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The Global Economic Crisis and the China Phenomenon:

The Asian Development Model Revisited

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Abstract

This paper places the current economic slowdown in China within the context of the historical patterns of rapid economic growth in East Asia and argues that China's GDP going below 8% this year is not unusual or unpredictable. Emergence measures to uphold the growth rate above 8% can be counter productive.

About the Author

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The Global Economic Crisis and the China Phenomenon: The Asian Development Model Revisited

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The global financial crisis since 2008 has prompted scholars and commentators to look back and compare it to the Great Depression in the 1930s. The underlying message appears to be that the scale and nature of the current economic crisis is comparable to the Great Depression and therefore a new Roosevelt-type New Deal might be justified in response. Indeed, rescue packages since last year by governments in countries from the United States to China, from Japan, Korea to the European Union, have built a sense of *déjà vu* among attentive observers over the classic debate on state-market relations in a modern economy.

On the other hand, there was a celebration of China's 30 years of rapid economic growth in 2008. Much of the attention however has been focused on the unique path of China's economic reform and social development, and how the emergent economic institutions and the enduring political structure worked together as an emergent system of political economy that no one can fully describe, using existing theories and concepts.

Ironically though, in both cases, the Asian financial crisis 10 years ago and more broadly the East Asian model of rapid economic growth since World War II have not featured well in the current debate. There have been whispers within some circles that the responses to the current crisis by governments around the world jibe with what the East Asian model is known for: government intervention to govern the market (Johnson 1982, Wade 1990). But overall, economists, political economists and politicians seem to be quiet about the striking resemblance between the rescue/relief packages of today in the free market economies and government intervention and guidance in the not so free East Asian economies in their rapid growth period.

There are strong reasons to believe that the model of China's rapid economic growth of the past 30 years shared many important features of the model of rapid economic growth in East Asian economies. But the distinct background of the socialist system prior to its current growth cycle and the fact that its "Asian model of growth" started much later than its fellow East Asian economies defy attempts from the very beginning to see China's growth as part of the East Asian model.[1] For many, because of China's levels of economic development and the complexity of its political and economic system, the Chinese economy and other East Asian economies are simply incomparable. More specifically, China's corporate governance and bank-firm relations are different, and the labour market is more flexible and competitiveness in the domestic market is much higher.[2]

As such, we do not learn much about the pattern of the rise and fall of the growth model in these East Asian economies. We learn how and why the East Asian economies rose, but not much of why and how they fell. At the end of the 30 years of rapid economic growth in China, we are more concerned about how the current downturn and the future direction of the Chinese economy would be determined by the external, global dynamics as well as predominant interests and demands currently within China itself. We have not learnt much about the lessons the historical experiences of rapid economic growth in East Asia have offered and the internal logic of this growth model itself. We insist that rapid growth above 8 percent should still be the sole target of the national economy. But we seem to have not paid enough attention to the fact that all the other East Asian economies experienced their rapid economic growth for about 30 years, and then fell below the 8 percent annual growth rate ever since.

In this paper, I shall first demonstrate the historical patterns of rapid economic growth in the East Asian economies,[3] and explain the underlying logic that has shaped such a recurrent pattern in these economies. I will then compare China's growth model and that of East Asian economies in general and see where they converge and where they depart. In the final part, I will discuss the different "modes" of exit out of the East Asian model and explore how the Chinese exit would feature. I will conclude by arguing that there are many factors that complicate the case of China being seen as an instance of the East Asian model. In the second half of its 30 year rapid growth in particular, China has experienced a fading away or removal of some of the key features of the East Asian model to the extent it can not longer be comfortably described as an East Asian model economy. In this context, the national campaign to keep the growth rate above 8 percent appears to be more a political exercise than a policy based on a realistic understanding of the historical logic of China's rapid economic growth.

[1] Indeed, Chinese political leadership was very careful not to be seen as following its East Asian neighbors' successful growth model in its early years of opening and reform in the 1980s.

