Suggested Solutions to China's Stagflationary Economy since the U.S.-China Trade War -A Lesson From the U.S. Great Stagflation Period

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Introduction

This paper examines both the economic and policy implications of the Great Stagflation in the U.S. and compares these implications to the Chinese economy in the period of the U.S.-China trade war while providing policy recommendations for the Chinese government. In 2018, U.S. President Donald Trump began imposing tariffs on various Chinese imports with the goal of forcing China to correct its "unfair trade practices and intellectual property theft." The U.S.-China trade war serves as an exogenous element that induced a severe negative shock on both the supply and demand side of the economy. The impact on aggregate demand and supply resulted in a decline in China's real economic growth, rising unemployment rate, and inflation.

Numerous scholars have written about the matter of stagflation. Some scholars believed the oil crisis in 1973 facilitated the stagflation in the U.S. Bernanke, Gertler and Watson analyzed the impact of oil price shocks of the 1970s and 1980s with respect to global macroeconomic conditions and concluded that they were propagated by the reaction of monetary policymakers, causing stagflation in the process. [1] Benjamin Hunt examined the macroeconomic implications of

[1] Ben S. Bernanke, Mark Gertler and Mark Watson, "Systematic Monetary Policy and the Effects of Oil Price Shocks." *Brookings Papers on Economic Activity*, 28, (1), 91-157.

large increases in the price of energy. [2] Hunt concluded that if the monetary authority misperceives the economy's supply capacity. and workers can temporarily resist some of the erosion in their real consumption wages resulting from the energy price increase, large increases in energy prices can generate inflation persistence similar to that seen in the 1970s. Other scholars emphasized the role of the U.S. government in causing stagflation during the 1970s. Alan S. Blinder summarized what economists do and do not know about the inflation and recession that affected the U.S. economy during the years of the Great Stagflation in the mid-1970s. [3] He discussed the basic concepts of stagflation, the turbulent economic history of 1971-1976, the anatomy of the great recession and inflation, and the legacy of the Great Stagflation. Robert B. Barsky and Lutz Kilian argued that oil price increases may not be an essential part of the causal mechanism generating stagflation as once thought. [4] Instead, they provide a model to explain the bulk of stagflation by monetary expansions and contractions without reference to a supply shock. Although there has been a steady stream of papers about stagflation in the U.S., few have touched on the stagflation in other economies or made comparisons between the features of the U.S. stagflationary economy and those of other economies. In this paper, I evaluate both the Great Stagflation and the current Chinese economic situation to examine the impacts of the U.S.-China trade disputes, pork swine, and the oil crisis on the macro monetary policies and stagflation. I bring together a large number of elements that would offer a coherent explanation of China's stagflationary economy and compare it to the Great Stagflation in the U.S. The contribution of this paper is synthetic.

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[2] Benjamin Hunt, "Oil Price Shocks and the U.S. Stagflation of the 1970s: Some Insights from GEM," *The Energy Journal*, Volume 27, (Number 4), 61-80.
[3] Alan S. Blinder, *Economic Policy and the Great Stagflation*, (New York: Academic Press), 1979.
[4] Robert B. Barsky and Lutz Kilian, "Do We Really Know that Oil Caused the Great Stagflation? A Monetary Alternative," *NBER Macroeconomics Annual 2001*, Volume 16, 2002.

This paper is structured in three sections. First, I conduct aggregate supply and demand analysis to explain the rise of inflation in both the Great Stagflation period of the U.S. and China's recent stagflationary economy. The inflation is initiated by an adverse shift in the aggregate supply curve, and such a supply shock could be caused by any of a variety of unpleasant events such as natural disasters. This could lead to scarcity of agricultural products or of some other commodities, resulting in price increases. [5] Both the U.S. and China experienced such shocks prior to the stagflationary period: the OPECs control of crude oil and the U.S.-China trade disputes have contributed to the significant domestic price and inflation rate increases in both countries. I conclude that China's recent economic performance is similar to that of the U.S. during the Great Stagflation period.

