

**Demetri Kofinas:** Today's episode of Hidden Forces is made possible by listeners like you. For more information about this week's episode or for easy access to related programming, visit our website at [HiddenForces.io](https://HiddenForces.io) and subscribe to our free email list. If you want access to overtime segments, episodes transcripts, and show rundowns full of links and detailed information related to each and every episode, check out our premium subscription available through the Hidden Forces website or through our Patreon page. Remember, if you listen to the show on your Apple podcast app, you can give us a review. Each review helps more people find the show and join our amazing community. With that, please enjoy this week's episode.

**Demetri Kofinas:** What's up everybody? I'm Demetri Kofinas, and you're listening to Hidden Forces where each week I speak with experts in the fields of technology, science, finance, and culture to help you gain the tools to better navigate an increasingly complex world so that you're less surprised by tomorrow and better able to predict what happens next.

**Demetri Kofinas:** My guest this week is Anne Stevenson-Yang, Co-Founder of J Capital Research, which provides institutional investors with primary research on China's economy and Chinese companies. Anne was formerly Co-Founder of a group of online media businesses called Blue Bamboo Ventures and also founded and operated a CRM software company, Clarity Data Systems, and a publishing company whose flagship magazine is City Weekend. Over 25 years in China, Anne has also worked as an industry analyst and trade advocate heading the US Information Technology Office and the China Operations of the US-China Business Council. She is also the author of *China Alone: China's Emergence and Potential Return to Isolation*.

**Demetri Kofinas:** This week's conversation is a continuation of two prior episodes dealing with China's economy and banking system but with a very particular focus on the renminbi-dollar peg which could become a significant source of financial instability across the globe as China struggles to prop up the value of its currency amid a declining current account, dwindling foreign exchange reserves, a surging foreign debt balance, illicit capital flight, and a banking system that is stuffed to the gills with nonperforming loans and trillions of dollars of newly-printed currency.

**Demetri Kofinas:** We also discuss the rampant amounts of fraud in Chinese companies listed on western exchanges, including the likes of Alibaba and Tencent, and why it matters for investors everywhere. With that, let's get right in to this week's episode.

**Demetri Kofinas:** Anne, welcome to Hidden Forces.

**Anne Yang:** Thank you, Demetri.

**Demetri Kofinas:** We started our last conversation with the question: What's happening or what's going on in China? I think I asked you: What's going on in China?

**Anne Yang:** Mm-hmm (affirmative).

**Demetri Kofinas:** My instinct is to ask you that question again, but to be more narrowed about it. So, you started me down this road with the show. I had an interest in this subject, but my episode with you really helped to plant the seed. We did an episode with you and one with Dinny McMahon on the Chinese banking system, the growth of debt in China. We also had a show with Elizabeth Economy where we talked about more to the political dynamics.

**Demetri Kofinas:** I think what's interesting today is to discuss not just where we are today. Because there are shifts and there are things that have been changing both with the trade war, also the changes in China's current account, which are impacting the peg of the renminbi. And the world looks like it might be much closer to recession today than it was two years ago. There are a lot of these forces that are intersecting. It feels like a lot of them may be intersecting in China.

**Anne Yang:** I think that's absolutely true. You have the world right now, and particularly China, poised in a kind of unnatural calm and stasis that doesn't portend particular well. So, I think we all believe, and especially the Chinese leadership believes, that China faces a real threat of a financial crisis. And even absent a financial crisis, China is going to go into a long period of low growth and recession. What I find is that we think a lot in the West about the threat imposed by China's strategic issues and development of its military by its technological progress and by its economic challenges or financial challenges to the US. But what we don't really talk about is the risk that it means for the international financial markets, so I think that is worth exploring.

**Demetri Kofinas:** What risks concern you the most? I mentioned that there has been a change in China's capital account and the direction of its capital account. They've continued to print massive amounts of money particularly since 2008. That's concerning because they can maintain that peg - given the fact that they have a closed capital account - they can maintain the renminbi peg to the dollar so long as they have the foreign exchange reserves to buy the goods they need in order to continue to build the products that they sell to get the dollars they need to keep the thing going. Right?

**Anne Yang:** Right. I would broadly arrange the threats into, let's say, four categories. The first one is that exactly. It's the renminbi and US dollar peg and what that means for international inflation, deflation, and asset values. The second one would be the fraud. Basically the fundamentally extractive nature of assets in the Chinese economy for elites.

**Demetri Kofinas:** The China Hustle.

**Anne Yang:** The China Hustle, but the China hustle was of a fairly small nature. What I'm talking about is China's many centuries of tradition of elites owning the salt monopoly, the iron monopoly, now all of the major companies, and believing that it's their right to own these assets and to extract value from them. What does that mean once US investors and international investors are funding these assets? I'd put that as number two.

**Anne Yang:** Number three, I would say the failure of Chinese institutions to adapt to the modernized economy and the politicization of Chinese institutions, which has meant the politicization of economic data. If you think about it, if you're an international company, you're dealing with reports on GDP growth of, let's say, 6.5%, but all of your own data is showing that growth is around 2%, what do you say to investors and how do you plan? That would be the third chunk.

**Anne Yang:** Then the fourth chunk would be financialization of the economy, something that we're very familiar with over here. But here you have companies like, let's say Tesla that are able to act in very uneconomic ways because they are so heavily financed...they have so much capital investment. Tesla, Uber, this sort of company. In China, that's basically all the companies that are internationally exposed. And as a consequence, you have a tremendous amount of manufacturing services and so on that are priced under cost. What does that mean for the economy, and as that changes, what will it mean?