[2] Lee, Hahn and Lin 2001; see also opposing views, White 1996, Baek 2005.

[3] The East Asian economies here refer to Japan, South Korea, Taiwan, Singapore and China.

1. Historical Patterns of Rapid Economic Growth in East Asia

In my research in the early 2000s on the patterns of rapid economic growth in East Asia (Huang 2005), I found a recurrent pattern in the waves of rapid economic growth during the 50 year period 1950 to 2000, first in Japan from the early 1950s to the early 1970s, then in South Korea, Taiwan and Singapore from the early/mid 1960s to the early/mid 1990s, and finally in China from the early 1980s to 2000 when my research period ended. I defined *rapid growth* as having consecutive annual growth rates above the average of the growth rates among the five economies over the 50 year period which was 7.93%. For Japan, this was the period from 1953 to 1973 with an average growth rate at 11.93%. Korea had an average growth rate of 8.52% over the 30 year period from 1963 to 1992; Taiwan, 9.17% over the same period; and Singapore, 8.88% over the period from 1968 to 1997. China only had close to 20 years of rapid growth by 2000 with the average growth rate at 9.98%.

As shown in the graphics below (Figures 1-5, Source: Huang 2008:7-9) where the black data line was the 5-year moving average of the GDP annual percentage of change over the previous year (constant in national currency). The grey data line is the same data of the United States as a benchmark. The grey box is the rapid growth period of each of the economies as defined here. I summarized the recurrent pattern as follows:

