



## Expert Comment

Doctors and medical students attend a rally against the government medical plan on 14 August 2020 in Seoul, South Korea. (Credit: Chung Sung-Jun/Getty Images/Getty Images AsiaPac)

Which economic model is more competitive? The West and the South after the Covid-19 pandemic

Vladimir Popov (2020)

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# Which economic model is more competitive? The West and the South after the Covid-19 pandemic

Vladimir Popov

## ABSTRACT

*China and other East Asian countries were able to deal with the coronavirus pandemic much better than most Western countries. Both the number of infections and the mortality rate were lower than in Western countries by two orders of magnitude. The economic recession associated with the pandemic is also likely to be much deeper in the West than in the South. These developments give new impetus to the view that the East Asian economic and social model is more viable than the Western model.*

*This paper argues that the East Asian model is superior to other models in the Global South, at least in terms of catch-up development and possibly even in innovations beyond the technological frontier. The East Asian model prioritises community interests (e.g., work collective, neighbourhood, nation-state, and all of humanity) over those of individuals with the possibility of limiting some human rights for the greater benefit of all. Crucial features of the East Asian economic model include relatively low income and wealth inequality, strong state institutional capacity (as measured by the murder rate and share of the shadow economy), high patriotism, and trust in governmental institutions.*

# Which economic model is more competitive? The West and the South after the Covid-19 pandemic

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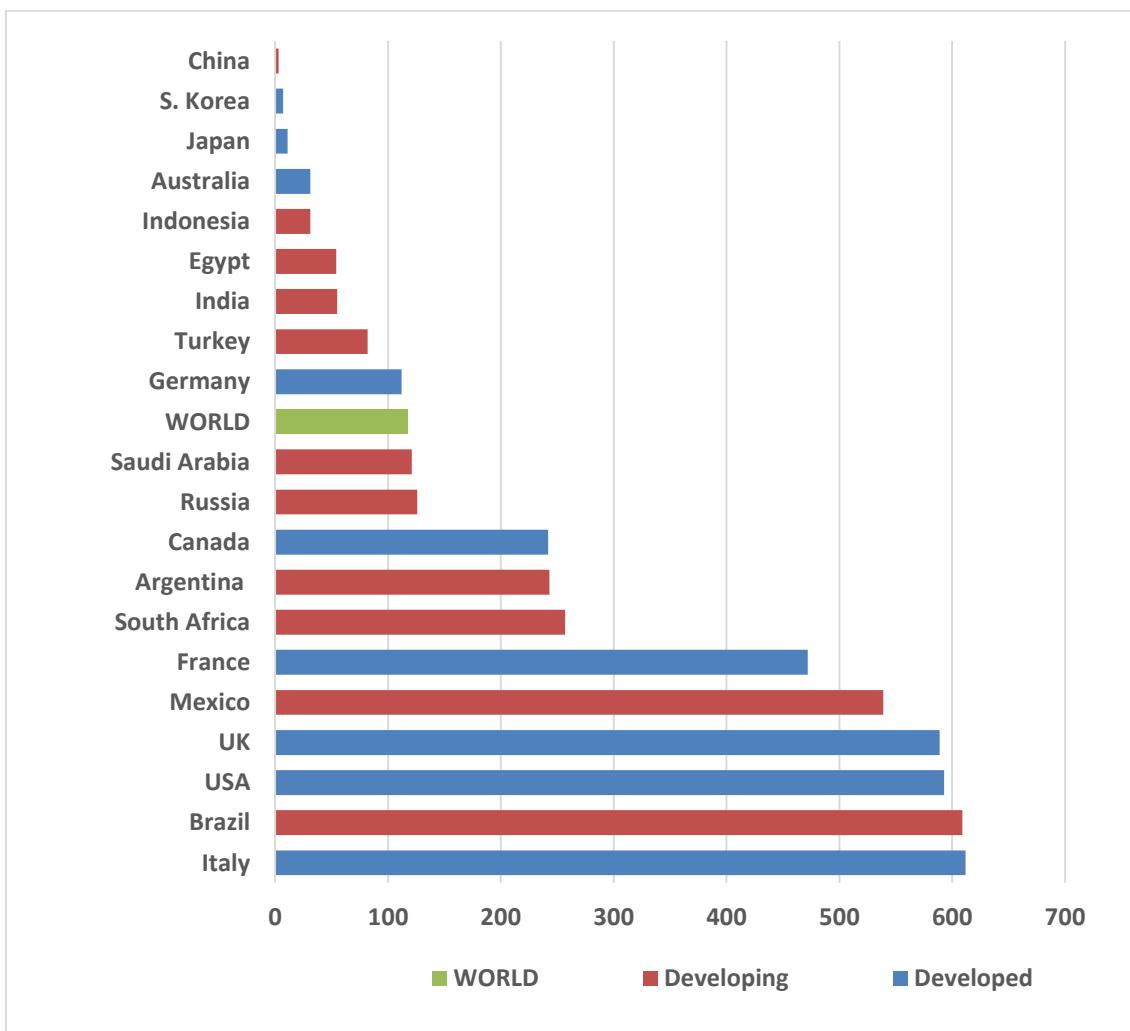
*“East is East, and West is West, and never the twain shall meet.”* Ever since Rudyard Kipling said this, his words have been extensively cited and debated. A more modest question discussed in this paper is this: does the East Asian economic model today differ radically from the Western one, and is it truly more competitive in the long run in terms of ensuring inclusive economic growth at low social costs?

Every world crisis ignites discussion about the efficiency, competitiveness, and viability of different economic models. The 2020 coronavirus pandemic has rejuvenated this enduring debate. China was the first country to be struck by the pandemic and the first to put an end to it through decisively strict quarantine measures. Other East Asian countries and territories – Hong Kong, Japan, South Korea, Taiwan, Vietnam, and others – were able to deal with the coronavirus pandemic much better than most Western countries. Statistics at the time of this writing (September 2020) are incomplete; there are also many issues with the compatibility of national statistics. But differences between the West and East, both in terms of the number of infections and the mortality rate, are too dramatic to be attributed to statistical reporting alone. The infection and death rates from coronavirus in most Western countries are higher than in East Asian countries by two (!) orders of magnitude (Popov, 2020b): the death rate is in the single digits per 1m inhabitants in China, Japan, and South Korea and in the hundreds in the US, France, UK, and Italy (Fig. 1).

The pandemic-associated economic recession is also likely to be much deeper in the West than in the South. In the first quarter of 2020, GDP declined by a 3.5% annual rate in the EU, by 4.8% in the US, and by 6.8% in China. The GDP in Hubei province (Wuhan, where the virus was first detected, is the provincial capital) fell by nearly 40% (!). In the 33

other administrative units of China (except Tibet), first-quarter GDP fell as well. Yet the Chinese economy had already begun to recover in March, and the second quarter was much better than the first. Meanwhile, in Europe and the US, a major reduction of output occurred precisely in the second quarter. The only country whose economy totally recovered in the second quarter of 2020 after the coronavirus recession is China – its second-quarter GDP in 2020 was 3% higher than in the same quarter of 2019. In all other G20 countries, it was lower, mostly by 10-20%, i.e., the recession has not only continued but was getting deeper (table 1).

**Figure 1: Death rate from Covid-19 per 1m inhabitants as of 10 September 2020, in G20 countries**



Source: Worldometers

For 2020 as a whole, the mid-year World Bank economic forecast projected a sharper decline in output in advanced economies (-7%) than in the developing world (-2.5%) and no decline in China (growth of 1%), compared to a 6% decline in the US. The OECD September

2020 forecast predicted a reduction of output in all G20 countries except for China (Table 2). It appears that the Global South will cope more effectively with the 2020 global economic downturn than the West, as was the case during the previous downturn – the Great Recession of 2008–09.

**Table 1: Growth rates of GDP in the first half of 2020 in major G20 countries, compared to the same quarter of the previous year, seasonally adjusted**

Country // Growth rates of GDP compared to the same quarter of the previous year, %	Q1-2020	Q2-2020
United States	0.3	-9.1
European Union – 27 countries	-2.5	-14.2
Germany	-2.2	-11.3
France	-5.7	-18.9
Italy	-5.6	-17.7
United Kingdom	-1.7	-21.7
Canada	-0.9	-13.0
Australia	1.6	-6.3
Turkey	4.4	-9.0
Russia	1.8	-5.6
Mexico	-2.1	-18.7
Argentina	-5.3	..
Brazil	-1.4	-11.4
Saudi Arabia		
South Africa	-0.2	-17.2
India	3.3	-23.5
Indonesia	3.0	-5.4
Japan	-2.0	-10.0
Korea	1.4	-2.8
<b>China (People's Republic of)</b>	<b>-6.8</b>	<b>3.2</b>

Source: G20, Quarterly Growth Rates of GDP in volume. OECD. Stat.