**Demetri Kofinas:** I guess the larger significance of this - all of these points - these things are challenges to overcome in order for this economy to liberalize and to become the type of more open Western-type economy that the hope had always been in the United States that China would become.

**Anne Yang:** Well, I don't think that's gonna happen. But I think the issue that we need to focus on in the West is: What does it mean as these things start to unwind? What does it mean for international investors? For example, how many people have their pension funds exposed to companies like Tencent and Alibaba? Tencent and Alibaba are not gonna be around forever on public markets. Once they shrink and go back private, what does that mean?

**Demetri Kofinas:** Explain that. Why are they gonna shrink and go back private?

**Anne Yang:** Well, without getting into arguments with particular Tencent and Alibaba investors, let me just generalize and say that I really have never seen a listed company in China that did not have significant and material fraud. I know that's a harsh statement, but it's really true. The nature of fraud in state owned companies is different from the nature of fraud in private companies. State owned companies tend to have high margins as they report, but they tend to have extractive mechanisms in the background where the founders and their families leach out the cash, so you need to sort of discount the cash. Private companies tend to overstate their margins and their profits and, as a consequence, overstate their balance sheets.

**Anne Yang:** There are a lot of very large companies that are traded in the US and that US investors invest in that have those problems. When they stop receiving so much in terms of capital investment, they will also stop seeing kind of headline growth. As they stop seeing headline growth, people will begin to disinvest. Their share price will start to deflate, and eventually they will no longer find it useful to be listed.

**Demetri Kofinas:** Well, let's go back to the renminbi, because this to me is the story that is most likely to prick the bubble. Would you agree with that?

**Anne Yang:** Yeah, because, look, we talked a little bit about the unnatural calm in the markets. You had a period, a long period, when the international economy was seeing low inflation and high growth because of the peg to the renminbi. You had the Chinese essentially just holding down the value of the renminbi and investing very heavily. China is essentially absorbing costs that the international economy doesn't see, so manufacturing moves to China. You have cheap manufacturing assets, cheap capital assets, cheap labor, and so on and so forth, so consumption booms internationally.

**Demetri Kofinas:** They were importing the world's inflation. They were exporting deflation.

**Anne Yang:** Exactly. Exactly, by holding down the value of the renminbi. Now, ever since late-2014, China had a big selloff of its foreign reserves in 2015, late-2014/2015. Since then, the reserves have really not risen. There's been a few little bumps here and there, but those are valuation bumps really.

**Demetri Kofinas:** How accurate are those reserve numbers? The official reserve numbers I've seen, I think, are 3.2 trillion US dollars.

**Anne Yang:** I forget what it is right now. It might be that, 3.19.

**Demetri Kofinas:** Something around there.

**Anne Yang:** Something in that order. Well, I would take them with a very serious grain of salt. It doesn't mean that they have only 1 trillion or something, but they rely very heavily ... And you can see this as the reserves fluctuate, the headline reserves fluctuate quarter to quarter ... on valuation issues. Valuation of their listed assets, valuation of some of their private equity assets, valuation of currencies and so forth. Those movements are not made visible.

**Demetri Kofinas:** What's the liquidity of those reserves?

**Anne Yang:** Well, we know that they hold about 1.1 trillion in US dollar reserves, foreign reserves.

**Demetri Kofinas:** That's an interesting point. That's right, because I've seen that number. That's why I'm curious how they would be at 3.2 trillion. I would have imagined that the US assets would constitute at least half of their foreign exchange reserves.

**Anne Yang:** Yeah, but I think the way you think of it is that the US assets are the liquidity tool. It doesn't mean that the rest of the reserves are not really reserves, but they're not reserves that they can tap easily. For example, international debt held by the China Development Bank would be part of the reserves, at least the portion that was traded for dollars years ago.

**Demetri Kofinas:** Right, which could be worth very little.

**Anne Yang:** That's right. You know, it could be worth something, but are you gonna get Venezuela to pay you \$40 billion tomorrow? No.

**Demetri Kofinas:** Right. Exactly.

**Anne Yang:** Absolutely not, so.

**Demetri Kofinas:** Those were tools of part of their state craft, right? You could think of that in a sense.

**Anne Yang:** Yes. Yeah, that's right. Then there are equities that can't be sold at that value. There's a significant holding in China's listed banks, which I believe a portion of which is included in the reserves for historical reasons that I won't bother to go into. The central government could sell those assets. But they wouldn't want to because it would tank the value of the banks, and they rely heavily on getting dividends. There's a lot of stuff like that. I think you can count on liquidity of one and a half trillion or so.

**Demetri Kofinas:** If China were to float, if they were to break the peg today, and they were to float the renminbi, what would be the revaluation in your view?

**Anne Yang:** Well, you tend to overshoot initially, so I'm thinking that it would drop by 30 to 40 percent, probably about 40%, and then it would bounce back. But bounce back by sort of 30%. It needs to get to a rate at which Chinese people no longer think it worthwhile to extract their assets. You have right now every taxi driver in Beijing who's earning a thousand US dollars a month in gross income has property that's nominally worth a million US dollars, right?

