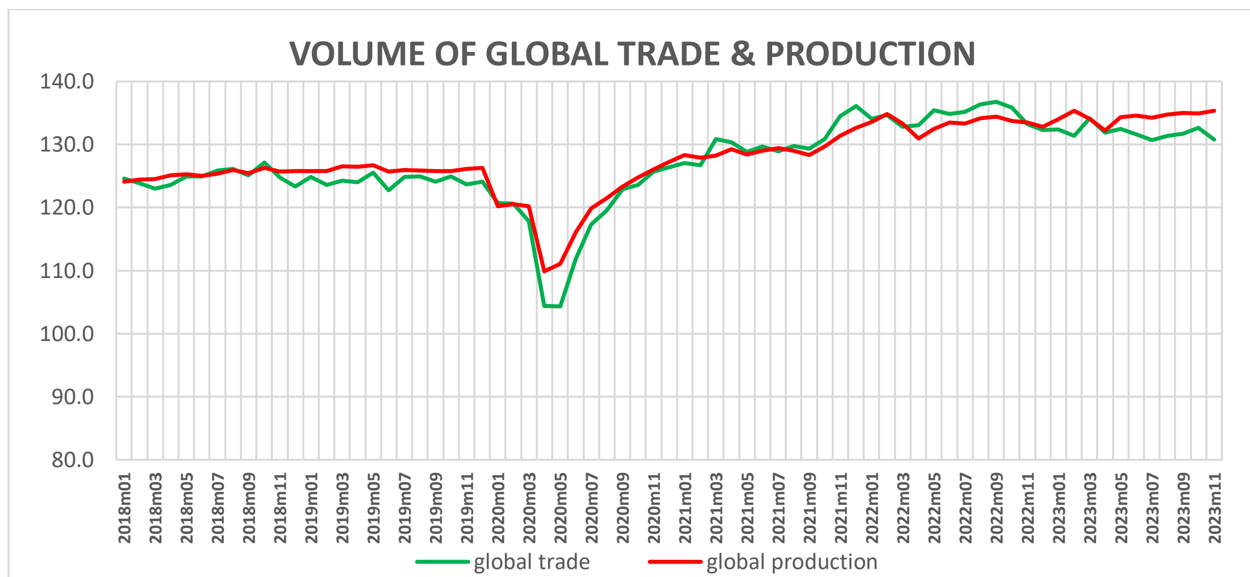
A PRELIMINARY ENQUIRY INTO THE RELATIVE PERFORMANCES OF THE US AND CHINESE ECONOMIES DURING 2023.

The papers submitted to Davos all pointed to geopolitical shocks threatening the world economy and its prospects, as being the major concern. In the vernacular, this represents the shock resulting from the economic war waged by the US on China. So how did the world's two largest economies fare in 2023?

To begin with it is always useful to examine the conflict between these two economies in the context of the state of the world economy as an expanding global economy tends to reduce frictions while a contracting world economy intensifies frictions. Below is the data provided by the *CPB Institute* based in the Netherlands which is one of the most comprehensive data banks for world trade and production. In Graph 1 we see a fall in global trade volumes and a slight increase in global production.

Graph 1.



(Source: CPB World Trade Monitor November 2023)

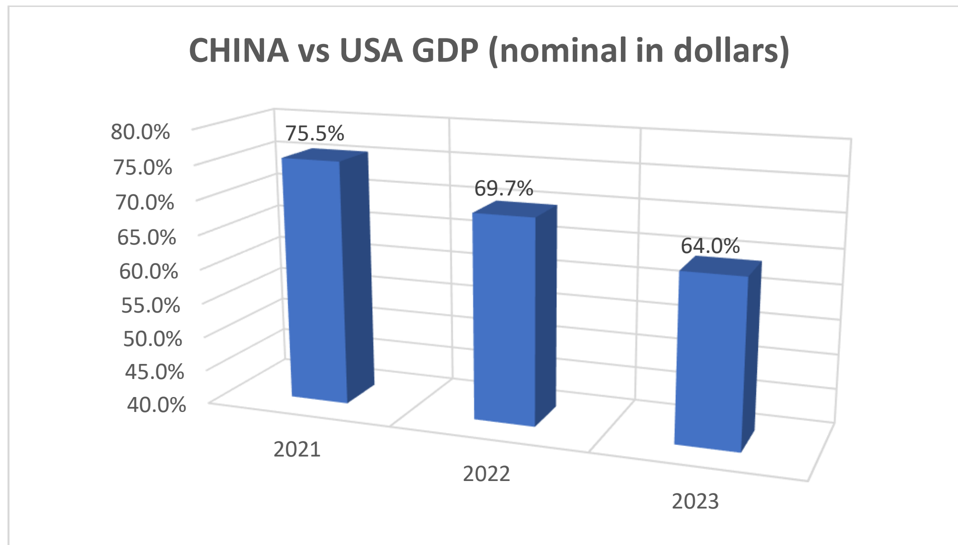
Compensating for the losses from the pandemic, current volumes of both are up <3% compared to 2019. This represents a stagnant world economy. The current flatlining being reminiscent of 2018-9.

