EVALUATING BOTH THE US AND CHINESE ECONOMIES MID-WAY THROUGH 2023.

Both the US Census Bureau and the Chinese Bureau of National Statistics have released sufficient information over the past two weeks to form a preliminary assessment concerning the state of both economies. The overall opinion is one of weakness and even accelerating weakness in both economies.

Before looking at the data I would first like to discuss labour relations in China with a view to confirming once again that the economy there is varnished Capitalist. Readers will be aware of the strenuous efforts by the USA and its allies to arrest China's technical development by means of embargoes as well as relocating supply chains away from China. Here we will deal only with relocations. One of the preferred sites has been India, and the problems with relocating there shine a harsh light on Chinese labour relations.

There are many reasons why India offers poor relocation prospects. The most often cited are poor infrastructure, slow port facilities, cumbersome procedures to register companies and erratic tax laws (now improved). The one issue which receives less attention is India's labour laws. Besides throw away remarks by anti-working-class bigots claiming Indian workers are lazy and don't like doing overtime, little else was heard until large corporations in the tech industry decided to relocate back to China from India. This U-turn was due to the difficulties transferring Chinese rates of exploitation to India.

The reason: Indian workers' resistance to the *labour flexibility* these pampered corporations had got used to in China which was difficult to replicate in India. It seems India lacks the "*do whatever it takes*" attitude found in China where companies and government gang up together to force workers to fulfil orders come what may. This article explains it all. The author is no friend of the worker, but its thoroughness makes up for its bias. It shows how Apple has forced down working conditions in India in order to re-establish Chinese working conditions there. Here are a number of observations. "*The Indian state of Karnataka* ***tweaked*** *an archaic national labor law to extend factories' work schedules from nine to 12 hours, and to allow women workers to do night shifts. Apple and its contract manufacturer Foxconn were among the companies that had lobbied for the change, reported Financial Times, as this would allow them to run round-the-clock, 12-hour production shifts at an upcoming facility in the state, similar to their practice in China." "Electronics manufacturers are able to hire and fire contract laborers more easily in countries like China and Vietnam, as compared to India, said Manur." (*My emphasis)

So in Communist China, this workers paradise, working conditions turn out to be far worse than in India which still has its federal based *Factory Act of 1948* which prohibits inter-alia, compulsory over-time. Here are a number of legal extracts covering labour laws in India. "*Overtime is the period for which an employee has worked in excess of their working hours. Under the overtime rules and policies defining work hours in India, an employee is subject to 8-9 working hours per day which equals a total of 48-50 hours a week. There are numerous overtime rules and procedures in India stipulating different periods of working hours under the labor law. Section 51 and Section 59 of the Factories Act - 1948[2] states, "No employee is supposed to work for more than 48 hours in a week and 9 hours in a day. Any employee who works for more than this period is eligible for overtime remuneration prescribed as twice the amount of ordinary wages." Additionally, Section 14 of the Minimum Wages Act, 1948[3] states, "When the minimum wages of an employee are fixed for a particular period of time and the employee works beyond that period, then the employee has to be paid overtime wages for the extra time." The total number of working hours in India in a day must be 12 and a half hours, limiting the maximum number of overtime hours in a day at 2 hours." "Any employer found to be contravening these provisions would be liable for punishment of* *imprisonment up to 2 years and fine of up to Rs. 1 lakh or both. If the employer continues to violate the provisions after conviction, a fine of Rs. 1000 per day is levied for each day of violation". "The overtime work must be voluntarily taken up by the employee and not forced through an involuntarily or fraudulently signed agreement."*

India has over 52 federal labor laws and 200 state enacted laws and amendments, creating a complex structure of legislation and compliances in the country.