**Demetri Kofinas:** Mm-hmm (affirmative). Mm-hmm (affirmative).

**Anne Yang:** It seems like it would make a lot of sense for that person to sell his property, take the money, and either just live or move overseas. You would have to make that property liquid, but, anyway, you have to-

**Demetri Kofinas:** You have to also be able to get the money out, and there's a huge vig to get your money out of China.

**Anne Yang:** Exactly.

**Demetri Kofinas:** Not everyone can do that, right?

**Anne Yang:** Exactly.

**Demetri Kofinas:** I've seen some figures in terms of precious stones that have been purchased out of Hong Kong. Then also bitcoin was a big pathway through which Chinese citizens were able to get their money out up until, I think, end of 2017, beginning of, yeah, beginning of 2018. Somewhere around there.

**Anne Yang:** Yeah, it was like September 2017, they closed down the exchanges.

**Demetri Kofinas:** Right.

**Anne Yang:** Yeah, those are all significant impediments as are culture and taxes and understanding the international real estate. But, nevertheless, if you're a fairly elite Chinese person and you earn the average Chinese elite educated salary of, let's say, 7000 renminbi per month ... a little less than a thousand US dollars ... and you're sitting on real estate that's nominally worth \$2 million, you're gonna be trying hard to sell that and get yourself to Canada where education and health are free more or less. You could just live on that money for quite a while. You could buy a house for \$300,000 in some rural area and then live on that money.

**Anne Yang:** You have to raise ... You're probably willing to spend 10 or 15% more than it's really worth in order to get your money out, but you're not willing to spend 30 or 40%. I think that's the key issue where the currency has to settle. Where are people going to think that the impediment is too high?

**Demetri Kofinas:** What happens in such a scenario? If they were to experience that level of inflation suddenly overnight, what would that mean for the CCP, for the Chinese Communist Party, and what would it mean for stability in China, which is its number one, two, and three goal?

**Anne Yang:** Well, I think, actually, for stability, it's a prop, because what would instigate it is a rapid decline in the value of property. Everybody has property in China. Everybody treats property like their retirement fund. It's more like a mutual fund than a thing.

**Demetri Kofinas:** You know what? Talk a little bit, because not everyone understands the reason why so many Chinese have purchased property. That has a lot to do with the financial repression in China, the difficulty of saving, because inflation perpetually runs above the rate of interest. China has negative interest rates for

how long? Right? That's how they've been able to keep the household sector so small and the consumption as a percentage of GDP so small and savings and investments so high. Right?

**Anne Yang:** Generally speaking that's true. That did change over the last few years. But, nevertheless, in a general sense that's true. People don't trust the banks in China. They certainly don't trust the banks to maintain the value of their money in the long term. They do trust property. So, the way people buy property is the way you and I would buy a mutual fund. You go down to the bank and you say, "Okay, so I'm having a child next month, and I'll buy this apartment. By the time the child is 18, he can live there or else he can sell it and go to the UK for school."

**Demetri Kofinas:** Mm-hmm (affirmative). Before I interjected with that point, you were answering a question that I posed to you about stability in the country and how this impacts stability. You were saying it's actually a prop for stability.

**Anne Yang:** Right, so as we began to see a glimpse of this last September because the Chinese authorities were trying to keep a lid on credit to the property sector, so the property sector not having enough liquidity started to cut prices so that they could sell and drive some cashflow. If you bought an apartment two years ago in an Evergrande Complex in Guangdong, and it hasn't been completed yet. You haven't moved in yet. Then the same complex cuts prices for new units by 20%, you're really pissed off, so you go and protest. That happened in seven cities as reported last September until the authorities ran in with truckloads of cash and stopped it from happening. If you broke the peg, that would happen. They would liquidate like crazy. Prices of assets would rise, and so that would probably stave off some of the popular anger.

**Demetri Kofinas:** That's interesting. What further effects would it have in the country, in China? Then I'm mostly curious to ask you what impact it would have on US financial markets and Western financial markets?

**Anne Yang:** Well, within China you'd also see the stock markets rise, and people on the balance sheet would feel richer for a little while. But that may not last a whole long period of time, because you couldn't take your renminbi overseas the way you could in the past.

**Anne Yang:** You know, remember ... You probably don't but ... in the 1960s Americans were just like traveling through Europe on cheap dollars and could buy anything and stay anywhere. Then it became Japanese in 1990s, and now it's Chinese. Chinese are very happy with that situation that they can go on safari to Botswana and do so on a very highly valued renminbi. That will change, and that will make elites unhappy, but for the short-term, asset values will rise. Internationally, I think you have one of two possibilities. One possibility is that you send inflation out into the world, right?

**Demetri Kofinas:** Mm-hmm (affirmative).

**Anne Yang:** Because Chinese renminbi valued goods are going to get a lot more expensive. But the other possibility is that as that happens, if your DVD players and your lawn mowers and all that stuff that you're importing from China, if that rises in price by 30 or 40%, you can really see the possibility that the international partners will just kind of lock China out of the trading system.

**Demetri Kofinas:** How would that unfold in your view?

**Anne Yang:** You initially do it by just raising tariffs to extremely high levels to compensate for the currency decline. Then China just decides to opt-out of WTO or ADB or whatever it might be.

**Demetri Kofinas:** You're saying they would raise tariffs because Chinese goods would become even cheaper and more competitive with Western goods?

