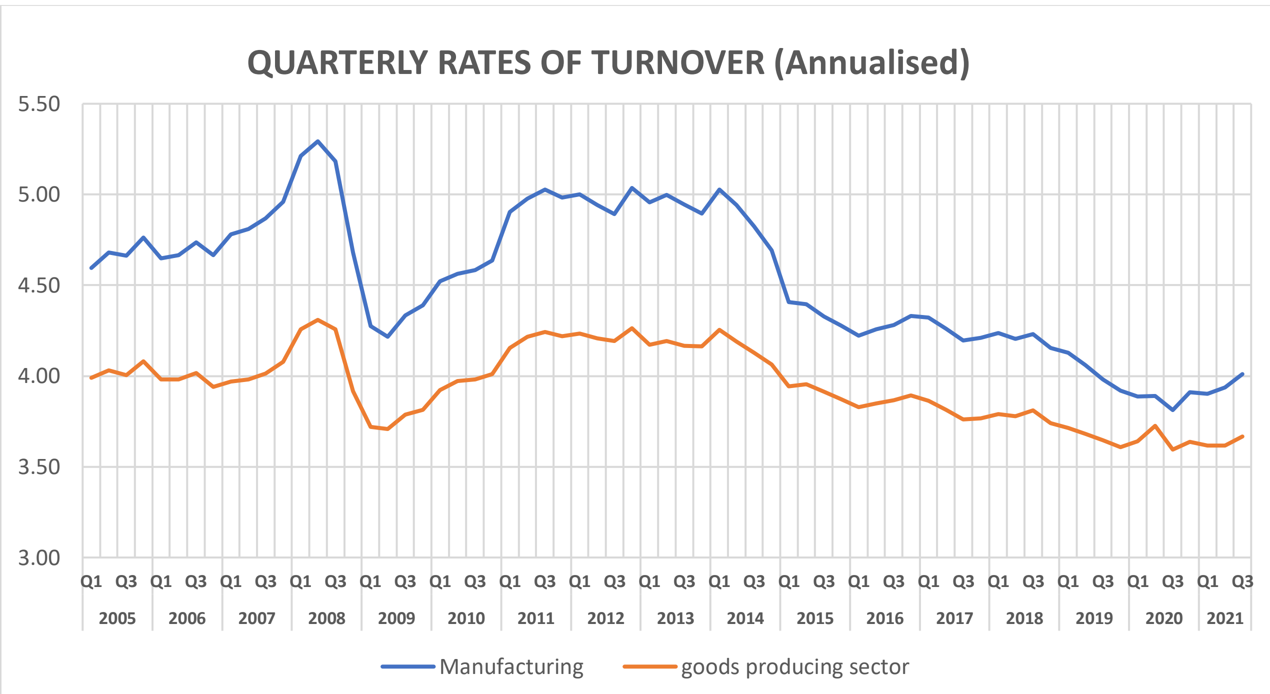
US THIRD QUARTER DATA AND PROSPECTS FOR 2022.

Data released by the BEA on the 22nd December allows for an estimate of third quarter turnover. Additionally the third release of GDP together with the final release of corporate profits on the same date allows for the updating of profits and the rate of profit for the corporate sector. Finally, high frequency data plus bank assessments are used to predict the direction of the economy in 2022.

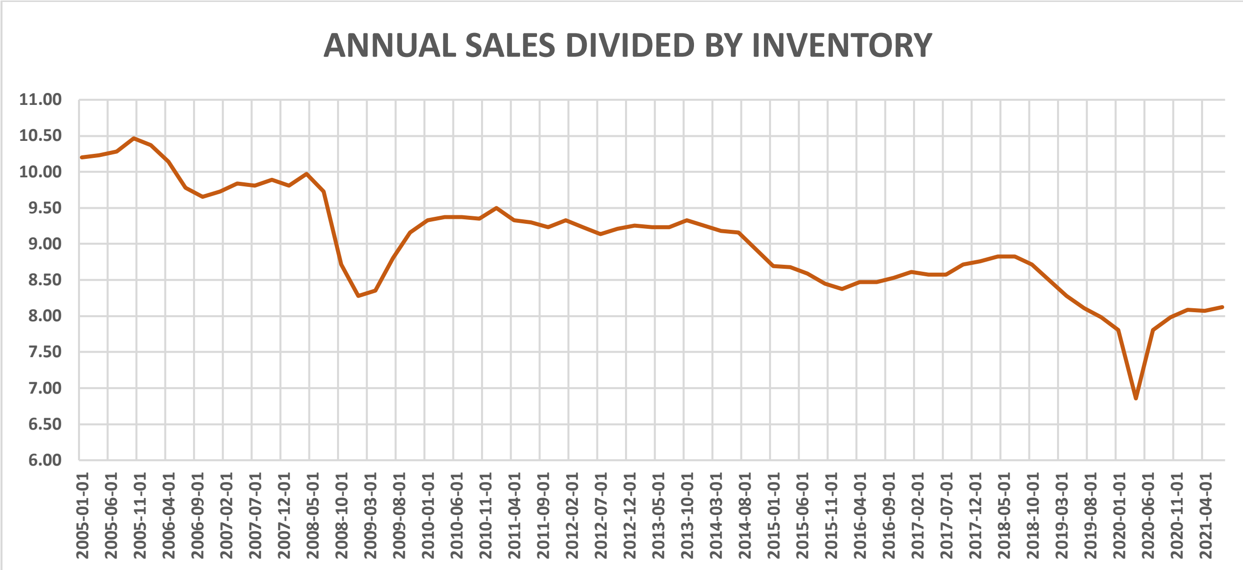
As usual we begin with the quarterly rates of turnover (annualised) for the manufacturing and total goods producing sector. We note there has been an acceleration in the rate of turnover during 2021 consistent with heated demand for goods and a shortage of inventory. (All data and calculations can be found in the two attached spreadsheets.)

GRAPH 1.