Second, I will provide empirical support to examine and compare the policy responses to stagflation by both the U.S. and the Chinese government. The 1970s marked a period of policy instability. The U.S. government first adopted rapid expansionary monetary and fiscal policies in an attempt to stimulate the economy but failed, then implemented contractionary monetary and fiscal policies abruptly, dragging the U.S. economy into deeper recessions.[6] On the other hand, China adopted similar expansionary policies to solve its stagflation problems. China's money supply growth has maintained as high as 14.92% since 2003 compared to approximately 5% in the U.S. [7] Furthermore, China's Central Bank injected $126 billion into the financial system in an attempt to stimulate its slowing economy in 2019.[8] I conclude that China should stop its expansionary monetary policies, which will only worsen the stagflation, and adopt policies

[5] Alan S. Blinder, *Economic Policy and the Great Stagflation*, (Elsevier Science: 1979), 1-21.
[6] Paul Ryan, "Thirty Years Later, a Return to Stagflation," *The New York Times*, February 13, 2009.
[7] Steve Hanke, "Is China Cooling?" *Forbes,* October 19, 2018.
[8] Alexandra Stevenson, "China Injects $126 Billion Into Its Slowing Economy*," The New York Times*, September 6, 2019.

similar to Reaganomics that will bring the economy back on the right track.

The remainder of this paper includes supporting graphs and data as well as concluding remarks.

II. The U.S. Economy in the 1970s

To understand how the recent Chinese economic performance is comparable to the United States' during the Great Stagflation, and why China could adopt policies of Reaganomics, it is important to understand and study the U.S. economy during the 1970s, known as the "Great Stagflation" period. The U.S. economy experienced a combination of stagnant economic growth, high unemployment, and high inflation during the 1970s.[9] The output level started to contract sharply in 1973 and grow slowly since 1974, while the inflation rate was high. In Figure 1, the inflation rate soared from around 3% in mid-1972 to 12% in 1975. Over a period of 12 months in the early 1970s, the average consumer prices were up 4.3 percent on average according to the Labor Department. The Consumer Price Index (CPI), which excluded food and oil, was 2.5 percent higher in January than a year earlier, significantly above the Fed's unofficial comfort zone of a 1 to 2 percent underlying inflation rate.[10] However, high inflation was not the only element that battered the U.S. economy, and the contemporaneous deep recession also contributed to the stagflation. In Figure 2, the economic growth rate plummeted significantly in the same period when inflation rose: there was a clear upward drift in inflation from around 6% in late 1972 to around negative 1% by 1975. The negative growth rate

[9] See Figure 1, Figure 2. In Figure 1, the inflation soared from around 3% in 1972 to 12% in 1975, and the high with contemporaneous deep recessions. In Figure 2, the economic growth rate plummeted significantly in the same period when inflation rose: there was a clear upward drift in inflation from around 6% in late 1972 to around negative 1% by 1975. The negative growth rate continued until the beginning of 1976. Additionally, Unemployment also rose sharply: the U.S. unemployment rate soared from 4.8 percent in the second half of 1973 to almost 9 percent in the second quarter of 1975.

[10] Graham Bowley, "That '70s Look: Stagflation." *The New York Times*, February 21, 2008.

continued until the beginning of 1976. Additionally, unemployment also rose sharply: the U.S. unemployment rate soared from 4.8 percent in the second half of 1973 to almost 9 percent in the second quarter of 1975.[11]

One way to explain the cause of high inflation and unemployment along with contraction of real output is to conduct aggregate demand-aggregate supply analysis. The main compositions of the aggregate demand are consumption, investment, government spending, and net exports. When these elements decrease, the aggregate demand will decrease. On the supply side, a firms' input costs are negatively related to the aggregate supply. According to the economic theory, the rate of inflation and the rate of real economic growth are determined by the macroeconomic equilibrium: the intersection of a downward sloping aggregate demand and an upward sloping supply curve. Inflation will result if aggregate demand races ahead of aggregate supply, and vice versa. Any retardation in the growth of aggregate supply will tend to produce an acceleration of inflation and a slow-down in real-economic growth, let alone the reduction of aggregate supply. The aggregate supply and aggregate demand shocks are highly descriptive of what happened to the U.S. economy during Great Stagflation: In October 1973, the Organization of Petroleum Exporting Countries (OPEC) declared an oil embargo upon supporters of Israel-western nations. As a result, the oil prices in the U.S. more than doubled during a few months from '73-'74.[12] Oil is involved in every aspect of the production of daily goods such as plastics, gasoline, sneakers. The oil shortage increased oil prices and production costs, thus raising prices of other commodities while shifting the supply curve to the left. Moreover, higher prices not only caused a higher inflation rate but also raised the expected inflation rate among the public in the future. [13]

