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CAN CHINA SET US AN EXAMPLE?

Introduction¹

Not long ago, on 28 July 2014 Hungary's prime minister Viktor Orbán delivered a speech at Tusnádfürdő (Băile Tușnad), Romania, entitled "What Will Follow Is a Work-based Society."² It drew much attention at home and abroad. I will consider here only a few sentences from its diversity of argument.

"There is a race on how to find the means of communal organization, the type of state, that will best be able to make a nation, a community, internationally competitive. This may explain... why the hot topic of consideration today is to understand the systems that are not Western, not liberal, not liberal democracies, perhaps not even democracies, and yet make nations successful. The stars according to international analyses today are Singapore, China, India, Russia, and Turkey."

It makes a strange list. What could be the features in all the countries cited that are absent in other, non-star countries? Let us look at *Table 1*. For long periods, even in and immediately after the crisis years, four of the five had far higher rates of GDP growth than many ostensibly declining Western countries, and higher also than Hungary had. For many, this justifies a "star" rating. But the odd country out is Russia, where the mean rate of GDP growth in 2009–13 was no faster than the United States' one. With the other attribute implied in the list, India is the odd one out. For unlike the other four, with their autocratic or dictatorial forms of government, India has been a parliamentary democracy ever since independence. No political force has been locked into power; all could be voted out, so that rival parties and groupings succeeded each other in government.

Table 1 Growth in "star" countries and some other countries during and after the recession

Country	Mean annual growth in 2009–13, %
India	6,9%
China	8,9%
Russia	1,1%
Singapore	5,3%
Turkey	3,9%
France	0,2%
Germany	0,7%
Portugal	-1,4%
Sweden	1,4%
United States	1,2%
Hungary	-0,9%

Sources: International Monetary Fund, World Economic Outlook Database, April 2014.

http://www.imf.org/external/pubs/ft/weo/2014/01/weodata/weorept.aspx?sy=2009&ey=2013&scsm=1&ssd=1&sort=country&ds=%2C&br=1&pr1.x=32&pr1.y=3&c=924%2C182%2C922%2C576%2C132%2C134%2C144%2C944%2C534%2C186%2C111&s=NGDP_RPCH&grp=0&a. Retrieved: August 12, 2014.

¹ The article appeared in the 2014 edition of the bi-annual Social Report series of the Hungarian Társi Social Research Institute. See: János Kornai: Példaképünk: Kína? in: Kolosi, Tamás - István György Tóth (eds, 2014): *Társadalmi riport 2014*. Budapest: Társi. pp 603-616. A somewhat shortened version in Hungarian was published in the weekly *Élet és Irodalom*, August 29, 2014 (pp. 3-4). My thanks are due to Brian McLean for his excellent translation. Ádám Kerényi contributed to assembling the statistical materials for this paper. I am grateful to him for his attentive, effective and devoted work.

² The section of the speech quoted was taken from the version on the government Internet site.

To argue this fully would mean analyzing the development in all five countries. I would like, for reasons of space, to confine myself to one: China. This clearly shows both distinguishing marks: very rapid growth and dictatorial government.

Here several questions arise:

What explains China’s rapid rate of growth?