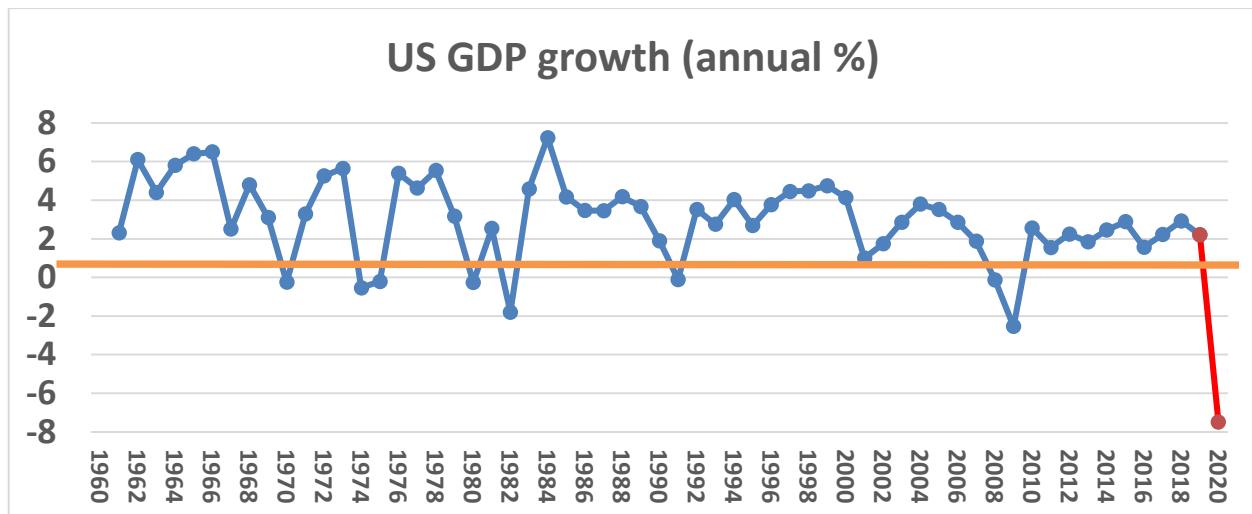
**Table 2: OECD economic forecast, September 2020 – GDP growth rates, %**

Country	2019	2020	2021
Argentina	-2.1	-11.2	3.2
Australia	1.8	-4.1	2.5
Brazil	1.1	-6.5	3.6
Canada	1.7	-5.8	4.0
China	6.1	1.8	8.0
France	1.5	-9.5	5.8
Germany	0.6	-5.4	4.6
India	4.2	-10.2	10.7
Indonesia	5.0	-3.3	5.3
Italy	0.3	-10.5	5.4
Japan	0.7	-5.8	1.5
South Korea	2.0	-1.0	3.1
Mexico	-0.3	-10.2	3.0
Russia	1.4	-7.3	5.0
Saudi Arabia	0.4	-6.8	3.2
South Africa	0.1	-11.5	1.4
Turkey	0.9	-2.9	3.9
United Kingdom	1.5	-10.1	7.6
United States	2.2	-3.8	4.0
World	2.6	-4.5	5.0
Euro area	1.3	-7.9	5.1
G20	2.9	-4.1	5.7

Source: OECD (2020).

Post-war economic recessions in most Western countries were largely mild; for example, US GDP did not fall by more than 1–2% annually. Even in the last recession of 2008–09, which was highly unique and known as the ‘Great Recession’, the reduction in US GDP totalled only 0.1% in 2008 and 2.5% in 2009 (Fig. 2).

**Figure 2: US GDP annual growth rates, %**



Source: World Development Indicators database.

If the reduction in output in major Western countries in 2020 totals 5–10%, this will mark the deepest recession of the post-war period and could be compared with the Great Depression of the 1930s. The US GDP at that time fell for four consecutive years and was about 30% lower in 1933 than in 1929. It finally recovered to the pre-recession (i.e., 1929) level in 1936, only to fall again during the recession of 1937–38.

Just a decade ago, a debate about the East Asian/Chinese and Western model was sparked by the Great Depression of 2008–09. The GDP in major Western countries fell in 2009 by several percentage points, whereas China experienced only a marginal decline in growth rates – from 14% in 2007 to 10% and 9% in 2008 and 2009, respectively (the rate increased to 10% in 2010). There was no shortage of articles during the recession suggesting that the Chinese model was more viable and that the West should learn from China: “We in the West have a choice,” wrote Anatole Kaletsky in *The Times*. “Either we concede the argument that China, in the 5,000 years of recorded human history, has been a much more successful and durable culture than America or Western Europe and is now reclaiming its natural position of global leadership. Or we stop denying the rivalry between the Chinese and Western models and start thinking seriously about how Western capitalism can be reformed to have a better chance of winning” (Kaletsky, 2010).

Is the East Asian model really more competitive and viable than the Western one?

## The Western model in crisis?

It is true that an optimistic observer can find a number of encouraging developments in the world in recent decades. Just before the coronavirus recession of 2020, the economic upturn after the Great Recession of 2008–09 continued for 10 years – one of the longest economic booms in the history of the world economy. The unemployment rate in 2019 was at historic lows. Businesses enjoyed favourable conditions; profit rates were high due to relatively low wages, low interest rates, and moderate resource prices. Many developing countries, mostly but not exclusively in East Asia, were catching up with developed Western countries. On average, living standards in the world as a whole – economic well-being, life expectancy, and educational levels –were as high in 2019 as they had been in human history. The proliferation of the digital economy and advances in globalisation were making countries increasingly interdependent and moulding the world into a unified economy and polity. Despite ongoing regional and ethnic conflict in different regions, war casualties as a percentage of the total population remained lower in the 21<sup>st</sup> century than in any other time on record.

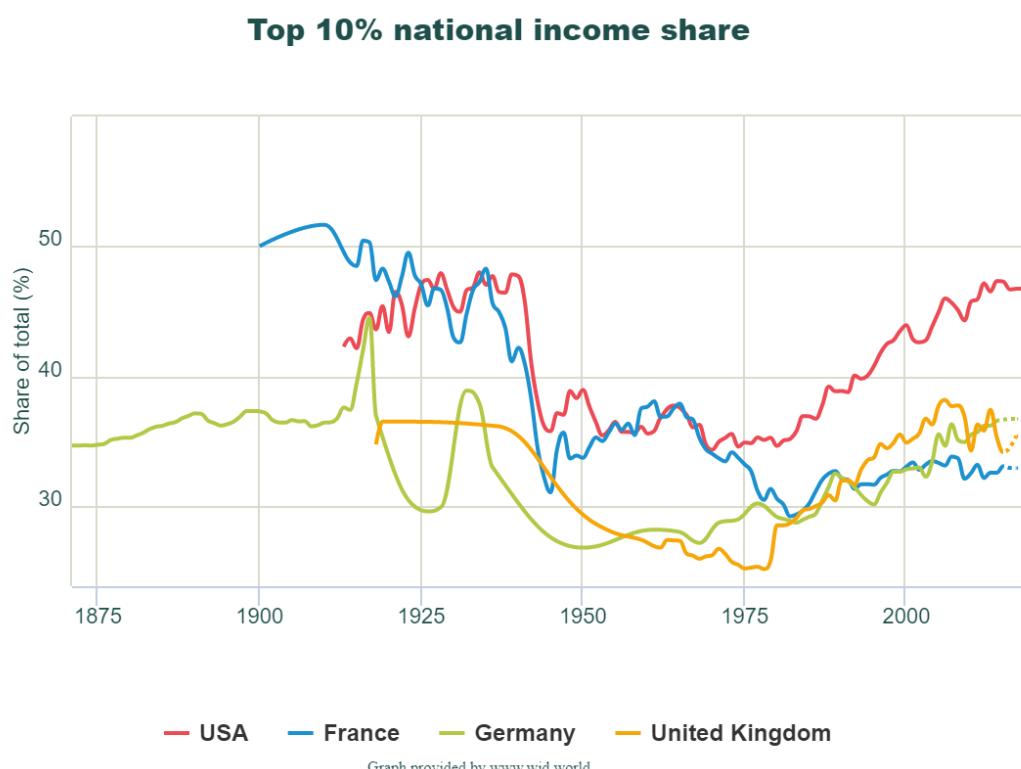
Yet several worrying trends have undermined the prospects for global prosperity and peace. The recent Covid-19 pandemic and newly exacerbated racial conflict in the US and elsewhere represent logical outcomes of the existing system's inability to ensure inclusive growth that leaves no one behind. There was, and still is, a large number of people who do not share the fruits of economic and social progress.

A prolonged period of decline in income inequality in major Western countries (1917–1980) was most likely associated with checks and balances imposed by the existence of the USSR and other socialist countries that provided a real alternative to capitalism (Popov & Sundaram, 2016). But since the early 1980s, once it became clear that the socialist system had lost its economic and social dynamism, income inequality in the West started to grow (Fig. 3). Rising income inequality within major countries since the 1980s posed a threat not only to social stability but also to globalisation. First, in countries where tensions around growing inequality are becoming unbearable, they are generating social turmoil. Second, because large groups of people are not benefiting from globalisation, fertile ground is available for the rise of nationalism and ethno-populism.

When globalisation is properly managed, it is advantageous for growth and income distribution and does not lead to nationalism. But if it is accompanied by a decline in real income for large groups of people, then nationalist political forces are given additional

ammunition to instigate anti-globalisation and isolationist tendencies. Brexit and ‘Trumpism’ now threaten globalisation; recent US trade restrictions and sanctions imposed on China, Iran, North Korea, Russia, Venezuela, and other countries, as well as the extraterritorial application of US laws (e.g., in the case of Huawei) with total disregard for UN procedures, are undermining the existing world order and are unsupported by many, if not most, world states.

**Figure 3: Income share of top income groups in major Western countries in 1875–2018, %**



Source: World Inequality Database

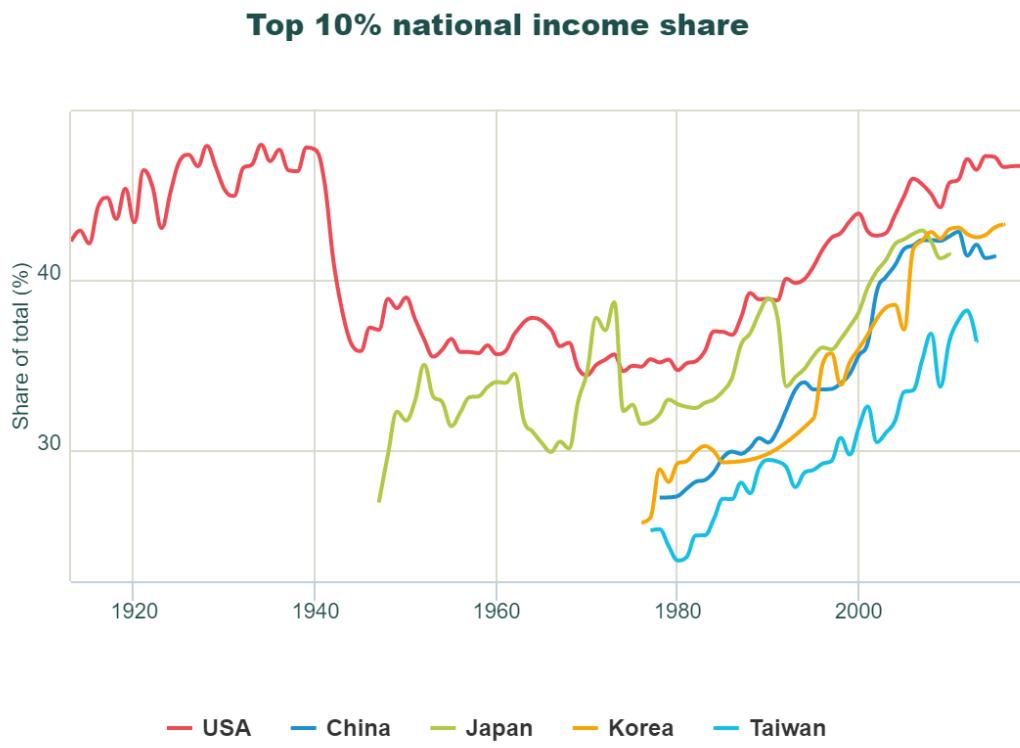
### Economic models in the Global South

Two basic economic models prevail in the Global South: one is the replication of the Western liberal model (e.g., in Latin America, Sub-Saharan Africa, and some former Soviet republics), and the other is sometimes referred to as an ‘Asian values’ model. These ‘Asian values’ are understood as the prioritisation of community interests (e.g., work collective, neighbourhood, national state, and all of humanity) over those of individuals with the possibility to limit some human rights for the greater benefit of all. Whereas the Western liberal tradition considers at least some human rights unalienable, in more traditional

societies – not only in Asia but also in other parts of the Global South – collectivist solidarity is more entrenched. The core feature of the latter is the statistically measurable indicator of low income and wealth inequality. It is argued that this ‘Asian values’ model seems to promote greater social cohesion and more successful catch-up development (Popov, 2014).

