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Remarks for The Heart of the Matter: Reassessing the Foundations of U.S.-China Relations
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China is nowhere close to being a true global economic challenger to the US now and is unlikely to become one

The Present

- China has caught up in GDP adjusted for purchasing power parity but this indicator makes no sense whatsoever and is published for purely political reasons.
- PPP is based on the idea that goods and services in competitive markets should have the same price. But most of China's GDP transactions do not occur in competitive markets. As a secondary matter, trying to estimate a single price level for the whole PRC to compare it to a single price level for the whole US in a timely fashion is a fool's errand.
- Credit Suisse puts Chinese private wealth $62 trillion smaller than the US in mid-2014 (most recent at this time – update later this month); on their numbers average Chinese wealth growth underperforms the world from end-2011 to mid-2014.
- US public sector debt is quite large but McKinsey says total Chinese debt has been rising far faster since 2007. When I tried in a Real Clear World piece to add in public sector assets and debt in both countries, I get an American net wealth advantage of $44 trillion.

The Future

- China will never acknowledge prolonged stagnation. And it can actually generate a huge number of empty transactions that count in GDP.
- But this will not enhance prosperity. Where will true growth come from?
- Land: without full rural property ownership, environmental depletion makes growth from land impossible. There is no sign of such rights being granted.

- Labor: migration must not only be legal but encouraged, with portable benefits, for labor to contribute to growth as China ages. Reform is headed in the right direction but very slowly and incompletely.
- Capital: similarly, aggregate debt in excess of $20 trillion could kill the net return on capital for many years to come. Financial reform would have to end state control of the financial system to allow capital to drive growth. That is nowhere in sight.
- Innovation: the primary driver of innovation is competition and China's refusal to let state-owned enterprises lose is a stark limit on competition. Innovation to bring a whole economy forward cannot be commanded from on high.
- China will not close a $44 trillion gap on this path. It will barely grow at all.

American Strategy

How can a good response to China be crafted when perhaps the single most crucial feature of the country is misunderstood? If the US sees China as a rising near-peer economically, it will exaggerate the challenge and misunderstand the motives of Xi and Party leadership.