Seems the Indian struggle for independence in the 1940s resulted in far more democratic labour rights for its workers than did the communist revolution in China at the same time. Of course the current reactionary Modi government has been doing its utmost to hammer farmers in rural areas and workers in urban areas with new laws which seeks to reverse or even cancel all their traditional rights. But so far it has failed, and the increasing unpopularity of the BJP makes it unlikely it will succeed. Even the changes to labour laws by various Indian states is unlikely to be enduring which adds up to another reason why India will not replace China, and why these hypocritical touchy-feely corporations when it comes to their consumers, are rethinking their stay in India. One can only look forward to a more conscious society where consumers are more concerned with **how** things are produced rather than **what** they can do.

In the meantime it exposes the oppression faced by the Chinese working class and the political danger this poses to the remnants on the Left who are duped by the Communist Party of China into thinking this country is somehow different. To hold to such a position marks a betrayal of the Chinese working class which has been so brutalised by successive Stalinists in pursuit of their market ambitions. There may be a Chinese economic miracle, but this miracle has been produced by efficiently oppressing and exploiting Chinese workers especially migrant workers living and working in inhumane conditions.

June data from the US is weak.

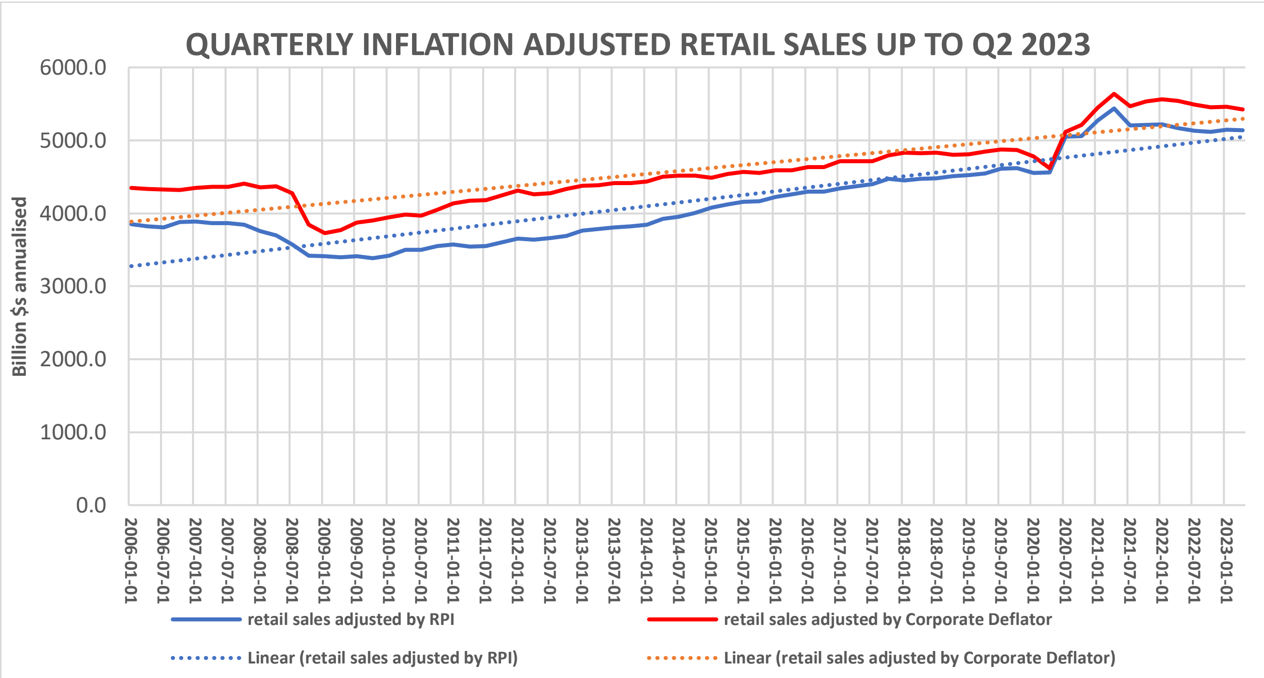
The base factors making inflation appear stronger than it was fell away in June. The official CPI number fell to 3% or 1% above the FED target. However if we exclude Owner Occupier Rent which is never paid but which in June represented 25.5% of the total CPI increasing by 7.8% over the year, it knocks 1.0% off the official number meaning the adjusted increase was only 2%. Thus the FED has reached its target, though like a jilted lover, it will be the last to find out.

