The China Boom: Why China Will Not Rule the World by Ho-fung Hung

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Reviewed by Salvatore Babones 25 January 2016

China is up, China is down. China is a savior, China is a bully. China lifts millions out of poverty, China oppresses millions with its authoritarian rule. China will be richer than the United States, China will collapse with its first recession. China will rule the world, China will... well, what then? No one seems to be quite sure. Ho-fung Hung poses the question in The China Boom: Why China Will Not Rule the World but leaves the answer for the future to tell.

Hung is keenly aware that people are prone to exaggerate and romanticize everything about China. He prefaces the book with a series of 18th-century quotes about China from Voltaire (China is up) and Kant (China is down). Hegel is in the basement: “the concept of virtue and morality never entered the head of the Chinese.”

For Hung, China is down—but not out. A native of Hong Kong who now makes his home in the United States, Hung prefaces the book by describing his family’s multigenerational involvement in China’s ups and downs. His maternal grandfather actually migrated to China in 1949 to participate in the new worker’s paradise, only to be marked as a pro-capitalist. Other relatives stayed in Hong Kong to work in the Communist union movement there.

If Hung’s family origins are in the Chinese Communist intelligentsia, his intellectual roots are in the American Marxist intelligentsia. Like estranged brothers, the two have much in common. Social scientists will see a big difference between Chinese state socialism and western Marxian analysis. Lay readers may not.

Hung is no capital-C Communist, but the first half of the book is firmly grounded in a Marxian account of China’s economic history, 1650-2008. Marxian economics is not necessarily wrong, but it is a particular—and in the Chinese case, ironic—lens through which to examine economic history. It may or may not be the most useful lens, depending on your perspective.

In a five-page summary of his theoretical approach, Hung references Max Weber, Immanuel Wallerstein, Fernand Braudel, Giovanni Arrighi and of course Karl Marx. Hung takes his theory of capitalism and growth directly from Marx’s famous M-C-M’ equation, in which Marx pointed out that capitalists invest money now (M) to get more money later (M-prime). Certainly true, but hardly profound.

Hung uncritically adopts the orthodox Marxian proposition that there is something called “primitive accumulation” (an initial accumulation of capital that can occur in non-market conditions, for example through conquest or—as Hung argues—under Communism) that can then be used as the foundation for a successful market economy. In this view, Europe’s primitive accumulation came from the plunder of the Americas. Capitalism took off from this launchpad.

Hung argues that China once had a similar level of primitive accumulation made possible by an agricultural revolution in the early Qing (1644-1911) dynasty. He presents data showing that around the year 1800 China had higher land productivity and similar labor productivity to England. China had the capital necessary for growth. The problem, according to Hung, was that China lacked the capitalists to take advantage of it:

“the reproduction of the urban entrepreneurial elite was constrained by the lack of the state’s unconditional support of the elite against contentious popular classes... China still lacked any vibrant
entrepreneurial elite capable of concentrating the agrarian surplus to bring forth a capitalist-industrial takeoff”.

Non-academics may be surprised to hear that Marxists have anything good to say about capitalists, but Marx was fully committed to the idea that capitalism was a necessary way-station on the road to socialism. In fact, many western Marxists were upset to see Russia and China turn communist because in their model of the world a successful communist transition could only occur in an advanced capitalist society. As history shows, they may have been right.

But if imperial China ever had the economic base to support a capitalist industrial revolution, by 1949 that base had been destroyed. The Communists had to rebuild China’s capital stock from scratch. Hung traces China’s post-reform economic growth directly to the urban capital built up by the Communist Party through its ruthless exploitation of the countryside and its inhabitants. When China finally allowed the return of capitalism in the 1980s, there was already enough “M” for China’s new capitalists to use in creating lots of “M-prime”.

This account is emerging as a new academic orthodoxy, but it can seem out of touch with reality. By western standards, China had virtually no fixed capital in 1978. The subsequent forty years of massive capital inflows seem to confirm that China was in fact capital-poor in 1978, not capital rich. And from a comparative perspective the Soviet Union certainly had much higher levels of physical and human capital when it let the capitalists in—and promptly went bust.

