

# China vs. the USA for Global Economic Dominance

James A. Kyrios / Originally published by [LA Progressive on May 15, 2021](#)

## **“When China awakes, the world will tremble”- Napoleon**

We had taken it for granted that the USA would continue to be the dominant economic power in the world as it had been during our lifetime. With the demise of the Soviet Union some thirty years ago, we breathed a sigh of relief.

China was starting to rise and we thought that if it became more prosperous it would become more democratic and cooperative internationally. We took steps to help China become more prosperous and China has spectacularly succeeded in becoming a powerful economic force in the world. But it has not become a more democratic and free society. To the contrary, it seems to be bent on becoming more authoritarian. President Joe Biden has recently said that he knows President Xi very well and that Xi does not have a democratic bone in his body.

The fear now is that China may soon eclipse the US in economic prowess and show the world that our brand of capitalism is not the wave of the future. We not only face an economic threat, we now also face an ideological threat and, in a worst-case scenario, a threat to our security either through cyber warfare or actual warfare. We even face the threat that the US may be a nation in decline and that Democracy is not the best form of government. This is what President Xi of China believes and he is not shy about saying so.

There is no doubt that past Presidents going back to the first President Bush, Clinton, Bush 45 and Obama had good intentions. They believed fervently in globalization and thought that China would benefit by becoming part of the global economic order. They thought correctly that China's economy would grow and prosper. They were willing to give China certain advantages that would help it grow. It did not hurt at all that these advantages would benefit major global corporations many of which were headquartered in the United States. In giving China certain advantages, they hastened outsourcing which in part led to large swaths of unemployment and the demise of the manufacturing base of the United States. One of the “tradeoffs” was lower consumer prices for American consumers since China could produce products much more cheaply than those manufactured in the United States.

Another effect of this faith in untrammelled globalization has been a deep political reaction which may very well have contributed to the rise of Donald Trump. He understood that, directly or indirectly, China (and of course other countries) was a threat to industries in the US and to the guy in Kansas who no

longer could get a job. He recognized a problem but as of today, there is no satisfactory solution. As will be shown later, our trade position with China is no better than it was five years ago.

## “Advantages” We Bequeathed to China

What were some of the “advantages” which we bequeathed to China? We allowed them to enter into the World Trade Organization but gave them advantages with respect to trade and investment opportunities. It is easy for everyone to understand that China would have an advantage on trade if its workers were paid a fraction of what the US worker received in salaries. Chinese consumer products flooded the US market at very good prices for the US consumer. To some extent, this opening of the US market to massive imports contributed to a lower rate of inflation in the US and was welcomed by consumers.

In a balanced, free trade environment, US goods would be sold to China as easily as Chinese goods are sold in the US. The US has excelled in making high quality sophisticated, technological products. However, we allowed China to erect trade barriers which made it difficult if not impossible to sell goods in China. In effect, China to a great extent was closed to many US exports. The economists are always touting the benefits of free trade but what occurred was not free trade at all—it was unfair trade to the benefit of China and to our detriment. To a great extent we allowed China to have this advantage and you cannot blame them for taking advantage of the situation.

There is also the question of international services. For example, Chinese-owned companies in the United States perform services for which they get money from the US with some of it being sent to China. Conversely, US companies in theory at least, can do the same thing in China. But because of existing laws and regulations, the Chinese market is much more closed to us than the US market is to the Chinese. Of course, this is blatantly unfair. A few examples will illustrate this point:

- There is a sharp limit on the number of US films which can be shown in China. There is no similar limit to the number of Chinese films which can be shown in the US.
- Major banks from China have a much greater presence in the US than US banks have in China.
- It is much more difficult and cumbersome for US companies to set up shop in China than it is for Chinese companies to set up shop in the US.
- Chinese investors and companies have many more opportunities to invest or even control US companies than the other way around.

No matter how you look at it, the rules of the game which have been allowed by the US do, in fact, favor China. These rules were put into effect many years ago when it was thought that China had to be given advantages because it was so far behind there was a legitimate (at the time) fear in China that American companies would dominate China.

## What Has Resulted Is Bad Business

The net result of all this has been that for years, to put it in laymen's terms, commercial interactions between the US and China have greatly benefitted China as the results clearly show (see later). If China and the US were companies you could say that there has been a large and persistent transfer of cash from the US to China. Companies which run out of cash need to borrow money or obtain more funds from owners (equity) and companies which have a surplus of cash can invest their money.