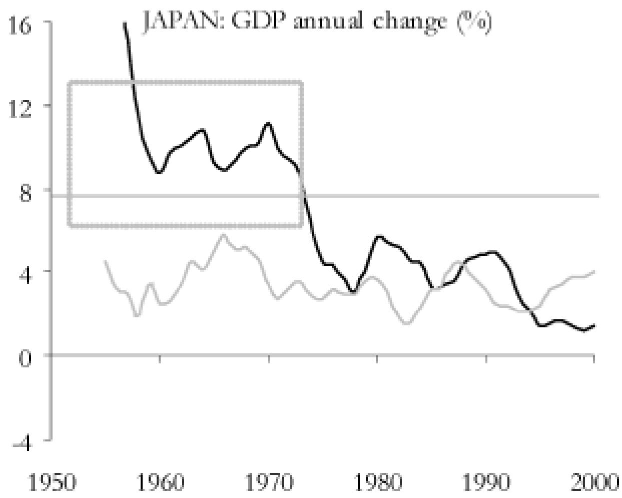

Figure 1: Japan's rapid growth pattern

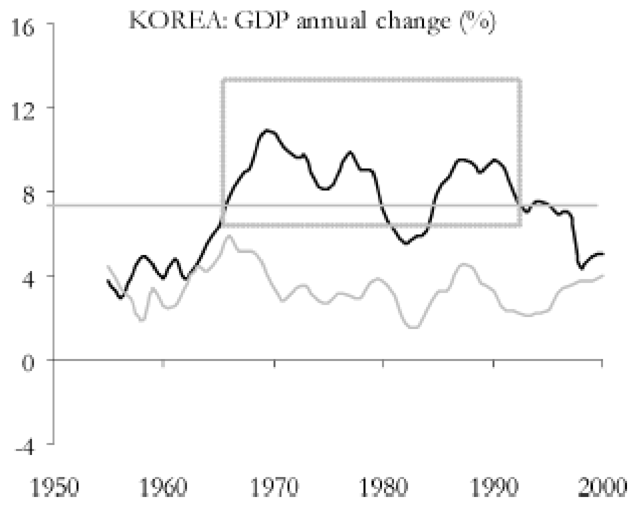

Figure 2: Korea's rapid growth pattern

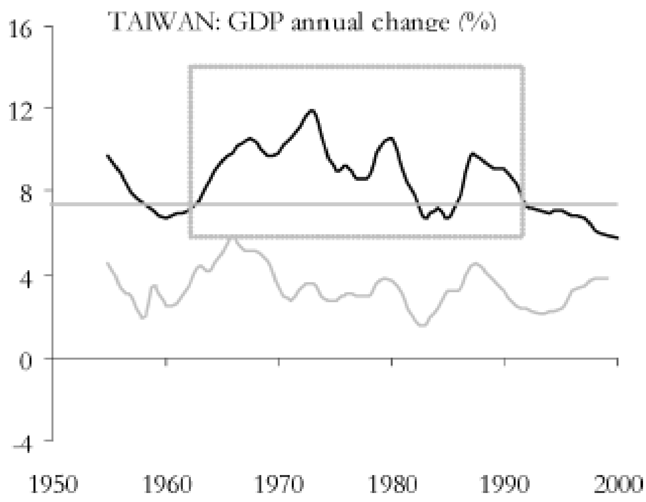

Figure 3: Taiwan's rapid growth pattern

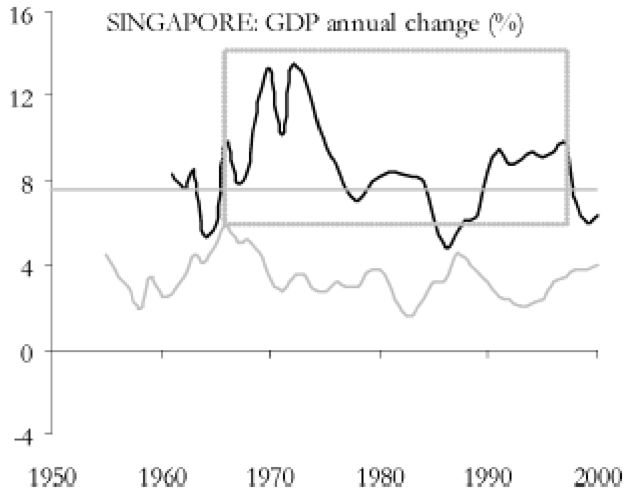

Figure 4: Singapore's rapid growth pattern

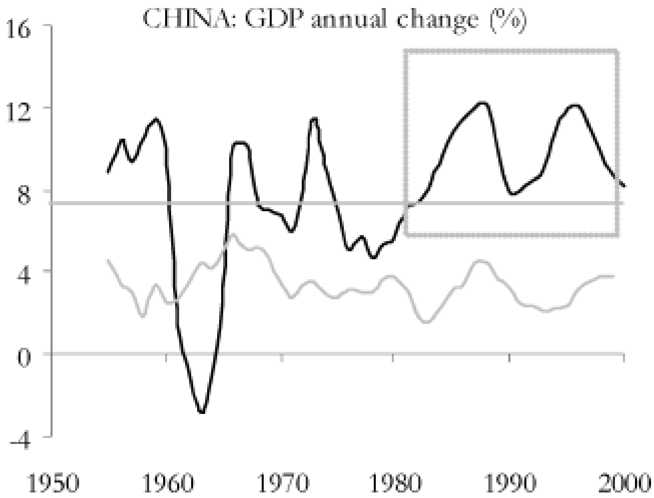

Figure 5: China's rapid growth pattern

a. Each economy had a rapid growth period with an average growth rate generally above 8% (there is the magic number!);

b. The rapid growth period ran for about 30 years;

c. The 20 year period of Japan and China are explained with their unique circumstances;

d. Their rapid growth period started at a different historical point and there was an end point for the rapid economic growth.