Besides the oil crisis, another more sizable supply shock that mainly contributed to the increase of inflation consists of crop failures, corn

[11] Alan S. Blinder and Jeremy B. Rudd, "The Supply-Shock. Explanation of the Great Stagflation Revisited," *NEBR Economic Research,* December 2008.
[12] See Figure 3.
[13] See Figure 4.

blight, and depleted inventories in many parts of the world that caused a serious food shortage in the United States. The food shocks have contributed more to the rising price index since food has a much higher weight than energy. [14] From 1973-1974, The Consumer Price Index (CPI) for food rose 20.1 percent from December 1972 to December 1973 and another 12.1 percent from December 1973 to December 1974. These statistics were much higher than those in the year before and after the shock: in 1971, the CPI was 4.6 %, and in 1975, CPI was 6.7%. [15]

During the 1970s, the oil crisis and food shortage doubtlessly caused not only a major negative aggregate supply shock that resulted in skyrocketing inflation but also a negative aggregate demand shock that led to severe GDP declines.[16] Because of this decline in Americans' real income, more people cut their spending, thus decreasing the aggregate consumption level. Furthermore, the oil shortage also created uncertainty about the economy, which led investors and purchasers of consumer durables to "pause" while the uncertainty got resolved.[17] In addition, until new, energy-efficient capital becomes available, firms may postpone their investment plans.[18]

In addition, the decrease in aggregate demand caused firms to cut jobs as the economy cooled down. During the 1970s, the labor slack was unusually high in the United States, while inflation did not diminish.[19] Another explanation for the high unemployment rate in a stagflationary economy is that rising expected inflation could cause an increase in nominal wage demand.[20] When the feasible growth of real wages fell because of the increasing production cost and falling productivity

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[14] Blinder and Rudd, *The Supply-Shock Explanation of the Great Stagflation Revisited,* 141.
[15] Ryan, "Thirty Years Later, a Return to Stagflation."
[16] "The United States Median Household Income 1950-1990". The figure illustrates the decreasing trend of the median household income during the 1970s.
[17] Ben S. Bernanke, "Irreversibility, Uncertainty, and Cyclical Investment." *Quarterly Journal of Economics* 98, 1983.
[18] Christopher Sims, "In: General Discussion." *Brookings Papers on Economic Activity*, 1981.
[19] See Figure 2.
[20] R. Jackman and R. Layard, "Cause of the Current Stagflation." *Centre for Labour Economics*, 1982.

growth, workers tried to achieve higher wages. Expectedly, the firms could not meet workers' demands on wage increase and thus had to lay off employees to cut costs, causing the soaring unemployment rate.

The decrease in aggregate supply caused higher prices, which then resulted in lower aggregate demand. Hence, the equilibrium level of output and employment subsequently fell. Additionally, this adverse shift in supply and demand was likely to be permanent, as no one knew whether and when the OPEC would rescind the oil price hike. The looming prospect of oil supply aggravated the uncertainty among investors and consumers, exacerbating the stagflationary economic recession.

III. The Chinese Economy since 2018

The Great Stagflation is a valuable reference for any economy that experienced low economic growth, high inflation, and unemployment. Particularly, it is observed that the Chinese economy in recent years is highly comparable to the United States' during the 1970s. Hence, the U.S. government's adoption of Reaganomics may provide useful guidance to solve the Chinese economy's stagflationary problem. Similar to the contribution of the oil crisis and food shortage to the Great Stagflation, the U.S.-China trade war incurred both negative aggregate demand and supply shock on the Chinese economy, and it not only accounts for a substantial reduction in consumption and investment but also results in a significant supply shortage. Consequently, China has suffered from surging price levels, soaring unemployment rates, and sluggish economic growth.

