



# CHINA'S Apparent Strength

Last week, while we were busy enjoying our booming (almost-normal) summer economy and getting ready for the 4th of July, China was celebrating the 100th anniversary of the founding of the Chinese Communist Party. While this didn't capture much attention in the American media, it should have. At the big rally in Beijing, not only did Chairman Xi dress up in Mao's famous gray suit—presumably to make a serious point—but he also made some very clear statements aimed directly at the United States and our position in the world:

While arguing that China is a country that hasn't engaged in territorially aggressive behavior historically, he warned that any threats to China would be met with a "great wall of steel."

While discussing China's willingness to work with other countries and the international order he paused to say "We will not, however, accept sanctimonious preaching from those who feel they have the right to lecture us." Supposedly, the crowd assembled for the event went wild at this statement.

On the subject of Taiwan, he said that "reunification is a historic mission and the unshakeable commitment of the Chinese Communist Party."

You get the point.

China appears increasingly willing to assert itself on the world stage. They are aggressively building-up their military and, with their One Belt One Road initiative, spreading tentacles of economic influence and control to the far corners of the world. There's a sense of inevitability to China's rising power, like it's just a matter of time. However, I am not convinced this is true and many of China's recent moves, like banning Bitcoin mining, seem to be signs of weakness rather than strength.

While almost nothing good came out of the Trump administration, he was indeed right about China. His willingness to point out the truth, however coarsely and poorly articulated, was probably good for America. It certainly woke a lot of people up. We are indeed competing with China and losing and the current global world order is neither good for the US nor sustainable. It's no surprise to me that the Biden administration hasn't made any moves to unwind or change our anti-China trade policies.

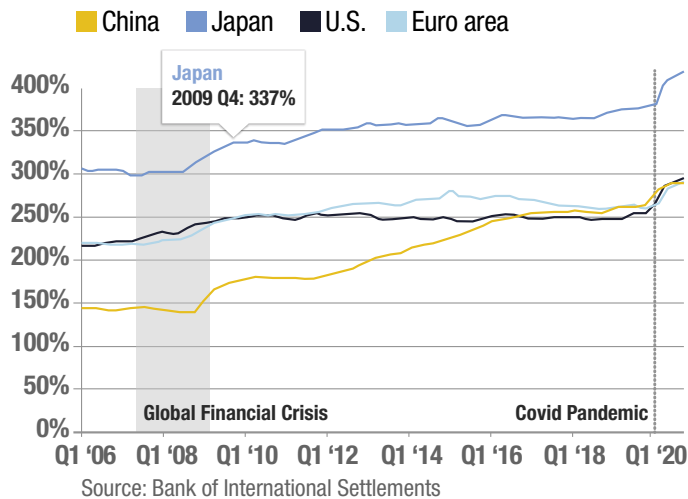
We are right to fear the rising power of China and certainly need to rethink many of our policies and positions on the international scene, but I don't think we should be too frantic or hysterical in our response. China isn't near as strong as it appears to be. America still holds the dominant

military position in the world and has the most innovative economy in world history. Oh and one not so minor point, in America we also value and protect freedom. And in case you haven't been paying much attention to history, this is kind of a big deal. More on this later.

The narrative of inevitable Chinese dominance stems in large part from their almost miracle story of economic growth. Let's put aside the question of whether we can actually trust economic data from China and just assume the numbers are true for now. Since 1978 China has averaged over 10% annual GDP growth. This is one of the most impressive economic growth stories in recorded history.

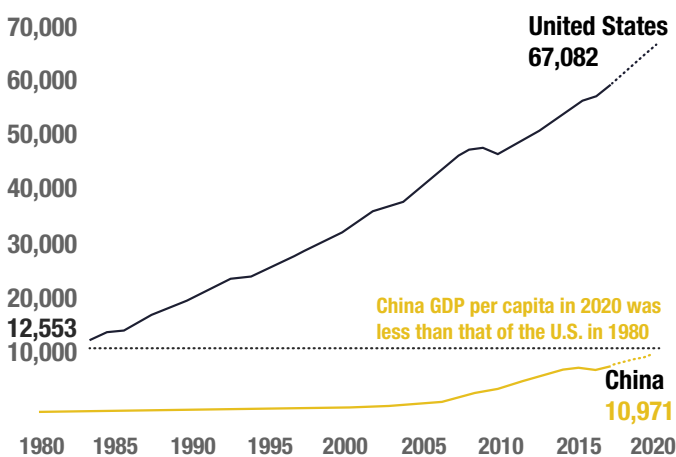
But it's only one part of the story. China actually has a bunch of problems with its economy and its future prospects are not so obviously bright as in 1978. First of all, they already have a ton of debt, as much as we do actually:

### Total debt-to-GDP ratios in major economies



### China VS United States: GDP per Capita Comparison

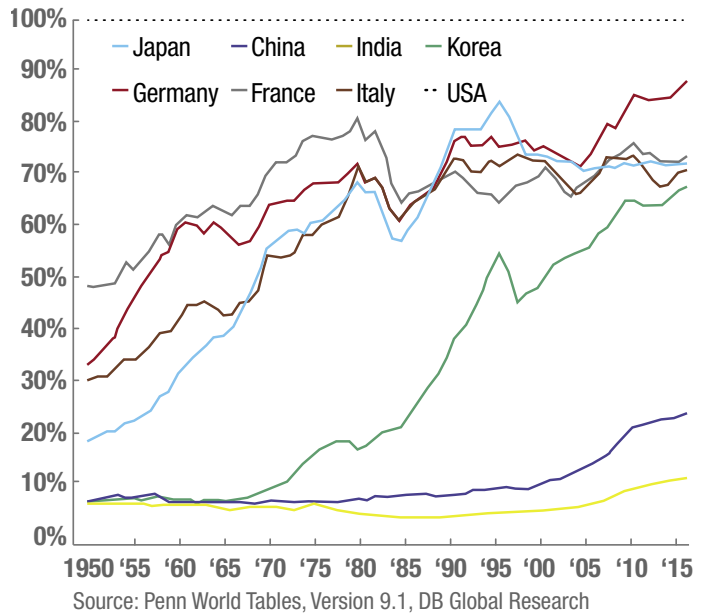
GDP per Capita, current prices (U.S. dollars per capita)



Data Source: IMF World Economic Outlook, October 2018  
Data Analysis by MGM Research

And as much as they have grown, they are still a relatively poor country, especially when you look at the level of the individual or the household:

### Real GDP per capita relative to the United States

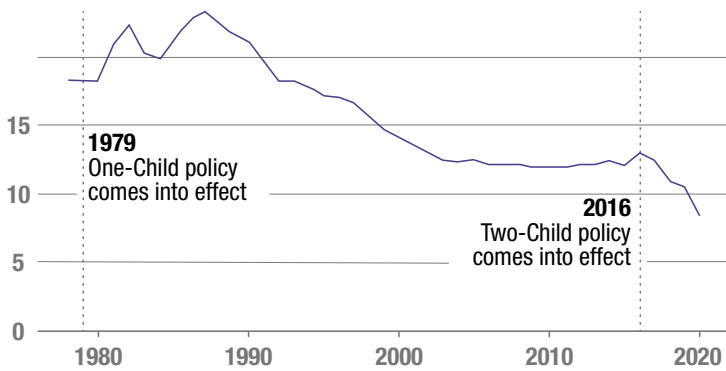


China's strength—Xi's "wall of steel"—is also its weakness. With 1.4B people it's hard to grow your way into a robust consumer-led economy like the US or the EU. Even though in absolute GDP terms China will soon rival the US, it'll be a long time before they do in relative per capita terms. What this means is that they will not be able to rely on consumer spending to drive their economy (like we do in the West) anytime soon. China will have to continue to seek economic growth by other means. They will have to make investments in either infrastructure or exports, both of which are under attack by the emerging new world order. On the infrastructure front, there are not enough natural resources in the world—especially if China is as serious about reducing CO2 as it seems to be—for China to try to urbanize their whole population. And now that the cat is out of the bag in the West about exports (I have to admit... thanks to Trump), this will be a tough road to go as well.

On top of all this China has really bad demographics. After pursuing the one-child policy for decades, they are now waking-up to the fact they are moving towards a demographic cliff and are looking at a situation, like most of the rest of the world, where they are going to have too many dependents and not enough working age people. Now the CCP is encouraging families to have kids and have moved quickly from 1-child to 2 in 2016 and now 3! Too little too late I'm guessing.

## China's birthrate has fallen in recent years

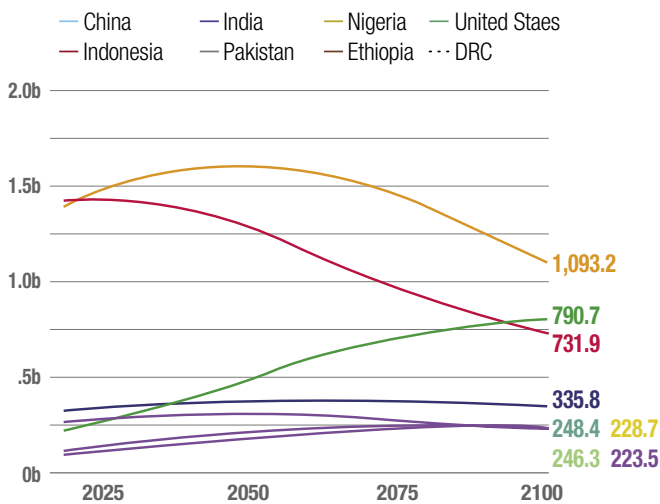
Total number of births in China per 10,000 people (1978-2020)