Income and wealth inequalities in Asia and the Middle East and North Africa (MENA) are lower than in Latin America (LA) and Sub-Saharan Africa (SSA). Gini coefficients of income distribution in East Asian countries are usually below 40%, similar to Europe, and the share of the top 10% income group is lower than in the US (Fig. 4). In China, the Gini coefficient of income distribution is above 40%, but the country is so large that it should be compared with all Europe or at least with the US<sup>1</sup>.

**Figure 4: Share of top income groups in total income in the US and some East Asian countries, %**



Source: World Inequality Database

<sup>1</sup> Three Chinese provinces (Guangdong, Shandong, and Henan) have populations exceeding 95 million. Another several provinces have populations of more than 50 million (i.e., larger than most states). Therefore, China should be compared with multistate regions (e.g., the EU or ASEAN) rather than with particular states.

Distinguishing *within-* and *between-country/-province* inequality produces especially telling results. In China (29 provinces), the general Gini coefficient of income inequality surpassed 40% with 24 p.p. attributable to between-province disparities. In the US, the Gini coefficient was similar (over 40%), but only 6 p.p. came from disparities in income between the states. In the EU 27 the Gini coefficient around 2005 was roughly 40% with 23 p.p. coming from between-country inequality. If China can manage to reduce the income gap between its provinces (and for the EU, between countries) to a level close to the disparities between US states, then general inequality between citizens will fall to be quite low (Milanovic, 2012).

Lower income inequality makes societies less polarised and is usually associated with a stronger institutional capacity of the state. *The institutional capacity of the state, according to a narrow definition, refers to the government's ability to enforce laws and regulations. While there are many subjective indices (e.g., corruption, rule of law, and government effectiveness) that are supposed to measure state institutional capacity, many researchers consider them biased (Popov, 2011b).*

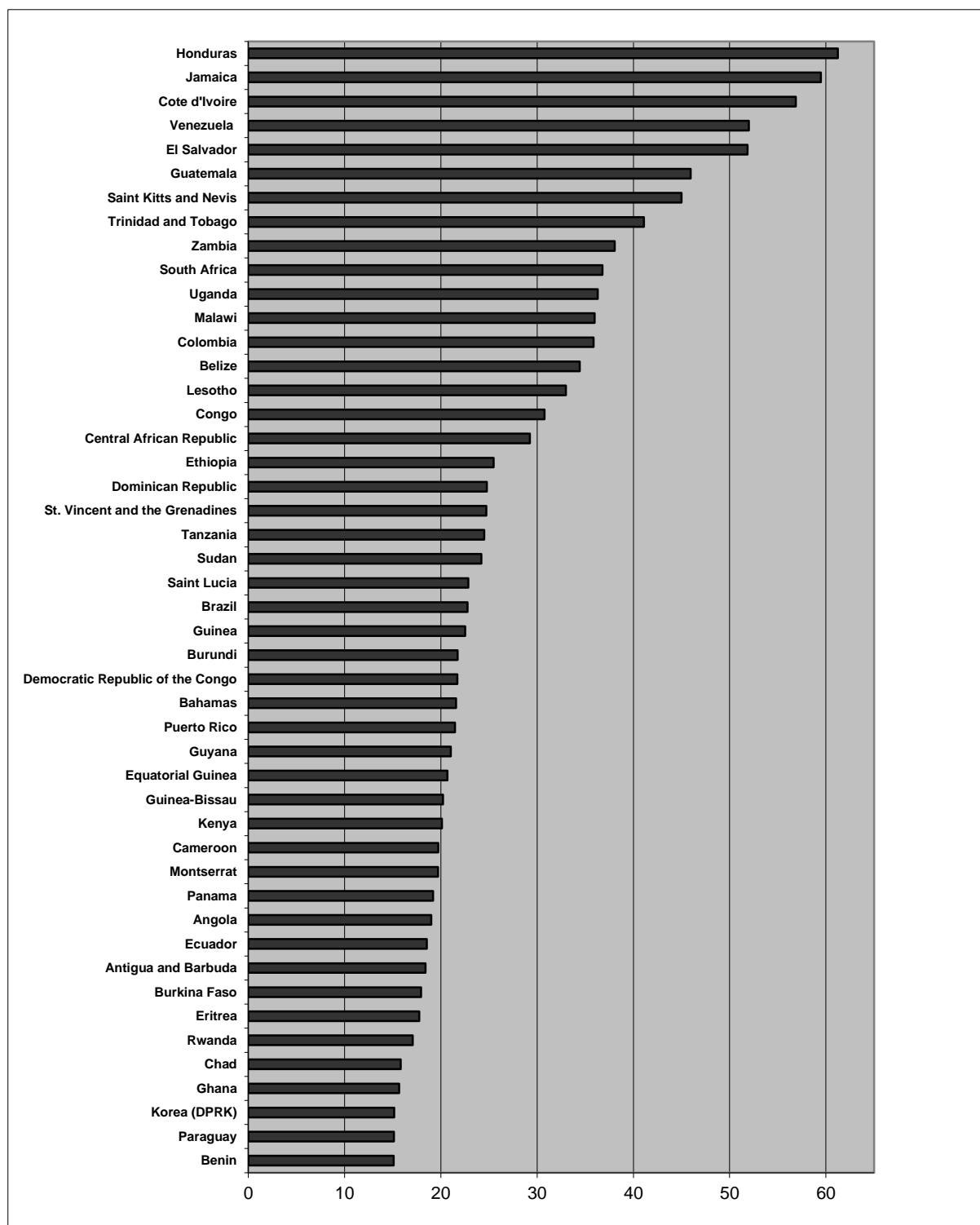
*Natural objective measures* of state institutional capacity are the murder rate (i.e., non-compliance with the state's monopoly on violence<sup>2</sup>) and the shadow economy (i.e., non-compliance with economic regulations). East Asia and MENA countries are quite different from LA and SSA on both measures: East Asian countries have one of the lowest levels of both indicators in the developing world, comparable to that of developed countries (Figs. 5, 6, and 7).

In China, for instance, there are only 1–2 murders per 100,000 inhabitants compared to 1–2 in Europe and Japan and 5 in the US. Only a few developing countries, mostly in the MENA region, have such low murder rates; rates are typically higher by an order of magnitude, as in LA, SSA, and many former Soviet Union states. The same pattern applies to the shadow economy: it constitutes less than 17% of Chinese GDP, lower than in Belgium, Portugal, and Spain. In developing countries the proportion is typically around 40%, sometimes even greater than 60% (Fig. 7). Only a few developing countries have such a low shadow-economy share, particularly Vietnam and several MENA countries (e.g., Iran, Jordan, Saudi Arabia, and Syria) – (Popov, 2011a).

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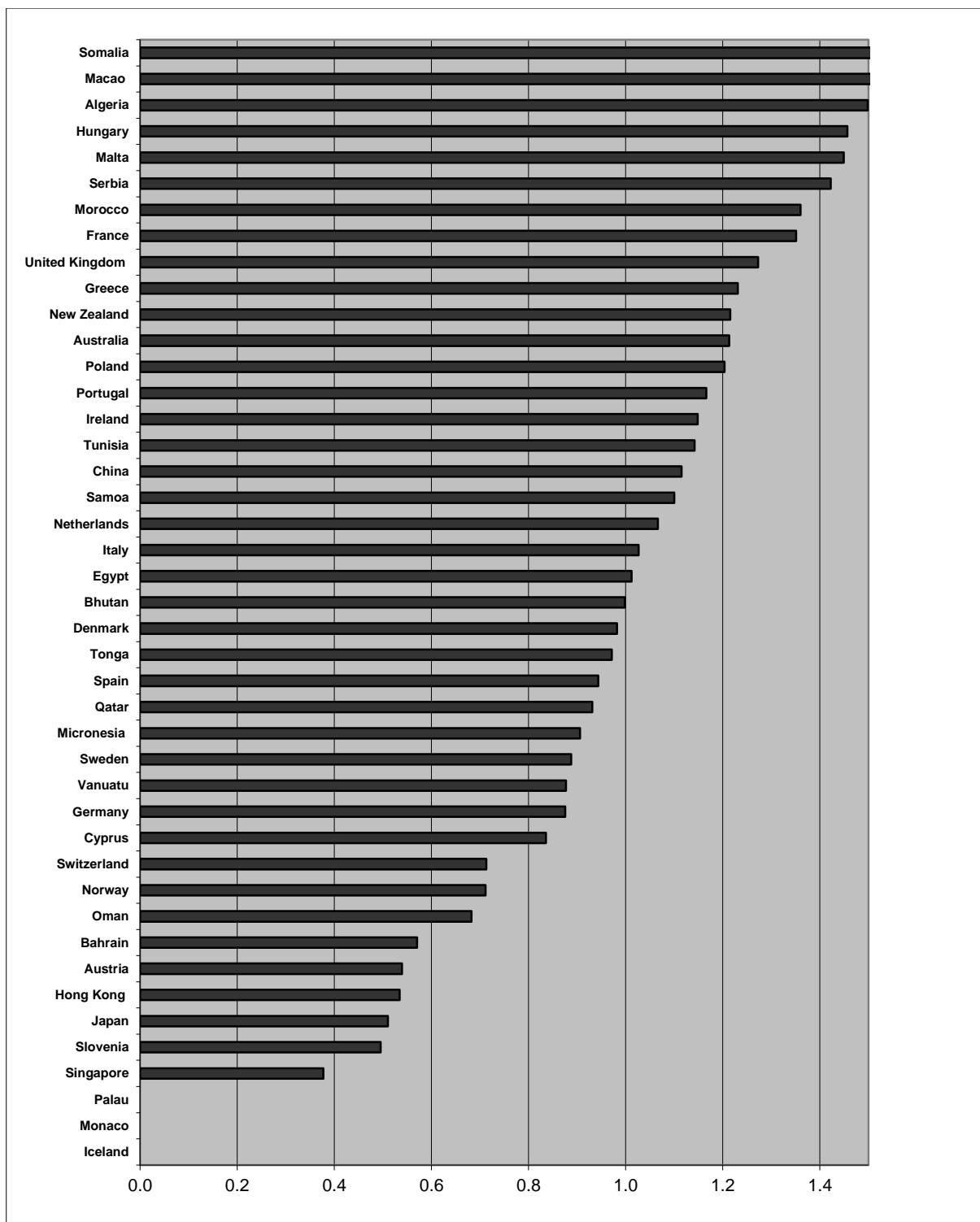
<sup>2</sup> Crimes are registered differently in different countries; higher crime rates in developed countries seem to be the result of more accurate crime records. But grave crimes, such as murder, appear to be recorded quite accurately even in developing countries, so international comparisons of murder rates are warranted.