The final observation is the fall in global trade below that of production. This is a function of the fracturing of globalisation as well as the growth of the Chinese economy absorbing imports for its own market rather than working them up in order to re-export them resulting in double-counting.

Comparing US and Chinese GDP.

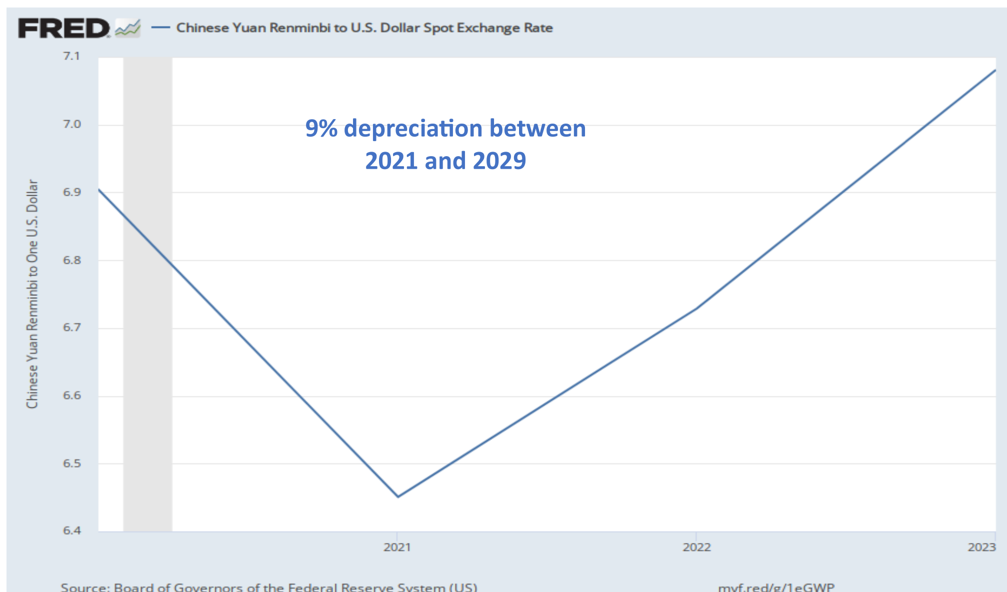
The first presentation will be in current US Dollars. When measured this way the US economy grew faster than the Chinese economy during the period 2021 – 2023. This was due to higher inflation in the USA as well as a stronger dollar. In this period measured by current dollars the US economy grew by 15.9% while the Chinese economy contracted by 1.7%. As a result measured in nominal terms and by current dollars, the Chinese economy shrank in relation to the US economy as Graph 2 shows.

Graph 2.



Of course this is confusing and therefore misleading. When re-interpreting the data in constant dollars, thereby excluding inflation, the nominal difference of 17.6% in favour of the US is reduced by 11.4% down to 6.2%, and when adjusting for the depreciation in the Yuan of 9%, the Chinese economy in real terms outgrew the US economy by 2.8% over this period.

Graph 3.



Nonetheless, as economies tend to be compared in current dollars, those who believe the US is *God's own Country* will no doubt claim the Chinese challenge, like the Japanese challenge before, is over. Certainly the Stock Exchanges in both countries believe it. In 2023 the S&P rose by 24% while the Shanghai bourse had a bad year falling 13.3%, a relative difference of 37.3%. However again a note of caution is in order. For the first time in 2023 the economic stressors moved from production to finance, with China experiencing a net outflow of foreign investment including in its share markets.