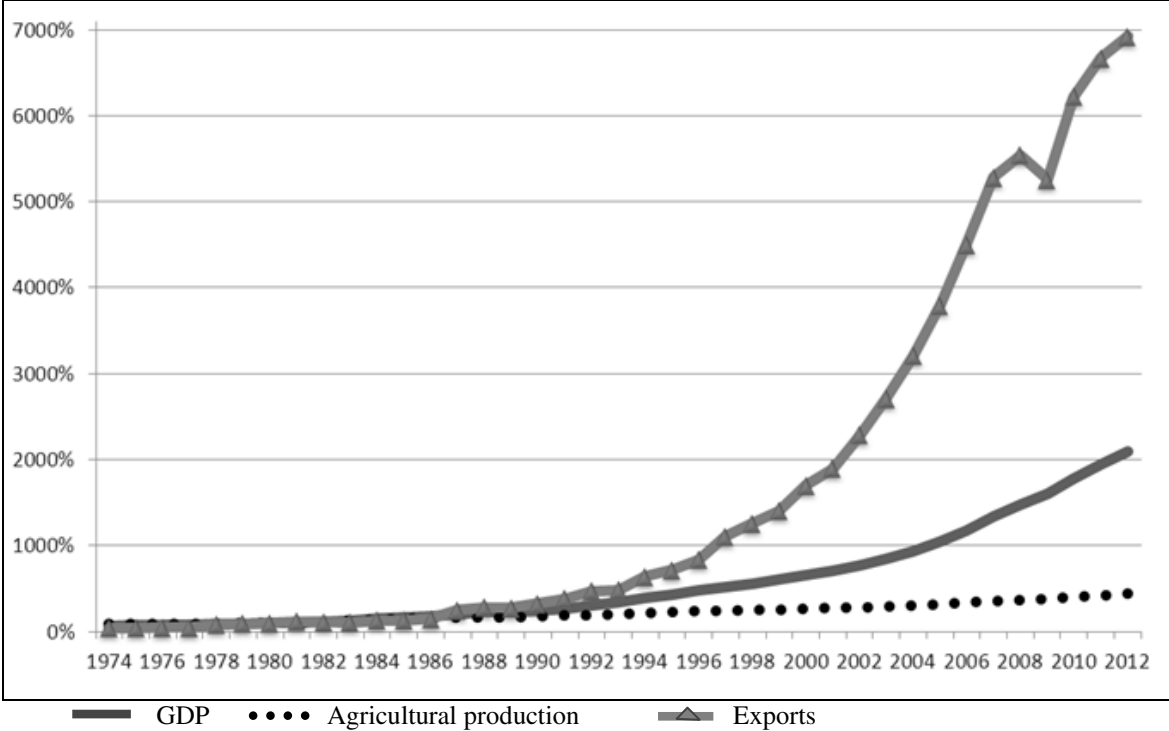
Can Hungary follow China’s example?

If it can, is it worth it? Would it benefit Hungary to follow China’s example?

China’s development path – the rapid-growth period

The death of Mao Zedong in 1976 ended a ghastly period of Chinese history, in which the oppression was particularly savage, even compared with other socialist countries. The inhabitants were weighed down by poverty, famine, and haphazard economic policy. The power struggles of the ensuing transition years gave way in 1981 to reform of the system, masterminded by Deng Xiaoping, after which the rate of production growth built up at tempestuous speed. (See the GDP curve in *Figures 1 and 2.*)

Figure 1 Growth of the Chinese economy In per cent, 1980 = 100



Note: Although the reform processes began before 1980, their effects made their appearance in that year. This is seen clearly in Figure 2, which magnifies the lower left section of this figure. That is why 1980 was chosen as the base year.

The sector represented in the lowest curve covers the sub-sectors of hunting, forestry and fisheries as well as agriculture in the narrow sense.

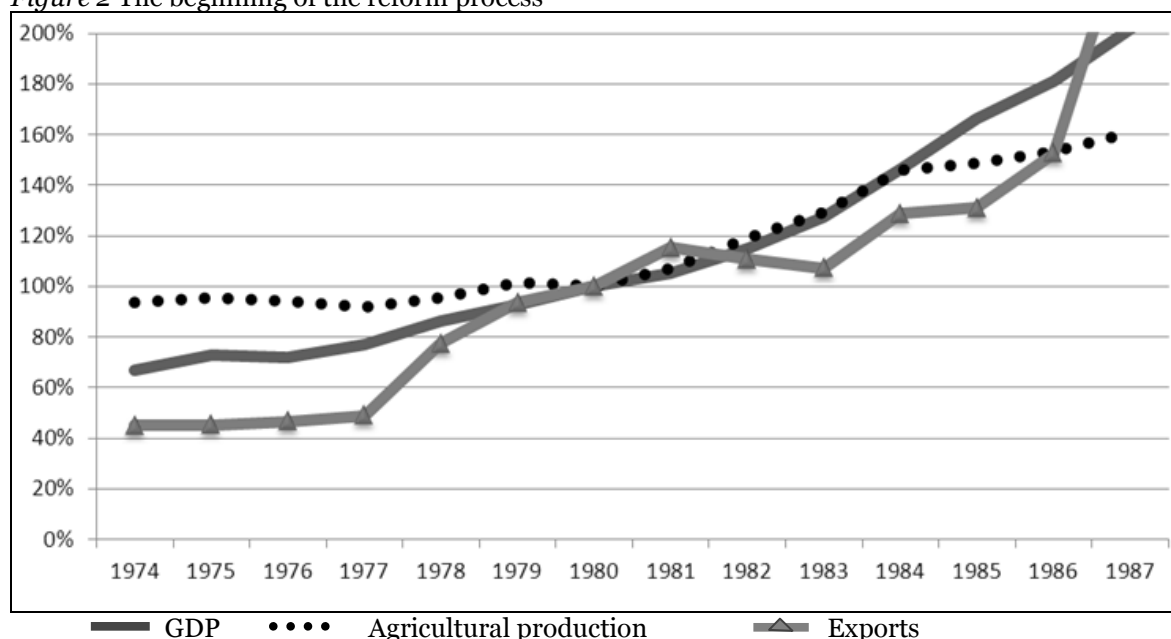
The absolute figures from which the indices were calculated were measured in the source in USD at unchanged 2005 prices.