Of course the markets were ecstatic over this fall which was better than expected. But the CPI figure is a poisoned chalice because it is a sign of economic weakness not strength. Thus it is not a positive omen but a negative one, but like the FED, the markets will be the last to experience a reality check.

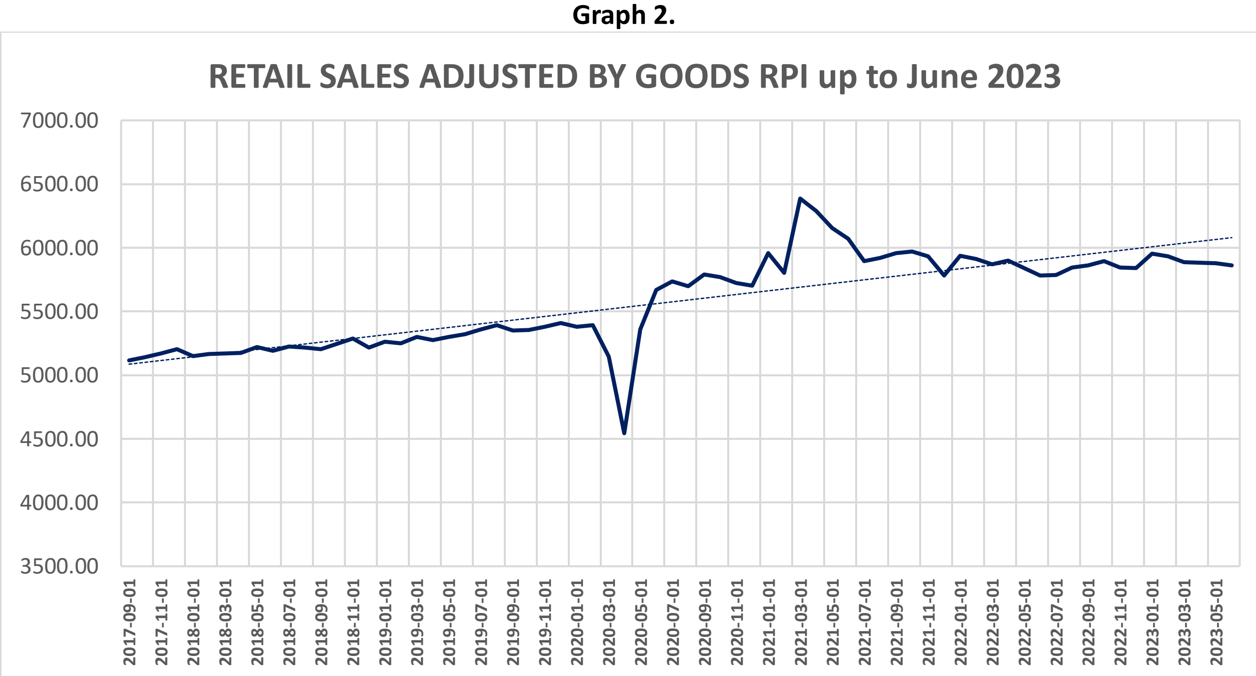
Preceding the Inflation figures, the employment figures for June were released and once again the markets lapped them up because they were weaker than expected. The added bonus was downward revisions in the previous months. As I have repeated before, many of the job losses are in higher paid jobs and much of the recruitment is in low paid work curbing demand, which is why retail sales have been anaemic.