**Figure 5: Murder rates in countries with more than 15 murders per 100,000 inhabitants in 2008**



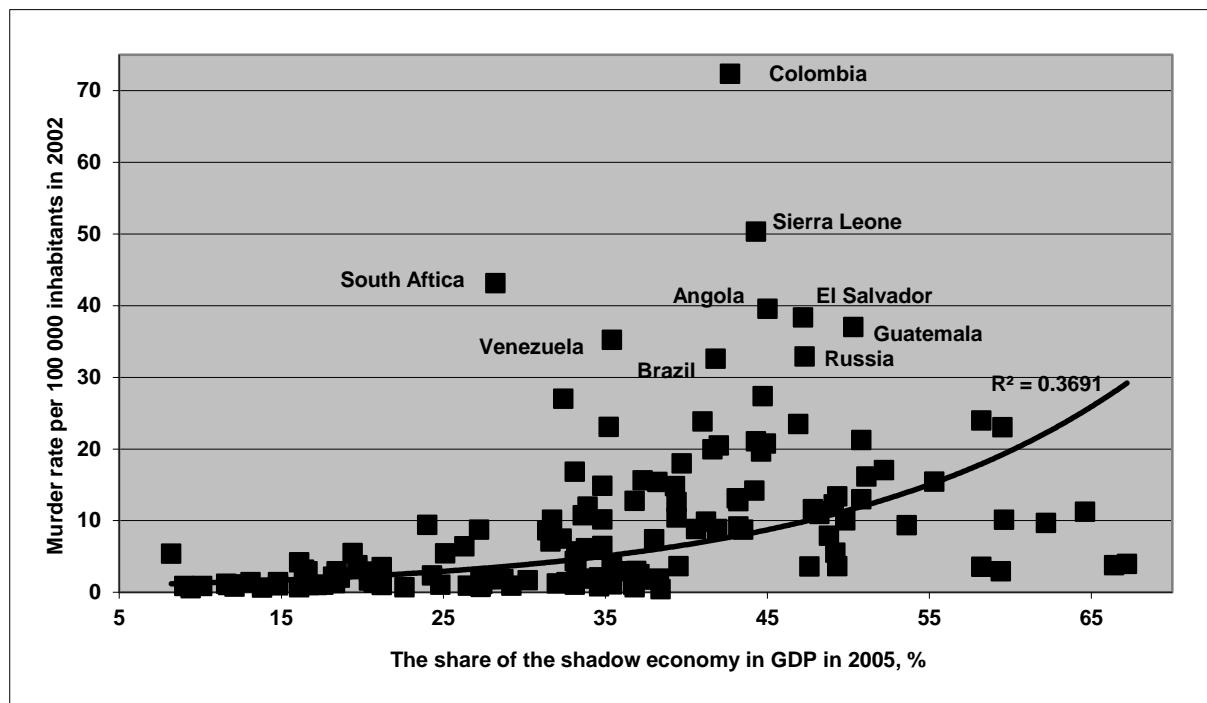
Source: WHO.

**Figure 6: Murder rates in countries with less than 1.5 murders per 100,000 inhabitants in 2008**



Source: WHO.

**Figure 7: Share of shadow economy in GDP in 2005 (%) and murder rate per 100,000 inhabitants in 2002**



Source: WHO; Schneider, 2007.

*The Chinese economic model (as well as the Vietnamese) is sometimes considered distinct from the East Asian model because of the authoritarian regime and Communist party in power. But the Chinese economic model per se certainly shares more commonalities than differences with East Asian tigers (e.g., Hong Kong, Japan, Singapore, South Korea, and Taiwan) and ASEAN countries. The Chinese economy is no longer either centrally planned or state-owned. The private sector dominates: 75% of GDP is produced in non-state enterprises, including joint stock companies and individual private businesses. China also has a relatively small share of government spending in GDP (about 30%), lower than in all Western countries and often lower than in developing countries with similar per capita GDP. There is no longer free education and health care (as were in place in Mao's era). Income and wealth inequality has increased dramatically in the past three decades. They are still lower than in the US but are roughly comparable to European countries and other East Asian states: a Gini coefficient of over 40% and nearly 400 billionaires in the mainland alone, according to a 2020 Forbes report – second in the world after the US, which is home to more than 600 Billionaires.*

*China once had a strong export-oriented industrial policy, mostly based on undervaluation of the yuan through the accumulation of foreign exchange reserves, which aligns closely with policies in Hong Kong, Japan, Korea, Taiwan, and Singapore in earlier*

*stages of development (Polterovich and Popov, 2004). Land is still not a private property in China and is not traded, but public ownership of land is not uncommon in other countries, albeit in smaller proportions. China also exercises control over the capital account; however, this policy is used by many developing countries and was used by European countries after the Second World War until the 1960s. Finally, China's authoritarianism is by no means unique: all countries/territories had it before. Some (e.g., Spain, Portugal, Taiwan, and South Korea) had it as recently as three or four decades ago, not to mention British colonial rule in Hong Kong before the 1997 handover to China.*

It has been argued that China's success is not limited to the recent (since 1979 or even since 1949) impressive catch-up in terms of GDP per capita (Lu, 1999). The other measure of success is the country's ability to become the most populous nation on the planet and to retain this status even as the country fell behind the West in terms of GDP per capita (1500–1950). By an integral criterion (total GDP), China is not only the most successful developing country today but also the most successful country in the world: China's PPP GDP in 2020 is higher than that of the US and the EU.

From this longer-term, millennium perspective, China's extraordinary success before the Opium Wars (mid-19<sup>th</sup> century) and after the Liberation (1949) is due to institutional continuity (Popov, 2014) – the ability to proceed along an evolutionary path without breaking down traditional collectivist structures (i.e., 'Asian values'). In a sense, Deng's famous "feeling for the stones while crossing the river" reform strategy is deeply rooted in the millennium-old Chinese tradition and represents this institutional continuity.

The argument is that East Asia and China in particular found another, more painless exit from the Malthusian trap. Western countries broke from traditional collectivist institutions at a low level of development (namely from the 16<sup>th</sup> to 18<sup>th</sup> centuries) and experienced a painful redistribution of income in favour of the rich, which led to rising income and wealth inequality; this phenomenon allowed the share of savings and investment in income, capital/labour ratio, and productivity to rise, but only at the price of high income inequality associated with the deteriorating quality of institutions and increased mortality under low income levels. China retained traditional institutions and low income inequality for nearly 500 years longer than the West, until technical progress enabled productivity and the share of investment in income to increase without causing mass deprivation of the population (Popov, 2014).

It follows that China's successful catch-up development, if it continues, will signal a turning point for the world economy not only due to the country's size but also because, for

the first time in history, successful economic development on a major scale will be grounded on an indigenous – not a Western-type – economic model.

The litmus test for such an interpretation of economic history is a question on which economists sharply disagree: where will the next economic miracles occur, if at all? If the suggested interpretation is correct, then the next large regions to enjoy successful catch-up development should be MENA Islamic countries (e.g., Turkey, Iran, and Egypt) and South Asia (i.e., India), while Latin America, Sub-Saharan Africa, and Russia can be expected to fall behind.

### **Is the East Asian model sustainable?**

Today, conventional wisdom seems to point to democratic countries that encourage individual freedoms and entrepreneurship, such as Mexico, Brazil, Bangladesh, and India, as future growth miracles, whereas rapidly growing and currently authoritarian regimes, like China and Vietnam or Iran and Egypt, are thought to be doomed to experience a growth slowdown – if not a recession – in the future. Proponents of these views say that without free entrepreneurship and democracy, technical progress will always suffer.

According to Jack Goldstone (2009), “a country encouraging science and entrepreneurship will thrive regardless of inequality: hence India and Brazil, and perhaps Mexico, should become world leaders. But I say countries that retain hierarchical patronage systems and hostility to individualism and science-based entrepreneurship, will fall behind, such as Egypt and Iran” (p. 3). Many believe that rapid growth can be achieved under authoritarian regimes only at the catch-up stage, not at the innovation stage: once a country approaches the technological frontier and it becomes impossible to grow simply by copying others’ innovations, a country can continue to advance only through free entrepreneurship, guaranteed individual freedoms, and a democratic political regime (Inglehart & Welzel, 2005).

This may or may not be true; we still do not have enough evidence of innovation-based growth. For one thing, on all measures of patent activity, Japan, South Korea, and China are already ahead of or rapidly catching up with the US. The US patent office, after consistently issuing the highest number of patents since 1998, was overtaken in 2007 by the patent office of Japan. China’s patent office replaced the European Patent Office as the fourth largest office in terms of issuing grants (the five largest patent offices –Japan, the US, the Republic of Korea, China, and the EPO – accounted for 74.4% of total patent grants).