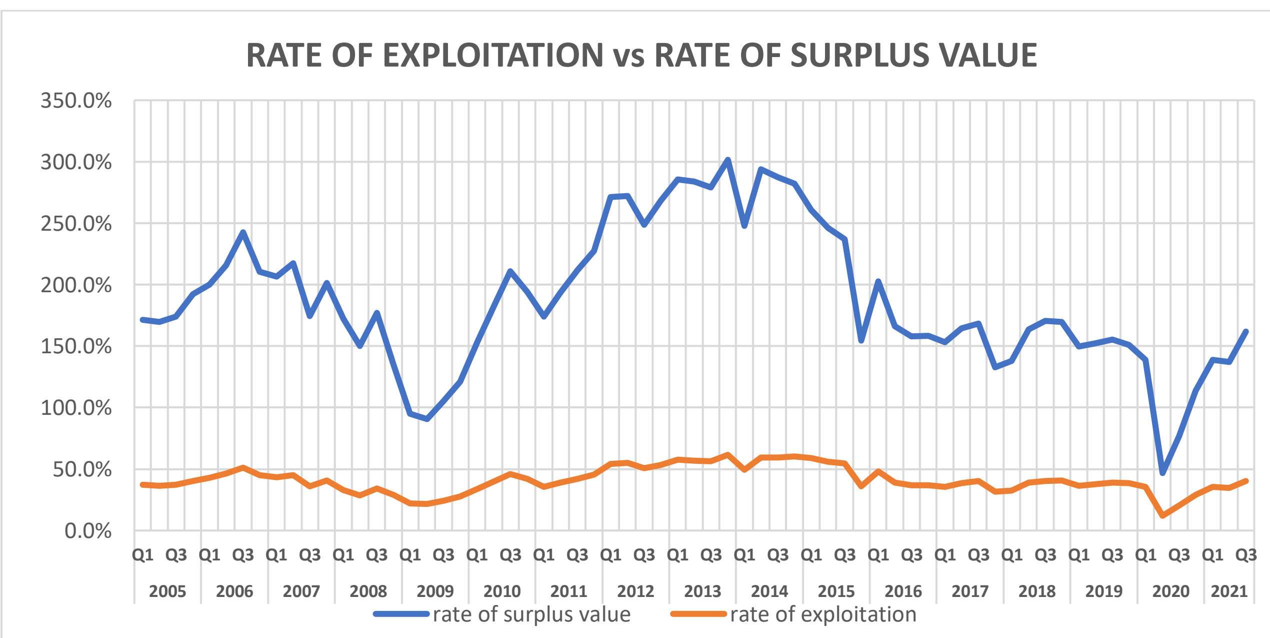
Turnover which bottomed in the third quarter of 2020 has accelerated by 5% to regain its 2019 levels. At roughly 4, turnovers are still 20% below the levels that obtained before 2014. In terms of period, and therefore days, the duration has risen by 18 days from 73 days to 91 days for manufacturing. The turnover trend can be compared to Graph 2 below which is the inverted 'inventory to sales' ratio for the manufacturing sector. (FRED Table MNFCTRIRSA) The profiles corroborate one another and only differ in the lead up to 2008. But together with Graph 1, it confirms that the Financial Crash did not have its origin in industry. By the time of the crash, the industrial (business) cycle was less than five years old as demarcated by the dotcom crash and sales remained bouyant.

Graph 2.



Obtaining the rate of turnover makes it possible to convert the rate of exploitation into the rate of surplus value. This is done by converting annual wages into variable capital by dividing wages by annual turnovers. Thus the annual wage bill for manufacturing in 2019 was $920 billion while turnover was 3.92, yielding variable capital of $235 billion, a big difference. (NIPA Table 2.2B for wages and Table 6.16D for profits.) Please note the ratios here are profits ÷ wages (brown graph) or profits ÷ variable capital (blue graph.) In these graphs we are not using annual compensation which includes items such employer paid health care. Annual compensation would be better, but it is not available at this time.

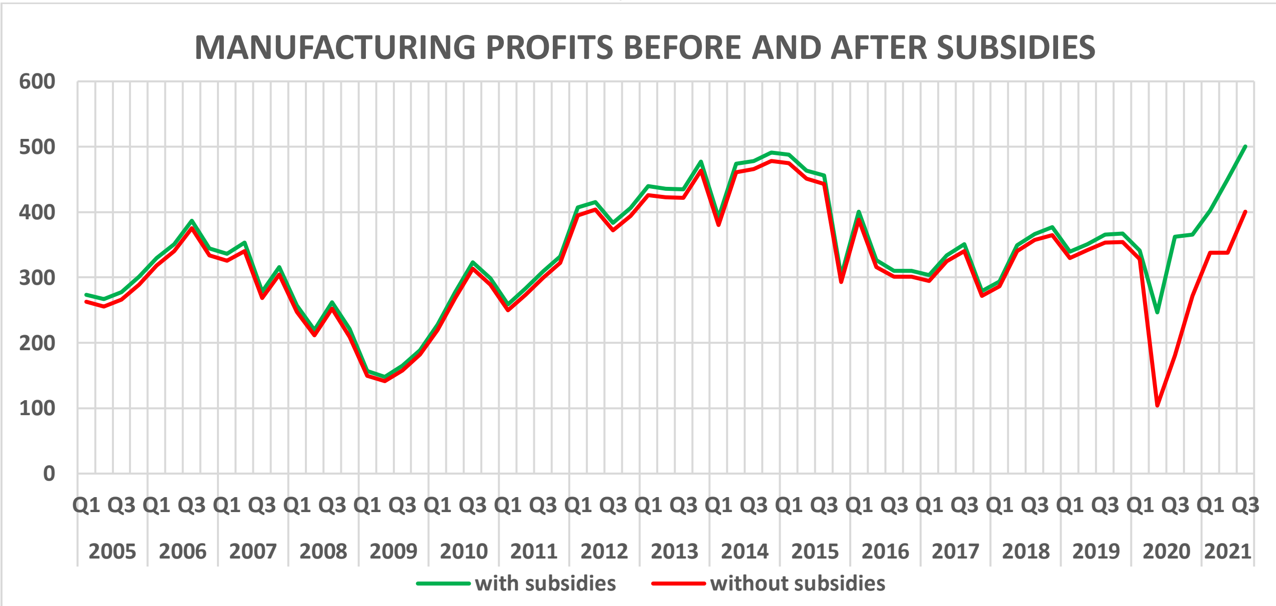
Graph 3.



(The profit figure is adjusted to remove the influence of subsidies which would distort the rates.)