Source: UN National Accounts Main Aggregates database <http://unstats.un.org/unsd/snaama/dnlList.asp> Retrieved: August 12, 2014.

The term “reform” covered a number of processes.

1. A very sudden and deep transformation occurred in agriculture. Communes and collective farming gave way to private farming, which freed huge forces that boosted agricultural production. (See the agriculture curve in *Figures 1 and 2.*)
2. The previous curbs on private enterprise were removed. New private firms appeared on a mass scale in all sectors of the economy.

Figure 2 The beginning of the reform process



Note: The figure “magnifies” the lower left section of Figure 1, for the period 1974–87.
 Source: See the source for Figure 1.

3. There appeared and very rapidly spread a new type of firm (known as a local enterprise) that rested on a specific combination of municipal and private ownership.
 4. The Mao period’s inward-looking exclusion from the West gave way to one of “opening up.” Export volume shot up. (See the exports curve in *Figures 1* and *2*.)
 5. China not only permitted, but positively invited in foreign investors. Foreign capital flowed forcefully into the country.
 6. China sought to learn from the developed countries. The desire for knowledge took numerous forms. For instance, tens of thousands of students were sent to study at the best universities in the West, and a high proportion returned after graduation.
 7. One accompaniment to the changes described in points 5 and 6 was rapid flow of modern technology into China. The country became increasingly incorporated into the world network of modern information and communication-based societies.
- It should be noted that changes 1–7 are not “unorthodox” in character. These were just the reforms recommended by the IMF and the World Bank and by foreign economists consulted by the Chinese leadership. Let us turn now to the growth factors that were *not* among the standard Western recommendations.
8. China kept a tight hold on wages and so on household consumption. Though consumption grew, its growth fell far behind that of production. Household-sector consumption as a proportion of GDP was low and fell further. (See *Table 2, line 2*.) Inequality of income distribution increased to a dramatic extent.
 9. The proportion of investment in the utilization of GDP was startlingly high. (See *Table 2, line 1*.) This obviously tied in closely with China’s very high rate of saving. There are few parallels to this distribution in the utilization of national income in the history of the world economy. (I will return to this.) Perhaps the only similar case was with the Stalinist industrialization under the first Soviet five-year plan. There is no Western country where the public would have borne with such a constraint on its share in the growth of production.

The economic-growth attributes listed grew out of the *institutional changes* that occurred in the period. These were inconsistent in many respects. There arose the *economic institutions* required for a market economy based on private ownership. These gave half to three-quarter (but not full or consistent) protection to private property and assertion of private

contract. On the other hand, there was still a weighty and influential sector in state ownership. A large number of state-owned enterprises are maintained artificially by state subsidies, cheap bank loans, and by other instruments of the “soft budget constraint” syndrome, despite serious trading losses.