This is roughly what has happened to China and the US over time. With its surpluses, China has been able to finance US deficits by buying US government and other bonds. It has also had the funds to make debt and equity investments not only in the US but also in the rest of the world. In the old days, it used to be said that the US was banker to the world. To a large extent, this can now be said of China. China is a major investor in places like South America and Africa. These investments reap dividends and interest and make China even more cash rich.

At this point, I would like to introduce a few concepts from international finance and economics.

**Balance of trade** – this is the difference between exports of goods and the imports of goods. In 2020, our trade deficit with China was \$310.8 billion which, of course means that this figure was China's trade surplus with the US.

**Current Account** — as noted above, there are also money flows related to services and furthermore related to financial transactions (i.e., interest and dividends). The British call these items "invisibles" because they relate to money flows for transactions not readily visible like say the sale of shoes. For many years the US had a marked advantage in invisibles. The positive invisibles are now starting to diminish for the US and the negative invisibles are starting to diminish for China as China develops a more sophisticated economy.

Current account figures for 2020 between the US and China are not yet available. However, on a world-wide basis, China has a current account surplus of \$330 billion while the US had a \$687.7 billion current account deficit. China's surplus is the largest in the world and the US deficit is also the largest in the world. The US current account deficit consisted of a negative \$904.6 billion in trade and positive \$216.9 billion in invisibles. The US, with companies like Google, Facebook, Apple, Amazon and Microsoft is pre-eminent in services. China is still more of a manufacturing country as shown by the composition of its current account surplus of \$330 billion—trade surplus of \$535 billion and an invisibles deficit of negative \$205 billion. However, China continues to decrease its invisibles deficit over the years as it becomes a more mature economy.

Some economists like to say that having a trade and current account deficit is not such a bad thing if the country can offset this by investments from abroad. This is in fact what has happened with the US. Investments from abroad in the US are a big plus in the sense that the country is considered worthy of investments. Where would you like to put your money- in the US or in China? It appears that Chinese as

well as Americans feel that America is the better choice. In the US there are deep and well-established money and capital markets and the laws of the nation protect investors. The same cannot be said of China.

Also, the issue of unfair trade practices is important and includes the fact that the Chinese government subsidizes state owned companies to take over foreign companies with the effect of stealing their technology and further driving out competition by selling their products at below cost. (See Wall Street Journal May 7, 2021 "China Sidesteps Tariffs with Overseas Factories").

Clearly there are problems on the economic front when a government can use its muscle to subvert markets in other countries and sidestep tariffs.

### **Current Account Deficits are Not Sustainable**

There is a weakness to the position of some economists that current account deficits are not necessarily a bad thing. The problem with this type of thinking is this: at what point will a surplus country like China start controlling or even have an undue influence on US assets? This is not only an economic risk, it can also be a political risk. Are we happy with the fact that China is getting so cash rich that it can buy the world? China now owns Greece's largest Port in Piraeus and it also owns one of that country's major utilities. It is making strategic investments in Africa and South America and even, to some extent, supporting the government of Venezuela.

These are serious economic issues. They can also be serious political issues.

The Trump Administration reacted by setting up a system of tariffs and trade blocks which were countered by China. Unfortunately, our trade position with China has not materially improved. As a matter of fact, the US current account deficit increased from \$481 billion in 2016 to \$687.7 billion in 2020. It is perhaps unfair to single out 2020 because of the distortions of Covid. Let's look at 2019 as compared to 2016. In 2016, the US Current Account Deficit was \$481 billion and this increased to \$498.4 billion in 2019. Therefore, the policies of the Trump Administration, which clearly identified the problem, did not make a dent in solving the problem.

### **What does this all mean in simple business terms?**

If the US and China are looked at as businesses as mentioned before, it is obvious to see that China is generating cash and the US is bleeding cash from its basic business. This reminds me of a conversation I had many years ago with my Father who owned a Delicatessen in Chatham, New Jersey. One day when I was a teenager, I was in the back of the store when the accountant had finished the books and proudly announced to my Father that the store had made a profit of whatever amount. After the accountant left, my Father looked at me and said in effect that the accountant did not really understand his business at all and he (my Father) did not particularly care about the niceties of accounting. I will never forget what he said next: "If on most days, there is a lot more money in the cash register at the end of

the day than at the beginning of the day, I know I am doing pretty good.” That’s right. Cash is King. China knows that and it is doing what any good business person knows needs to be done.