**Anne Yang:** Yes, that's right.

**Demetri Kofinas:** That's what would initiate it.

**Anne Yang:** That's right. Yeah. Yeah. That's opposite of what I should just said, isn't it? Sorry.

**Demetri Kofinas:** No, no, no.

**Anne Yang:** Currency is always so difficult, which direction.

**Demetri Kofinas:** Yeah. Am I off track here? Because I am sort of a bearish person, and I do tend to sort of ring alarm bells, so I don't like to do it outside of my head.

**Anne Yang:** Yeah, I know how that feels for sure.

**Demetri Kofinas:** But, you know in the 1920s and the '30s, Germany experienced a depression, a hyper-inflationary depression actually. It led to the rise of national Socialism. The Chinese already have a strong nationalist feeling in the country. That's something that they've had for a long time. They've been expanding geopolitically with the Belt and Road Initiative, with the islands in the South Pacific. Is that a legitimate concern that if their economy was to go south and they were to turn inward, that the way they would stabilize the country politically without having the promise ... without being able to fulfill their promise on economic growth ... would be by basically pointing externally towards some foreign boogeyman? Whether it's the United States or some other country and militarizing, and then we end up in some place some years from now which is not dissimilar to where we were pre-World War II?

**Anne Yang:** I think that the chain of connections and probabilities and causal relationships is just too lengthy and too complex to make that calculation. I don't really

understand very much about countries and their strategic ambitions and their military threats. I do observe that where we're here in 2019, right?

**Demetri Kofinas:** Mm-hmm (affirmative).

**Anne Yang:** The US financial crisis occurred just over 10 years ago. It took seven years ... I mark it until the 2016 election ... until the United States realized the incredible upsurge of popular anger that led us to the current political situation. Now consider that China will be much worse.

**Demetri Kofinas:** Right, because China doesn't have the reserve currency that it can print.

**Anne Yang:** That's right.

**Demetri Kofinas:** Right?

**Anne Yang:** Yeah, that's the simple reason. The imbalance of social resources, the wealth imbalance in China, has become really, really acute.

**Demetri Kofinas:** So, Bob Wittbrot, who writes under the name Deep Throat IPO, has a theory around this, which is a layer on top of what we're describing, which is that the Chinese aren't simply going to allow the peg to break. That if they see they can't sustain the peg that they're going to begin to use the dollar assets they have in foreign banks, which he calls China dollars, the equivalent of Euro dollars, to begin to, systemically attack Western financial institutions. Are you familiar with this theory? He calls it the Xi Sell Button.

**Anne Yang:** No. I've missed that blog.

**Demetri Kofinas:** Oh, really?

**Anne Yang:** That must have been his most recent posting.

**Demetri Kofinas:** I think it's a pretty extreme, I actually found a beautiful picture that works really well with that. How you couldn't get more literal, right?

**Anne Yang:** Right.

**Demetri Kofinas:** But it's classic financial warfare. He says that there are at least 21.4 trillion both on and off balance sheet assets of known non-bank dollar debt lurking outside of the United States. That, in other words, outside of the Fed's purview. He thinks that they could start playing whack-a-mole with US assets. It sounds far-fetched to me. It's far-fetched, I suppose, only in the sense if you don't believe the CCP is just this really militarized organization that is intent on bringing down the United States. I'm just curious. I thought since you had him on the show, you might have heard of it.

**Anne Yang:** No, and I need to read that blog and talk to him about it, so I don't really understand the details. But I would just say this. Number one, dollar assets are dollar assets. If you don't own dollars, you have to have dollar assets. You can sell this one and buy that one, but you're not trading out of dollars fundamentally on it.

**Demetri Kofinas:** Right, but I think his point was, let's say, if they own x amount of equities or treasuries or whatever, if they can sell a large enough amount that the market doesn't have the liquidity to cover, they could begin to destabilize global markets in a way that's inconsequential to them because they're already gonna have to withdraw anyway. It's a very aggressive theory.

**Anne Yang:** I don't see it. I think that countries are much more focused on their own financial well-being than on screwing with others.

**Demetri Kofinas:** Do you think Americans, maybe not all Americans, but that the sentiment in America today views China incorrectly, let's say the Steve Bannon's of the world, are they missing something about China? Are they seeing China in an unfairly hostile light?

**Anne Yang:** I think that the heightened suspicion toward China is actually appropriate and that there are too many Chinese violations of international norms and international rules that we've been eliding and avoiding noticing for 10 years because it was lucrative to do so. I think that the Steve Bannon-type remedy is also wrong. I think what you do is you find ways to mitigate risk. There are plenty of risks with dealing with other countries as well as China.

**Anne Yang:** There are risks ... We've discussed, I think, 5G and the build-out of 5G and the new efforts by a number of countries to ban Huawei from new 5G networks. There's a legitimate concern that previously wasn't really voiced about Huawei as an arm of the Chinese government and its buying activities and things like that. Okay, so that's true. But is it not also a risk that the United States has allowed our own telecom suppliers to die and to be killed by the massive volumes coming out of China and to some extent elsewhere?

**Demetri Kofinas:** Well, that's goes back to one of your four points, which was the subsidies-

**Anne Yang:** The financialization of the economy.

**Demetri Kofinas:** Exactly.

**Anne Yang:** Exactly. Exactly, so that's a concern, too. As a carrier, you don't want to be 100% dependent on any one supplier. Having Huawei in the mix is probably important. The issue is how to mitigate the risk, not how to just not have Huawei in your network anymore.