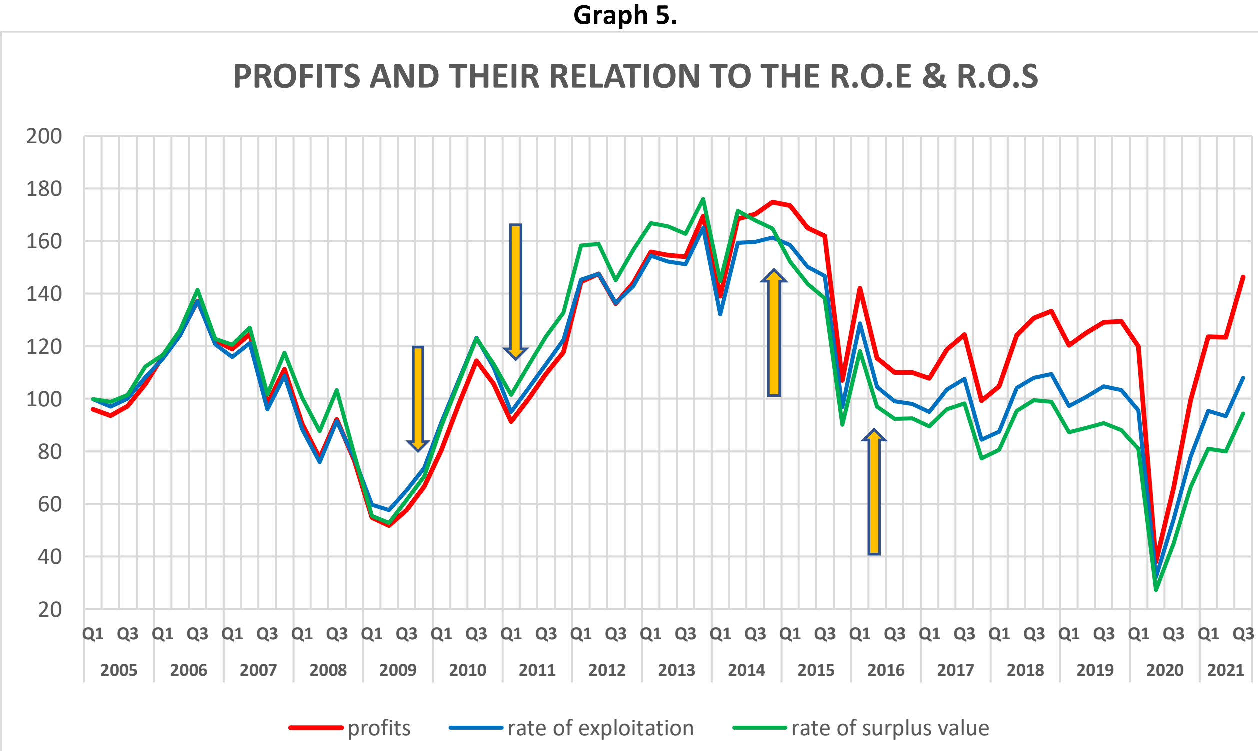
We note a sharp improvement in the recent rate of surplus value which feeds directly into profit generation. The sharp improvement is a combination of the rise in exploitation multiplied by the acceleration in turnover which is why the improvement is relatively greater than for exploitation.

Graph 4.



We note that in nominal terms, with subsidies included, profits have reached their 2014 peak, but adjusted for inflation they are still 20% below that peak in real terms. Without subsidies nominal profits have only exceeded levels found in 2019 but adjusted for inflation they would be well below that figure.

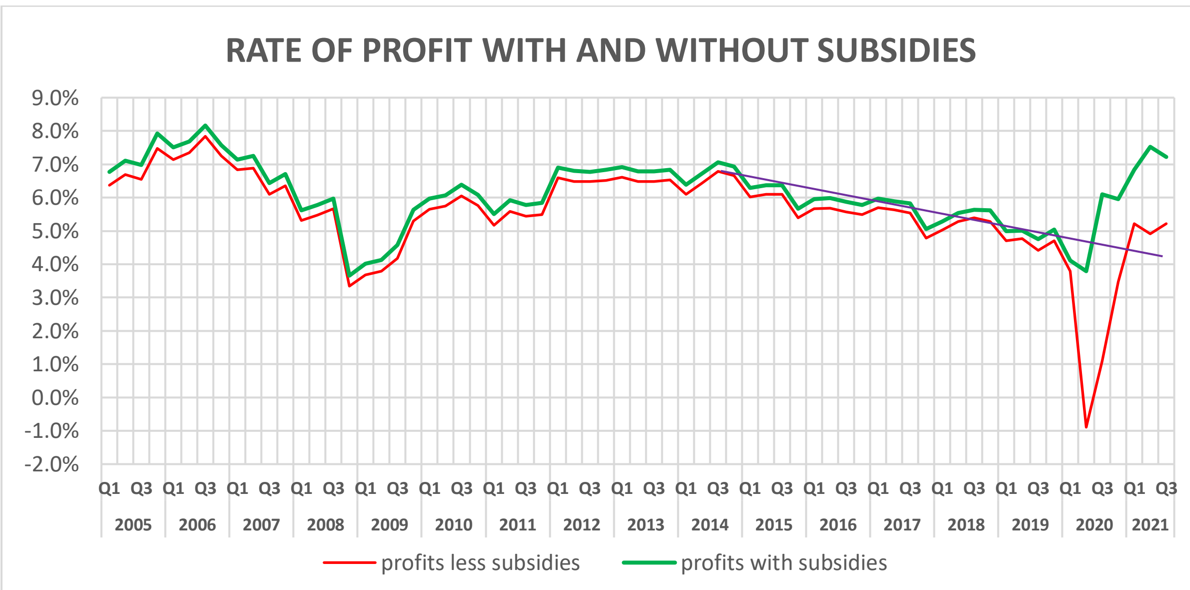
Graph 5.



The graph above shows the complex interplay between profits, exploitation, and surplus value. When turnover accelerates, it pushes the rate of surplus value above the rate of exploitation. This is associated with a subsequent rise in profits. Conversely when turnover decelerates pushing the rate of surplus value below the rate of exploitation, this is associated with falling profits. (Note the arrows.) This can be more clearly seen in previous graphs which I have produced covering a period longer than fifteen years.

As rates of profit are real not nominal, i.e. capital at current cost is compared to profits at current cost, and as it is usual for capital to increase due to investment, the rate of profit will have fallen despite the increase in nominal profits. As Manufacturing does not provide sufficient data to estimate this, we now turn to the Non-Financial Corporate Sector, which does. The rate of profit estimated below is an update on the rate found in a recent article titled: *US NON-FINANCIAL CORPORATE PROFIT IN QUARTER 3*. https://theplanningmotivedotcom.files.wordpress.com/2021/12/us-q3-2021-profitability.pdf The profit figure chosen here is 'Profits before tax (without IVA and CCAdj)', Line 37, NIPA Table 1.14.

Graph 6.



The with-subsidies-rate-of-profit has reached levels last seen prior to the 2008 recession courtesy of $139 billion in subsidies this quarter amounting to 28% of pre-tax profits. The clean rate of profit or the produced rate of profit has only risen back to its 2018 levels. Thus it is still 2% or nearly a third below its 2014 peak. In terms of the trend since 2014, the current rate of profit is 1% above trend but is likely to snap back to trend in the coming two quarters as economic headwinds grow.