Graph 1 below is based on quarterly data taking us back to the period pre-the financial crash in 2008. It shows inflation adjusted sales are trending back down towards their pre-covid levels. Graph 2 is based on monthly data, and it shows that retail sales have not grown for two years and are trending down as well. Finally the *Red Book Retail Index* which is 80% the size of the BLS cohort demonstrates a much steeper fall. In fact, by June yoy sales without price adjustments had fallen into negative territory. The same is true for the value of online sales collected by Adobe Analytics covering 50% of all e-commerce sales including groceries which fell by 2.2% yoy in June, and finally it is confirmed by Costco which saw US monthly sales fall by 2.5% including ecommerce sales which fell by 0.7%. On the flip side, shoplifting has soared leading many chains to shutter branches in downtown areas helping turn them into wastelands. Another indication of the social breakdown occurring in the USA as Covid support, food stamps and the moratorium on evictions ends.

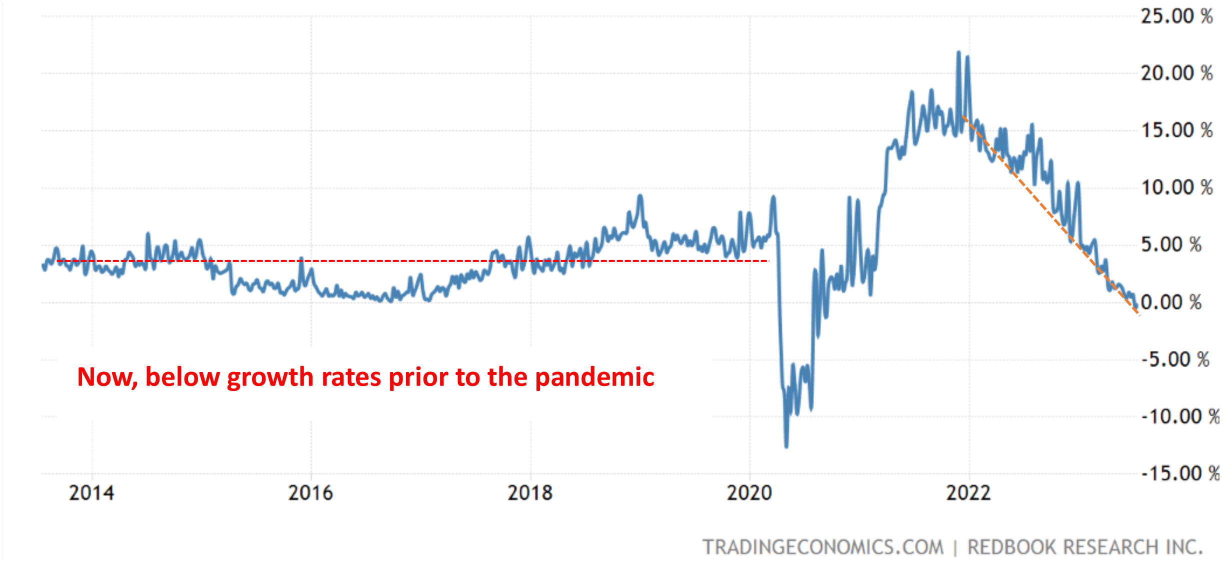
Graph 1.



Graph 2.