**Demetri Kofinas:** Mitigate the risk and then also how do you get to a place where you can replace them so they don't exist where you don't have to rely just on Ericsson?

**Anne Yang:** Yeah, and also how do you start? All of the big retailers, many years ago, started a supply chain management process where they started to look at where supplies came from, was it child labor? Are you getting minerals from war-torn countries? Things like that. You need to start implementing the same process with technology. Where does the software come from? Where do the chips come from? Who has access to it? You need a certifications process that we've probably been to loose about.

**Demetri Kofinas:** Is anyone talking about this in Congress?

**Anne Yang:** Yeah, I think they are, but I find that the level of sophistication about China in Congress, and particularly in the current administration, is pretty low. The debate tends to be: Should we hate China or should we love China? What are the practical ways to deal with China?

**Demetri Kofinas:** How much of that is ignorance and how much of that is that China has been very effective in using money to lobby American interests so that they can continue to operate in the way that they've operated?

**Anne Yang:** It uses money in a much softer and, in a way, more pernicious way than say Russia does. Russia we know funds the NRA and uses sort of formal lobbying circuits as well. Or, you know, informal as they must be. But China's great drawing card has been its economy. If you're an investment bank, the ability to float one of their companies or raise debt for one of their companies, and for people like just regular old people like me, the chance always held over your head that they might recall your visa and not let you in, and that destroys your livelihood.

**Demetri Kofinas:** If you speak out in any way that they consider to be a negative.

**Anne Yang:** Exactly, so if I were to, let's say, write an article about Xinjiang, I could count on not being allowed into China again.

**Demetri Kofinas:** How does that impact you?

**Anne Yang:** Well, let's not talk about me in particular, because I'm a small sesame. But there's a whole community as they say in Chinese. Sorry, this is small potato.

**Demetri Kofinas:** That's all right.

**Anne Yang:** There's a whole community of people. I think that this is why, for example, China has not had an effective dissonant movement until the unfortunately, slightly mad, Falun Gong movement. Why Falun Gong? Because they're bared from entering China, so they have nothing to lose. But all of those Tiananmen

dissonants, they all eventually made their, or most of them made their fortunate in business in one way or another. They had incentive to downplay the human rights issues and just decide, "Well, you know, I've now joined X fund and human rights are not relevant to x fund, so I won't talk about it."

**Demetri Kofinas:** These are Chinese nationals living in China?

**Anne Yang:** No, Chinese nationals who fled China after the Tiananmen Square Massacre, and then found a way to get into business.

**Demetri Kofinas:** What impact has the trade war had on the Chinese economy? Then how is that gonna boomerang back to the US do you think?

**Anne Yang:** I don't think the trade war has had tremendous effect on the Chinese economy. After all the Chinese renminbi depreciated almost in tandem with the US tariffs. It's had a tremendous psychological effect, and Chinese people tend to blame the weak Chinese economy on the US and the trade war. Until the Jerome Powell pivot last December, it made US dollars more scarce, and that is very threatening to China for all the reasons we discussed.

**Demetri Kofinas:** Well, that, the trade war, and the Fed tightening was like a pincer movement, because as the current account declines ... They're getting less dollars through trade through income ... they have to rely more on the debt market, and at the same time they have to rely on borrowing dollars, interest payments on dollars are going up.

**Anne Yang:** Exactly. Exactly.

**Demetri Kofinas:** And they've got, I think, over 50% less than a year ago, it was something like 63% of foreign debt was short-term.

**Anne Yang:** Mm-hmm (affirmative). Exactly right. Now, there were some ameliorating factors like we had the so-called Tax Reform Act of 2017. Was it 2017 or '18? I forgot now. I think it was 2017.

**Demetri Kofinas:** I thought it was '18. I'm sorry. I thought it was '17, but I might be mistaken.

**Anne Yang:** Yeah, so I think it's '17, but that in effect was a type of QE, because you really borrowed a trillion dollars to invest in corporations, so that kind of eased the US dollar. Now you have Powell ending the rate hikes and increasing the bond buying, so that changes the international landscape as well. But overall, the trend is not positive for China.

**Demetri Kofinas:** What happened? Let's switch a little bit to the US since we're kind of on the border there. How do you see that moving forward? The expectation is that the Fed is pausing, at the very least, if not possibly cutting if we head into a

recession. Do you think that we are in a recession? What do you think the likelihood is that we're in one or we're gonna be in one in the next 12 months?

**Anne Yang:** I'm no macroeconomist. I share with you a rather dark view. I believe that recession is coming, that it's not here yet, but that is coming. I believe that the Fed will cut and not increase rates. One of the sad things about the Fed is the increasing politicization very similar to what happens in China. If we see Herman Cain appointed to the Fed, the Fed, the Supreme Court, the SEC, all sorts of institutions now are really tools of the political powers-

**Demetri Kofinas:** Of the Executive.

**Anne Yang:** ... of the Executive rather than independent institutions. That's rather sad to see. I do think it will change in the next administration.

**Demetri Kofinas:** Well, it also creates a lot of instability for financial markets. Because if they started thinking that every change in the Executive Branch is gonna lead to a significant change at the Fed or some of these other stable institutions, that changes the entire dynamic for speculation?

**Anne Yang:** It does. The political nature of Chinese institutions and Chinese data have introduced a degree of volatility into international financial markets that I think was not there before the late 1990s when China really emerged as a factor. I think the same is true with the United States. The politicization of these institutions introduces greater volatility.

