

CHINA'S \$GDP TEMPORARILY OVERTAKES THE USA.

Donald Trump's credo appears to be: "not what I can do for the country but what the country can do for me and my family". The result is ineptitude spiced with recklessness. In the face of the pandemic, this comical combination has toppled the USA from its perch as the world's largest economy based on current \$GDP. The drums of war grow louder, Tik Tok, Tik Tok, Tik Tok.

This is part of the series assessing the balance of forces between the US and China. Comparisons between the dollar size of the Chinese and US economies is often a case of comparing apples with oranges. In my last post I indicated how the household sector and the non-profit sector had grown in the USA. Therefore, for comparison purposes we will be comparing GDP which excludes these sectors and government. In the US this is called Domestic Industry and In China it is called the "Three Industries Classification". For more information follow this link as well as for the Chinese GDP data used. http://www.stats.gov.cn/enGLISH/PressRelease/202007/t20200717_1776596.html

Using the data provided for the first six months, and at an exchange rate of Yuan 7 to \$ 1, the Three Industries GDP translates into \$13,046 trillion annualised. In the case of the USA the latest NIPA Table 1.13 provides a figure of \$14,003.2 at the end of 2019. Given the 10.8% contraction in GDP since then, it is likely that domestic business fell by the same amount. In that case Net Value Added (NVA) fell to \$12.515 trillion annualised. However, to provide equivalence, \$1.72 trillion (NIPA Table 1.14) of depreciation needs to be added back to bring NVA up to Gross Value Added (GVA) yielding a figure of \$14.235 trillion.

Although this is nine percent higher than China, the US figure is inflated by imputations. For example, housing inflates the size of the real estate sector located within domestic business due to the preponderance of owner-occupied rents (paying oneself a rent to live in one's own home) equal to 7.2% of GDP. This on its own covers the difference in respective GDPs. <https://apps.bea.gov/iTable/iTable.cfm?reqid=19&step=2#reqid=19&step=2&isuri=1&1921=survey> Then of course we need look only at the hideously wasteful expenditure on healthcare in the USA which results in the US spending three times as much on private healthcare compared to China which once again inflates Domestic Industry more than the Tertiary Industry in China.

Therefore, for all intents and purposes, adjusted for anomalies and duplications, China's real GDP has overtaken that of the USA. Will China maintain its top ranking? That depends on how quickly the US rebounds from the virus, if at all.

Profits. China versus the USA.

The National Bureau of Statistics of China recently issued its latest profit data. For the first six months industrial profit totalled Yuan 2.511 billion or \$358.7 billion at an exchange rate of 7 Yuan to 1 Dollar. http://www.stats.gov.cn/enGLISH/PressRelease/202007/t20200728_1778968.html The closest data set in the USA is non-financial corporations. Profit data for the USA covering the second quarter of 2020 are not yet out, but according to FactSet's latest release it looks likely that US second quarter S&P 500 profits will be down around 35%. Taking that figure, we can estimate that US pre-tax profits for the half year will be around \$418.5 billion. At \$418.5 billion, this is the closest the two country figures have been, with the US only 17% higher despite its continued monopolisation of strategic areas of the world economy. For the rest of the year FactSet expects profits to continue to fall in the USA but at half this rate. Nonetheless, the overall annual fall in non-financial profits looks likely to be 25%. https://www.factset.com/hubfs/Resources%20Section/Research%20Desk/Earnings%20Insight/EarningsInsight_073120A.pdf As Chinese profits turned positive in June, it is likely the gap between the two will be eroded in the future.

Those pesky retail sales figures again.

It is a source of dismay that BEA estimates have become so irregular. Inflated sales and employment figures making headlines, together with Central Bank monetary support, has created a toxic combination intended to keep the share markets aloft. It appears cold war adjustments have replaced seasonal adjustments. It is all reminiscent of the dying days of the USSR.

In an earlier posting I proposed examining US retail sales more closely through the prism of auto sales, its biggest component. This could not be done until auto firms released their financial statements showing both value and volume sales. These figures are now in. (To prevent references cluttering up the figures they are to be found at the end of this section.)