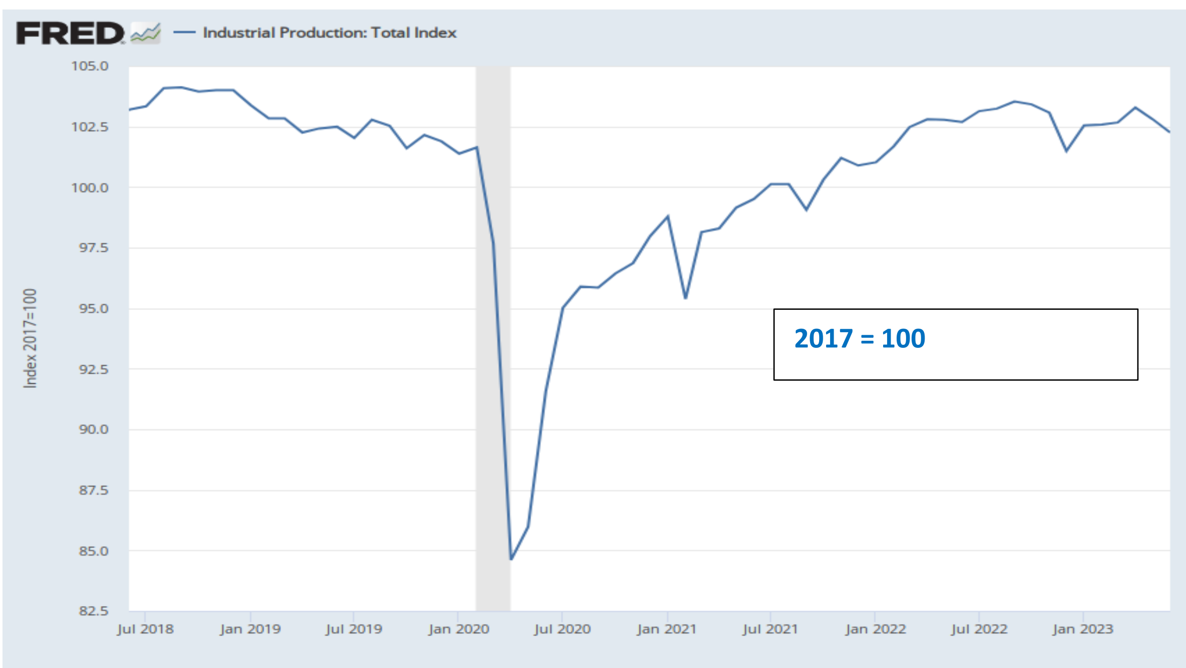


Graph 3. (Red Book Retail Sales YOY)



The fall in the volume of retail sales, which I continue to believe is understated due to inaccurate official deflators, has had a knock-on effect on imports as well as production. Industrial production has fallen yoy including manufacturing (-0.3%) to levels below 2019. In fact over 6 years production is up only 2%. Thus, despite Biden's various supports and subsidies, no industrial renaissance is yet visible in the data.

Graph 4.



Though surveys for the service sector continue to show strength, anecdotal evidence is pointing in the opposite direction. Take the much-vaunted airline industry. Millions of passengers are abandoning planes for the busses because of overpriced airline tickets and crumbling airports. The recent earnings release by

American Airlines confirms this. Additionally, popular destinations like Disneyworld, are well not so popular. The earnings report from Disney out shortly should make interesting reading.

Finally, the housing market having taunted interest rates in May by rising, resumed their fall. Housing starts, permits and existing house sales all fell in June. Housing starts fell by 8% from May and are down 8.1% from June 2022. Permits fell 3.7% from May and are down 15.3% from a year ago. Completions however rose. Existing sales of homes fell to 5.12 million down 3.3% from May and 18.9% from June 2022. Mortgages for purchases are down 25% yoy.

Of interest is the lack of concern by the markets towards an increasing number of office buildings (CRE) being sold off to vulture capitalists with discounts of up to 60%. The reason it appears is that the losses are being borne primarily by the non-banking sector e.g. private equity. Does this leave the banking system unscathed? Definitely not, as much of the financing used by Private Equity and Hedge Funds for these deals takes the form of bank loans. Thus the losses are indirect and delayed but in the end unavoidable.

In conclusion the important leading index issued by the Conference Board which accurately tracks recessions continued to fall. "*The Conference Board Leading Economic Index® (LEI) for the U.S. declined by 0.7 percent in June 2023 to 106.1 (2016=100), following a decline of 0.6 percent in May. The LEI is down 4.2 percent over the six-month period between December 2022 and June 2023—a steeper rate of decline than its 3.8 percent contraction over the previous six months (June to December 2022)". "The Leading Index has been in decline for fifteen months—the longest streak of consecutive decreases since 2007-08, during the runup to the Great Recession".*

The debate over whether or not the US economy will fall into recession, have a hard or soft landing, is a false one. The US economy is already in a shallow recession which will become more apparent when the stock market nose-dives shortly.