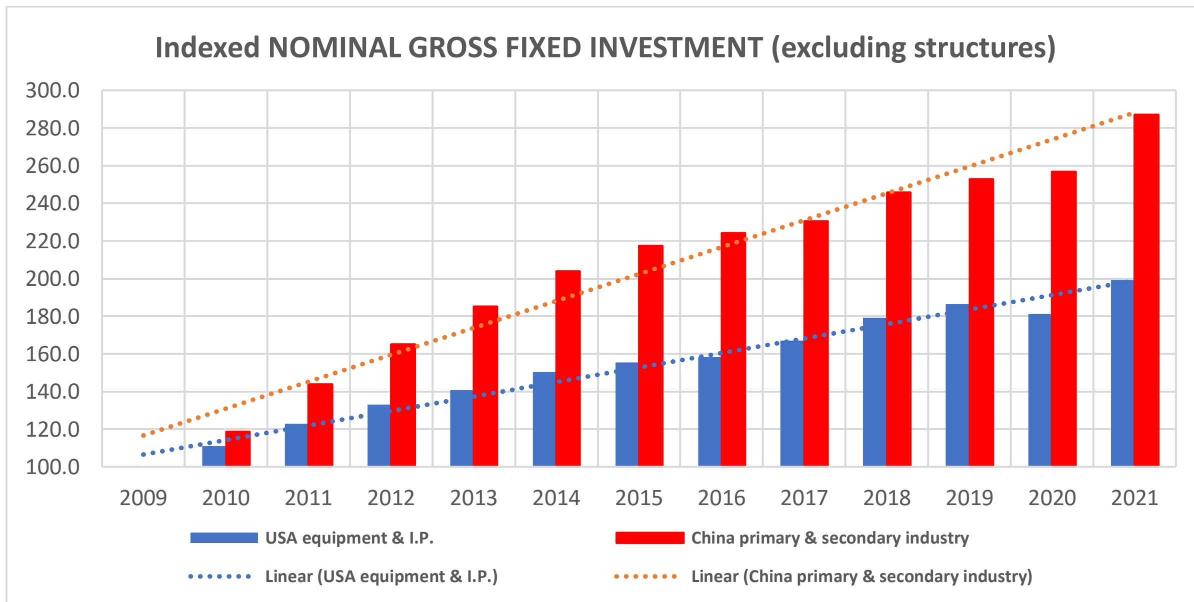
Graph 4. (Shanghai Stock Exchange)

(Source: CNBC)

A more granular examination.

The obvious starting point when comparing the two countries is there respective rates of investment. Here the value of investment continues to increase much faster in China than it does in the USA. Investment is the starting point because it represents the growing potential for any economy. Thus the much larger Chinese industrial economy will continue to achieve a greater and greater potential both absolutely and relatively when compared to the US economy, especially in terms of productivity.

Graph 5.



(Sources: Chinese Statistical Yearbook Table 10-4, BEA Fixed Assets Table 4.7)

Within the general investment found in China, there were significant areas which experienced faster investment and that was in the more advanced sectors. *"In 2023, the investment in fixed assets (excluding rural households) reached 50,303.6 billion yuan, up by 3.0 percent over the previous year, or up by 6.4 percent after deducting price factors. Specifically, the investment in infrastructure went up by 5.9 percent,*

manufacturing up by 6.5 percent. ***the investment in high-tech industries grew by 10.3 percent****, 7.3 percentage points faster than that of the total investment. Specifically, the investment in high-tech manufacturing and high-tech services grew by 9.9 percent and 11.4 percent respectively. In terms of high-tech manufacturing, the investment in manufacturing of aerospace vehicle and equipment, manufacturing of computers and office devices and manufacturing of electronics and communication equipment grew by* ***18.4 percent, 14.5 percent and 11.1*** *percent respectively. In terms of high-tech services, the investment in services for transformation of scientific and technological achievements and in e-commerce services went up by 31.8 percent and 29.2 percent respectively."* (My emphasis) This shows the efforts being made in China to overcome technical chokepoints as well as raising technical levels in those areas most subject to international competition. And it relates to the growth of its war economy.