**Demetri Kofinas:** Do you think Trump's gonna stay on after 2020?

**Anne Yang:** You mean if he wins or if he loses?

**Demetri Kofinas:** Do you think he loses? Do you think he wins? What impact do you think a recession would have on that outcome? If we're in a recession during the election?

**Anne Yang:** Well, clearly he has the lowest approval ratings for anybody in an economy that ostensibly is doing well.

**Demetri Kofinas:** Mm-hmm (affirmative). What are his approval ratings right now?

**Anne Yang:** Well, they're always at 41 or something.

**Demetri Kofinas:** That's what they were before he got elected, too, right?

**Anne Yang:** It is always, always, always. Yeah. There's a hard core of people out there who just are not gonna change their minds no matter what. They're hard core on either side. But I don't think those numbers ... The number change 90 basis points here and there, but they don't really change no matter what. Now he has

a whole vanguard of people like guard dog Barr who will be releasing a CliffsNotes report on Good Friday probably in order to protect him from further falling ratings.

**Anne Yang:** No, I don't think that Trump is going to win, but you never know. I do believe that the chances are pretty good that we see a progressive era now for the next 20 years with radical changes to US policy and progressive politics. But we could go farther into what I view as American Fascism.

**Demetri Kofinas:** What do you think is driving that more than anything else? Is it the economics? Is it the incredible disparity of wealth? The unworkable disparity of wealth, not just the incredible but the unworkable?

**Anne Yang:** I think so, and I think there's a little bit of Republican overreach. There was a long period when there was a significant Republican contingent that was genuinely for small government and quasi-Libertarian policies, low taxes and so forth. It's basically-

**Demetri Kofinas:** Like Reagan Republicans?

**Anne Yang:** No, Reagan was basically the-

**Demetri Kofinas:** You're talking about before that?

**Anne Yang:** Yeah, before. Yeah. Rockefeller Republicans as they called them.

**Demetri Kofinas:** These are Rockefeller Republicans.

**Anne Yang:** Right. Then you started the period of The Long Con when basically the poorer conservative, mostly white working class populations, were persuaded that all those poor little fetuses were worth sacrificing their economic interest for.

**Demetri Kofinas:** Mm-hmm (affirmative). Well, the Republican party became an issues-driven party in the '80s and '90s.

**Anne Yang:** It's more ideological and less about fixing problems. The Democrats are the party of government. One of the interesting things that happened after the 2016 election is that all of these Democrats, myself included, the reaction was not to go to the street in protest but instead to get active in local government and build local institutions, go on voter registration drives and so on and so forth. I think that's very healthy.

**Anne Yang:** You also see a lot of sort of yin-yang reaction. Like for example, the fact that Medicare for All is absolutely standard in the political dialog now among Democrats, that wouldn't have happened if the Republicans had not spent two years trying to withdraw Obamacare.

**Demetri Kofinas:** Mm-hmm (affirmative). My biggest concern economically is the wealth disparity and the debt. Because I find that that is, first of all, it's unfair. It's fundamentally unfair that so many people in order to get a start need to take on so much debt. It's just fundamentally unfair.

**Anne Yang:** It is, indeed. As you know, I have very strong opinions about all these things, but it's not my area of expertise.

**Demetri Kofinas:** Right. Let me ask you another question to bring it back to China. Have you looked at all at the Sesame Credit System. You mentioned sesame before, the big sesame. What was it? The big sesame, big potato?

**Anne Yang:** Oh, small sesame. Right.

**Demetri Kofinas:** Oh, small sesame. Your friend, James Mulvenon, when he came on, he taught me something that I love, and I've used it now and then. He said, "They're getting a little high on the raisin as we say in the South." I love that. I love that expression. This is concerning to me because it's part of a larger concern that I have. We had a guest on the program called Shoshana Zuboff. I don't know if you heard that episode.

**Anne Yang:** Yeah, yeah. I listened to that episode. I bought her book. I'm almost finished with it.

**Demetri Kofinas:** What do you think of her book?

**Anne Yang:** I've very impressed. I think it actually could have been a little trimmer, a little cut down, but I think it's-

**Demetri Kofinas:** There's a lot of redundancy built into the book. It's also very poetic. It's not really a dry read.

**Anne Yang:** Yeah, but it's a paradigm shift. There's a whole set of assumptions that you bring to it like, "Well, so what? What's the big deal? I get this stuff for free and they measure my action." You really don't think about what it means on a social engineering level. But I think it's very interesting and important.

**Demetri Kofinas:** Well, the way she talks about it is so disturbing, particularly this idea of this rise of Instrumentarianism.

**Anne Yang:** She clearly is a deep reader of Hannah Arendt and thinks of herself as a successor to Hannah Arendt. Hannah Arendt genuinely did come up with a paradigm and an understanding of Fascism which really hadn't existed before. I think Zuboff is trying to jolt us into a realization that this is a degree of social control. It's not the same as the Fascists' desire for social control, which is to hollow-out the individual, but it bears a certain similarity. What it means is that we are in the matrix. We're corpses that are there to be mined for information.

**Demetri Kofinas:** It's that distinction between Totalitarianism and Instrumentarianism as she calls it.

**Anne Yang:** I think ironically, that's not the case. Ironically because if you look at the way Alibaba, Tencent, Baidu and the other big IT companies use data, it's way behind Facebook and Google and Apple and Microsoft. That's because of the government's overweening interest in controlling this area. Yet the government has much cloudier objectives. It does have sort of social harmony and social good objectives, but it doesn't have those clear let's drive foot traffic to McDonald's objectives. In an ironic way, despite the tremendous number of layers of surveillance in China, it's a little bit less scary.