As of September 2019, the U.S. has imposed tariffs on more than $360 billions of Chinese goods across more than 1300 categories, including steel and aluminum. Similar to the oil shortage, which indirectly discouraged consumption and investment while creating uncertainty among the public that further weakened the US economy during the Great Stagflation period, the imposed tariffs on Chinese steel and aluminum discouraged China's domestic production of those

materials.[21] As a result, decreasing production of steel and aluminum has significantly decelerated domestic infrastructure and real estate investments which were important drivers of Chinese economic growth.[22] The rising uncertainty about the economic prospect thus disincentivized the investment and consumers' spending that further contributed to the cooling economy. On the domestic front, manufacturing investments have continued to decrease as well, posting potential negative economic growth in 2019. Externally, uncertainty surrounding the U.S.-China long-term trade relationship hit export growth and reduced the incentive to invest. The prospective export and import growth rates are estimated to be -2.9% and -2.7%, respectively.[23]

Plummeting levels of consumption, investment, and net exports shift the aggregate demand curve to the left and are reflected in a reduction of the Gross Domestic Product (GDP) that measures real economic growth. In the third quarter of 2019, China's GDP grew by 6%, the slowest annual rate in 30 years, preceded by a GDP growth rate at 6.4% in the first quarter and 6.2% in the second.[24] Another measuring method that provides strong evidence on China's economic slowdown is China Cyclical Activity Tracker (CAT), an alternative way to measure fluctuations in Chinese economic activity. The CAT also suggests that that economic activity has slowed noticeably since 2017 to a pace slightly below trend.[25]

Throughout this ordeal, China has retaliated with tariffs on more than $110 billion of U.S. products, including automobiles, pork, and

[21] "A Quick Guide to the US-China Trade War", BBC, September 2, 2019.
[22] Pan Helin, "274 Real-estate Enterprises Declared Bankruptcy-Reshuffling of the Real-estate Industry is Needed", (XinhuaNets: 2019). The data of real-estate firms' bankruptcy announcement at China's The People's Court Announcement shows that as of July of 2019, 274 real-estate enterprises declared bankruptcy. This is a rise of 50% from a year ago.
[23] "China's Big Decision", J.P. Morgan, June 13 2019.
[24] John Fernald, Neil Gerstein, and Mark Spiegel, "How Severe Is China's Slowdown? Evidence from China CAT," *Federal Reserve Bank of San Francisco*, 2019.
[25] See more at The China Cyclical Activity Tracker published by the Federal Research of San Francisco. The China CAT index measures fluctuations in Chinese economic activity by combining eight non-GDP indicators in order to measure deviations in year-over-year growth relative to trend.

soybeans.[26] The economies of China and the U.S. are highly interdependent, as China is the largest trading partner of the United States, and the U.S. runs a huge trade deficit —$419.2 billion — with China.[27] This means China does not have much room to impose retaliatory tariffs on U.S. imports because China does not import much from the U.S. Among China's U.S. imports, the main categories are machinery, automobiles, and agricultural goods. Although the total amount of these imports may not be high, they are indispensable for firms' production and people's food consumption. Despite the fact that China's manufacturing industry and food supply heavily depend on the U.S., China still decided to impose 25% tariffs on U.S.-produced goods. The tariffs on these industries and livelihood necessities contributed to a significant negative aggregate supply shock and raised the price levels, just like the impacts of the Oil Crisis of 1973 and crop shortage during the Great Stagflation. The surging price levels thus raised the domestic inflation rate: As of November of 2019, the pork prices surged 110%, and fresh fruit prices climbed more than 40%.[28] China's consumer inflation also rose by 2.5 percent from a year earlier.[29]

Another vital element of stagflation is the high unemployment rate, along with high inflation and low economic growth. Besides the decrease in aggregate demand, the intensified U.S-China trade war adds exogenous pressure to the rising unemployment in China, as lots of foreign-owned multinationals withdrew investments from China to avoid decreasing aggregate demand and potential tariffs. The intensified

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[26] Michael Collins and David Jackson, "China Slaps Tariffs on $60 Billions of US Imports, but Trump Insists U.S. is Well-Positioned in the Fight." *U.S.A Today*, May 13, 2019.