One of the circumstances for China was the fact the 50-year period only allowed a 20 year observation time for China. It was the expectation from the observed pattern that China would have another 10-12 years from 2000 to continue to have

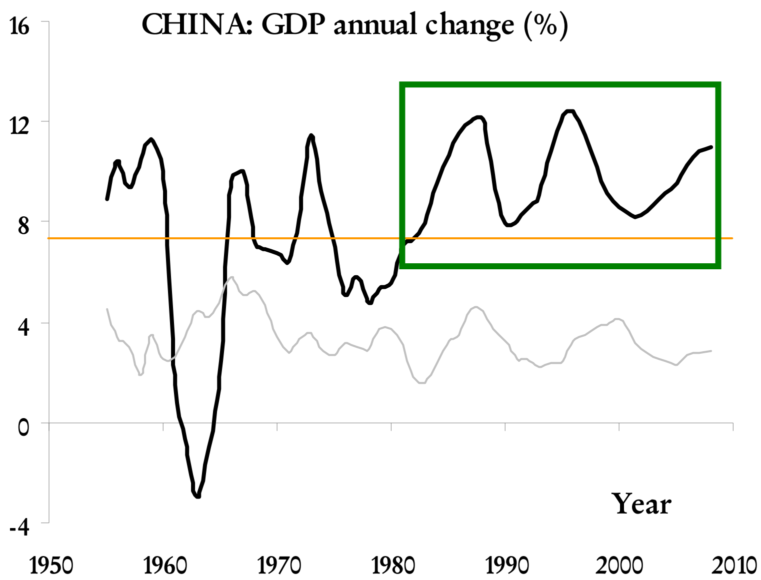

Figure 6: China's rapid growth pattern updated

rapid economic growth. 8 years have passed since then. We now have more evidence to test the model on China. I plotted the latest data from 2001 to 2008 to the original graphic as seen in Figure 6.

As we can see here, the general pattern of 30 year rapid growth stands well. The claim is particularly strong with the feared scenario that China's growth rate will move below the 8% line in the next few years.[4] The question here is whether China can have its rapid growth beyond 30 years and why. To answer this question, the underlying dynamics behind the 30 year pattern of rapid growth and how China fits into this needs to be understood.

2. Chinese and East Asia models Compared

The 30-year pattern of rapid growth, in my view, is not accidental. Research has identified, for example, that initial low-income levels may be responsible for speedy growth during a catch up period (Solow 1956, Abramovitz 1986, 1989). Indeed, all these five economies started their rapid growth period at very low levels of economic development except Japan, which was afflicted by war devastation. This in part might have contributed to its shorter period of rapid growth. However, the catch up theory may explain the historical span and timing of rapid growth, but not why rapid growth took place in the first place. Many countries were and perhaps still remain at a very low level of economic development.

The 30-year pattern of rapid growth in East Asia has more to do, in my view, with the underlying logic of the growth system itself. In my early work (Huang 2005 and 2008), I suggested there were four shared features of the historically dynamic model of rapid growth in East Asia:

First, the initial conditions required national coordinated efforts in manufacturing exports. These conditions included the challenge of national survival with the economy collapsing, political chaos and security threats; inflows of foreign capital and their repayment in hard currency; limited domestic purchasing power and resources, and international demands for national products.

Second, export concentration did not come naturally. It required (1) the separation of the domestic market from the international market, (2) reorganization of national production to provide competitiveness in international markets, and (3) redirecting of domestic economic forces and resources and growth activities to export industries.

[4] The World Bank in its latest China Quarterly Update on 17 March 2009 put China's growth rate in 2009 at 6.5%.

Third, reorganization and redirection happened at three levels. The government implemented policy and deployed "rents" under the general category of industrial policy to promote and direct growth activities and control distributional demands. Corporations, particularly small and medium sized businesses, managed themselves following the model featuring strong influence of the family structure and relations, giant corporate groups of institutionally rather than legally connected firms, and close access to and interaction with the government to ensure trust, efficiency and cost control. Individuals were integrated into the national campaign for growth and development, and developed with more compatible attitudes and values regarding money, profit and competition.

Fourth, all these added to the competitiveness of the national economy as a collaborative whole in the international market, not so much through conventional sources of competitiveness such as more capital, better technology and scientific management, but rather through institutional arrangements that developed from the reorganization and redirection. The emergent institutions for rapid growth therefore included a three-tier structure of state management that involved:

(1) The political leadership (a single dominant political party in most cases); a delegated and insulated bureaucracy; and intermediate industrial associations that bridged the government and the business community.