Source: China Statistical Yearbook

## Large population decline expected in China and India

Expected size of the population in the most populous countries on earth\* (in millions)



\*in the year 2100 Middle estimate Source: The Lancet

To make matters worse, almost no one wants to immigrate to China so that potential solution to the ageing population problem (aka America's great advantage) is out the window. This is where you start to see how important freedom is. Here in America, frustrated by gridlock and the growing ineptitude and corruption of our democratic system, we like celebrate the efficiency of China's autocratic way. But in the safety of our hard-earned and rare freedoms, we've forgotten all about the profound weaknesses and problems of autocratic governments. We've forgotten that in China today you are not free. You can't take your money out of the country. You can't mine Bitcoin. You can't even search the internet freely. And you're definitely not able to speak out against the government. The lists of "can't dos" is growing rapidly. This is weakness, not strength. China may have created a system that produces economic growth but it's a system that no one really wants to voluntarily be a part of.

There has never been a more dangerous time for the proliferation of autocratic control than today. The technology of our age is just mind-blowingly powerful. It makes the stuff the 20th century monsters used look like child's play. So to live in China today is an increasingly scary proposition. There are no privacy protections to speak of and the government is literally monitoring everything—every communication, every transaction.... Already in China there are facial recognition surveillance cameras everywhere. And they have been experimenting with social credit systems, which seek to permit or restrict access to things like public transit, commercial activities and loans based upon a person's behavioral history. These are powerful elements of state control. Already we are hearing stories of journalists and dissidents who dare to speak out against the regime being blacklisted and cut-off from operating in the world.

Wealthy Chinese have understood this problem for a long time. This is why real estate trades at such crazy prices in places like Hong Kong and Singapore. This is why the EB-5 visa program was so successful in America. People will do almost anything to get their wealth into a safe jurisdiction—that is, one that actually respects property rights—even pay irrationally high prices for real estate. The Chinese people are afraid of their own government and rightly so. Not even the titans of industry are safe. Jack Ma gave one speech that was mildly critical of the regime then disappeared for 3 or 4 months. Many presumed he was dead but he returned but with less control and ownership of his own company and some new outlooks on things. Who knows what happened there.... Just this past week, Chinese ride sharing company Didi Chuxing, found itself in the crosshairs of the government and woke-up one day to an order removing its wildly popular app from every app store. Didi's alleged infraction involves something like improperly collecting personal data on its users but its real crime was probably its ties to American companies and leaders and its decision to IPO in New York instead of at home.

One of the biggest problems of the Chinese system is that it requires a closed capital account. To keep their exports competitively priced in the global market they peg their currency at an artificially low (and unfair) level relative to the US Dollar and Euro. To pull this off they have to exercise almost complete control of what their citizens and businesses do with their money. The current rule, in place since 2007, permits Chinese citizens from taking only about \$50,000 out of the country each year. This, I'm convinced, is what the ban on Bitcoin mining is all about. While the official CCP line is that Bitcoin mining is inconsistent with China's climate change goals, the truth is that Bitcoin represents an existential threat to their system. I think this is also why they moved against Jack Ma's fintech empire Ant Financial. China is afraid of anything that takes financial

transactions outside of their official banking system, where they can exercise almost complete control.

So behind their apparent strength, behind Xi's bellicose rhetoric, China has some serious problems. They have too much debt, bad demographics, a relatively poor population and a closed financial system. Their growth engines—infrastructure investment and exports—are both under assault. While the Chinese people have thus far tolerated an unprecedented level of government meddling in and control over their private lives, the question remains whether they will continue to do so in the face of slowing GDP growth or a sustained bout of inflation or a domestic financial crisis. This, to me, is one of the most important questions of our era.

The recent moves that China has made—like banning Bitcoin mining or taking control over Jack Ma's business or potentially putting Didi out of business overnight—while they appear to be shows of strength are nothing more than clear signs of weakness. Each time China makes another

move towards control they betray a fundamental truth and problem of their system. China doesn't value freedom. The Chinese system is not a viable alternative to the American world order and never will be.

So though China is a rising power their continued success is certainly not inevitable. America still has a chance to compete with China on the world stage and do so successfully. Undoubtedly, we should be wary of China—not the Chinese people obviously but their leadership—because they are pursuing a world view that is diametrically opposed to ours and appear willing to use technology in ways that are fundamentally detrimental to the freedom of the individual. But we shouldn't be afraid of them. We are America, the place of freedom. As an individual you might be able to find personal freedom in other places, like the EU for example, but in America you have a nation strong enough to actually defend that freedom. This is worth something and, perhaps, everything. □