**Demetri Kofinas:** Well, the state Capitalism or the Surveillance Capitalism would be the driving of the foot traffic. The Instrumentarianism would be converting that commercial end to a state end. But what it sounds like you're saying is that the commercial apparatus is not as sophisticated in China, therefore the systems are not as sophisticated. Therefore, the Instrumentarian impulses, which are greater in China, are not able to exercise the same level of control or power because their systems aren't as sophisticated.

**Anne Yang:** Well, it's not because they're not as sophisticated because the government has interfered and not allowed them to monetize the data to the same extent. There are some other economic forces at play. But it's basically like that. The government meanwhile, having all this data, doesn't have as clear a purpose as the Instrumentarian Surveillance Capitalists do.

**Anne Yang:** That doesn't mean it's benign. In China, you have a history of at least, I don't know, at least since the Ming Dynasty, so that's since the 14th Century of personal files on individuals. Personal files on individuals contain all sorts of stuff that the individual is not allowed to know. If you hate me and you're my neighbor and you're a Party member, you can get it inserted into my personal file that I have affairs with everybody. I'll never know that, and I won't get a promotion, so the Sesame-

**Demetri Kofinas:** That prevents you from getting a promotion if you have affairs?

**Anne Yang:** If you're a Party member, yeah.

**Demetri Kofinas:** If you're a Party member. Is that the same for men and women?

**Anne Yang:** It certainly happens an awful lot. I think it depends on how discreetly and with whom. Certainly I know guys who like hire women to travel with them, because its so low status not to have a girlfriend if you've married.

**Demetri Kofinas:** Really?

**Anne Yang:** Yeah. If you're a public official.

**Demetri Kofinas:** Really?

**Anne Yang:** Yes.

**Demetri Kofinas:** That sounds just like France, a France pre-

**Anne Yang:** Yes, it's a whole like, I guess so, right. Mitterrand France.

**Demetri Kofinas:** Yeah, exactly.

**Anne Yang:** At any rate, so the central government has had an ambition to digitize these files for a long time. Because ever since 1995 when they implemented a labor law and allowed people to change jobs, the files have fallen into some disuse. The central government depends on this atomic control of individual information to control people. They hoped that it was gonna happen when they inserted a chip into the individual identity cards. It didn't really happen. They didn't integrate their databases properly. Now Sesame Credit is designed to do that. The mistake that people make is thinking that it's about credit scoring. It's not. It's about social merit.

**Demetri Kofinas:** Interesting. What's the distinction there between social merit and credit scoring?

**Anne Yang:** Well, credit scoring is, "Should I borrow money?"

**Demetri Kofinas:** Oh, you're talking about credit in terms of financial credit?

**Anne Yang:** In financial credit.

**Demetri Kofinas:** Oh, I thought it was always in terms of social credit. Is that what you mean by merit? Social credit?

**Anne Yang:** Yeah, but Alibaba and others and many investors kind of pretended like it was about financial credit. There are a number of smaller companies that claim that they sell these files to the banks, which actually is not true. But at any rate, there's a lot of that, "Oh, we're gonna collect all these files. Then we're gonna create this great rating system. Then we can extend credit in a more efficient way." But it's not really about that.

**Demetri Kofinas:** Mm-hmm (affirmative). You know what's interesting, Anne, something I was thinking about before we turned on the microphones? The rise of China has been seen as quite remarkable. The speed with which the country has grown. But in some sense what's equally unremarkable is how they've done it. In other words, I think Westerns ... I for example ... have a hard time thinking about China as being a non-Capitalist country even though it's not. Because it has all the shiny exterior of a very successful Capitalist country.

**Demetri Kofinas:** But at its heart, it is a Communist country. I wonder, does China have more in common with the Soviet Union today than it does with the United States? Even though, granted, it has much more wealth and take away all the technology and this sort of stuff. But the struggle here is to transition to a market economy. They intervene so heavily ... There's so much state involvement and party involvement in the economy ... that to me it seems from the outside to have more in common with the USSR pre-1989 than it does with the United States.

**Anne Yang:** I would say it has certain isolated elements in common with each country, but it's not really similar to either country. There's no effort in China to transition to a market economy. That's not a thing. There was for a long time a benefit for the Chinese leadership in presenting themselves as a market economy in order to capture capital, and that continues to go on. You're not going to proclaim that you're not interested in Capitalism anymore as long as you have listed companies that are raising money. But when that stops, that will stop a well. Those processes have gone backwards for quite a long time.

**Anne Yang:** As for the Soviet Union thing, I think they're culturally super-different. But in political culture and social culture and everything, but I think a similarity is that Russia also had an imperial system. Under the imperial system, the emperor actually technically owned the land and the resources. In China, it was the same thing. Individuals have use rights to assets in China, but those can be alienated at any time. I think the separation of powers that came about through separate estates owning different assets in the West, whether it be the church, the crown, that characteristic dramatically changed the nature of economic development there versus Russia and China.

**Demetri Kofinas:** How far do you think the CCP is willing to go in order to maintain stability in the face of a contraction? What is their resolve, do you feel, at this stage? This is now 30 years after.