Over the period of the pandemic the unadjusted rate of profit has averaged 5.9% while the produced rate of profit has averaged 3.3%. That puts it below the nadir of 3.7% found in the final quarter of 2008. The difference in the two rates is due to the $1.158 trillion in subsidies given to corporations during this time.

This rate of profit seems to be contradicted by the Price to Earnings ratios found on the markets. However, under the surface, reported earnings by S&P 500 companies is not so rosy. "*The S&P 500 is up about 21% YTD but if you remove the performance of five dominant stocks, Apple, Microsoft, Facebook/Meta, Nvidia, and Google, the overall S&P is up less than 6%.*" [*https://eu.heraldtribune.com/story/business/2021/12/16/joan-lappin-record-insider-selling-may-warning-investors/8906012002/*](https://eu.heraldtribune.com/story/business/2021/12/16/joan-lappin-record-insider-selling-may-warning-investors/8906012002/)

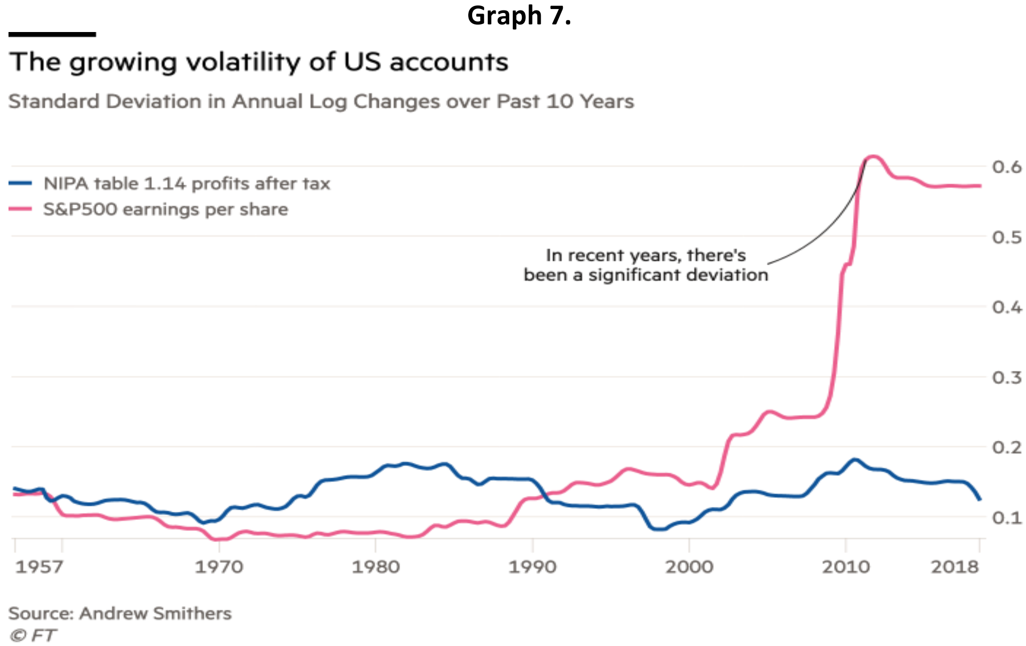
Perhaps this is the reason insiders are selling so much stock in leading corporations. "*As of Monday, sales by insiders are up 30% from 2020 to $69 billion, and up 79% versus a 10-year average, according to InsiderScore/Verity. The selling is likely to increase even more as December is often an active month for sales due to tax planning. "super sellers" — Musk, Bezos, the Waltons and Mark Zuckerberg — account for 37% of this year's total. Google founders Larry Page and Sergey Brin have each sold about $1.5 billion of their Alphabet shares as part of 10b5-1 plans. Microsoft CEO Satya Nadella sold off nearly half of his Microsoft shares last month for about $285 million."* https://www.cnbc.com/2021/12/01/ceos-and-insiders-sell-a-record-69-billion-of-their-stock.html To this we can add Tim Cook's $750 million sale of some of his Apple shares. It appears these billionaires are heading for the door early leaving the retail investors to carry the can as usual.

This deluge of insider selling has not stopped the year-end 'Santa Rally'. As always the Santa rally serves the interest of those who run the large funds because their bonuses are based on year end results. However, when Santa rallies are baseless the reckoning always comes in January, and this rally is an extreme example of baseless manipulation.

GAAP vs non-GAAP Profit reporting.

Generally the headline profit figures relayed to Wall Street and the Share Markets are non-GAAP profit figures, which we may define as the musings of Chief Financial Officers. The divergence between the two sets of profits can be seen below.

Graph 7.



https://www.ft.com/content/e4b555f0-41c0-11e9-b896-fe36ec32aece

The above graph prepared by the Financial Times shows the deviation of reported earnings (non-GAAP) from produced profits as estimated by the BEA which are then presented in Table 1.14. The reported earnings, the blue graph, is actually worse than it appears when we factor in cumulative share buy-backs. The blue graph shows there was no basis for the extended rally in share prices, other than the availability of cheap money, literally free casino chips with which to speculate.

The debate between GAAP reporting and non-GAAP reporting continues to rage. And rightly so. An authoritative study in 2016 showed that the discrepancy in rates had already risen to 30%. And in recent times the use of Non-GAAP has grown. "*In 1996, 59% of S&P 500 companies used at least one non-GAAP earnings measure, whereas, in 2018, 97% of S&P 500 companies used at least one non-GAAP earnings measure in company filings."* https://corporatefinanceinstitute.com/resources/knowledge/accounting/non-gaap-earnings/ It is likely that non-GAAP reporting will reach fever pitch in the current quarter as the quality of real profits deteriorates.

The proponents of non-GAAP profits advocate its' use because they say it correlates more closely to the movement of actual share prices. But this is tautological. Of course share prices correlate with non-GAAP earnings because they form the headline profit figures which drive share prices, particularly amongst retail investors. But the fact that share prices are being manipulated in this manner is no reason to use it. *https://www.uafrs.org/#:~:text=Uniform%20accounting%20is%20achieved%20by%20adjusting%20the%20as-reported,of%20those%20metrics%20made%20from%20uniform%20financial%20statements.*

The advocates of non-GAAP profits also point to the more rapid technological destruction of assets in the current information age, particularly inanimate assets. They claim this jaggedness needs to be smoothed out by what they call 'uniform accounting practises. Paradoxically, in Graph 8 above, the BEA does just that following the 2012 revisions where R&D and in-house software expenditure, large contributors to jaggedness, are now smoothed out by capitalising these costs to provide a steady stream of depreciation.

