China’s Economy Now Number One? Not Quite

Following the announcement by the International Monetary Fund (IMF) that China’s economy has just surpassed that of the United States, headline writers and establishment economists had a field day. According to the *Wall Street Journal’s* Business Insider, “China Just Overtook the US as the World’s Largest Economy,” while London’s *Daily Mail* chortled, “America Usurped: China Becomes World’s Largest Economy — Putting USA in Second Place for the First Time in 142 Years.”

A cursory glance at the charts and graphs provided by these worthies shows the size of the U.S. economy at $17.4 trillion by the end of this year compared to China’s, which is predicted to be $17.6 trillion. The IMF estimated that as recently as 2005 China’s economy was less than half that of the United States, and forecast that in another five years it will be 20 percent larger than that of the United States. By that time the IMF estimates that the U.S. economy will be at $22 trillion to China’s almost $27 trillion.

All this is based on so many ethereal and esoteric assumptions as to be borderline ludicrous. The first assumption is that the comparison, based on something called “purchasing power parity,” is fair and honest. The idea is that the purchasing power of the yuan inside China differs substantially from the purchasing power of a dollar inside the United States. And so the worthies involved pored over reams of statistics to determine how to calculate China’s GDP when compared to that of the United States.

This makes things look a lot better for China than if the dollar/yuan exchange rate were used. In that case, China’s economy is less than $10 trillion in size.

This is not to denigrate the remarkable achievements in China since the economic reforms were installed in December 1978 by reformists inside the Communist Party led by Deng Xiaoping. That program came in two stages starting in the late ’70s and into the early ’80s, which involved the decollectivization of agriculture, the opening up of the country to foreign investors, and granting of government permission to citizens to start their own businesses.

The second stage of reform, about a decade later, involved the privatization and contracting out of much of state-owned industry, along with the lifting of price controls, which had greatly reduced incentive to producers. Many protectionist policies were eliminated, as well as some of the most onerous regulations.

From then until now, China’s economy has grown at nearly 10 percent a year. Put in the simplest terms, it doubled every seven years since 1978. In 2010, it became Asia’s largest economy (surpassing Japan), and the world’s second-largest.

One of the assumptions underlying the IMF’s report, however, is that the numbers coming out of China under its communist-controlled information outlets can be relied upon. Another is that China’s economy will continue to grow at more than nine percent, at least over the next five years — far outpacing (at least on paper) growth in the United States.

There are numerous grievous challenges and difficulties facing China that the establishment media pundits and economists failed to mention. For instance, since 2005, the Hu-Wen administration has reinstituted many of the previous restrictions lifted under Xiaoping.

In addition, much of the growth in China is phony. In August, CBS News rebroadcast Leslie Stahl's program *China's Real Estate Bubble* from March, 2013, where she visited the ghost cities of China for the very first time. The program opened with this:

> As we first reported in March last year, [Chinese authorities] may have created the largest housing bubble in human history. If you go to China, it's easy to see why there's all the talk of a bubble. We discovered that the most populated nation on earth is building houses, districts and cities with no one in them.

Stahl took with her on her revelatory trip Gillem Tulloch, a financial analyst from Hong Kong, who was one of the first to expose China's real estate bubble. She questioned Tulloch:

> **Stahl**: "How important is real estate to the Chinese economy? Is it central?"
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> **Tulloch**: Yes. It is the main driver of growth and has been for the last few years. Some estimates have it as high as 20 or 30% of the whole economy.
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> **Stahl**: But they're not just building housing. They're building cities.
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> **Tulloch**: Yes. That's right.
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> **Stahl**: Giant cities being built with people not coming to live here?
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> **Tulloch**: Yes. I think they're building somewhere between 12 and 24 new cities every single year.

Stahl continued,

> Unlike our market-driven economy, in China it's the government that has spent some $2 trillion to get the cities built as a way of keeping the economy growing.
>
> The assumption is "If you build it, they will come."
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> But no one's coming.

And then there's what the *New York Times* called "China's Brutal One Child Policy" written about by Ma Jian in his novel *The Dark Road*. According to Jian, since 1971, China has conducted 336 million abortions and 222 million sterilizations. "These figures are easy to quote," he wrote, "but they fail to convey the magnitude of the horror faced by rural Chinese women" under that policy. He concluded:

> The atrocities committed in the name of the one-child policy over the last three decades, rank among the worst crimes against humanity of the last century. The stains it has left on China may never be erased.

One of those stains has been a fertility rate in China that has for years remained substantially under the replacement level. In developed countries the fertility rate must be at least 2.1 children born per woman. Less than that and the population begins an inexorable decline. Since at least January 2000, China's fertility rate has been below that number and is currently at 1.66. Simply put, China's one-child policy is slowly depopulating the country.

Economist Mark Perry reviewed the IMF report, ran some numbers, and concluded, "There's really nothing that the US has to feel sorry about. We're still almost 75 years ahead of China when we consider economic output per person." With China's population more than four times that of the United States, the average output per Chinese citizen is about where it was in the United States back in 1940.

Perry also noted that even if China grows as the IMF estimates that it will, it will take another 10 years for its per capita GDP to reach the level that the United States hit in 1965. And it would take another 20 years after that for per capita GDP in China to reach where it is in the United States today.

It is helpful to remember that the United States is not only the world's largest producer of oil and natural gas, but also the largest manufacturer on the planet, generating 1/5 of the total global output. Of the world's 500 largest companies, 132 of them are headquartered in the United States — twice that of any other country.

There are many lessons to be learned in the IMF report. First, not every number is to be believed. Second, not all numbers were considered. Third, China's one-child policy is killing off its population and sending it into what may be terminal decline. Fourth, the U.S. economy is beginning, albeit slowly, to recover from the Great Recession, so just when China's economy is beginning to slow, that in the United States is accelerating.

Another important lesson is just how remarkable the free market is when it is left unfettered and free to flourish. In the space of less than 36 years, China's relatively free market has turned a stagnant, inward looking country into a major economic powerhouse. It can only be hoped that those policies will be continued and expanded, and that self-destructive policies and overweening regulation by China's Communist Party that are now threatening that growth will be reversed.

So remarkable has been China's astounding emergence from a backward country over the last three decades or so that it might cause sufficient numbers of politicians and elected officials to consider unleashing the same free market here.

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