China.

The outlook for China continues to deteriorate. The best barometer for that is the sucking up noise coming from the CCP as it approaches the private sector. "*The guideline promised to improve business environment, enhance policy support, and strengthen the legal guarantee for development of private economy, which came after a recent series of meetings held by the Chinese leadership and multiple government departments including the top economic planner, with private company representatives to discuss and learn about their business situations and operating difficulties". "The necessary and timely guideline sends a clear message that the central government wants to revitalize the private sector…"* Or in the words of the CCP, which like a driverless car yet to learn how to swerve safely, the following immortal words: "*namely unswervingly consolidating and developing the public sector and unswervingly encouraging, supporting and guiding the development of the non-public sector."* Perhaps the most important measure will be to grant private businesses greater access to state banks. One of the issues highlighted and of major concern, is the one I have focused on in my numerous reports on the Chinese economy, namely sluggish turnover primarily due to the length of time it is taking to pay invoices outstanding. "*For example, delays to settling invoices are now the main reason why private enterprises are struggling."*

In addition China has halted its crackdown on the TECH sector realising that at a time of economic weakness it needs a vibrant and freed up TECH sector as found in the USA. "*That mission has seen top* *officials roll out the red carpet for Mr Elon Musk and other executives, draw a line under a tech crackdown that tanked the world's biggest initial public offering, and even visit US-based Bain & Company's Shanghai office in an apparent end to immediate worries about a probe into consultancies that spooked global investors". "China's outreach comes as the nation's post-pandemic recovery loses steam. The nation's property market is showing signs of weakness, exports are shrinking and deflationary risks loom. Without "the lure of a rapidly growing economy", China is finding it difficult to attract Western business, said Ms Diana Choyleva, chief economist at Enodo Economics."* On Friday, the Financial Times published an article titled: *China Billionaires back Xi's Recovery Plan* which recorded the effusive praise from these billionaires for the efforts by the CCP to heal relations.

So here we have the Chinese Communist Party cracking down on workers while entertaining capitalists. This is called laying the material conditions for a future workers' society. Hmmm

Additionally, Chinese state planners announced they would be offering two new concrete policies to support private businesses. "*The two forthcoming policies will focus on promoting business investment and their overall development, said Li Chunlin, deputy director of the National Development and Reform Commission."* These policies will be announced shortly.

June data was mixed to middling. GDP growth is limping along. *"The quarter-on-quarter growth of GDP in 2022 and in the first and second quarter of 2023 are 1.0 percent, -1.9 percent, 3.2 percent, 0.5 percent, 2.2 percent* ***and 0.8 percent*** *respectively."* (my emphasis) Investment overall grew by 2.34% annualised over the first half of the year but fell in the private sector. The annualised growth rate for retail sales over the first half of the year is under 5% though the market for luxury goods is stronger in China than in the USA where it is languishing. This from Swiss based Richemont's latest earnings release where sales in the Americas fell by 4%. "*Strong rebound in Asia Pacific more than offsetting muted sales in the Americas*." The same all-round weakness was found in Chinese foreign trade. "*In the first half year, the total value of imports and exports of goods was 20,101.6 billion yuan, an increase of 2.1 percent year on year. The total value of exports was 11,458.8 billion yuan, up by 3.7 percent."* Of interest is the observation that trade by the private sector which accounts for 52.7% of total trade, grew more strongly by 8.9%. This being so, it means foreign trade by the state sector actually fell. What is clear from this data is that the spike in exports from the pandemic is well and truly over. Equally important is that Chinese trade is now too anaemic to support global trade meaning that in May and June global trade fell even faster. 'All power to boycotts.' (We will know more on July 25th when the CPB releases its global trade monitor for May 2023).