Table 2 China’s GDP utilization

	1974	1975	1976	2007	2008	2009	2010	2011	2012
Gross capital formation	40,9%	42,1%	39,9%	42,0%	42,4%	46,3%	46,9%	47,1%	47,4%
Household consumption	54,8%	52,4%	55,2%	36,7%	36,3%	36,5%	35,8%	36,1%	36,3%

Note: The GDP data that form the starting point of the calculation agree with the data based on which the indices shown in Table 1 were calculated.

Source: UN National Accounts Main Aggregates database.

<http://unstats.un.org/unsd/snaama/dnlList.asp>. Retrieved: August 12, 2014.

With *political* institutions, the reforms did not break the one-party system, the political monopoly of the communist party. The form of government remained a dictatorship, but the brutal cruelty of the Mao period eased somewhat. Greater scope was given for debate, and official party ideology was imposed more lightly on education and intellectual activity. The party’s composition changed gradually from that of the Stalinist/Maoist communist party. Within it there was increasing collusion between the political apparatchiks and the social groups of the new capitalist owners and technocratic managers.

China’s development path – the period of deceleration

Production in China grew for a long time at a record rate, but it emerged that this breakneck speed could not be kept up forever. Looking at Table 3, GDP increased by 15 per cent in 1984, then slackened somewhat, then the growth rate jumped again to 14 per cent in 2007. Thereafter there has been a clear tendency of deceleration. There were two years in which the growth rate of the record 1984 was halved.

The most important event in the period after the reform began occurred in the political sphere, not the economic. The effect of loosening oppression in the 1980s was not to produce satisfaction or a sense of gratitude to the rulers of the system, but to awaken a desire for freedom. The scattered protest movements built up strength, culminating in the vast mass protests of 1989, when Tiananmen Square in the center of the capital was occupied for several days by students and other citizens demanding human rights, freedom, and an end to corruption. This civil disobedience was brought to a brutal and bloody conclusion by military force, on the orders of Deng Xiaoping. Then came reprisals and the dictatorship hardened again, although the regime never returned to the crazed brutality of the Mao period.

It is hard to say whether there is a direct causal link between the Tiananmen Square episode, which began so eagerly and ended so bloodily, and the steady slowing of economic growth. A sufficient explanation of the latter can be found in the change in economic conditions.

On a theoretical level growth in the socialist countries divides into two phases. The first, *extensive phase* is marked by an ample supply of free labor, to which the state provides the capital required for production. Production can grow rapidly because rising amounts of capital are combined with rising amounts of work, but this cannot be continued indefinitely. Growth increasingly encounters bottlenecks: appropriately qualified labor and/or accessible sources of investment are not available in the places desired. The growth gradually passes into its *intensive phase*, at which production growth can be achieved mainly (later perhaps

exclusively) by raising *productivity*. In the intensive phase growth is necessarily slower than in the extensive.

Table 3 China's growth rate as a percentage of the data

	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998
GDP growth rate	15.2	13.5	8.8	11.6	11.3	4.1	3.8	9.2	14.2	14.0	13.1	10.9	10.0	9.3	7.8
Agriculture growth rate	12.9	1.9	3.3	4.7	2.5	3.1	7.3	2.4	4.7	4.7	4.0	5.0	5.1	3.5	3.5
Export growth rate	20.1	1.9	16.3	62.4	13.4	-2.1	18.0	17.9	22.4	3.7	32.1	11.3	17.4	32.1	14.1
	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
GDP growth rate	7.6	8.4	8.3	9.1	10.0	10.1	11.3	12.7	14.2	9.6	9.2	10.4	9.3	7.7	7.7
Agriculture growth rate	2.8	2.4	2.8	2.9	2.5	6.3	5.2	5.0	3.7	5.4	4.2	4.3	4.3	4.5	n.d.
Export growth rate	11.1	21.4	11.3	20.8	18.4	18.5	18.2	18.5	17.4	4.9	-5.1	18.3	7.3	3.7	n.d.

Note: The figures in the table show the difference in the index between the given year and the previous year as a proportion of the value for previous year, i. e. the rate of growth in percent.

