



Letter n°69

The new faces of globalization (1): United States, 11 advantages to exploit.

"The Americans are very tough, they are voracious, they want an undivided power over the world. It is an unknown war, a permanent war, apparently without death, and yet a war to the death." François Mitterrand in an interview with Georges Marc Benamou in 1994.

This statement by Mitterrand, an unconditional ally of the United States during the Gulf War and a convinced Atlanticist, reflects the relationship of attraction and rejection aroused by American power.

Based on the figures, we will try to come to an objective conclusion to demonstrate that the US economy is not declining and that the premium on the US stock market, the difference of several points between the PER of the American market and other markets, is justified.

We will consider the following 11 points to support these assertions:

- ***The advantage of resilience:***

The US economy is more resilient than other economies around the world. In 2020, during the Covid crisis, GDP fell by 3.4% in the United States compared to 6.4% in Europe. In 2009, US GDP fell by 2.6% while the European GDP fell by 4.6% and then again in 2011-2012 when the European economies declined during the Greek crisis. And the list of comparisons goes on as we go back in time.

Since 1945, the country has suffered a dozen phases of recession, and the one expected by the markets should be small.

- ***The advantage of higher growth:***

Growth is stronger in the US than in Europe: over the last two decades, GDP/capita has increased by 29% in the US against 22% in Europe according to recent Eurogroup statistics.

China's GDP by 2030 will certainly exceed the US GDP but the most important thing for the people is the GDP/capita, which is four to five times higher in the US. China does not have and may never have the GDP/capita of a rich country because there are more than 300 million poor people. China is only 75th in the world in terms of GDP/capita.

Today, despite 8 rate hikes, the labor market remains well oriented. There are still 10.7 million unfilled job vacancies in November. The unemployment rate is still low at 3.7% compared to 6.5% in Europe.

- ***The advantage of the leading stock market:***

It's been a bad year for the stock market with the US index performing much worse than Europe, Japan and many Asian markets. But since 1945, the country has experienced 15 episodes of decline of more than 20% in less than a year and each time the rebound has been rapid.

The US accounts for less than a quarter of global GDP but nearly two-thirds of global market capitalization compared to 10% for China. At the end of October, at the bottom of the market, it had fallen to \$42 trillion before recovering. But over the year, the Nasdaq is still losing some \$7 trillion.

If the number of listed companies in the US has fallen from a peak of 7,500 in 1997 to 3,600 in 2016, it is the consequence of many mergers and acquisitions, a factor that drives the market. 7/10 of the world's largest capitalizations are American and 59 of the world's top 100 companies are American compared to 13 for China.

In high-tech sectors, the advantage is even more obvious: in healthcare, 7/10 of the largest companies are American, in technology, it is 6/10.

- ***The attractiveness of the American market:***

Even before the adoption of the IRA, the Inflation Reduction Act, the United States once again became the number one destination for Foreign Direct Investment (FDI) in 2021 with \$506 billion, thus bringing the total to \$4,977 billion according to the IMF, an amount to be compared with China's \$3,578 billion.

Between 2019 and 2022, according to a study on industrial investment in the world by **McKinsey**, the percentage carried out in the US has increased from 20 to 30% and with the IRA, we can expect this trend to accelerate. Europe's share has remained stable at 13%, while Asia's share has fallen slightly.

The passage of the IRA in August 2022 will be remembered as the highlight of the Biden presidency, even if the amount is much lower than his initial \$3.5 trillion Build Back Better plan.

A \$370 billion plan of credits over ten years and subsidies to decarbonize the economy. A plan that the planet should welcome because it is about promoting renewable energies, wind power, hydrogen, solar panels and electric cars. A plan to try to reduce their emissions by 50% by 2030. It is an essential plan for a country that is the 2nd largest polluter in the world with 12.5% of greenhouse gas emissions behind China which accounts for a third of GHG emissions. A plan that should sound like a wake-up call for competitor countries, especially in Europe because it offers substantial advantages to industrialists producing on American soil. A plan denounced as protectionist by some, but presented by the Americans as a plan to revive the industry.