**Anne Yang:** You mean how brutal will it get?

**Demetri Kofinas:** Sure. How far are they willing to go in order to keep control and to maintain power?

**Anne Yang:** Oh, far. Far, but-

**Demetri Kofinas:** Do you think they're willing to go as far as they went in 1989?

**Anne Yang:** Oh, absolutely. It will be broader and bloodier than that.

**Demetri Kofinas:** Do you think that's the population's expectation as well? Because in the West we have certain ideas and expectations. How misaligned are ours with the population in China and how aligned are the Chinese citizens with the elites in terms of their expectations about the role of the government in the face of a crisis and the face of a revolt and how they would respond?

**Anne Yang:** I think that Western analysts often overestimate the importance of popular revolt in China. I think that the real threat to the Chinese system comes from the bureaucracy rather than from people in the streets. But as for the willingness of the central government to use repressive measures, I don't think anybody has any confusion about that. Look at what's happening in Shenzhen.

**Demetri Kofinas:** Do you mean a rebellion in the ranks?

**Anne Yang:** Yeah. Why has Xi Jinping closed down so many think tanks and doesn't allow conferences anymore, things like that? Because that's a key strategy for organizing. If you're a government official in a special zone in, let's say Hunan, and you have a new idea for how you should run special zones, then you write a white paper. You hold a conference, and then there develops a faction of officials who agree with you, and this becomes a pressure point against the central government. That's why Xi Jinping doesn't really allow this sort of debate anymore.

**Demetri Kofinas:** One of the interesting points that Michael Pettis has made is that Xi Jinping accumulated so much power in part because that was the only hope that China could possibly have to transition to make this transition from an economy built on repression of savings and the financial repression, investment-led growth to consumption.

**Anne Yang:** Yeah, I've heard that argument before. I think it's just nonsense to be blunt about it. I think that it's ahistorical and illogical. Ahistorical because you never find a system where people aggregate power in order to give away power. If they do that, then they lose power tomorrow. Illogical, I guess, because of the same reason. You're just fundamentally not able to do that. In fact, what you see with political systems as they mature is an increasing reliance on a smaller and smaller cohort of supporters. Increasing reliance on hereditary lines of rule as we've seen in the United States.

**Anne Yang:** Because if you're a key supporter of this particular government official and your support is needed for that official to maintain his position or to gain position, but it's a very contested and dangerous sort of position to be in, you have to have a lot of assurance that this official will maintain the policies of the past guy that have benefited you. What's the best way to be assured of that? It's his son. Right?

**Demetri Kofinas:** Mm-hmm (affirmative).

**Anne Yang:** Or his widow or whoever it might be. I think you see an increasing trend toward hereditary politics as you have seen in China as well as in the US.

**Demetri Kofinas:** Isn't this also part of the problem exactly? So this is a Trans-Pacific problem. It's a problem everywhere, which is that we've enriched an increasingly small class of people. Talk of reform ultimately means that those people have to lose.

They've got to give up some power. They've got to give up some money, and the incentives are misaligned. The concern is have we gone so far in the opposite direction where there's no rebalancing that can happen that isn't violent?

**Anne Yang:** Yeah, I think that's right. That's why you tend to see these cycles in China where generally extending over a 30-year period where you have opening in reform and then tightening. Then you have civil war, and then you have blossoming of pluralities again. Because the strength and the weakness of the Chinese system is its centrality and it's ability through its centrality to aggregate resources to itself and deploy those resources so you can create these tremendous growth and also tremendous disasters. You can have the Taiping Rebellion where millions of people died. You can have the famine of the late-1950s. You can have the development of the 1990s through today.

**Demetri Kofinas:** I think that's also part of the problem, which is that they're such a large country. There are countries much smaller than them, like Hong Kong, although Hong Kong's not really a country. But South Korea, other Asian Tiger economies that manage to pursue this type of a growth model, but it's much easier to do this effectively when you're a very small country. When you're as large as China, I think that's the ultimate fundamental problem, I think, for China is if they were a much smaller economy, this could have worked, right?

**Anne Yang:** Well, it did work. But because of China's size, it's gotten bigger than anybody has ever seen before.

**Demetri Kofinas:** No, you can't do an export-led growth model with a billion people. You run into some problems with that.

**Anne Yang:** Yeah, well they-

**Demetri Kofinas:** You run out of consumers.

**Anne Yang:** Yeah, but they did it very effectively for a long time. They had this huge growth trajectory. It's just that what I think you point out that a lot of people miss is that it's not unusual. It's not the first time we've seen this in the world. We've seen it a bunch of times, over-investment in order to create one's own growth leading to crash and decline.

**Demetri Kofinas:** Right. Exactly. Anne, thank you so much for coming on the show. I want you to stick around for our overtime segment.

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**Demetri Kofinas:** Anne, thank you so much for coming on the show.

**Anne Yang:** Well, thank you, Demetri.

**Demetri Kofinas:** That was my episode with Anne Stevenson-Yang. I want to thank Anne for being on my program. Today's episode of Hidden Forces was recorded at Creative Media Design Studios in New York City. For more information about this week's episode or if you want easy access to related programming, visit our website at [HiddenForces.io](http://HiddenForces.io) and subscribe to our free email list. If you have access to overtime segments, episode transcripts and show rundowns full of links and detailed information related to each and every episode, check out our premium subscription available through the Hidden Forces website or through our Patreon page.

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