Of course the acid test for the divergences in profit reporting has to do with the phasing of the business cycle. When real profits are on the up the divergence is less and when profits are declining the divergence is greater. It appears the proponents of non-GAAP reporting want keep their cake while wanting to eat it. They seek to treat profits differently to losses; profits can be taken immediately but losses need to be delayed or smoothed out over a period of time. (Note 1.)

Let us conclude with the final observation by the authors of an authoritative study titled: ***Non-GAAP measure disclosure and insider trading incentives in high-tech IPO firms*** published 10 December 2021 *"The authors find that the top executives of high-tech IPO firms with NGM disclosures are significantly more likely to sell and sell significantly more insider shares at the lock-up expiration than those of high-tech IPO firms without NGM disclosures. At the same time, while high-tech NGM firms have stock returns similar to their counterparts without NGMs for the period before the lock-up expiration, their stock returns are substantially lower after insider selling following the lock-up expiration.*

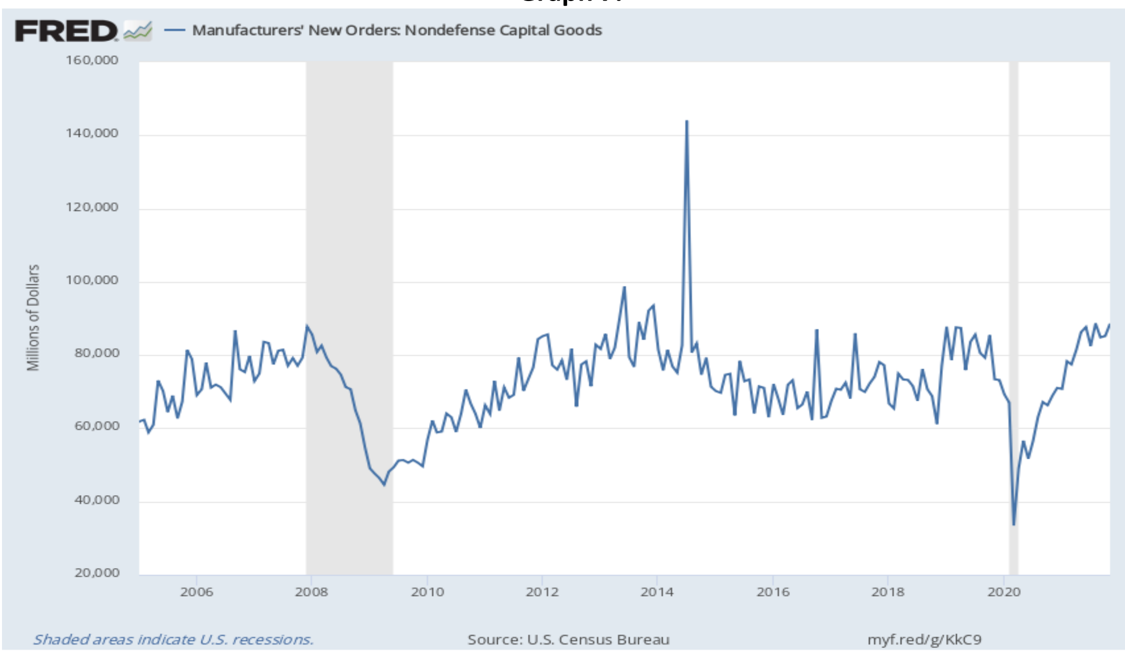
By documenting the negative association between NGM disclosures and post-lockup expiration stock performance, the study highlights managerial deliberate optimism about the firm's prospects which may not materialize. Hence, investors should take the NGM disclosures with a grain of salt. https://www.emerald.com/insight/content/doi/10.1108/ARJ-01-2021-0016/full/html (NGM means non-GAAP disclosures.)

Marx noted, how in Volume 3 the divorce between ownership and management turned capital into social capital, and how it freed management from bearing personal losses resulting from the loss of capital in their firm. Recent events have shown the converse is equally true. The inducement of share ownership by these managers has led to a greater manipulation of profit data to boost stock prices and thus improve their prospects of cashing out these shares. (Note 2.)

Current high-frequency data.

Capital goods orders growth has stalled (see Graph below). Nominally, they are 3.5% higher than in 2019 but adjusted for inflation they are over 5% lower despite the shift in consumer preferences towards goods.

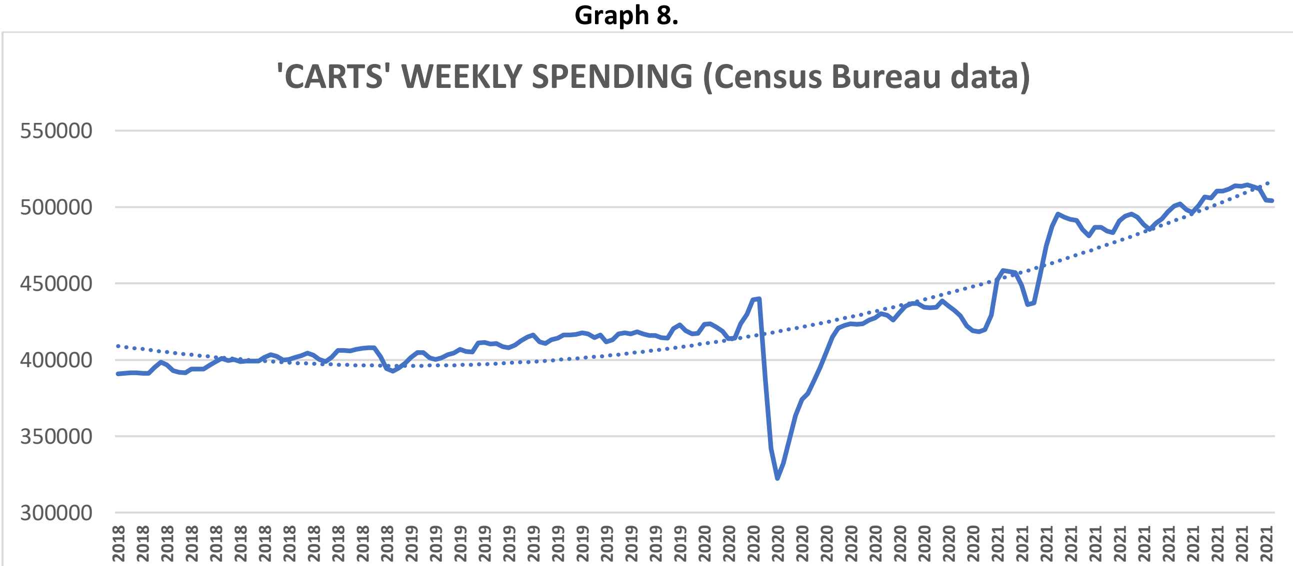
Graph 7.