Furthermore, much of the increase in value added was contributed by SOE's or state organised enterprises. *"The total value added of industrial enterprises above the designated size increased by 4.6 percent over the previous year. In terms of sectors, the value added of mining was up by 2.3 percent, that of manufacturing up by 5.0 percent and that of production and supply of electricity, thermal power, gas and water up by 4.3 percent. The value added of equipment manufacturing went up by 6.8 percent, 2.2 percentage points faster than that of the industrial enterprises above the designated size. In terms of ownership, the value added of the state holding enterprises grew by 5.0 percent, that of the share-holding enterprises up by 5.3 percent, that of the enterprises funded by foreign investors and investors from Hong Kong, Macao and Taiwan increased by 1.4 percent and that of private enterprises up by 3.1 percent. By products, the production of solar cells, new energy vehicles and power-generating units (power-generating devices) grew by 54.0 percent, 30.3 percent and 28.5 percent respectively. In December, the total value added of the industrial enterprises above the designated size grew by 6.8 percent year on year, or up by 0.52 percent month on month."*

Of course in the end the technical development within China is more consequential than developments in the property sector. While attention has been focused on its property sector, admittedly the largest single asset class globally, China has been investing heavily in its technical sector. Investment here is increasing at the rate of 10% p.a., much higher than the average investment rate.

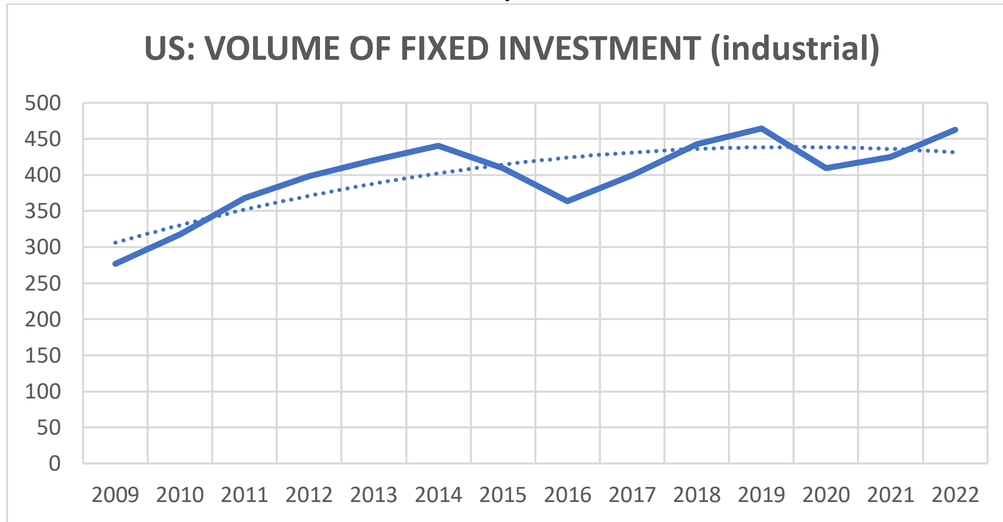
Table 1.

20-1 Basic Statistics on Scientific and Technological Activities

Item	2018	2019	2020	2021	2022
Statistics on R&D Input					
Full-time Equivalent of R&D Personnel(10 000 man-years)	438.1	480.1	523.5	571.6	635.4
Basic Research	30.5	39.2	42.7	47.2	50.9
Applied Research	53.9	61.5	64.3	69.1	74.1
Experimental Development	353.8	379.4	416.5	455.3	510.3
Expenditure on R&D (100 million yuan)	19677.9	22143.6	24393.1	27956.3	30782.9