To obtain a tax credit for the purchase of electric vehicles, a significant proportion of American components is required. Specifically, the \$7,500 subsidy for the purchase of an electric vehicle requires that the batteries contain at least 40% of locally mined minerals. Subsidies can be as high as \$13,000 if the electric car is assembled by unionized American workers. There is undeniably stiff competition for Mexico and Canada.

The subsidies are also worrying European countries, which are already penalized by the difference in energy prices between the two sides of the Atlantic.

The Americans justify these protectionist measures by the need to ensure international security and point out that 2/3 of American imports are duty-free.

- ***The advantage in agriculture:***

Only 1.5% of the working population is employed in agriculture but this is enough to make the country the world's leading exporter.

- ***The advantage in commodities:***

Since the start of production of shale oil fields, the US has had oil production comparable to that of Saudi Arabia and slightly higher than that of Russia. With Saudi Arabia having decided to reduce its production, the US is in fact the world's leading producer.

The advantage is even more evident in gas where the prices of American gas available to American manufacturers are 3 to 4 times lower than the price of gas offered to Europeans; an unquestionable advantage in sectors sensitive to energy costs, such as paper, chemicals, steel...

- ***The advantage in technology:***

The US has 5/10 of the most prestigious universities in the world and the largest research budgets.

The US has the advantage of research spending, 3.2% of GDP, a higher percentage than the EU and China at between 2 and 2.3% of GDP.

Between 2016 and 2022, North America received 30% of semiconductor investment, Europe only 7%, Asia, mainly South Korea and Taiwan, 63%, according to the Institute for Reindustrialization in France.

The Chips Act, also concocted by the Biden administration, will give \$50 billion to American semiconductor manufacturers. With this Act, the US will regain positions lost in recent decades. It has just obtained from the Taiwanese company TSMC, the world leader in the sector, a tripling of its investment project to \$40 billion in its factory in Arizona.

GAFAM have a formidable financial force and in order to maintain or strengthen their positions, they have increased their investments by 30% each in 2020 and 2021 and again by 20% over the first 9 months of 2022. Apple alone spent \$100 billion on research between 2016 and 2021.

- ***The advantage of the \$ as a reserve currency:***

The advantage of a reserve currency is that it can run deficits, eventually allowing the currency to depreciate and shifting the burden onto other economies.

In the 1960s, General de Gaulle already denounced the exorbitant privilege of the \$. The € was conceived as a possible alternative to the \$ in the long term, the Chinese intend to promote the role of the Yuan, which is a complex exercise because the Yuan is still not convertible, the Russians and Iranians are constantly criticizing the pre-eminence of the \$ but it is not likely to disappear soon.

This year's evolution is quite striking. In February, the Chinese and Russians, and even Indians, showed their determination to do without the \$ but it is clear that the trend has been the opposite. In these times of crisis, the \$ has been, as always, the safe haven. The \$ has appreciated against almost all currencies, the weight of the \$ in international transactions has slightly increased to 59.5% while at the same time the weight of the € has stagnated at 19.8% as that of the Yuan at 2.8%. We are far from a currency revolution.

- ***The demographic advantage:***

The US has a population growth advantage, 0.5%/year compared to a stagnation in Europe and a decline in China of more than 0.5%/year.

The US has always been a land of migrants and the dynamism of capitalism benefits from this. As ***Philippon*** observed, the three most successful laboratories in developing Covid vaccines are run by three immigrants: a Turkish couple founded BioNTech, a Lebanese of Armenian origin created and runs Moderna, a Greek runs Pfizer. Examples of a diversity that China cannot afford.

- ***A new active role on the international scene:***

To Trump's nationalism, Biden opposes universalism, to Trump's disregard for democracy, he opposes a respect for values, to unilateralism he opposes a return to multilateralism.

With Trump's nefarious parenthesis closed, Joe Biden rightly set about strengthening the cohesion of the democratic bloc on the international stage.

