How much economic profit do Chinese firms generate? Is corporate China catching up with the United States powerhouse?

We examine whether China’s tremendous economic growth this century has a counterpart in significant economic profitmaking by its firms. We find that Chinese companies only started to generate significant economic profits after 2019. The largest firms in the consumer discretionary, IT, and industrial sectors have driven this recent upturn. Yet, these developments appear vulnerable. Furthermore, even with the recent increases, Chinese firms only create 34% of the economic profits of their US counterparts.

‘China is a sleeping giant. Let her sleep, for when she wakes, she will shake the world’ so goes a famous quote, which is often attributed to Napoleon Bonaparte. During the last decades, we have indeed witnessed a meteoric rise of the Chinese dragon – with substantial ramifications on the geopolitical, economic, and military fronts. Chinese GDP has soared but did that translate into economic value creation by Chinese firms? Are they catching up to their US counterparts? And in which sectors have Chinese firms created more value?

Traditional macroeconomic metrics (like GNP and GDP) are not ideally suited for answering these questions because the direct link to corporate performance gets largely lost in national income accounting. Common financial metrics (like accounting profits and Free Cash Flows) can also be misleading as they penalise firms that choose to make R&D outlays while ignoring the opportunity costs of capital.

The economic profit estimates, which the Crux of Capitalism project derives for over 39,000 publicly-listed firms around the world since 2005, however, provide insightful bottom-up information that is ideally suited for studying the developments in the Chinese corporate sector. Here we summarise four of the findings from our economic profit calculations.

First, our analysis reveals that the Chinese corporate drag has indeed awoken, but only recently. Taken together, Chinese firms created little value prior to 2019. The light green line in figure 1 shows that the economic profits generated by publicly-listed Chinese firms rose from just 26 billion USD in 2019 to almost 249 billion USD in 2022. If we adjust these values to take non-listed firms into account (as shown in our third CoC Insight), the rise from 53 billion USD in 2019 to 620 billion USD is even more impressive (dark green line). As far as the comparison to the US is concerned, however, the Chinese corporate drag still has a long way to climb. In 2022 Chinese firms created about 34% of the total economic profits generated by their US counterparts (grey dotted line). By contrast, China’s GDP was 70% of the United States’ level in 2022.

Second, our economic profits data highlight that not all publicly-listed Chinese companies seem to have contributed to this recent boom in value creation. As one can see in figure 2, more than four in ten firms actually ‘destroyed’ value in 2022. The share of very strong firms creating more than 100 million USD in annual economic profits, however, is significantly larger than the share of large value destroyers with economic losses of 100 million USD or more (11% vs. 3%). A look at the developments this century reveals that the Chinese corporate sector appears to be very vulnerable during periods of macroeconomic turmoil. During the instability witnessed during 2015-2016, for example, the share of firms with negative economic profits rose to a staggering 64%. This apparent fragility is a concern as China’s current deflation challenge is likely to push up real funding costs.

Third, China’s corporate value creation is mostly driven by a rather small group of particularly successful ‘superstar’ firms. Figure 3 shows that almost three-quarters of all positive economic profits are generated by just 5% of companies. The top 10% and 25% of publicly-listed firms create a stunning 84% and 96% of all profits, respectively. These percentages were rather stable throughout the past 18 years, with the exception of 2015-16 when the top value creators seem to have translated their relative resilience into a larger profit share.

Fourth, about half of China’s economic profits are currently generated in the industrial, IT, and consumer discretionary sectors (see figure 4). While the consumer discretionary sector has proven to be a rather reliable and consistent value creator over the years, results in the industrial sector has been very volatile. The growing contribution of the research-intensive IT sector is particularly striking. Starting with a contribution to total Chinese economic profits of only 2% between 2005 and 2013, the sector accounted for almost 25% of profits during the second half of our sample. On the basis of such findings, the Chinese dragon seems to be increasingly successful in turning itself into a profitable, global innovation leader. At the other end of the spectrum, the utilities sector has been a very weak value generator since 2005, while the energy sector has seen massive swings in positive and negative directions.

In sum, only in the past few years has China’s growing economic footprint translated into its firms making significant economic profits. Whether that performance can be sustained remains to be seen, not least given repeated reports this year about headwinds facing the Chinese economy.
Figure 1: Total economic profits of Chinese firms in billion USD and as a share the comparable total for the United States, 2005 to 2022

Note: All economic profit values are adjusted for inflation by applying the relevant national GDP deflator. Data on countries’ GDP deflator was sourced from the World Bank Development Indicators. The base year used is 2022. Economic profits of publicly-listed Chinese firms represented by the light green line have been adjusted for missing values to take account of any data gaps in the Compustat database. Economic profits of all Chinese firms represented by the dark green line have been further adjusted reflecting shares of publicly-listed and non-listed firms. We thereby used data on the annual asset-weighted share of firms in each country and asset size class that are publicly-listed according to the ORBIS database. Data availability for balance sheet assets and other fields is very limited on ORBIS before 2014. The dark green line may thus not be well representative prior to 2014.

Figure 2: Shares of listed Chinese companies by range of economic profitability, 2005 to 2022
Figure 3: Shares of economic profit accounted for by the largest Chinese firms, 2005 to 2022

Note: This figure only looks at Chinese firms with positive economic profits.

Figure 4: Sector contributions to total economic profits of listed firms in China, 2005 to 2022 (in %)