The number of resident patent filings per \$1 of GDP and \$1 of R&D spending is already higher, sometimes considerably so, in Japan, Korea, and China compared to the US (WIPO, 2009).

Evidence for catch-up growth is controversial to say the least. Successful technical progress and high rates of economic growth (including labour productivity and TFP) in the USSR in the 1950s are inconsistent with the view that individual freedoms and free entrepreneurship are prerequisites for successful growth. The USSR launched the first satellite into space in 1957, followed by the first cosmonaut in 1961 – all without a stock market and democratic elections. In the 1960s–80s, the USSR enjoyed more freedoms than in the 1950s but less growth. Individual freedoms, entrepreneurship, and the flow of ideas really flourished in the 1990s, but this was also a period of economic decline, not growth – a time of technical degradation and collapsing R&D. Fundamental research was in disarray, applied research by enterprises virtually stopped, high-tech industries experienced dramatic decline, and the share of machinery and equipment in exports fell. To put it differently, comparing of R&D, innovations, and technical progress in the former Soviet Union to Russia's current technological landscape is akin to comparing a mountain peak to a swamp.

The history of economic forecasting is similarly telling. Imagine for a moment that the debate about future economic miracles were happening in 1960: some are betting on a freer, democratic, and entrepreneurial India and Latin America, whereas others forecast the success of authoritarian (even sometimes communist), centralised, and heavy-handed government interventionist East Asia... Today, we know who would have won the bet.

What is unknown, however, is whether the gradual weakening in the reform-period capacity of the Chinese state will continue, which would transform China into a 'normal' developing country (Lu, 2009). In this case, China's rapid growth would come to an end and there would no longer be a question of what is so special about the Chinese economic model.

"For other developing countries, the Chinese Government's national mobilization capacity remains strong, highlighted by the relatively effective organizational leadership of the Government in responding to emergencies, such as natural disasters and post-disaster reconstruction. However, the downward trend in government capacity seems to be a clear fact. It has the ability to organize forces to fight SARS, but cannot effectively control some resurgent infectious and local diseases, cannot ensure that everyone has a medical treatment, it can act as a 'fire brigade', but cannot effectively maintain the production safety of coal mines, cannot guarantee that all workers have income, it can launch again and again

campaigns against criminal activities and pornography, but cannot sweep the triads" (Lu, 2009).

The continuation of rapid Chinese growth is just one of several possible scenarios, and many factors could prevent it from materialising. First, there is a controversy among economists regarding whether rapid Chinese growth is sustainable. Krugman (1994) drew parallels between East Asian and Soviet growth. He argued that there is no puzzle to Asian growth; it was mostly due to the accelerated accumulation of factor inputs (i.e., capital and labour), whereas total factor productivity growth was quite weak – lower than in Western countries. He further presumed that East Asian growth would end in the same way that Soviet growth did: by overaccumulation of capital undermining capital productivity.

Predictions of an impending crash of the Chinese economic model and political system are by no means in short supply. Chang (2001) predicted a collapse within five years back in 2001,<sup>3</sup> whereas Yang (2006), Pei (2006), and Hutton (2007) each asserted that, without democratisation, the Chinese economy is doomed to at least slow down if not collapse completely<sup>4</sup>. Huang and Khanna (2003) made a different argument: China, as compared to India, lacks homegrown entrepreneurs and is highly dependent on foreign direct investment. They also contended that China lags behind India in terms of corporate governance, innovations, and access to external financing.<sup>5</sup> Gilboy (2004) showed that early-2000s China was still behind Korea and Japan 20 and 30 years ago, respectively, in terms of the share of high-tech goods produced by domestic (not foreign) firms in total output and export, in R&D spending as a proportion of GDP, and other metrics. Gilboy (2004)

<sup>3</sup> "Peer beneath the surface, and there is a weak China, one that is in long-term decline and even on the verge of collapse. The symptoms of decay are to be seen everywhere." Chang believed that China has about five years to get its economy in order before it suffers a crippling financial collapse – a timeline he seriously doubted could be met.

<sup>4</sup> "In the absence of an alternative to the vision of liberal democracy, the authoritarian Chinese ruling elite will find it no easy task to juggle all the competing demands that come its way" (Yang, 2006, p. 164). "The lack of democratic reforms in China has led to pervasive corruption and a breakdown in political accountability. What has emerged is a decentralized predatory state in which local party bosses have effectively privatized the state's authority. Collusive corruption is widespread and governance is deteriorating. Instead of evolving toward a full market economy, China is trapped in partial economic and political reforms" (Pei, 2006, cover text).

<sup>5</sup> "In fact, you would be hard-pressed to find a single homegrown Chinese firm that operates on a global scale and markets its own products abroad" (Huang & Khanna, 2003, second paragraph). This is not factually correct: Huawei; Baosteel; Chery; Cosco; Haier; Konka; Lenovo (Legend), which purchased the PC business of IBM; and TCL are just a few examples. Twenty Chinese companies (all under Chinese control and nearly all state-controlled) were on the Fortune 500 list of the world's largest companies already in 2006 as compared to six Indian companies (US -170, Japan -70, Britain -38, Germany -35, Russia -5).

further concluded that China was experiencing growth without development and that it could not compete technologically with the US. Ocampo (2013) deemed technological sophistication the real measure of development success and believed that East Asia is not succeeding in this respect despite rapid catch-up in per capita income.

Second, some posit that China's rise will continue but that this ascension does not actually represent a threat to the West because the Chinese model is developing in the direction of Western liberal democracy and a 'normal' capitalist market economy based on private property (see discussions in Bergsten, Gill, Lardy, & Mitchell, 2006; Peerenboom, 2007). Experts have argued even more so that inside China, much like other developed and developing countries, inequality in income distribution appears to have been on the rise since the early 1980s.

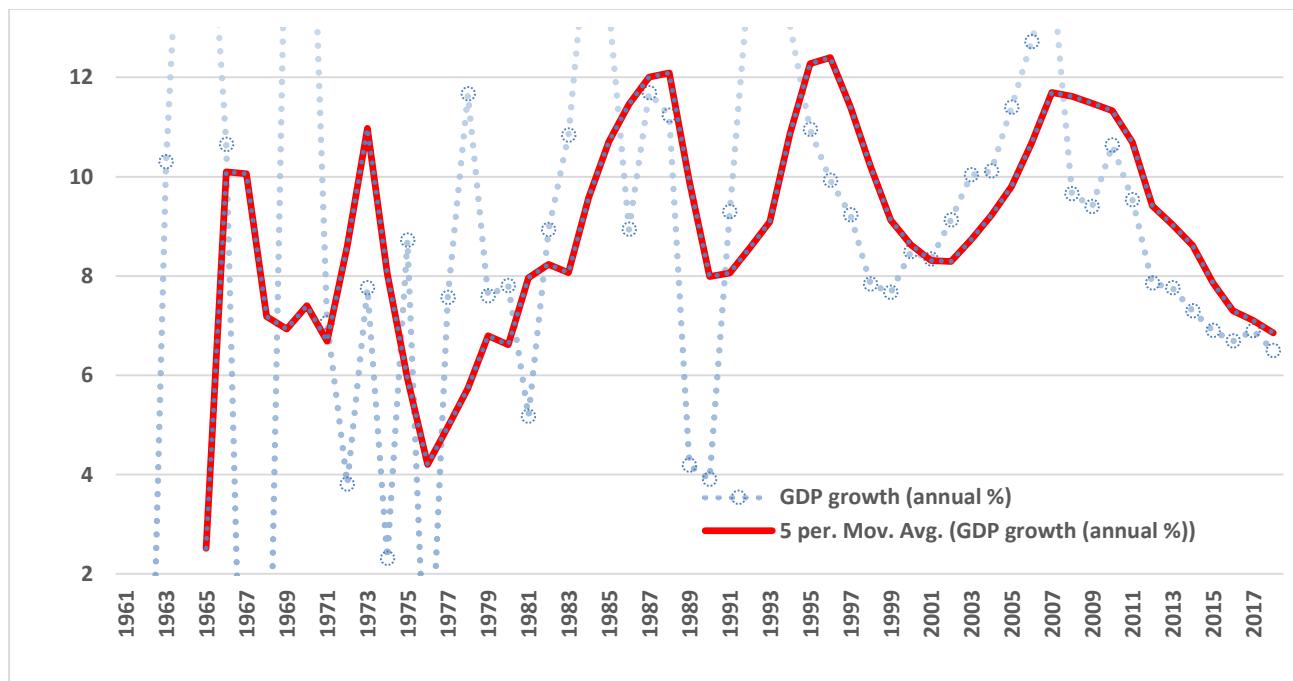
To be fair, the Chinese elite have definitely monitored Western predictions of the coming crash carefully in an effort to identify forthcoming dangers. "Chinese intellectuals, academics, and policymakers – especially those who are members of the 'fourth generation' – are keenly aware of Western musings about the coming collapse of China, and they are even more interested in using this work to identify and correct flaws in their system that will serve to revitalize their nation and buttress the power of the Communist Party. This might be cause for us to reconsider the likelihood of a coming Chinese collapse in plotting the future course of American policy," concluded an American expert (Marsh, 2002, paragraph #10).

*The question is whether the Chinese model will gradually evolve into the Western model, and if so, will it look more like a European (i.e., more state-led) model or like an American model with high income inequality, limited social guarantees, and state involvement in the economy? If the Chinese model does indeed evolve in the Western direction, then the geopolitical change – China becoming the leader instead of the US – will look more like a replacement of one state by another within the existing world system (similar to the US replacing the UK after the Second World War). But if the Chinese model retains its present characteristics or evolves into something different from the Western model, the consequences for world economic order would be far-reaching. There may be a true democratisation of international economic relations and more favourable conditions for the economic development of the Global South.*

## Slowdown of growth in China

Even before the coronavirus recession, China's economy was slowing down. In 2007, Chinese GDP grew by 14%. Growth rates have since declined by more than half, to 6.1% in 2019 (Fig. 8). The five-year moving average growth rate is at its lowest since reforms began in 1978, more than four decades ago.

**Figure 8: GDP growth rates in China since 1960, %**



Source: World Development Indicators.

Economists have pointed to various factors as slowing China's growth, including the decline in the population growth rate and the ageing of the Chinese population (Lin, Wan, & Morgan, 2016). These factors are real but have been exaggerated. The working-age population and employment each grew at 2% annually from the 1980s, but such growth declined earlier this century before coming to a halt in 2014. This pattern could explain the decline in the GDP growth rate by up to two percentage points yearly.