Thus, according to the official figures (1) retail sales jumped 7.5% in June. Within this auto sales for the first half of the year compared to the same period in 2019, fell by only 6.8% in Dollar Terms. The BEA on the other hand puts the fall at 13% in Dollar Terms or double that amount. (2). Once again two government departments, in this case the census dept and the commerce department, are at odds.

Both however are at greater odds with the data from individual firms as found on their investor relations sites.

General Motors (3)	-21.3% (Volume figures for all)
Fords (4)	-24.1%
Chrysler (5)	-39.8% (includes Canada)
Volkswagen (6)	-22.2%

Nissan and Toyota have issued similar volume falls. (Toyota's Q2 financial statement is still pending.) Only Mazda seems to have bucked the trend. It appears that overall, volume sales are down at least 25%. Last time I made the sarcastic comment that price rises may have compensated for volume falls because dashboards were inlaid with mother of pearl and wheel rims with 24 carat gold. However, this was not the case, volume falls were aggravated by price falls as well. Average prices fell by a quarter of a percent over the same period. (7)

If we assume that the realistic fall in value was at least 25.3% based on firms reporting, versus the 6.8% by the census bureau, then auto sales were inflated by at least 18.5%. This is equal to over \$100 billion as auto sales are 21.8% of total retail sales amounting to \$2600.5 trillion over this period (1). The effect of this difference would be to shave 0.5% off GDP growth and to deepen the fall in retail sales over the 6 months from 0.6% to close to 5%.

And this is only one industry amongst many. I also am concerned by ecommerce sales and whether returns are calculated accurately or simply logged as sales once they are resold. This has been particularly true over the Covid period when customers went online to buy things they normally tried on in brick and mortar stores before buying.

I remain concerned that Personal Consumption Expenditures, which includes retail sales, the driver of US GDP growth has been inflated over the last three years. This could explain in part why the USA has been the outrider, appearing to grow faster than its advanced capitalist competitors, when this may not have been the case, notwithstanding the bonanza on Wall Street.

(1)https://www.census.gov/retail/marts/www/marts_current.pdf#:~:text=The%20U.S.%20Census%20Bureau%20conducts%20the%20Advance%20Monthly,food%20service%20firms%20located%20in%20the%20United%20States.

(2) NIPA Table 7.2.3B. Real Motor Vehicle Output, Quantity Indexes

(3) <https://investor.gm.com/static-files/bbf9429a-3c44-4070-ae6f-f1f149bd86c5>

(4) https://s23.q4cdn.com/799033206/files/doc_financials/quarterly/2020/q2/Ford-US-Second-Quarter-2020-Sales-Results.pdf

(5) https://www.fcagroup.com/en-US/investors/financial_regulatory/financial_reports/files/FCA_NV_2020_06_30_Semi-Annual_Report.pdf

(6) https://www.volkswagenag.com/presence/investorrelation/publications/interim-reports/2020/HY_2020_e.pdf

(7) NIPA Table 7.2.4B. Price Indexes for Motor Vehicle Output

Conclusion.

We are living through one of the defining periods of history. Some historians claim that the US became the largest economy in the world in 1871. Others say only 1916, because in that year US GDP overtook that of the British Empire. Thus, the US has been the largest economy for over a century and the dominant economy since 1943 or over 75 years.

Its rise was prepared by some masterful diplomatic moves. It stayed aloof from the battles in Europe in the First World War (not a true world war) allowing Britain, France and Germany to bleed each other white. It only intervened when it looked likely the Germans would capture Paris and emerge victorious. In the Second World War (a true world war) it physically crushed Japan, invaded Europe to manage its affairs, and above all, bankrupted the British Empire through Lend Lease, toppling the Pound as the world's pre-eminent currency.

It is unlikely that China will have such room to manoeuvre in a world dominated by nuclear weapons and an urbanised international working class. Nevertheless, China is playing for time. It recognises that time is on its side and against the USA. It thus absorbs the blows and insults reigning down on it from the USA, with only sufficient retaliation to indicate to the USA and its English-speaking allies that it will not bend the knee.

But this will not prevent the USA from driving for war. Without its economic hegemony and that of the dollar, the USA will be a giant Italy, no more no less. The US has everything to gain from war and nothing to lose, which is what makes the period so fraught. A collapsing empire is like a wounded animal, at its most unpredictable and dangerous.

Brian Green, 1st August 2020.