At the end of the day, my Father would walk to the bank and deposit his cash. What do you do when you have cash? You can spend some of it and you can invest some of it. What do you do when you are bleeding cash? You have to borrow more if you can or you have to get someone to give you more cash by taking an ownership interest in your assets.

A big business that is bleeding cash needs investments (whether debt or equity) from others. A big business that has a surplus of cash can make investments. This type of thinking applies to countries too. China knows this all too well and as President Biden recently said it is “eating our lunch”.

The numbers show very clearly that we have an economic problem internationally and China does not. I do not know what the precise answer to this problem is but it must be solved or else the United States of America will lose its position of pre-eminence in the world in the future.

The United States of America has now been running Current Account Deficits for over 20 years and it is now doing it at record levels.

### **What can the US do now to improve its international economic situation?**

The growth of China in the last 30 plus years has been remarkable. China is now an economic superpower. It is also a threat to the US. The economic relationship between China and the US is one sided. It is most likely unsustainable.

The US and China to a very great extent are economically dependent on each other. China needs to open up its markets to products, services and investments to the outside world including the US. This can be done peacefully, or it can be done in a more “hostile” manner whatever that might mean.

Any future system has to take into consideration that free trade, but unfair and unbalanced trade is not sufficient. There must be fair trade and there must be an agreed-upon set of rules regarding openness of markets. There cannot be one set of rules for China and another set of rules for the US. To the extent that this has been the case, it is our fault for allowing it.

President Xi is no doubt a highly intelligent man. He must know that the current economic relationship between the US and China is unsustainable. Diplomacy is better than hostility and certainly better than war — whether cyberwar or the old-fashioned kind.

### **Obama’s Answer to the Problem**

The US did have an answer during the Obama Administration. It was called the Trans-Pacific Partnership (TPP). Because of political considerations both Hillary Clinton and Bernie Sanders came out against the TPP during the Democratic primaries in 2016 Presidential campaign. During the Presidential

campaign, both Hillary Clinton and Donald Trump were against the TPP. On his first day in office in January 2017, President Trump signed a statement explicitly abandoning the TPP.

The TPP became unpopular in certain circles because of a reaction to globalization which supposedly led to an outsourcing and the loss of American jobs. It was supposedly pro-business.

What did China think about the TPP? Because of my contacts in international banking and finance, I know firsthand that the Chinese were very threatened by the TPP. Perhaps better than most Americans, they realized that the TPP was a very clever Trade Agreement which would benefit various countries including the US and which would limit China's ability to continue to circumvent international trade norms. One of my friends told me that the Chinese were deeply troubled (the term used was much more graphic and not something printable) at the prospect of countries surrounding China joining this free trade group. The TPP was a very clever way of containing China economically!

When the danger was over, the Chinese wasted no time in organizing trade agreements all over the world. This included Regional Comprehensive Economic Partnership (RCEP) which was signed on November 15, 2020 by 15 countries in Asia and the Pacific. According to the Wall Street Journal (November 16, 2020 article entitled "Asian Countries Forge Trade Pact"), the RCEP "...creates a regional bloc that covers around a third of global economic output. The accord poses an early test for the incoming Biden administration...". The US is not part of the deal. The deal is more limited in scope than the TPP. The RCEP could be ratified as early as January 2022. It is hoped that the RCEP will revive American interest in the region and in reconsidering the TPP.

In addition, the 11 countries that were to be signatories of the TPP with the United States continued to negotiate the agreement without us. This led to the "Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTTP) signed in March 2018. There is room for others to enter this Agreement including the US and China.

Perhaps more disheartening is the fact that the European Union (EU), despite pleas from the incoming Biden Administration, finalized an investment agreement designed to also increase trade with China on November 30, 2020. The "Comprehensive Agreement on Investment" would open up the largest single market in the world to China. This can be perceived as a "slap in the face" by the EU to the US. However, it now has appeared that China has overreacted to criticisms (by the US, the United Kingdom and the EU) of China's alleged human rights abuses in the country's Xinjiang region. China's retaliation included sanctions of 10 EU politicians. There is now serious doubt that the agreement will be ratified by the European Parliament.