(2) Various arrangements and mechanisms that internalized costs of production: extended families that performed economic functions; Conglomerates that neutralized effects of business cycles within single companies; state-brokered management-labour relations that kept labour costs under control.

(3) A generally centripetal society where the boundaries between state and society/individual are blurring at the best; and

(4) Finally, a separation of the domestic and international market either through internal control and/or because of external barriers. This is where the government promotion for exports became possible. For all these, competitiveness of the East Asian economies was essentially institutional.

Fifth, the provision of institutions incurred costs. Government subsidies, corporation bail outs, and labour subordination only temporarily brought costs down. But these costs were either delayed, shared or accumulated somewhere else in the system. Over a longer period, these costs would eventually erode the capacity of the institutions to continue to function effectively. Moreover, effects of institutions can be isolated and monopolized by growth participants and their intended effects will gradually lose over time. This is where corruption and rent seeking activity became rampant. In the end, the overall institutional setting can no longer effectively direct or even generate growth activities.

Above are the essential properties of the growth model underlying the 30-year pattern of rapid growth. In each East Asian economy this rapid growth has come to an end one after another, not necessarily because of the rights or wrongs of the model, but because of the internal logic and hence the life cycle of the growth system itself. China, for much of its rapid growth, fitted roughly into this model. One can find all these five defining features in China's rapid growth. However, there have been some significant developments since the mid 1990s that have effectively allowed China to grow out of the model (rephrasing Barry Naughton's "growing out of the plan" Naughton 1995). The most profound of these developments has been the gradual integration of the domestic and international market.

The landmark development in that direction has been China's entry into the World Trade Organization in 2001, along with substantive presence and continual expansion of multinational corporate interests and operations in the Chinese economy. The goal underlying the new relationship is that there should be no boundary between the Chinese economy and the world economy. This effectively challenges one of the key foundations of the East Asian model: the separation of domestic and international markets. Without such a separation, or with the weakening of such a separation, there is no effective institutional support for government's efforts to promote a manufacturing export-led economy. The concept of "national" economy thus became problematic. Corporate identities and interests are ambiguous in relation to national and government interests with the growing extent of the mixture of multinational corporations in the national economy. Government's "industrial policy" faces a problem of "country of origin" in reserve.

Not only have the separation of domestic and international markets become problematic. There has also been the issue of the capacity of government in "governing" the market. Public Sector reforms in China have been profoundly influenced by the New Public Management movement of the 1990s and the larger ideological environment of Neoliberalism at the time. Decentralization, service delegation, transparency, accountability, and local autonomy have been the dominant themes for institutional reforms. The government is not exactly bureaucracy-centred, politically protected, and insulated with an unchallenged, exclusive command of national resources, as seen in the typical East Asian model. The early phase of China's rapid growth under the East Asian model benefited significantly from its socialist system of central planning, public ownership, and government's control of national economic activity, as well as the complete separation of its economy from the rest of the world. In the process of the reform or decline of the socialist system over the years, these features have gradually weakened and yielded to market forces, local government, corporate and other distributional interests, and a more open, transparent and competitive economic decision making process. Consequently, government's ability to govern the market is much more constrained than in the typical East Asian model.

Finally, the model of manufacturing exports as a primary source of growth has been increasingly challenged with intensifying competitiveness, uncertainty and fluctuations in the international market; as well as the global movement of capital uniquely towards China, and the growing potential of the domestic market in China itself as an alternative source of growth. The "Internal Demand Drive" appears to be not just temporary relief of the export congestion, but a significantly different model of growth from the typical East Asian model. The key to whether China can more effectively move away from the East Asian model than its fellow East Asian model economies is the potential of its domestic market.