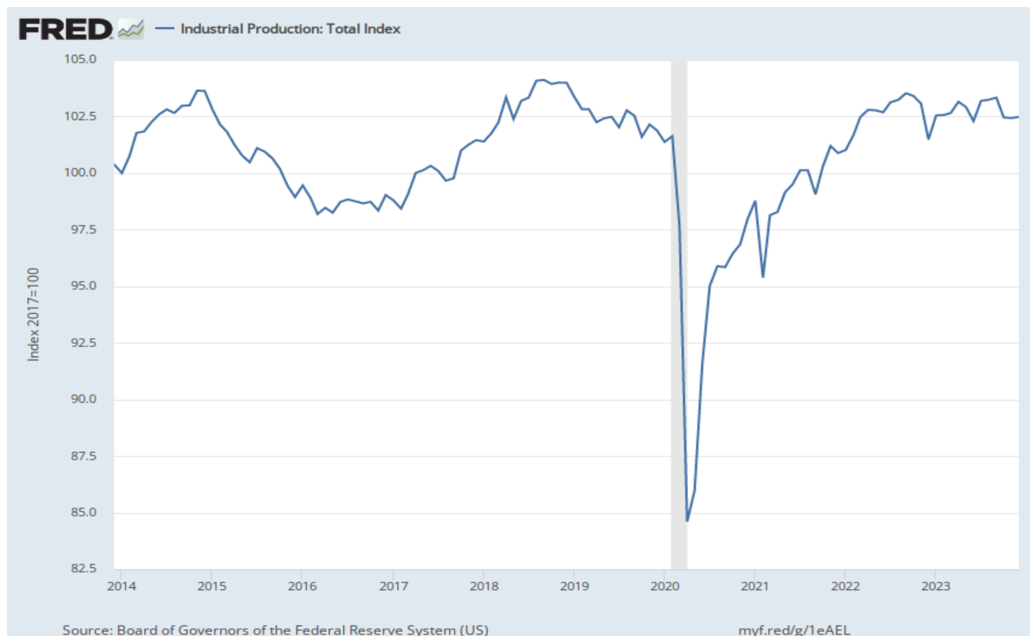
In the USA industrial investment continues to lag the rate found in China. The volume has grown by under 5% over 10 years or by less than the annual average achieved in China over this period.

Graph 6.



This is consistent with stagnant industrial production which has yet to reach 2018-9 levels.

Graph 7.



In addition retail sales continued to grow faster in China than in the USA or 7.2% vs 2.1%. However because of the appreciation of the Dollar, retail sales in China for 2023 amounted to $6.71 trillion at an exchange rate of 7.0 Yuan to the Dollar compared to the US figure of $7.25. Clearly in volume terms the Chinese retail market is far larger than the US one, which can be seen when applying PPP exchange rates.

Finally what about standards of living. *In terms of permanent residence, the per capita disposable income of urban households was 51,821 yuan, a nominal growth of 5.1 percent over that of the previous year and*

a real growth of 4.8 percent after deducting price factors. In the US pay went up by 4.3% against PCE inflation of 3.7% yielding a rise of 0.8% after deducting price factors. In comparative terms the per capita disposable income in the USA is around $20,580 which compares to the Chinese figure of $7,400 at an exchange rate of 7. Adjusted for purchasing power the Chinese figure rises to $10,900 or over half the figure for the USA. However, I remain sceptical about this rate of improvement in Chinese standards of living.

Given the deflation in both the retail sector and the producer sector in China I am also somewhat sceptical of the increases in the volume of income and investment found in China, as their strength would suggest price stability at worst, rather than falls. *Among the producer prices for industrial products, the price for means of production decreased by 3.3 percent, affecting the overall level of the producer prices for industrial products decreased by about 2.44 percentage points.* This is not a comment on the quality of data in China compared to the USA, merely an observation. In any case, readers of my site know I lament the deteriorating quality of US data ever since the economic war with China began.

Turning to the USA. Once again the empirical data does not support the exuberant GDP data, but is more consistent with the GDI or Gross Domestic Income data, which should match, but unusually has diverged for many quarters.

Profitability.

According to The Fortune Global 500, the top 500 corporations generated $41 trillion in revenues in 2022/3 and earned $2.9 trillion in profit. Of this $2.9 trillion in profit, the USA contributed $1.1 trillion versus China's $0.53 trillion. Profit per US corporation was even higher as it had 136 corporations in the top 500 compared to China's 145. This 2:1 ratio in favour of the US correlates to total corporate profits in the US vs China. The sizeable US profit was primarily due to the contribution by the top ten US corporations which contributed a staggering 46% towards the total of $1.1 trillion. The powerhouse sectors globally were Technology, Finance, and Energy which earned 63% of the $2.9 trillion global profit.