### **Can and should we resurrect the TPP?**

This certainly seems like an opportune time to resurrect the TPP. President Biden said he was open to entering the TPP but there would have to be certain changes including more protection for labor and the environment. According to The Council on Foreign Relations (see [www.cfr.org](http://www.cfr.org), article entitled

“What’s Next for the Trans-Pacific Partnership?” by James McBride, Andrew Chatzky and Anshu Siripurpu, updated February 1, 2021): “The goal of this megaregional deal — one spanning several continents and covering some 40 percent of world trade — was to create a fully integrated economic area and establish consistent rules for global investment. For Obama, the pact was a means to ensure that ‘...the United States—and not countries like China—is the one writing the century’s rules for the world’s economy.’”

## What does the TPP do?

The TPP was certainly ambitious and was to be the largest regional trade deal in history. In an article by Kevin Granville (“What is TPP? Behind the Trade Deal that Died”- see [NYTimes.com/interactive-](https://www.nytimes.com/interactive/2017/01/23/business/tpa.html) updated Jan. 23, 2017), a business editor of the New York Times explains that the TPP would have set the terms of trade between the US and 11 other Pacific Rim nations. The 11 other nations are: Canada, Japan, Mexico, Vietnam, Brunei, Malaysia, Singapore, Peru, Chile, Australia and New Zealand. The group including the USA, with a GDP of about \$28 trillion would represent about 40% of the world’s GDP and about one-third of world trade. “The goal was to bind Pacific nations closer through lower tariffs while also serving as a buttress against China’s growing regional influence. An independent study said that it would raise incomes and exports in the United States, but not jobs over all.”

According to Mr. Granville, the TPP was divisive because it was perceived to be a gift to business and would encourage more outsourcing. It was also accused of encouraging higher prices for pharmaceuticals by spreading US standards for patent protection to other countries.

Mr. Granville further explains that the TPP addressed “...a number of festering issues that have become stumbling blocks as global trade has soared, including e-commerce, financial services and cross-border internet communications.” The TPP would also have dealt with more traditional trade issues including establishing formal trade agreements with Japan, Malaysia, Brunei and Vietnam while also strengthening NAFTA, the then current agreement with Canada and Mexico. “In short, the pact was an effort to create a Pacific Rim free-trade zone.”

Mr. Granville lists and explains the following specific benefits of the TPP:

- Level the playing field by imposing rigorous labor and environmental standards on trading partners and supervision of intellectual property rights.
- Countries would agree not to block transfers of data online across borders
- Enhance opportunities for service industries which “...account for most of the private jobs in the American economy.”

Thomas Friedman, the well-known columnist of the New York Times was and is a big fan of the TPP. Before the TPP “died” in 2017, Mr. Friedman wrote an article pointing out the major positive aspects of the proposal. (See “Let Trump Make Our Trans-Pacific Trade Deal”, New York Times March 16, 2016). He pointed out that “...since 80 percent of the goods from our 11 TPP partners come into our country duty-free already, if we eliminate 18,000 tariffs, we’ll be able to keep more production at home and sell

more abroad.” He noted that “our workers can compete if we level the playing field....our average applied tariff is already 1.5 percent while the tariffs of these Pacific countries can range much higher—Vietnam has peak tariffs of over 50 percent on cars and machines—so if we get rid of those tariffs our exporters are poised to benefit.”

Here are the major benefits of TPP according to Mr. Friedman:

- The other 11 TPP countries would agree to give workers the freedom to form independent trade unions. This would include also adoption of laws on minimum wages, hours of work and occupational safety and health.
- Custom duties for digital products which are a major growth area for the US
- Take steps to halt human trafficking.
- Put restrictions on state-owned companies which compete with our private businesses.
- Criminal penalties for stealing our industrial secrets.
- Strong intellectual property protections for America’s software industry which is one of our major expert assets.
- Take an approach to pharmaceuticals which “...splits the difference between what the big drug companies want in the way of intellectual property protections for their products and what generic manufacturers want.”
- Combat trafficking in endangered wild parts and end all subsidies which encourage overfishing.

Friedman predicted that “...if we walk away from the TPP all our friends in the Pacific will just sign up for China’s R.C.E.P., or Regional Comprehensive Economic Partnership, which will set trade rules in Asia and include weak intellectual property protections, no labor or environmental protections and no disciplines on state-owned industries.” Unfortunately, Mr. Friedman’s prediction has come true.