In summary, China's growth model over the past 30 years has exhibited the essential features of the East Asian growth model. However, because of China's unique background of the socialist system and subsequent pro-market reforms, and the changing conditions in the world economic system, China has effectively been growing out of the model in the later period of its 30-year rapid growth. What is unclear here is the direction of China's future growth, which will inevitably continue to be affected by these conditions.

3. Exit Out of the Model and Future Chinese Growth

There have been very different or even contrasting "modes" of exit out of the East Asian growth model among the East Asian economies. I use here the word, "mode," to suggest that the ending of the rapid growth among the East Asian economies was neither intended as part of a strategic plan, nor happened randomly. Unlike many East Asian model advocates, I do see the ending of East Asian growth as the logical consequence of the maturing of the model. The difference here is the form and timing the East Asian growth ended in each of these economies. The ending in Japan in the early 1970s was largely the influence of global economic dynamics: the oil crisis in the 1970s, changes in global trade and financial regimes in response to the rise of the Japanese economy, as well as US pressures for structural changes in Japan. Moreover, Japan's pre-war levels of industrial development were much higher than those of its fellow East Asian countries. This made it relatively quicker for Japan to go through the rapid growth period. Overall, the ending in Japan was smooth and over a longer period.[5]

[5] Features of the East Asian model lingered on in Japan until the early 1990s: a single dominant political party, corporation-government relations, and bank-corporation grouping (see Pemple 1999 for discussion for regime shifts in Japan).

Taiwan, Singapore and Korea experienced, in my view, a standard ending of the 30 year East Asian growth – standard in the sense that their rapid growth all spanned around 30 years and ended as the logical maturing of the East Asian growth model. However, the ways they ended were different – due very much to the extent the emergent global dynamics could have an effect on their system and due to some of the unique conditions of each system. Taiwan and Singapore were on the smooth side. While rapid growth was no longer by the mid 1990s, their growth systems however were less exposed to the global swings of forces. As for South Korea, neoliberal reforms were introduced much earlier and its corporate operations and financing were much more internationalized. The Korean economy collapsed under the forces of the Asian economic crisis of the late 1990s, which constituted a "hard' ending of the model.

China has already been inching out of the East Asian model over the years and at the same time has been able to maintain rapid growth. The current global economic crisis has very similar effects on national economies. China in this sense is more in the category of Taiwan and Singapore a decade ago: it has reached the maturing point of East Asian Growth model and the global economic crisis is finally forcing China out of this model. But two unique conditions in China make it a challenge to argue whether rapid growth above 8% will end this year or next year and how China will look 5 years from now. First, as discussed earlier, China has been reforming not only its socialist system of 30 years ago, but more subtly its East Asian growth system in the past decade or so. If a substantive part of its East Asian growth system has been transformed and its rapid growth in the past decade has been achieved under the emergent system, it is possible that China can continue to produce this above-8%-growth rate under this new, evolving system. Second, the domestic market drive can provide new sources of growth in place of manufacturing exports. While the domestic market campaign looks more like a fiscal policy solution, over time it can generate structural changes and movements that can sustain rapid growth for a considerable time.

4. Conclusion

In conclusion, the East Asian economies experienced a rapid growth period of roughly 30 years in duration under a similar growth system. This growth system featured a separation of the domestic and international market, organization of national economic growth by government in partnership with corporations and other grow participants, with a concentration on manufacturing exports and competitiveness of its strategic products on the efficient reorganization of national production, and political and social support for the working of such a growth system.

China's rapid growth of the past 30 years has been largely the function of a similar growth model, though this growth model rose and functioned in China under some very different historical and institutional conditions. The mode and timing of the ending of its East Asian growth therefore will be determined not only by the internal logic of the East Asian growth model itself but also by the enabling conditions in the organization and operation of the Chinese economy.

The campaign to secure 8% growth rate this year is therefore slightly off the mark. Not only is this unnecessary, but it might also be counterproductive – particularly when this is done mainly through deficit based fiscal policy. We should allow the growth rate to be determined by economic fundamentals, rather than the other way around. Ironically, this is very much a key lesson of the East Asian growth model.

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