In terms of consumer spending, high frequency data is conflicted. *Mastercard's* spending report is more positive. "*Holiday spending rose 8.5% compared with the year-earlier period, according to Mastercard SpendingPulse. He said an increase in gift cards will buoy purchases in the last week of December and early January*." (Gift card spending attributed to Macys) https://www.cnbc.com/2021/12/27/holiday-sales-jumped-8point5percent-as-shoppers-shrugged-off-higher-prices.html

On the other hand the more authoritative CARTS report by the Chicago Fed is more pessimistic.

Graph 8.

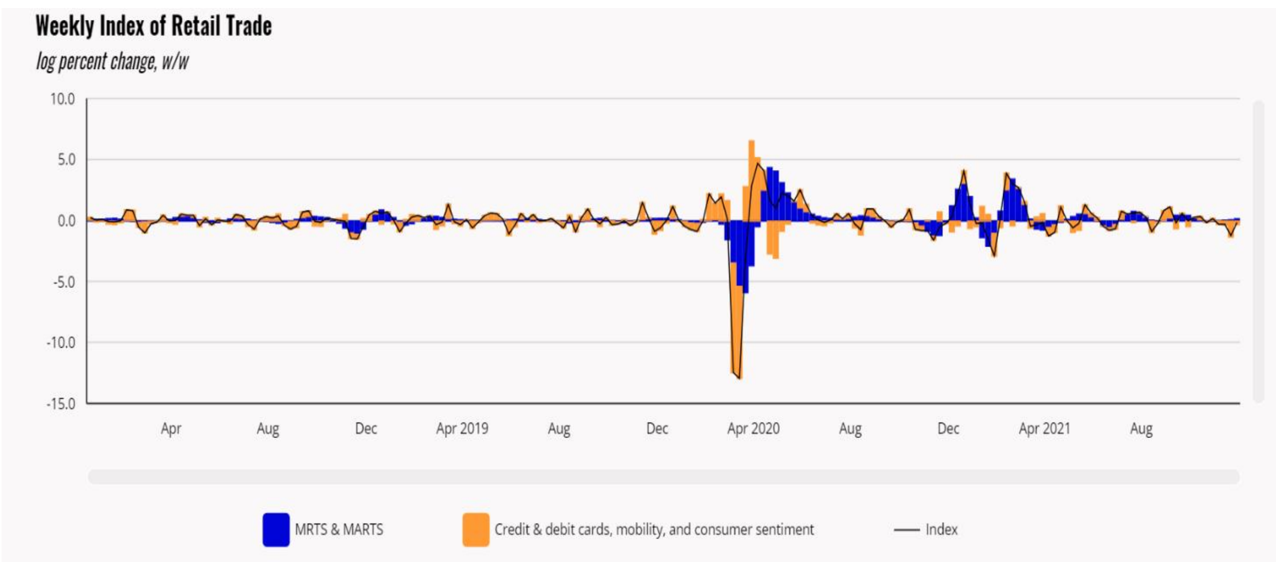


The November Mastercard data suggested retail sales grew by 0.8% when the preliminary official release put growth at only 0.3% or below inflation. The data provided by CARTS on the other hand was bang on the button. It is likely that the current CARTS release is also a better estimate. The data in Graph 8 covers the fourth quarter up to the second week of trading in December and can be found on the following link https://www.chicagofed.org/publications/carts/index. Thus it covers only half of December.

Taking the quarter up to the second week of December, retail sales excluding cars are down 2.1% in nominal terms or close to 4% in real terms compared to the third quarter. Real sales in December are now no higher than at the beginning of the year. It is likely that October was the peak month after which time spending has softened. Unless there was a surge in spending in the week before Xmas, the picture is unlikely to have changed significantly and it is probable that consumer spending will not drive GDP growth in the fourth quarter nor the first quarter of 2022.

More detail in the weekly change in sales can be seen in the graph below prepared by the Chicago FED. (What is interesting is to note is how the peaks in spending correlate to the influx of COVID Relief funds.) Historically the CARTS data provided by the FED more closely aligns with the Census Bureau Data estimates than does the Mastercard data.

Graph 9.



https://www.chicagofed.org/publications/carts/index

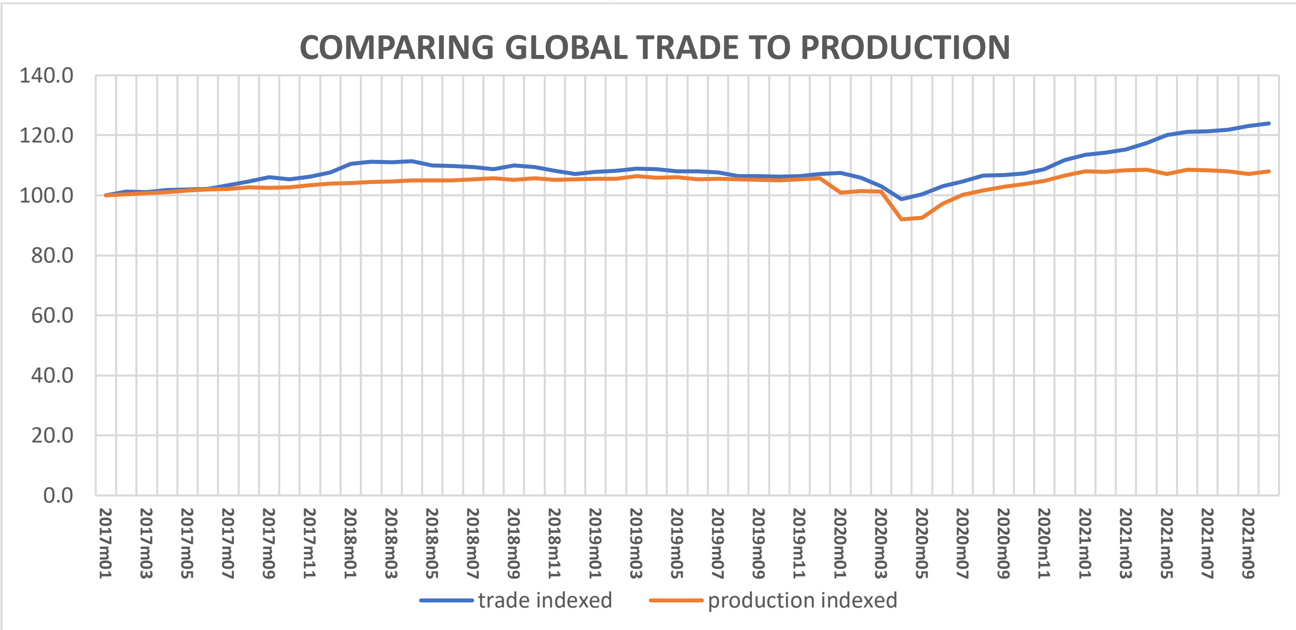
Of course none of this has deterred the Atlanta division of the FED projecting a +7% annual rise in GDP in its most recent GDP NOWCAST. We shall see.