In terms of countries:

Graph 8.

Before departing the global profit picture a parting shot at those Marxists intimidated by finance capital and financialisation. Here are the top 5 sectors, with Finance equal to 30% of the top 5 total. Within the USA the financial sector only earned one eighth of all corporate profits. It is also worth pointing out from the report that much of the profits earned in global finance were contributed by the giant Chinese banks, the world's largest.

Graph 9.

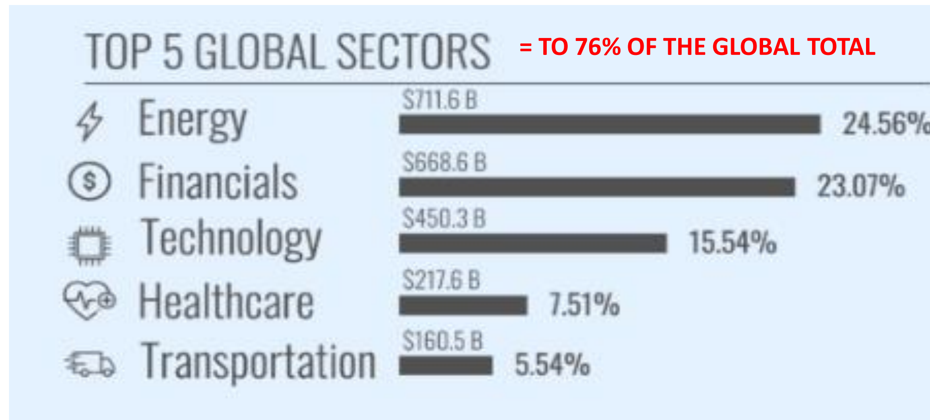


Table 2.

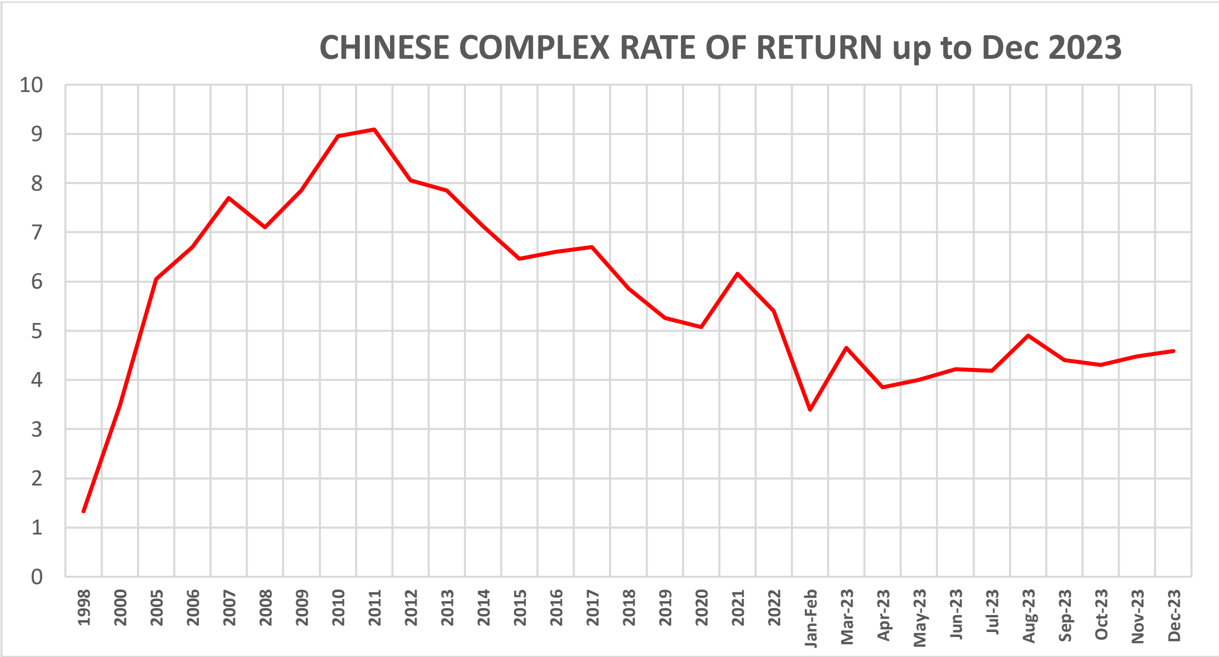
Rank	Bank name	Total assets (2022) (US$ billion)
1	Industrial and Commercial Bank of China Limited	5,742.86
2	China Construction Bank	5,016.81
3	Agricultural Bank of China	4,919.03
4	Bank of China	4,192.12
5	JPMorgan Chase	3,898.33
6	Bank of America	3,051.38