[27] According to a report from the Office of the U.S. Trade Representative, the top US exports to China in 2018 were machinery ($14 billion), electrical machinery ($13 billion), and vehicles ($9.4 billion). The U.S. total exports account for more than 40% of the total Chinese imports of agricultural goods. Leading domestic export categories include: soybeans ($3.1 billion), cotton ($924 million), hides & skins ($607 million), pork & pork products ($571 million), and coarse grains (ex. corn) ($530 million).

[28] Huileng Tan, "China says pork prices surged 110% in November." CNBC, December 10, 2019.

[29] Yawen Chen and Kevin Yao, "China's Soft Factory-gate Inflation Raises Prospect of More Stimulus," Reuters, January 10, 2019.

U.S.-China trade war severely hurt China's job market by hitting its manufacturing industry that employs more than 112 million people, 15% of the entire labor market. The negative impact on the Chinese labor market results from the fact that 50% of Chinese exports to the U.S. are exported by wholly foreign-owned companies or joint ventures with Americans. These American companies are closing their manufacturing factories in China.[30] It is these foreign-owned factories that employ millions of Chinese for cheaper labor. However, to avoid impending tariffs posed by the Trump administration, more than 40% of foreign companies were forced to relocate their supply chains out of China to Taiwan, Vietnam, and India. [31] The decreasing demands for manufacturing workers resulted in a loss of millions of jobs in China. In July of 2019, China's unemployment rate hit 5.2% after a sharp increase from around 4% at the beginning of 2019.[32] Given the substantial size of China's labor market, a 0.5% increase in the unemployment rate equals more than 5 million jobs lost in six months, and this number will potentially rise soon.

Collectively, I have examined both and compared both the U.S. economy during the Great Stagflation and the Chinese economy after the U.S.-China trade war. Both economies have experienced exceptionally similar issues such as low to negative economic growth, high inflation and unemployment simultaneously. The aggregate demand-aggregate supply analysis can also explain the stagflation problems in both countries. Furthermore, both economies are highly comparable because the stagflation in both countries was preceded by exogenous events that resulted in a supply shortage. The negative supply shock thus resulted in surging price levels and inflation rates which caused the aggregate demand to shrink. The supply-shock that led to stagflation posed a serious threat on both the aggregate and individual level, trapping both the U.S. and China economies in a

[30] Kenneth Rapoza, "More U.S. Companies Seen Leaving China After September." Forbes, August 8, 2019.
[31] Kenneth, "More U.S. Companies Seen Leaving China After September."
[32] Trading Economics, "China Urban Survey Unemployment Rate."

vicious circle because the supply shortages such as the Oil Crisis and the U.S.-China trade were likely to be permanent and caused high inflation to sustain. The high inflation not only killed confidence in consumers and businesses and created uncertainty that discouraged consumption and investment, but also devalued the savings day by day. A decrease in aggregate demand thus further reinforced the high unemployment rate, and consumers have less money to spend which in return further decreased the aggregate demand. The next section will provide careful analysis on solutions to stagflation.

IV. Lessons from the Carter and Reagan Administration

While many scholars acknowledge the damage of the stagflation, we must learn from the policies that successfully solved the stagflation issue. The solution to the stagflation, as the economist Robert A. Mundell stated: "The correct policy mix is based on *fiscal ease* to get more production out of the economy, in combination with *monetary restraint* to stop inflation. The increased momentum provided by the tax cut will cause sufficient demand for [money] to permit real monetary expansion at higher rates."[33] Dr. Mundell was correct. The expansionary fiscal and monetary policies implemented during the Ford and the Carter administration worsened the stagflation while the supply-side economic policies adopted during the Reagan administration led the economy out of the Great Stagflation. The U.S. economy during the Great Stagflation and the Chinese economy after 2018 are quite similar. Therefore, China should abandon its current expansionary and fiscal, monetary policies while gradually changing its state-dominated economic structure to let the private sector stimulate economic growth.

This section will focus on the inflation side of the stagflation; it will also explore why China's current monetary policies may not solve the stagflationary problems after examining the Federal Reserve's policies during the Great Stagflation while providing policy recommendations for the Chinese government.

[33] Brian Domitrovic, "Stagflation? We Can Cure That." Forbes, June 21, 2011.