We can therefore successively analyze the relationship with China, with other democracies, with Africa and the Middle East:

Between the US and China, the war is above all economic and technological. Biden has maintained Trump's steel tariffs even though they are upsetting automakers who are angry about rising steel prices and consumers who are angry at paying more for vehicles purchased in the US. At best, these steel taxes will have allowed the establishment of a few units at Nucor, US Steel, but not a revolution on the competitiveness and profitability of a sector plagued by overcapacity.

The US trade deficit with China has not narrowed in recent years. In the first 10 months, exports to China rose 8% to \$124 billion and imports rose by 13.6% to \$462 billion. In addition, there are US purchases from Vietnam and Bangladesh, purchases that were previously made from China.

Biden wants to expand the G7 to Australia, India and South Korea. He intends to strengthen the American presence in Asia.

If the Americans want to align themselves with the Europeans, the Japanese and the South Koreans in their policy of firmness towards China, they would have to make concessions, for example, making European or Korean electric vehicles eligible for the IRA.

Biden is re-engaging with Africa and has invited some 50 heads of state to Washington. While China-Africa trade currently stands at \$260 billion and China has made \$700 billion in loans or investments on the continent, American trade with Africa does not exceed \$80 billion, but the Americans are committed to providing \$55 billion in aid over the next three years. Americans are particularly interested in lithium and cobalt reserves and Biden wants to attract the 45 million African-Americans.

Finally, Biden recognizes that he cannot abandon the Middle East if it means handing it over to China.

- ***The advantage in defense:***

Some people talk about an American decline, but that ignores the numbers. The Americans alone, at \$730 billion, spend more than the next eight countries.

At a time when Putin is putting the economy in a state of war, requisitioning civilian companies for the production of arms and increasing his budget from \$50 to \$70-75 billion, the US is voting in Congress to increase the budget by 10%, \$75 billion, to \$825 billion. The discrepancy is glaring and yet there is no mention of the greater precision of American weapons.

The major American defense groups - Northrop Grumman, General Dynamics, Boeing, Lockheed Martin and Raytheon Technologies - should benefit from the image given by the more than \$60 billion in US aid to Ukraine.

Conclusion: "Americans will always do the right thing" Churchill.

Churchill's word rings true and he is neither the first nor the last to denounce the selfishness of a nation in its constant quest for self-interest. The observation is correct but let's face it, all nations do the same and this is one of the missions of political leaders. But coming from the world's leading power, it's just more showy.

If we cannot ignore the size of the US trade deficit, \$970 billion in 2021, \$166 billion in the first nine months of 2022 with the EU despite gas sales, \$338 billion with China also in the first nine months; If we cannot ignore the size of US debt in foreign hands and if we cannot ignore the poor image of the US in many countries, we must recognize their primacy and the attractiveness of their market.

If, with ***Thomas Philippon***, we must observe that the US is no longer the most competitive country in the world because, in many sectors such as air transport and telecoms, concentration has developed and prices are higher, the losers are consumers and winners are the companies, sometimes less innovative but benefiting from higher rates of profit.

If the growth rate of real GDP/capita has declined: 3.1%/year in the 1960s, 2.1%/year in the 1970s, 2% in the 1990s, 0.8% in the 2000s, 0.6%/year between 2010 and 2017, it is a phenomenon that has been observed in many other countries because new waves of technological progress have less impact on productivity.

At a time when China is showing an ideological stiffening and is now unable to maintain the growth rate of above 10% per year as observed between 1980 and 2010 and at a time when Russia is weakening and tarnishing its image as a power, no country seems likely to weaken the primacy of the US.

This year, the US market (S&P – 18%, Nasdaq – 30%) has, as expected, underperformed the EU (EuroStoxx – 11%, CAC 40 – 9%) and Japan (-4%). At the same time, IPOs in 2022 fell by 78% in numbers and 90% in volume, the lowest amount in 20 years.

However, in light of the various points analyzed in this Letter 69, let us quickly anticipate a new outperformance of the US market, which will undoubtedly be the first to initiate a rate cut at the end of 2023.

Geneva, 20th December 2022

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