The effect at a more granular level of these extraordinary level of profits by a handful of US corporations can be seen in FactSet's most recent weekly report. "*Six of the seven companies in the "Magnificent 7" are projected to be the top six positive contributors to year-over-year earnings for the S&P 500 for Q4 2023: NVIDIA, Amazon.com, Meta Platforms, Alphabet, Microsoft, and Apple. In aggregate, these six companies are expected to report year-over-year earnings growth of 53.7% for the fourth quarter. Excluding these six companies, the blended (combines actual and estimated results) earnings decline for* ***the remaining 494 companies in the S&P 500 would be -10.5%*** *for Q4 2023. Overall, the blended earnings decline for the entire S&P 500 for Q4 2023 is -1.4%."* (My emphasis.) Thus the US economy is dependent on 6 corporations plus the expanding fiscal stimulus.

If -1.4% is the actual fall in profits this implies a fall in the non-financial corporate rate of profit below 7% for the first time since Q3 2020. This is still nearly 2% above its 2019 value. In contrast the Chinese Complex

Rate of Return which underestimates the rate of profit due to the inclusion of financial assets remains three quarters of a percent below its 2019 level. However while the US rate of profit is steadily declining that of China is gently rising from its low point this year. Methodological note: The monthly figures represent from January to that month, so December data is for the full year, January – December.

Graph 10.

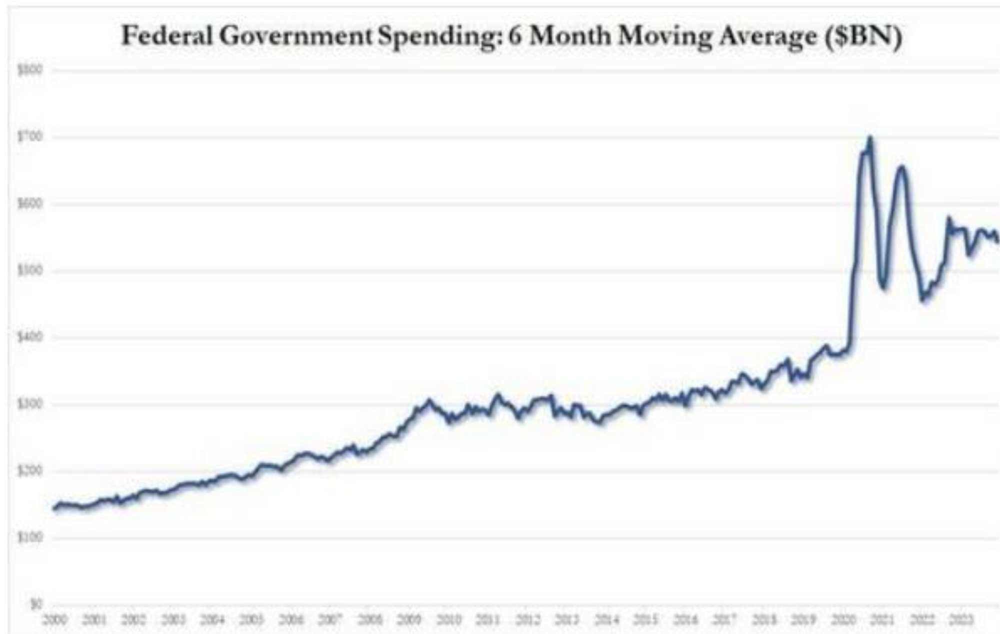


The unhealthy driver of the US economy.