### **But there is still a chance**

We have all read that the Chinese think that America is a declining power. It certainly does not help that we are, as a nation so politically polarized. We need to understand that the enemy are not other Americans. We are engaged with China in an economic and ultimately ideological battle for supremacy. We need to take another look at the TPP which according to many economists and experts is a good way for the US to reassert itself as the dominant power in the world. The basic idea behind the TPP is that there should be a level playing field.

### **But what are the problems with the TPP?**

Although the TPP would benefit the US overall, it may have negative effects on the manufacturing sector. It will not satisfy certain workers and labor unions to tell them that the TPP will benefit certain sectors of the economy (e.g., farm exports and intellectual property type exports) but be damaging to other industries. There were political repercussions in 2016 and there could be more if the TPP is revived.

- Larry Summers, President Clinton's Secretary of the Treasury believes that the TPP benefits higher income workers and penalizes lower income workers and would therefore increase inequality.
- The Trade Agreement could result in certain financial services regulations being superceded.
- It is unclear to what extent the TPP would improve the US trade position which is highly negative. One of the arguments against it was that it would encourage more outsourcing by US companies and increase the trade deficit while leading to the loss of more manufacturing jobs. It seems clear however that the TPP would significantly improve our services positions. But this would benefit huge companies like Apple, Amazon, Microsoft, Facebook and Google. To what extent would it help the average worker? This has to be better understood because the acceptance of a TPP-type Agreement is ultimately a political matter.
- In addition, there is a provision which would allow companies to avoid US courts and be subject to international arbitrators. This could be troublesome and could be a "deal breaker".

### Let's End on a Positive Note

Martin Wolf, the Chief Economics Commentator for the (London) Financial Times, has written an interesting and informative article ("China is Wrong to Think the US faces decline", April 28, 2021 issue of the FT).

"Its economic assets are too great, and while America could falter, that would be its choice and not its fate." Here is what he explains are our big assets, especially in economics:

- We have been the world's most innovative economy for more than 150 years and remain so today.
- Seven of the ten most valuable companies in the world and 14 of the top 20 are US companies. This list includes Apple, Microsoft, Amazon, Alphabet (Google) and Facebook. China only has two companies in the top 20 (Tencent and Alibaba).
- We have 12 of the top 20 technology companies while China has three.
- In Life Sciences, the US has seven of the top 10 and 11 of the top 20. China has none.
- US companies are globally dominant and almost all the valuable firms outside the US belong to allied countries.
- The US is the world leader in venture capital.
- We by far have the best universities in the world. Half of the top 20 universities in the world are in the US and only one is in China. Wolf comments that centralized control, as it exists in China, "never fosters sustained originality".
- I will add to this list by stating that the most important banks in the world are primarily US banks and this includes commercial as well as investment banks. The money and capital markets in the US are unparalleled and the envy of the world.

Wolf notes that "a great US asset has been its ability to attract the world's best and brightest. Two men born in India now run Microsoft and Alphabet respectively".

He ends his column by stating: "The US is unlikely to remain the world's dominant power, simply because China's population is over four times bigger. Yet, provided the US remains democratic, free and open, it has a good chance of staying the world's most influential country far into the future."

Wolf does not mention that the overwhelming majority of world trade is conducted in US Dollars with just a miniscule amount in Chinese Yuan. When there is trouble, money from all over the world inevitably winds up in the US investing in safe securities especially US Government Bonds. The US dollar is the only reserve currency in the world. In the old days, countries settled their obligations in gold. Today, countries settled their obligations overwhelmingly in dollars. When we speak of cash in an international setting, we are speaking about US dollars. This is not about to change in the near future.

## Summary

It is clear that the US is bleeding cash while China is generating cash. This is not a sustainable situation for our country. In plain English, this is not good business. We need to figure out how to make our country competitive internationally. Our problems are self-induced and not the result of some fundamental economic weakness in the country.

Our economic problems are ultimately political problems which need to be solved. I may be old fashioned but I still believe what Warren Buffett says: "Don't bet against America".

Whether some form of the TPP is appropriate, I cannot say. This is a good starting point and we can see what is beneficial economically and possible politically.

Americans must sooner or later come to realize that our foe is not our neighbor who has a different political opinion. Our real foe is a surging China which does not care at all about freedom and democracy. We all need to wake up before it is too late.

We have had challenges before, and we have shown what we are made of. Let's show Mr. Xi that he does not understand the United States of America. As always, the world is counting on America. We must not fail future generations here and in the world. It is time for America to wake up.