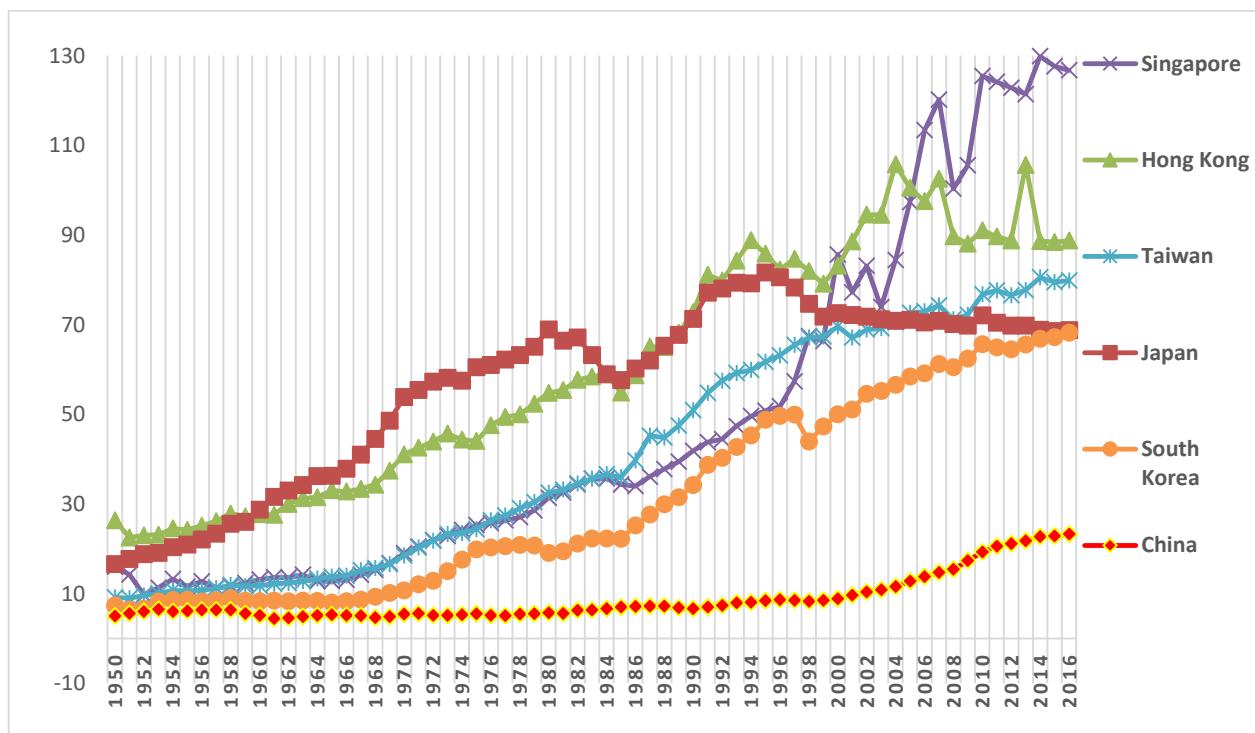
Another factor is exhaustion of the advantages of economic backwardness: it is easier to catch up from a low base, especially because devising cutting-edge innovations is more difficult and costly than copying pre-existing technologies, whether for free or by buying patents and copyrights. Developed economies have rarely grown for extended periods at the breakneck pace of East Asian 'miracle' economies when they were 'catching up' or

converging; growth tends to slow in fast-growing economies as they approach the technological frontier.

But growth slowdowns of East Asian “tigers” and “dragons” have taken place after their per capita incomes surpassed half that of the US, whereas Chinese per capita GDP (at purchasing power parity; that is, even at comparable prices) is currently still less than a quarter of the US level (Fig. 9). In fact, marked slowdowns have only occurred in Japan and Hong Kong, whereas the other ‘tigers’ have continued to grow rapidly while eluding the supposed ‘middle-income trap’. If these experiences are any guide, China’s growth slowdown should still be a couple of decades away, if it happens at all (Lin, 2019).

Another explanation for China’s growth slowdown involves economic policy changes. Some argue that for four decades, Chinese growth has been due to deliberate exchange rate depreciation, promoting exports, and discouraging imports by rapidly accumulating foreign exchange reserves (Polterovich & Popov, 2004).

**Figure 9: Per capita PPP GDP in some East Asian economies as a % of US, 1950–2016**



Source: Maddison project database (2018)

After the first half-decade of the 21<sup>st</sup> century, however, China gave in to US-led international pressure for the renminbi to appreciate. The real exchange rate of China’s RMB – understood as the ratio of Chinese to international prices, as measured by the ratio of its

dollar GDP at the official exchange rate to its purchasing power parity GDP – rose for a decade from 2003 to 2013, especially during 2006–2011. China's exports as a share of GDP peaked at 35% in 2005 and then started to fall. Domestic consumption rose while savings, investments, and growth inevitably slowed. The investment share of GDP peaked in 2013 at 45% and began to decline thereafter (Popov, 2019).

### **Analysis: Do low income inequality, solidarity, ‘Asian values’, and strong institutions ensure inclusive development better than guarantees of human rights and individual freedoms?**

This debate has persisted for at least several hundred years and implies an answer to the questions “How did the West get rich?” and “Why are some developing countries catching up with the West faster than others?”

The gap between the West and developing countries was expanding in 1500–1900, reaching a 6:1 ratio in terms of per capita GDP, and it was not closing in the 20<sup>th</sup> century: in 2000, the ratio of per capita GDP in the West and the developing world was still 6:1. The USSR, in the 1920s–60s, was the first major non-Western country to experience successful catch-up development and to narrow the gap with the West, although the gap then stopped narrowing (1970–80s) and later widened (1990s and beyond).

In the 1950–80s, however, five developing countries managed to catch up with the West and join the ‘rich country club’ for the first time in history. Japan, South Korea, Taiwan, Hong Kong, and Singapore were the only developing states to successfully catch up with the West and become developed. In recent decades, a similar process has been underway in Southeast Asia and China. Together with a recent acceleration of growth in India and some other developing countries, we may have reached a tipping point in the ‘Great Divergence’: from now on, the world could gradually experience a global convergence in income level. If these trends continue, the share of the West in the global economy could fall from 35% today (PPP GDP, 2019) to only 20% by 2050, just slightly more than the share of the West in total population (it is expected that, out of 10b people on Earth, a mere 1.5b will live in Europe, the US, Canada, Japan, Australia, and New Zealand in 2050).

There are two major schools of thought to explain these changes. According to the first, the evolutionary school (as per Landes [1998] and Mokyr [2002], to name a couple contemporary authors), the growth of Western countries in 1500–1900 that allowed them to become the wealthiest in the world was the inevitable result of social changes introduced during this period. Many interlinked social changes have been deemed crucial: the abolition

of serfdom and guaranteed human rights, the Reformation and Protestant ethics, the *Magna Carta*, and the European Enlightenment are all said to have inspired the openness, flow of ideas, and technological innovations that ultimately led to the Industrial Revolution and acceleration of growth. “The conventional wisdom, endorsed by many economic historians, most notably by Douglass North, points to a connected set of legal, economic, and social institutions that are thought to be necessary for or at least especially conducive to sustained economic growth. The most important are the rule of law itself, secure property rights, relatively untrammelled markets, and a degree of social mobility. They function by reducing the uncertainty surrounding saving, investment, and entrepreneurial activity, and by sharpening the incentives for able people to devote themselves to economic activity instead of violence and prayer. The Industrial Revolution happened when it did because these background conditions were met as they had not been met before; and England is where they were met soonest and most fully” (Solow, 2007, p. 8).

This point of view, that freedom and democracy are responsible for long-term economic success, was recently defended by Acemoglu and Robinson (2012, paragraph #8), who claimed that countries “such as Great Britain and the United States became rich because their citizens overthrew the elites who controlled power and created a society where political rights were much more broadly distributed.”

Another school of thought has questioned the logic of evolution triggered by social forces (Diamond, 1997; Pomeranz, 2000; Wong, 1997 – once again, to give several contemporary examples) and pays special attention to seemingly minor historical events – fortunate and unfortunate, but mostly accidental – that pre-determined the development of countries and continents for centuries to come. “In this view, Western dominance was the by-product of natural forces that reflect no credit on Western civilization: geographical accidents such as location of mountains and coastlines, geological accidents such as the ready availability of coal or gold or arable land, climatological accidents such as the timing of the ice ages or the direction of the ocean currents, and biological accidents (not always so accidental) that affect the susceptibility of various population groups to lethal diseases” (Tetlock, Lebow, & Parker, 2009, p. 9).

The rise of Asia in recent decades has given additional credibility to theories rejecting the superiority of the Western economic model and the inevitability of Western success. “As Japan, the Asian Tigers and China developed into major economic powers, more and more scholars concluded that theories explaining West’s success through long-term cultural, environmental, or racial causes simply could not be right. The big story in the world history,

they began suggesting, was not the long-term inexorable rise of the West; it was the tale of multipolar world, which the West had only recently, temporarily, and perhaps even accidentally come to dominate" (Morris, 2013, p. 2).

Diamond (1997), for instance, argued that the lack of wild animals suited to domestication in pre-Columbian America, Africa, and Australia, coupled with the abundance of these animals in Eurasia, gave the latter a huge advantage. Or perhaps the origins of comparative development can be traced to climatic and environmental conditions on the Eurasian continent that allowed for sufficiently high agricultural productivity to support a high-density population – a necessary pre-condition for the spread of technological innovations and rapid economic growth.

Popov (2014) proposed a different explanation, particularly that Western countries exited the Malthusian trap by dismantling traditional collectivist institutions: this pattern was associated with increased income inequality and even decreased life expectancy but enabled the redistribution of income in favour of savings and investment at the expense of consumption. The elimination of collectivist (community) institutions was a risky experiment that placed masses of the population below the subsistence minimum and resulted in a reduction or slowdown of population growth – the foundation of military might (number of people–number of soldiers) in the Malthusian growth regime.