A more global view and prospects.

The 'CPB world trade monitor' is always a good place to start. The most recent report covers the period up to October 2021. It provides an overview of both global production and global trade. I have presented these results in the graph below. Global production is up 3% compared to 2019 while trade is up 10%. According to the CPB, October's trade momentum is 0% while production momentum is -0.3%. In October, which I now consider to be the peak month, monthly trade vs September improved while production deteriorated.

Of interest, is the divergence between trade and production since 2020 reminiscent of the pre-2008 period. The likely reason being the surge in demand in the EU and the USA resulting from the effect of Covid related funds.

Graph 10.



https://www.cpb.nl/en/world-trade-monitor-october-2021

It is likely that both the trade and production momentum's has subsided since October and that the gap between production and trade will close or even reverse in the new year due to the build up of stocks in the EU and the USA.

Looking forward to 2022 the current consensus is for world growth of between 4% to 4.5% next year. *In both the United States and the euro area, we expect growth to normalise lower to 4%. In the UK, we expect growth of about 5.5% and in China we expect growth to fall to about 5% given the real estate slowdown."* So says Vanguard, one of the world's largest investors controlling $7.5 in assets, (only Black Rock is bigger). https://www.vanguard.co.uk/content/dam/intl/europe/documents/en/vanguard-economic-and-markets-outlook-2022-eu-en-pro.pdf Despite the surge in Omicron infections the OECD still maintains an outlook for 4.5% global growth. The more heavily qualified IMF forecast is even more rosy with the expectation of 4.9% growth in its October report.

On the other hand TED (The Conference Board) provides a lower forecast as can be seen in the Table below. Its December release anticipates GDP growth of 6.1% for the US economy in this quarter not far distant from the current GDPNOW forecast. What is of interest in the table below is that when the 2020 contraction is subtracted from the 2021 growth, the result is close to 0 or will be when all the December 2021 data is in. Thus the pandemic has cost the world economy two years of growth equal to $11 trillion. If we then add in the $11 trillion in Covid Relief funds globally the total is $22 trillion for both losses and debts. If only the capitalists had prepared for pandemics they could have saved trillions in dollars and millions in lives, but then they would not be capitalists.

In addition TED has always dismissed the official Chinese GDP growth figures as inflated. Instead it provides its own adjusted growth figure. Based on its own adjustments, TED has the US economy growing faster in 2022 than the Chinese economy. This will be a first in a very long time. TED has been wrong in the past but this time the growth differentials between the two economies may be closer than usual.

Table 1.

Real GDP (average annual % change)	Actual	Actual	Actual	Estimate	Forecast	Forecast	Trend	Trend
	2000-2009	2010-2019	2020	2021	2022	2023	2022-2026	2027-2031
United States	1.9	2.2	-3.4	5.7	3.8	3.0	2.1	1.8
Europe	1.7	1.7	-6.6	5.0	4.1	1.7	1.2	1.1
Euro Area	*1.4*	*1.3*	*-6.9*	*4.7*	*3.9*	*1.5*	*1.0*	*0.9*
United Kingdom	*1.6*	*2.0*	*-9.7*	*7.0*	*4.5*	*1.4*	*1.1*	*0.9*
Japan	0.4	1.2	-4.7	2.5	3.3	1.4	0.8	0.8
Other Mature	3.6	3.1	-2.2	5.2	3.8	2.7	2.5	2.4
All Mature Economies	**1.8**	**2.0**	**-4.6**	**5.1**	**3.9**	**2.3**	**1.7**	**1.5**
China	8.9	6.3	2.2	5.0	3.3	3.2	3.7	3.3
India	6.8	7.2	-7.1	7.5	8.5	4.3	4.0	4.1
Other developing Asian economies	4.9	5.1	-2.9	3.1	4.8	4.4	3.5	3.7
Latin America	2.8	1.7	-7.5	6.4	2.2	1.7	1.6	1.7
Brazil	*3.4*	*1.4*	*-4.4*	*5.2*	*1.5*	*1.5*	*1.7*	*1.7*
Mexico	*1.4*	*2.7*	*-8.5*	*6.1*	*3.0*	*1.7*	*1.4*	*1.4*
Middle East & North Africa	4.6	3.1	-2.5	3.8	3.8	2.4	2.6	2.9
Gulf Region	4.4	3.5	-4.7	2.4	4.3	2.3	2.9	2.9
Sub-Saharan Africa	5.7	4.0	-1.7	4.2	4.0	3.6	3.4	3.8
Russia, Central Asia and Southeast Europe	5.0	3.1	-1.5	5.6	2.3	2.4	2.5	2.4
Russia	*5.4*	*2.0*	*-2.9*	*4.5*	*2.1*	*1.8*	*1.6*	*1.8*
Turkey	*3.9*	*5.8*	*1.6*	*8.9*	*2.5*	*3.3*	*3.6*	*3.1*
All emerging and developing economies	**5.7**	**4.7**	**-2.1**	**5.2**	**4.0**	**3.2**	**3.2**	**3.2**
World	**3.4**	**3.3**	**-3.3**	**5.1**	**3.9**	**2.8**	**2.5**	**2.4**
Addendum:								
China (Official)	10.3	7.7	2.3	8.3	5.5	5.2	5.4	4.8

https://www.forbes.com/sites/stevebanker/2021/11/03/the-economic-outlook-for-2022-will-be-impacted-by-supply-chain-and-labor-issues/?sh=4c5693783f1e

It is not only TED who is downrating China's future prospects. McKinsey has identified Chinese Residential Property to be the biggest asset class in the world today. Residential building was considered the primary driver of recent GDP growth in China after consumer spending disappointed and industrial investment retrenched. Alas, this sector is now insolvent with a number of prominent builders in default. China is not so much building a future society according to our Shanghai Marxist Professors as engaging in speculative building under the all-seeing leadership of the Chinese Communist Party. Never mind, there is always something else to speculate on, such as wrist watches. Investors need no longer look up when they can now look down at their wrists. "*China's once enthusiastic property investors are turning their attention to luxury watches as a better store of value in the face of slowing economic growth and President Xi Jinping's intensifying campaign against housing speculation. Multiple high-end watch resellers told the Financial Times that business had taken off in recent months as wealthy individuals stopped buying additional homes and instead spent their extra cash on luxury timepieces such as Rolex and Patek Philippe. The shopping spree, said experts, has contributed to a 40 per cent surge in China's imports of Swiss watches in the first 10 months of this year even as the broader economy cooled off.* Also "*Customs officials either won't notice your watch or may not know how much it is worth," said Wang. "That creates a safe and efficient way to take your money abroad."*

https://cpp-luxury.com/chinese-wealthy-opt-for-luxury-watches-instead-of-housing/#:~:text=Chinese%20wealthy%20opt%20for%20luxury%20watches%20instead%20of,President%20Xi%20Jinping%E2%80%99s%20intensifying%20campaign%20against%20housing%20speculation.