(a) Inflation:

Milton Friedman once said: "inflation is always and everywhere a monetary phenomenon."[34] The monetary growth usually accelerates inflation increase when the aggregate demand cannot grow in balance with the money growth. During the Great Stagflation, as analyzed above, the aggregate demand experienced a sharp decline. However, the Federal Reserve still decided to adopt an expansionary monetary policy in an attempt to stimulate economic growth. In 1972, the Federal Reserve System (Fed) was concerned about the soaring unemployment rate rather than inflation. Therefore, the annual money supply growth rates over the 2-year period 1970:4 to 1972:4 were 7.5% for M1 and 11.3% for M2. Both rates were extraordinarily exuberant by historical standards. [35] The spikes in monetary growth in 1971-72 preceded the soaring inflation, causing a stagflationary economy. Some economists argued that the aggregate demand had already been declining because of rising production costs, unwilling consumption, and investors' uncertainty. But the injection of more liquidity into the market only pushed up the price levels as money further devalued and people were less willing to spend. The aggregate demand thus deteriorated. The inflation continued to rise after 1972, so the Federal Reserve contracted the monetary policies abruptly in 1973, though it was ineffective. As the U.S. economy stepped further into stagflation, the Federal Reserve again adopted strong expansionary monetary policies in 1974 and continued to decrease the interest rates. [36] However, these monetary policies were not effective, as the inflation rose higher while the GDP growth went negative.

Similar to the Federal Reserve's actions before and during the Great Stagflation, China's Central Bank: "People's Bank of China (PBOC)" has relied on expansionary monetary policies to stimulate economic

[34] Milton Friedman, "The counter-revolution in monetary theory: first Wincott memorial lecture, delivered at the Senate House, University of London, 16 September, 1970." Wincott Memorial Lecture: 1970.
[35] Alan S. Blinder, *Economic Policy and the Great Stagflation.*
[36] Barsky and Kilian, "A Monetary Explanation of the Great Stagflation of the 1970s", National Bureau of Economic Research, 2000.

growth for the past decades, which has reinforced China's stagflationary problems. Since 2009, China's M2 money supply has grown over nearly $20 trillion, and during the same period, China's annual GDP grew roughly $8.4 trillion. During the same period, the U.S. M2 money supply increased by 'just' $6.1 trillion, while the U.S. economy grew by $6.09 trillion. The fast growth of the money supply in China would only lead to high price levels and financial bubbles because, in a healthy economy, the real economy, indicated by the real GDP, should grow faster than the money supply. [37]

Before the U.S.-China trade war, China's economic growth relied on exponential high monetary supply growth, and credit expansion had been slowed down. However, even as the Chinese economy slid into stagflation, the PBOC still decided to inject liquidity into the market, which failed. In September of 2019, the PBOC declared that it would decrease the required reserve for Chinese financial institutions, which would release nearly $150 trillion into the market. [38] This would only further increase the high price levels in China as the pork and fresh fruits prices surged even higher after September of 2019. The U.S. during the Great Stagflation tried expansionary monetary policies in the hope of stimulating the economy. China is in a remarkably similar situation as its money supply has grown tremendously prior to the U.S.-China trade war, and its interest rates have been low.[39] The Fed failed to lead the U.S. economy out of stagflation under expansionary monetary policies, and so will China if they continue as is.

(b) Reaganomics

The expansionary monetary policies have failed to solve the stagflation problems in the United States during the 1970s. When President Reagan took charge in office, he initiated a series of supply-

[37] Taps Coogan, "China's Money Supply Has Outgrown Its Economy over Two Fold Since 2009." The Sounding Line, 2018.
[38] Yao and Chen, "China Cuts Banks' Reserve ratios, Frees up $126 billion for Loans as Economy Slows" Reuters, September 6, 2019.
[39] Laura He, "China's Central Bank is Cutting Interest Rates by Stealth." CNN Business, August 19, 2019.