"A great civilization is not conquered from without until it has destroyed itself within," remarked Will Durant about the Roman Empire (Durant, 1980, Epilogue, second paragraph). But apparently this diagnosis could also explain the collapse of many ambitious civilizations. Early attempts to ensure the priority of individual rights over the rights of the community at the expense of collective interests and low inequality (i.e., Greece, Rome, and the Byzantine Empire) led to the impoverishment of the masses, higher mortality, and foreign conquests. Only in Northwest Europe in the 16<sup>th</sup>–18<sup>th</sup> centuries did this policy somehow succeed for the first time in history.

It is not the abundance of competition, entrepreneurship, or ideas for technological innovations that allowed the West to accelerate productivity growth rates by orders of magnitude; it is first and foremost the abundance of savings and investment that resulted from growing income inequality and allowed the capital/labour ratio to increase and to cast in iron the ideas for new products and technologies. To put it differently, the West became rich not thanks to its inventiveness and entrepreneurial spirit but due to the cruel and merciless dismantling of agricultural community that previously provided social guarantees to the poorest.

When the same pattern was applied to developing countries (i.e., the colonialism in Latin America and SSA or voluntary Westernisation in an attempt to catch up, as in the Russian Empire), it resulted in the destruction of traditional institutions, growing income inequality, and the worsening of starting positions for catch-up development. This group of countries replicated the Western exit from the Malthusian trap: they experienced an immediate increase in income differentiation, rising savings and investment, and growing productivity, but all at the price of rising social inequality and deteriorating institutional capacities.

Other developing countries (e.g., East Asia, South Asia, and MENA) were less affected by colonialism and managed to retain their traditional institutions. This delayed their transition to modern economic growth (Kuznets, 1966) until the mid-20<sup>th</sup> century but fostered the preservation of a sound starting position for economic growth – low inequality and strong institutions. Eventually, slow technical progress allowed these countries to find another (and less painful) exit from the Malthusian trap: slow increase in income allowed to raise the share of savings and investment in GDP without a major increase in income inequality, without worsening their institutional capacity or decreasing life expectancy.

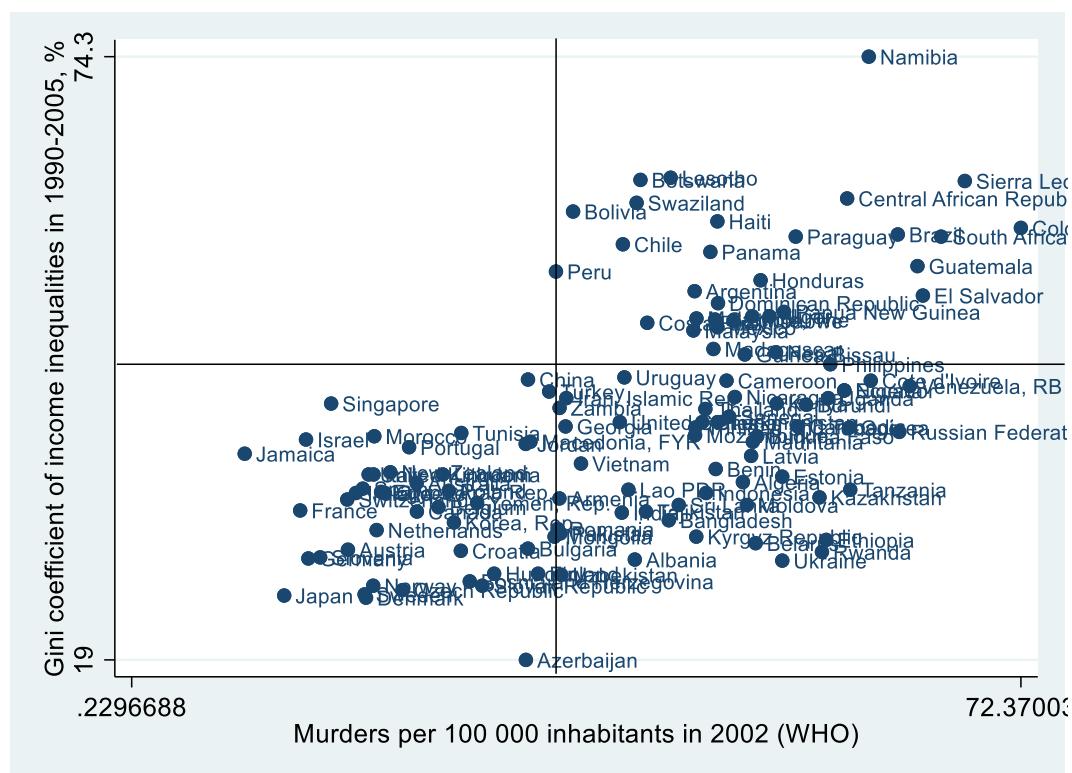
More Westernised countries in the Global South (i.e., LA and the Russian Empire) boosted their savings-investment rate and exited the Malthusian trap earlier than the rest – in the 18<sup>th</sup> century – but at the price of undermining necessary conditions for future growth, specifically low inequality and strong institutions. As a result, subsequent LA and Russian growth was then insufficient to catch up with the West. The colonisation of SSA (except for South Africa), unlike the colonisation of LA and the Westernisation of Russia, did not result in considerable transfer of technology and human capital; it only increased inequality and undermined institutions. SSA countries were therefore disadvantaged on all counts and had the worst growth record in the world. On the contrary, most less-Westernised countries in East/South Asia and MENA managed to preserve low inequality and efficient collectivist institutions. Their savings-investment ratios stayed below 10% until the mid-20<sup>th</sup> century. They did not grow before that, but once savings increased, it turned out that they possessed all the preconditions for fast growth. Some of these countries became economic miracles, rapidly catching up with the West (i.e., East Asia); others have accelerated their development in recent decades (i.e., South Asia); and still others (i.e., MENA countries) will probably become economic miracles in the future.

Today, low income inequality is generally tied to strong institutional capacity (e.g., low murder rate and low shadow economy), but to be more nuanced, it may make sense to distinguish between three groups of countries (Fig. 10):

- low inequality and strong institutions (e.g., developed countries; some East Asian and MENA states);
  - relatively low inequality and poor institutions (e.g., former socialist countries and some MENA and East Asian states);
  - and high inequality and poor institutions (e.g., LA and SSA).

Similar (but not identical) results can be observed by plotting several subjective measures of solidarity from the World Value Survey – trust in government and willingness to fight for one's own country<sup>6</sup> (Fig. 11) – against the murder rate, an objective indicator of institutional strength. Here we can distinguish between four groups of countries (Fig. 12):

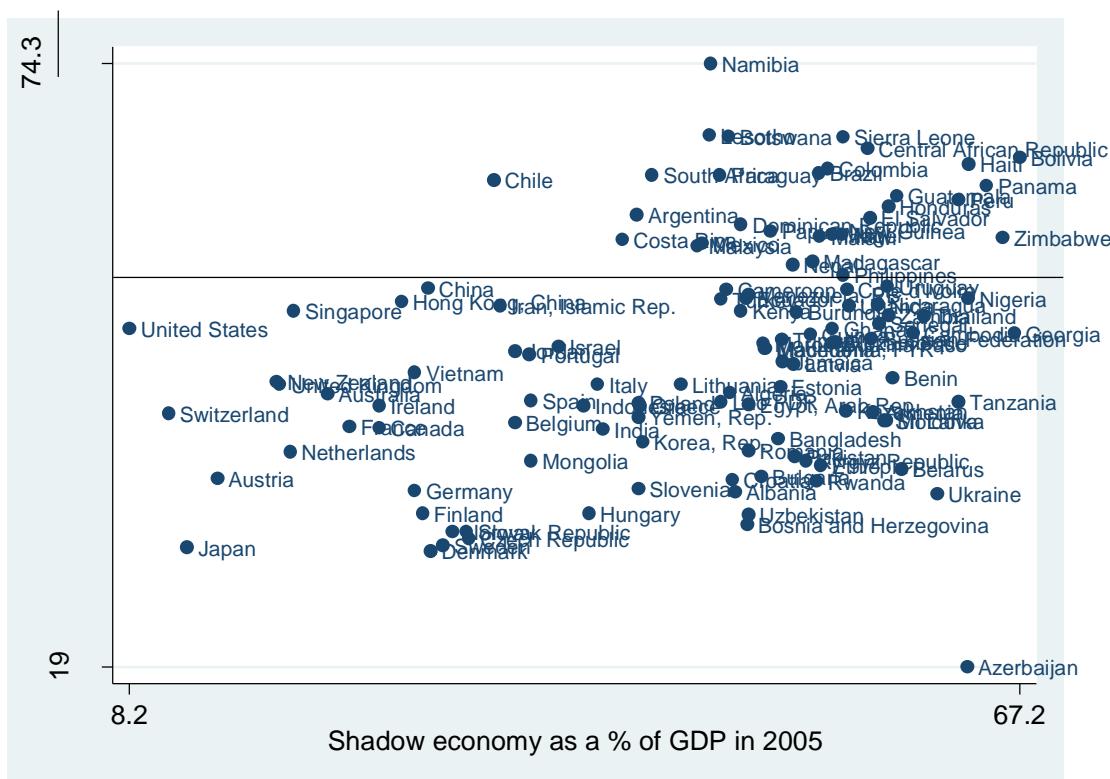
**Figure 10: Gini coefficients of income distribution, murder rate, and shadow economy**



<sup>6</sup> The patriotism index and trust-in-government index are computed as the ratio of positive answers to negative answers in Round 6 (2010–14) of the World Value Survey.