Hung sees China’s boom coming to an end now. He shares the conventional wisdom that China has relied too much on investment to drive growth and he points to the usual suspects as evidence: overcapacity in manufacturing, empty office blocks, and falling producer prices. He points especially to overcapacity in steel, an important indicator sector for the wider economy. Profitability is low and the banking sector is plagued by bad debts. Hung is certainly correct that these are not signs of an economy poised for another four decades of record-breaking growth.

What Hung fails to mention is that the China boom is ending while China is still much poorer than such global laggards as Mexico and Russia. The China Boom shares the common shortcoming of most contemporary writing on China: it analyzes China in isolation and in comparison with the developed West but not in comparison to its peers. For China specialists (both Chinese and Western) it may seem as if China has no peers. But that kind of thinking is on a plane with Voltaire, Kant, and Hegel. Not bad company, perhaps, but in the 21st century we can do better.

Despite these blinders, the book gets the diagnosis right. China needs greater levels of consumption by ordinary people to stimulate domestic demand. China’s massive foreign currency reserves are symptomatic of an unsustainable reliance on exports. Hung reiterates the now-conventional prescription that China must make a transition from investment-led growth to consumption-led growth. He agrees with most economists that China’s massive dollar holdings are as much to blame for global imbalances as are America’s massive trade deficits.

But since the book went to press China’s currency reserves have rapidly deteriorated. In December alone the outflows were more than US$100 billion. At the same time China’s state budgets have shifted into deficit despite the fact that the government has slowed the pace of public investment in infrastructure. Are these the first signs of much-advocated rebalancing of the Chinese economy toward domestic consumption? Or are they worrying signs of lost confidence in China’s future growth?
China surely needs a “profound redistribution of wealth and income that will let average households share a larger slice of the pie”, but then so do Brazil, India, Mexico, Russia, South Africa, Saudi Arabia, Turkey and most of the developing world. Those other countries have high levels of consumption, moderate levels of investment, and no massive dollar hoardings. How are their households doing? Has “consumption-led growth” worked for them? What these countries need is more investment, not less. So does China.

Ironically, academic Marxian analyses and popular investment punditry come to the same conclusion: China’s economic model is unsustainable and China must change course to continue to grow. The academic Marxist wants higher wages to raise consumption. The popular pundits want economic liberalization to raise consumption.

But no country ever consumed its way to prosperity, not even the United States. China’s economy is faltering precisely because China’s leadership does not have the political will to make the additional investments necessary to boost China from middle-income status to high-income status. China doesn’t need a new course. It needs to double-down on the old course.

The problem is that the old course—massive government investments in education and infrastructure—is expensive. For four decades, the bills paid themselves as tax revenues outpaced spending growth. Economic liberalization generated easy money just by removing the fetters of inefficient Communist Party central planning.

Now the easy growth has come to an end. The hard growth requires China to keep investing in education and infrastructure despite its budget constraints. That can only be done by raising taxes, and in a big way.

China’s total combined government revenues for all levels of government are just 23 percent of GDP. Compare that to 35 percent in the United States and 45-50 percent in Western Europe. The Chinese state needs more money to fund continued public investment: to build schools, to hire teachers, to improve public health, to expand transportation networks, to— in short—bring China up to first-world levels of development. Investments like these would soak up the excess capacity that Hung and other pundits worry so much about. They might even rescue state banks by turning some of their bad loans good. And they would raise ordinary people’s living standards, just as they did once upon a time in what are today the rich countries of the world.

The China Boom is too carefully argued to take such a leap into the unknown.

That said, it is no intellectual door-stopper. It is a fast-paced, highly readable, thoroughly provocative, and (rare for an academic book) truly enjoyable account of 400 years of Chinese economic history right up to the present day. It is Marxian in orientation but is no Marxist screed. It is an intelligent and (leaving aside a few pages on theory) relatively conventional account of China’s rise and current place in the world.

In this book Hung captures the zeitgeist of the moment, the pervasive feeling (inside and outside China) that China must change course to continue to grow. If the zeitgeist turns out to be wrong, it won’t be his fault.