side economic policies that attacked the stagflation successfully. Specifically, Reagan pledged a cut in money supply while cutting income and capital gain taxes. Why was Reaganomics successful? First, Reagan's tax cut was high enough that corporates were incentivized to initiate investments, and people were willing to consume. By Reagan's last year in office, the top income tax rate was 28 percent for single people making $18,550 or more. Furthermore, anyone who made less paid no taxes at all.[40] The tax cut greatly increased confidence among the public and the consumption level began to rise as people had more money to spend. Once consumption and investment started to grow, the aggregate demand increased. The increasing aggregate demand shifted out the aggregate demand curve, which would theoretically raise the inflation rate. On the other hand, Reagan adopted contractionary monetary supply at the same time, which tamed the double-digit inflation. The Reaganomics policies successfully led the U.S. economy out of stagflation. In only four years, the inflation rate plummeted from 13% to 4%. The unemployment rate also fell significantly from 10.8% to 5.4% during this period. Furthermore, the GDP grew over one-third during Reagan's presidency, an over $2 trillion increase.[41]

V. Conclusion

This paper first compares the Chinese economy to the U.S. economy during the Great Stagflation. It then examines the phenomenon of the Great Stagflation as well as recent Chinese economic stagflation. The success of Reaganomics can potentially serve as guidance for Chinese monetary policymakers. The exponential money supply has funded China's unsustainable economic growth. The U.S.-China trade war worsened the inflation rate and curbed both the aggregate supply and demand. Furthermore, many foreign companies have been leaving China, further decreasing the aggregate demand and supply. Therefore, the solution should be to increase the real economic level. To increase

[40] Kimberly Amaded, "What is Reaganomics, Did it Work?" *The Balance*, 2018.
[41] Rich Danker, "Reagan's Monetary History." *Forbes*, February 14, 2011.

the real output level, a considerable tax cut given to the private-owned companies can not only relieve their financial pressure from the decreasing consumption but also rebuild confidence among the investors, as the public will have more money to distribute and spend. Currently, the Chinese economy is dominated by state-owned enterprises that have usually had easy access to credits. However, state-owned enterprises are not only inefficient but sluggish. As President Reagan confronted the stagflationary economy by cutting taxes to energize the private sector, China should do the same to incentivize consumers and business owners. The Chinese private sector contributes 60% of China's GDP, and is responsible for 70% of innovation, 80% of urban employment, and provides 90% of new jobs. Private wealth is also responsible for 70% of investment and 90% of exports. Today, China's private sector contributes nearly two-thirds of the country's growth and nine-tenths of new jobs.[42] As China continues to seek solutions to the stagflationary economic conditions, it may be worthwhile to take lessons from the Reagan administration and reform its economic structure. Future improvement can include the analysis of the role of government spending in solving the stagflationary problem and analyze why China should also decrease government spending to stimulate real economic growth further.

[42] Rainer Zitelmann, "State Capitalism? No, The Private Sector Was And Is The Main Driver Of China's Economic Growth," *Forbes,* September 30, 2019.

Appendix

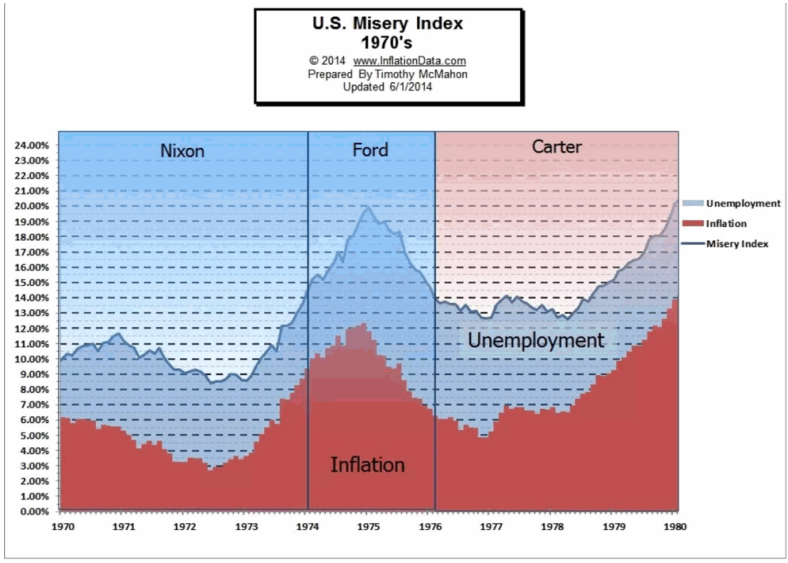

Figure 1: The U.S. Misery Index, Inflation Rate, and Unemployment Rate in 1970s
(Source: InflationData 2014)