Thus if we exclude the booming stock market in the USA, China like the USA has very few areas of economic strength or drivers. The advice from any sympathetic doctor or economist under these trying conditions would be, stop beating each other up because your economic hearts can no longer take it.

Chip wars.

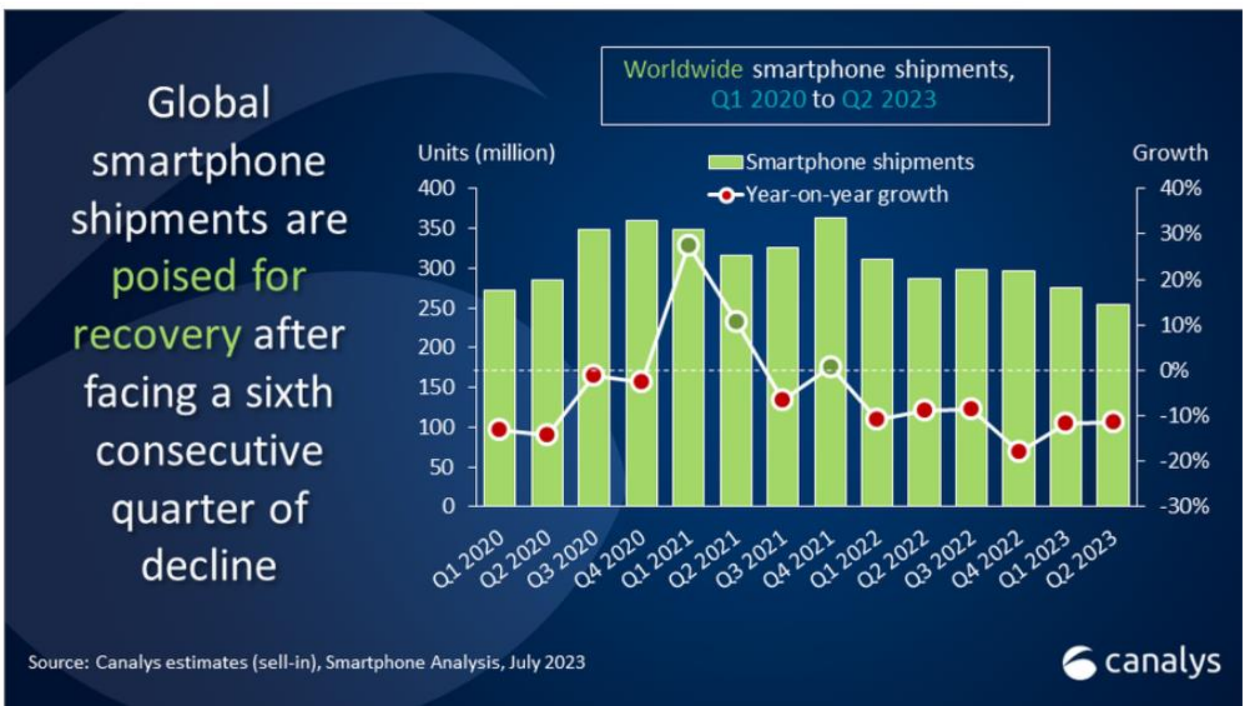
Over the last few months I have suggested the collateral damage to US, European, Japanese, and South Korean corporations from the Tech Embargoes have been underestimated. No longer. Samsung's profits collapsed 96%. TSMC which dominates global chip production saw its profits fall by 23%. Over the next few weeks US chip suppliers will be releasing their earnings reports and they are likely to surprise on the downside including Nvidia.

For the first time, China has started to retaliate by withholding strategic materials. This is either a sign of desperation or confidence as China conquers new technological heights. Such retaliations will further jolt and fracture the world economy.