Michael Roberts is quite wrong in his estimation of the drivers of the economy during 2023 in the USA when GDP increased 2.5%. Personal consumption contributed 2.2%, private fixed investment was down 1.2%, foreign trade did not contribute anything, but government spending contributed 4.0%. This data can be obtained from NIPA Table 1.1.1 when it is modified to provide annual rather than quarterly data.

In other words the biggest driver has been the fiscal deficit, the government spending more than it taxes. Why is this stimulatory? When the government borrows to cover its spending, its mops up idle hoards and converts it into actual spending by paying pensions and benefits, paying for health care, investments and so on (excluding interest payments most of which goes back into hoards). The current Federal spending of around $550 billion is up $150 billion per month compared to 2019. Earlier, this was equal to 22.3% of nominal GDP in 2019 ($21.521 trillion) rising to 24.1% of nominal GDP in 2023 ($27.356 trillion). This growth in fiscal spending can be seen in the graph below. Over the four years this contributed 5.6% to GDP in real terms compared to the 10.8% growth rate for the entire economy, or over 50% of the growth rate. Without it, annual growth would have averaged just 1.3%. Even real growth in 2023 of 2.5% would have reduced to 0.7% as confirmed by Table 1.1.1. However such a growth stimulus is unsustainable in the longer term as it cumulatively builds up debt.

Graph 11.



And weakness in the rest of the economy is consistent with all the granular data. Analysing the revenue for the year at the dominant railroad corporations - Union Pacific, CSX, and BNSF - we find volumes down over the year including inter-modal which deals mainly with consumer goods. The same applies to Cass Freight Index. On a y/y basis, the index declined 7.2%. UPS also released its earnings report this week. Here is the summary for the US segment. "*Revenue decreased 7.3%, driven by a **7.4% decrease in average daily volume**.*" (My emphasis) Volume declines for the year were even higher.

The same applies to the reports from many of the largest household names in the USA. Volumes were either down or flat which can be viewed here for Proctor & Gamble, and here for Kimberly Clark and here for Colgate Palmolive. In the case of North American sales by Colgate Palmolive volumes rose by 0.5% but interestingly this was way below the growth in its international sales. The same applies to: 3M, AT&T, and Verizon. Even at General Motors sales of motor vehicles for the final quarter was up by only 2,000 vehicles compared to the final quarter of 2022 though full year sales were higher.

What the preliminary data shows that during the fourth quarter, profit gouging via higher prices finally came to an end, 6 months longer than I anticipated. Average price rises currently appear to be in the 3 to 4% range compared to 6 to &% in the third quarter. This means profit margins will be squeezed and by the end of the first quarter of 2024 on current trends they would have fallen back from the heights achieved by a combination of Covid funds and supply chain blockages. It will be back to business-as-usual which means squeezing the cost price or what is the same thing labour.

This is confirmed by the Glassdoor Employee Confidence Index. This Index estimates how confident workers are for their company's prospects over the next 6 months. In the latest report, confidence fell to 45.6% from 47.5% in December, marking the lowest point since the Index started tracking in 2016. The main driver for the fall in confidence was the rise in firings and the fall in hirings. And of course we should

include the catastrophically bad batch of regional FED surveys which include New York, Texas, Kansas, and Philadelphia where employers' views mirrored their workers' dire view of current conditions.

Conclusion.

There are undeniable positives in the US economy centred around energy, and deep learning programmes together with the chips that drive them. But this could turn out to be a double-edged sword. Currently Wall Street is playing seven card stud poker. But again this cannot last. The *magnificent seven* or as I call them the *seven brothers* enjoy monopoly sized margins. In short they are sucking in profits from the rest of the corporations. But these corporations are their customers at the same time. As corporate America weakens, which it is, their ability to suck in profits will be diminished by their customers' unwillingness or inability to meet their terms. At that point the bluffing will end, and the showdown will commence. We await this week's financial reports where many of the seven will be revealing their current hands. At some point in 2024 the bluffing will end, and the showdown will take place.

I was of the opinion that the advantages the US enjoyed over China during 2023 would be short-lived. And so it has come to pass. In the latter part of 2023, despite the disingenuous GDP data, the US economy weakened. On the other side their was a relative strengthening of the Chinese economy. While the prospects for both are grim in 2024, primarily due to the weather, the US economy is the more fragile.

Brian Green, 30th January 2024.