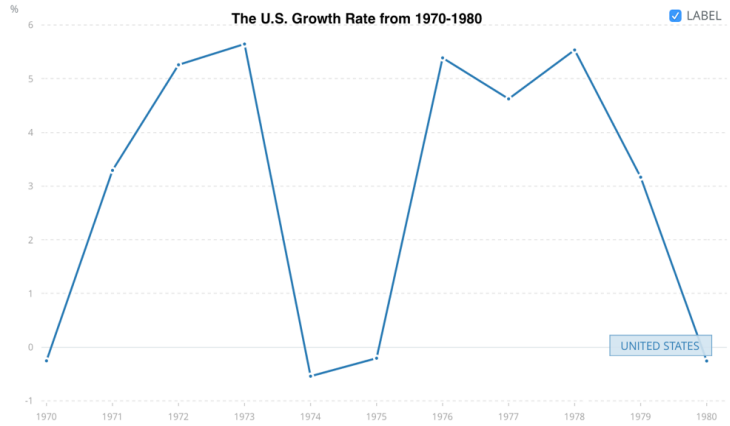

Figure 2: The U.S. Growth Rate from 1970-1980
(Source: World Bank 2019)

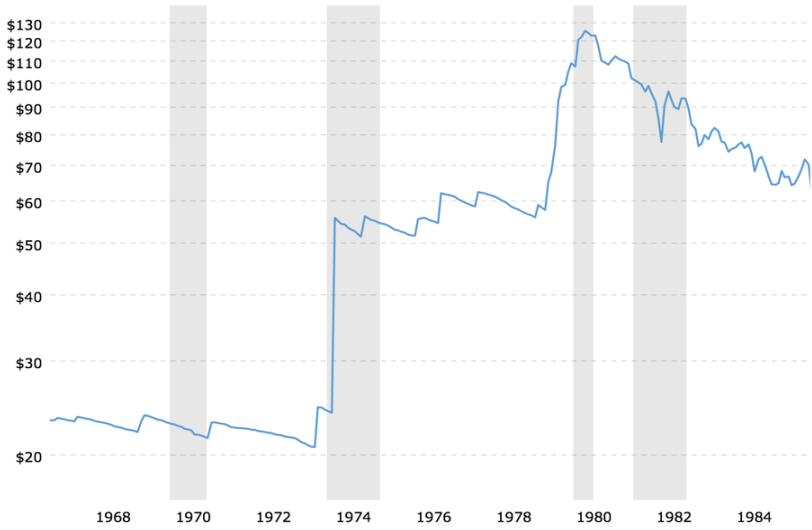

Figure 3: The Crude Oil Prices from 1968 – 1984
(Source: MacroTrend 2019)

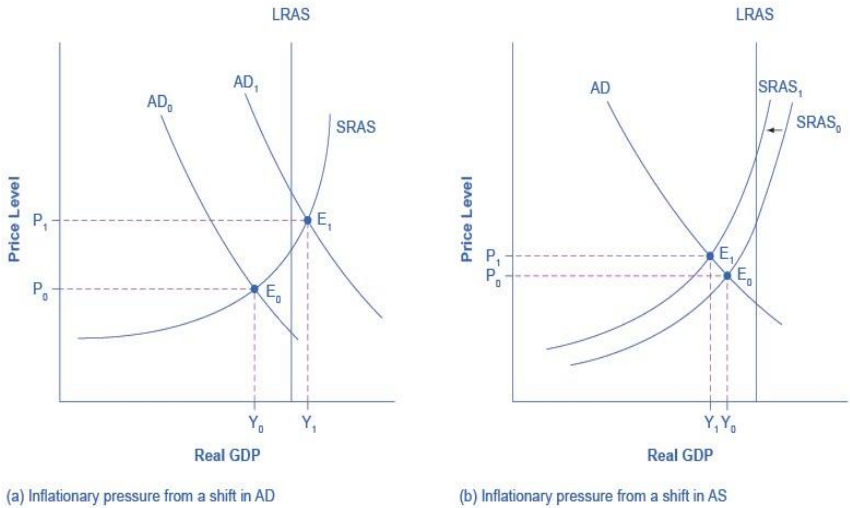

Figure 4 AD/AS and Inflation Graph
(Source: Khan Academy)

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