Whatever the case, US vendors are growing increasingly desperate to maintain a foothold in the Chinese market and to curb the US state department ratcheting up further embargoes. The US-based Semiconductor Industry Association *"said that further rule-tightening by US officials risks "disrupting supply chains, causing significant market uncertainty and prompting continued escalatory retaliation by China".* They called upon the Biden administration to refrain from any further sanctions. It is unlikely that Biden will oblige especially now that western security agencies such as M.I.6 are alleging that China is aiding Russia's war effort in the Ukraine. Yet another excuse to explain away Ukraine's crumbling military. Linking China to Russia's war effort is a very sinister development representing a clear escalation on the part of Western Imperialism which can only increase the likelihood of military action in the Pacific itself.

In addition, the chip wars should be seen against the background of a contracting world economy and with it the market for chips. The biggest user is the smartphone market whose sales fell by 11% in Q2 2023 to a level below that found before the pandemic. Apple's share of the premium global smartphone market has also tumbled by 8% from 25% to 17% over the last two quarters.

Graph 5.



(Source: Canalys)

Nor will the AI revolution endure, at least not in its general form*. Reports are coming in of a looming major problem. As these mass language learning programmes are rolled out increasing their user base and hoovering up more information and dis-information, the quality of their results is degrading, and they are hallucinating more. The launch by Microsoft was always premature based on maxing it share price. And alongside this immaturity and flaws, piracy claims and privacy issues are multiplying. Taking all of this into account it is likely that the AI bubble will soon pop. (*As always I distinguish between these general systems and dedicated business systems tailored to the needs of a particular corporation and or profession. It is these specific systems which will lead to substantial job losses not the general CHAT programs which will continue to entertain and mislead laptop users at home. It is unlikely these dedicated systems will degrade in line with the general systems.)

This unexpected degradation of the language learning programmes highlights the difference between human intelligence and artificial intelligence. Real human intelligence based on contemplative critical awareness not only absorbs information, but challenges it, tests it, and theorises over it. On the other hand artificial intelligence without human supervision absorbs all information indiscriminately regardless of the quality of that information. And we know just how littered the internet is with dross amplified by all those baseless personal opinions. Thus while knowledge can sharpen human intelligence it necessarily dumbs down artificial intelligence which is what is happening now to CHAT, because the likes of Microsoft and OPENAI aim to contain labour costs relative to the burgeoning mass of information being gathered, thereby diluting human supervision.

And finally the Chip wars and actual wars are taking place against the background of worsening weather events. In fact the First US area to be declared uninhabitable without air-conditioning, Phoenix, has just been named**. Serves the rich right. As they migrate from California, Chicago, and New York to southern states they are swopping higher taxes for a furnace. In the meantime, as the rich migrate South, Southern reactionary governors are bussing and flying migrants and the homeless North where at least sleeping outside is not a death sentence in summer. (**Perhaps we should send all the climate deniers to compulsory summer camps in Phoenix where they can contemplate the state of the planet in their tents.)

Conclusion.

Heatwaves in parts of Europe, China and the USA will impact productivity and crops driving up cost prices. Already we have seen recent agricultural prices spike as crops wilt, Indian rice exports are curbed, and Ukrainian exports are stymied. This is in addition to the rise in cost prices due to disrupted supply chains and the loss of least cost options. All of this will continue to raise cost prices behind the veil of inflation which will squeeze profit margins. FactSet's most recent estimate for S&P500 profits saw blended profits decline by 9.0% last week compared to the smaller decline of 7.2% predicted the week before. It now puts profit margins at 11.1% down from 12.2% last year. More ominously for the markets, FactSet now sees no profit growth in Q3 having earlier predicted a bounce back.

Of course the capitalists both in the USA and China will try and reverse falling profitability on the back of their workers. However it is likely that workers, already resentful over their falling standards of living and deteriorating work conditions, will be less willing to oblige. Just as we are entering unchartered waters with climate change, so we are beginning to enter unchartered waters regarding the class struggles ahead.

Brian Green, 22nd July 2023.