To this of course we should add, not so much the adornments of wrists as arms spending. An arms race is brewing between China and the USA. China is applying its industrial might to building aircraft and ships. It's projected requirement for J20 fighters is now put at 500 and with a price tag of around $100 million each this adds up to $50 billion. That's a lot of Rolexes. The Stockholm International Peace Research Institute estimates Chinese military expenditure to be 36% higher than official figures. https://www.sipri.org/publications/2021/other-publications/new-estimate-chinas-military-expenditure So instead of desalinating the sea to make the deserts bloom, China and the USA are throwing labour into the sea through spending it on arms.

In all other matters strategic, capitalism has been found wanting despite its in-industry-record-of-innovation. Green electricity has been shown to be defective because there was no pre-planned storage for wind and solar, nor any pre-planned intercontinental grids to link up wind and solar in different climatic and time zones. The losers have been priced out consumers and the planet as carbon emissions rise this year. There has been no Manhattan project to develop scalable batteries nor grids, since such projects seem to be reserved for the purposes of destruction rather than production. Electric vehicles are hitting the bumpers because cars which have been built around their batteries, which require individual charging points which cannot keep up with surging sales of vehicles. Its not only the pandemic which has shown capitalism to be defective, but as life becomes more complex and capitalism increasingly relies on the wisdom of the market, it is falling flat on its face.

Conclusion.

As the tide of covid funds ebbs and the euphoria over bounce back dwindles, the economic carnage caused by the pandemic and the negligence of the capitalist class, can be seen more clearly. Crushed standards of living for the majority of society, rising homelessness and indebtedness are some of the obvious signs. Nor is it likely that there will be more Covid funds in the pipeline as the various Treasuries of this world lick their debt wounds. And what is scandalous in the dominant economies, is a human catastrophe in the poorer dominated economies.

The USA and England are playing with fire by currently refusing to impose restrictions as they prioritize keeping businesses open and workers working to avoid paying furlough. In the UK daily infection rates are about to cross 200,000 and in the USA 500,000. In England, the increase in infections is up by 45% over the last 7 days trumped only by the increase in hospital admissions which are up 65%, showing how effective the vaccines are not against this variant. Seems the vaccinators are firing duds because the vaccines have not been updated. If the NHS is crushed as appears likely, that will be the end not only of Johnson but of the Tory party itself. The same can be said for the Democrats and their inaction in the USA.

Paradoxically, China is now the more vulnerable nation. Repeated waves of infection in the West have led to widespread immunities, while in China successful lockdowns has led to little or no immunity adaption, and it is an open question whether previous lockdown measures will prevail against the more transmissible Omicron variant.

But despite all the uncertainties, the markets march on convinced Omicron is much milder. Clearly these perfect markets are acting on perfect information. They may be in for an unwelcome surprise in January.

It is best to avoid annual comparisons for GDP growth because of the distortions thrown up by the Pandemic. It is better to rely on quarter-on-quarter growth data to gauge the state of the economy. In the 3rd Quarter quarterly growth came in at 0.57%. It is likely that 4th Quarter growth data will be no higher or even lower, and not the +2% envisaged by the commentators quoted earlier and GDPNOW. Inflation which raised its ugly head in 2021 will be less of a problem in 2022 when swollen inventories signal that underproduction has given way to overproduction.

It is also likely that despite the adornment of profits by non-GAAP measures, headline profit growth will falter because of the effect of waning subsidies. While FACTSET eulogises about 2021, which in their view witnessed record growths in profits, profit margins and revenues, their estimate for the 4th quarter is starting to take on a negative tinge. *"Fewer S&P 500 companies have issued positive EPS guidance for Q4 2021 compared to recent quarters as well. At this point in time, 95 companies in the index have issued EPS guidance for Q3 2021, Of these 95 companies, 57 have issued negative EPS guidance and 38 have issued positive EPS guidance. Over the past four quarters, 60 S&P 500 companies issued positive guidance on average for the quarter. However, over longer time periods, fewer companies typically issue positive EPS guidance than negative EPS guidance. The percentage of companies issuing positive EPS guidance for Q4 2021 is 40% (38 out of 95), which is equal to the 5-year average of 40%."* There is likely to be more negative guidance shortly. And it is more than likely that record profit margins will not be revisited as higher input prices collide with weaker final demand in the form of consumer spending. https://www.factset.com/hubfs/Website/Resources%20Section/Research%20Desk/Earnings%20Insight/EarningsInsight_121721A.pdf

January will be a testing time for the world economy and the markets on which it relies. The growing evidence of a slowing world economy and subsiding profits may end up choking the markets, putting into question the most sustained and elevated financial bubble in the history of this cruel and dated economic system.

Note 1. *One consequence of this shift is a decline in the correlation of GAAP earnings changes in stock market valuations. The ironic consequence of all this is that investors increasingly rely on non-GAAP numbers for valuation. These are not only idiosyncratic, and thus not always capable of comparison, they are also devised by bosses whose views may well be richly coloured by their own outsize incentives.*

Another important area is restructuring costs and loss on sale of assets. As we argued in a previous article, the pace of corporate creative destruction has increased. Technological progress is accelerating, and products and businesses are becoming obsolete faster. As a result, firms close unremunerative business segments more frequently, sell those assets at a loss, and pay severance to workers. Those costs are rightly deducted from GAAP profits. https://hbr.org/2021/05/mind-the-gaap

Note 2. Of course the SEC (regulating body) pretends to curb this practice. It's rules are about as effective as placing chewing gum on the pavement to deter pedestrians- easily sidestepped. *"The current set of rules creates a "safe haven" for corporate insiders and companies to trade their own equity as part of pre-announced portfolio management plans. By declaring in advance when and how they plan to trade, executives protect themselves from future accusations of insider trading".* So there you have it.

Additional Note. On the first spreadsheet (INDUSTRIAL PROFITS UP TO Q3), there is a graph which shows that profits in the Financial Sector have not grown as a share of total industry profits once FED profits are removed.

Brian Green, 29th December 2021.