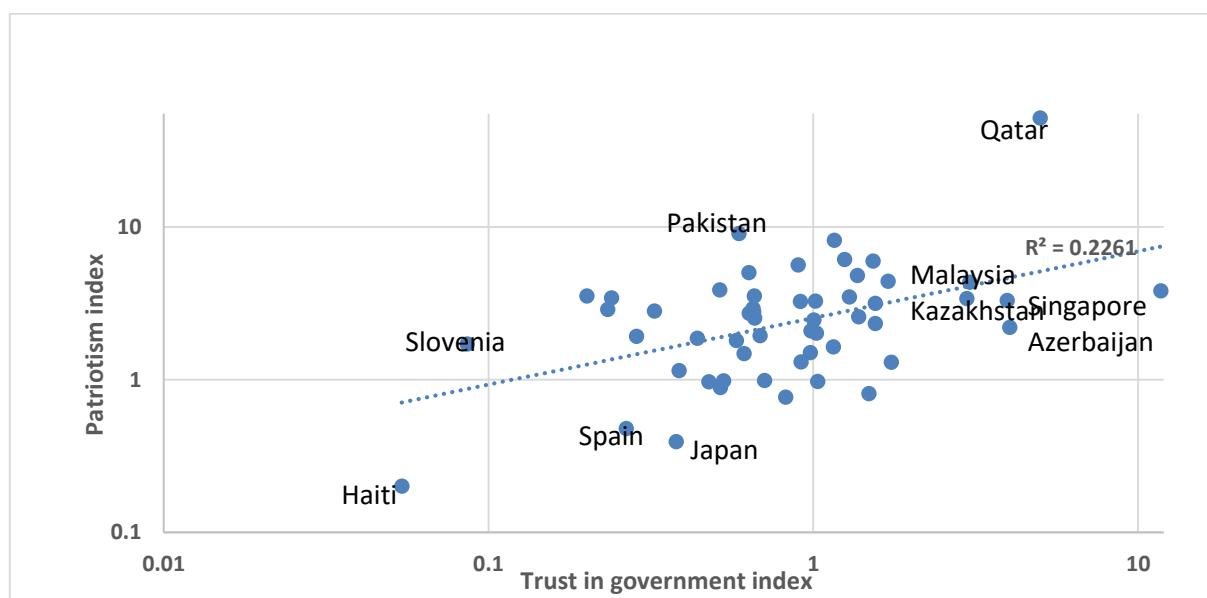
Question about patriotism (V66): Of course, we all hope that there will not be another war, but if it were to come to that, would you be willing to fight for your country?

Question about trust in government (V115): How much confidence you have in the government (in your nation's capital): is it a great deal of confidence, quite a lot of confidence, not very much confidence or none at all?



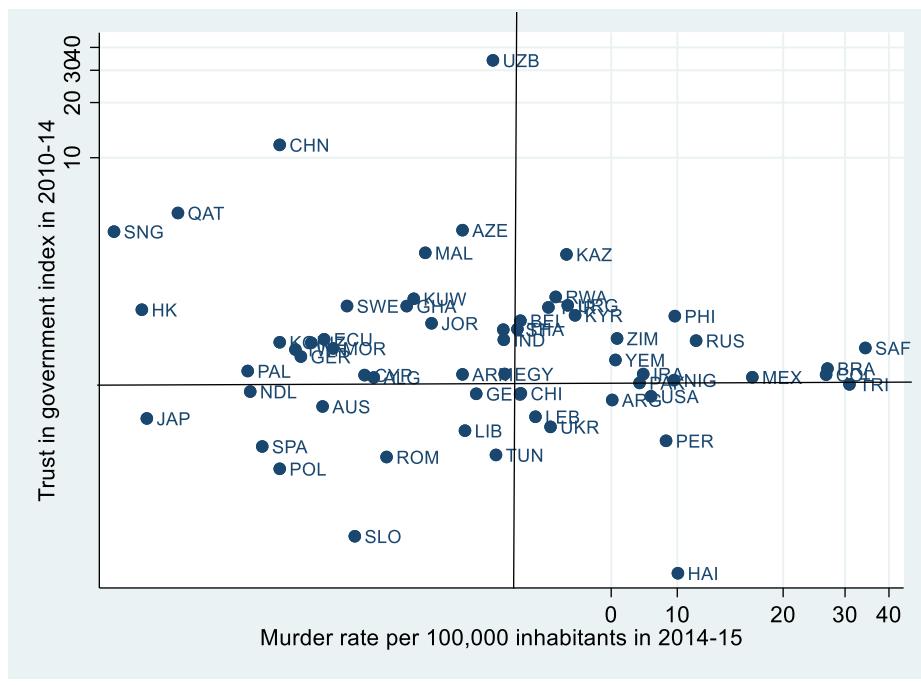
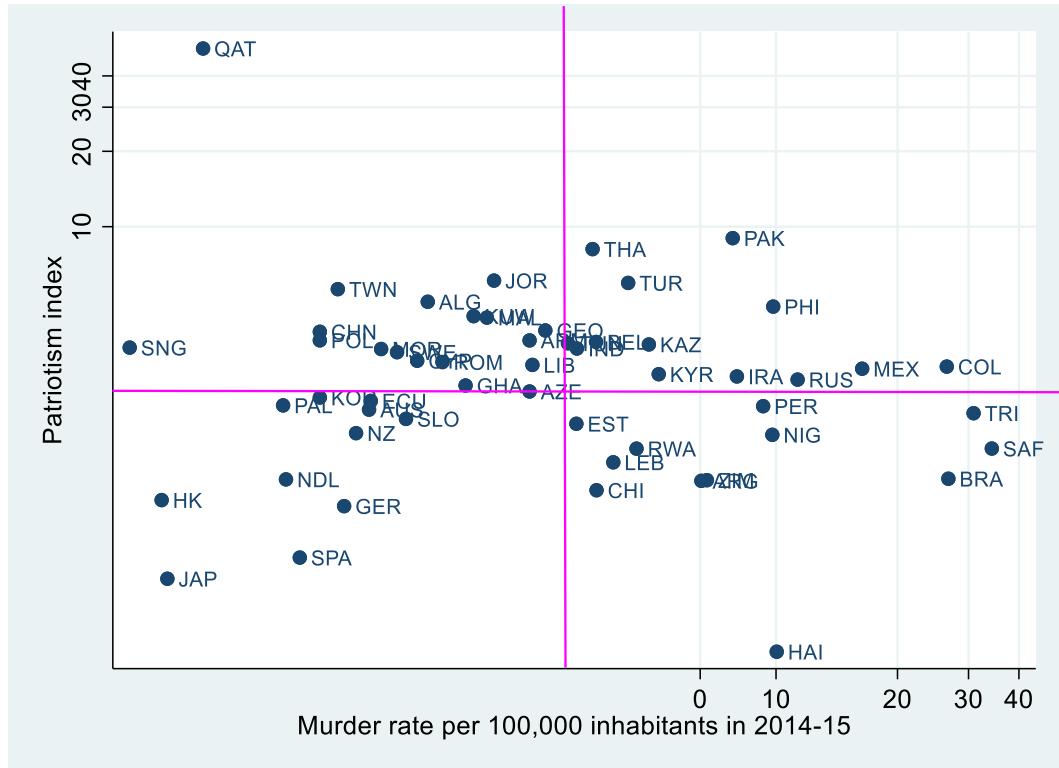
Source: World Development Indicators database. Data on shadow economy are from Schneider, F. (2007). Shadow economies and corruption all over the world: New estimates for 145 countries. *Economics. Open Access, Open Assessment E-Journal*, 2007(9) (measures of the shadow economy are derived from divergence between output dynamics and electricity consumption, demand for real cash balances, etc.).

**Figure 11: Trust-in-government index and patriotism index**



Source: World Value Survey

**Figure 12: Patriotism index, trust in government, and murder rate**



Source: World Values Survey

- East Asian and MENA countries have generally low murder rates and higher patriotism and trust in government;
  - Developed countries have low murder rates and low trust and patriotism;

- Many LA and SSA countries have lower indicators of trust and patriotism and high murder rates;
- and members of the former Soviet Union (e.g., Belarus, Kazakhstan, Kyrgyzstan, and Russia) have high murder rates along with high trust in the government and patriotism.

It can be hypothesised that higher trust in governmental institutions and stronger patriotism (i.e., willingness to fight for one's own country) can build social cohesion and solidarity in difficult times, even if objective measures of institutional strength (e.g., murder rate and the shadow economy) are not that impressive. Conversely, strong institutions may not be enough to respond effectively to crises if social solidarity is weak. This trend may explain why, in advanced countries struck by the coronavirus, quarantine and isolation measures were less strict and enacted after a delay compared to East Asian and MENA countries, leading to much higher infection and death rates in the former.

### **Implications of the rise of the Global South: New world economic order?**

The implications of the rise of 'the Rest' are often seen in forthcoming geopolitical shifts (e.g., China as a new rising superpower together with or instead of the US), in emerging resource shortages leading to new increases in raw material prices, and so on. But there may be less-expected and farther-reaching consequences as well.

First, the rise of East Asian economies, if it continues, would become a turning point for the world economy: *successful economic development on a major scale would be based on an indigenous, not Western-type, economic model* for the first time in history. This model is based on solidarity and cooperation more than competition – low income and wealth inequality, strong state institutions, and prioritising common-good interests over individual ones. Such 'coopetition', as they say today, may be not only better for social harmony and cohesion, but also more economically efficient than pure competition.

Because the East Asian growth model became so successful in ensuring catch-up development, it is no surprise that the model has become extremely appealing in the developing world. The current attractiveness of the East Asian model of economic growth could be compared with the popularity of the Soviet model of catch-up development in the 'third world' in the 1960s. Even though the Soviet model collapsed, the East Asian/Chinese model became its logical and natural heir – China is no longer a centrally planned economy,

but it is by no means a model of a liberalised market economy that is recommended by the advocates of Washington and even post-Washington consensus.

Second, the rise of ‘the Rest’ can lead to profound reform of the world economic order and international relations. Trade protectionism, industrial policy, undervaluation of the exchange rate via accumulation of foreign exchange reserves, and control over international capital flows (not only short-term but also foreign direct investment) can become legitimate tools for catch-up development. We may also see new regimes related to the protection of intellectual property rights and technology transfers, new regulations for international trade in energy and resources, new rules for international migration, new agreements about cutting emissions of pollutants (e.g., reconsideration of the Kyoto protocol), and so forth.

Third, principles of international relations can change radically as well. The ‘Beijing consensus’ may not yet be a rigorous term, but it is clear that the Chinese approach to international politics (i.e., no interference in domestic affairs, no military intervention, and no trade embargoes) provides the developing world with a real alternative to building relations with other countries. China rejects the use of force, embargoes, and sanctions in international politics nearly as a matter of principle. Even in its relations with Taiwan, China was always pushing for wider economic and cultural exchanges, whereas Taiwan authorities resisted. The new rules of international relations may (1) explicitly limit the use of force only to cases of severe violations of non-political rights (i.e., mass repression, hunger, or ethnic violence) and prohibit the use of force against liberal authoritarian regimes (just for the sake of ‘establishing democracy’) and (2) prohibit unilateral military interventions (without the UN’s consent).

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