Fixed-asset investment - or spending on things like housing and manufacturing plants - accounts for about 45 percent of the nation's economy, and that is the focus of the effort, analysts say.

Just months ago, Chinese leaders were warning that growth was too strong and risked stoking inflation. Now, Chinese officials say they want to do their part to keep the global economy from slipping into recession.

In America, consumers have closed their wallets. Parts of Europe are already in recession. And in Asia, Japan and Hong Kong now say that they too have slid into recession.

The ripple effects are being felt everywhere in China. Hard-hit airlines and automakers have appealed for government aid. Local governments that raised millions of dollars auctioning off land rights are confronting lower bids and depressed sales, which essentially means lower tax revenue.

Lead smelters, which produce material for the battery industry, and aluminum producers are shutting down production lines. And cement makers - one of the pillar industries in a nation perpetually under construction - are depressed.

"This is a bleak winter for the cement industry," says Yang Dongsen, an analyst at Merchant Securities in Shenzhen. "There's a nose dive in real estate construction. In south China and east China, two places where real estate boomed, many projects have suddenly stalled."

Last month, electricity production in China dropped for the first time since early 2005, a sign that big industry, the largest consumer of power, is in retreat.

"Global commodity prices collapsed. People got scared, and many activities just stopped," said Liang Hong, the Goldman Sachs economist. "Many turned off the lights."

Steel producers are among the worst off. Slowing demand has forced many to idle plants. Australian and Brazilian iron ore suppliers - which reaped huge profits from China's building boom - say demand from China has already slowed sharply.

Here at Ma'anshan Iron and Steel, executives are pondering what happened just after the middle of the year, after they began operating a huge new mill that they say is much more efficient than older mills. Ma'anshan's average steel price peaked at $768 a ton around June, then began falling sharply. In November, prices dipped as low as $490 a ton.

Steel executives say weak consumer spending reduced demand for things like cars and refrigerators, which contain finished steel. But most say falling property prices had an even bigger impact.

Ma'anshan recently reduced its production by about 15 percent. But company executives say they are hopeful about the government rescue effort, one that will put China back to building.

"I'm quite optimistic about the stimulus package," Hu Shunliang, board secretary at Ma'anshan Iron and Steel, said. "It's not just theater. It will stimulate other industries and help bring us more investment."

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