There are no miracles. China too is undergoing such a gradual switch of phases. Ever greater weight must be given to increasing productivity, which makes many demands on the quality of capital and labor. Capital-intensive (and so expensive) investments are needed over a widening sphere. Ever more skilled labor is called for, including highly qualified intellectuals, without whom there cannot be technical development or innovation. People must be better paid. Specialist training involves developing education and research. Better living conditions are required. More attention needs paying to workforce health. Establishment of a welfare state, at least on a modest level, cannot be postponed any longer.

As a result of all these developments, wages must be raised faster, and on top of wage costs come taxes and levies, to cover the mounting state welfare expenses (on education, health, and pensions). One result is that Chinese goods intended for export will be more costly and their competitiveness will fall.

Falling export capabilities, or the eventual prospect of them, increases the temptation to turn inward.

This line of argument has been so far deducted from the internal regularities of the economy, that is, the inevitable change in the ratio of consumption to investment. But the change is not all due to blind internal compulsions: humans have a say too. Protests against local grievances become commoner, strikes occur more frequently. Many small local movements are pacified by bribes to the organizers or harsh police action. Nevertheless, there is perceptible pressure from a public demanding a bigger share in the gains from growth.

The country's leadership, in the rush to expand, failed to address damage to the environment. The warnings are no longer confined to foreign observers. Action against air pollution and other environmental problems has become inescapable. This draws further resources off from investment that could contribute instantly and directly to GDP growth.

China has a robust economy but cracks are appearing in its vast edifice. Much budget expenditure goes into the support of loss-making state owned enterprises. A large number of SOEs and NGOs are heavily indebted. As for the bank sector, it suffers under a weight of non-performing loans.

Attempts are made to curb the slowdown or even return to acceleration by raising the investment proportion in the utilization of GDP, which increased to 47 per cent in 2012. This is a record in the economic history of the world! One of every two units of production

(measured in value terms) is being invested. So the proportion of household consumption has also reached a negative world record: it is only 36 per cent. Never has so little (just a third of the GDP generated) been consumed by households. (See *Table 2*.) The tensions caused by this grave internal conflict in the Chinese economy – a contributor to the slowdown – seem to be worsening, not easing.

The tensions can be sensed in the mood of the public. Though one fortunate result of the huge growth has been to save hundreds of millions from direst poverty, close to famine, it has also brought vast income inequalities between the opulent uppermost stratum and the hundreds of millions of very poor.

One response to discontent has been “toughening up:” proliferating repressive measures (police brutality, intimidation with harsh sentences), perceptible especially in the last year or two. The other is to distract people by stirring up underlying Chinese nationalism.

What will China’s future be?

Who can be sure of the future? There is no excluding the possibility of the leadership effecting correctives that “let off steam,” as from a boiler edging toward a blow-out. Real wages are raised, elements of a welfare state installed one by one, at least to a level proportionate to China’s development, and growth-retarding effects coolly acknowledged.

Social tensions would be eased by the changes mentioned and by measures that redistribute contributory burdens and state services in a way that reduces income inequality. This would allow mitigation of repression, and collectively might lead sooner or later to democratization of the political institutions.

Many would like to see China take this route – not just most foreign politicians and China experts, but the internal opposition to the present Chinese system: enlightened teachers and students, writers, artists, journalists, and former or even present party functionaries.

Of course, events may go another way. The leaders may try to squeeze faster growth out of the economy by curbing wages and state welfare spending. Tensions and protests may be met by stronger retaliation. If conditions worsen so much that it is necessary, according to those in power, for “the nation to fall in line,” they may set out to incite nationalism or even try a military adventure.

There is no telling how the dilemma of turning outward or turning inward will be resolved. If the latter predominates, it could mean looser ties with the West, with many economic effects and a brake on China’s dynamic rate of technical advance.

The economic results are unpredictable. All that can be foreseen is that “hardening up” cannot bring a lasting return to the startling 15 per cent growth rates of the first period. Nor is it sure that the present 7–8 per cent growth rate will stabilize for a long period and halt a further slowdown.

Can Hungary follow China’s example?

In a word: *no*. But I would like to say a little more. I have outlined the attributes of China’s growth precisely so that I can justify my negative answer in more detail.

There is no assigning a future line of development to a country at will, any more than history places before the “central will” a bill of fare with courses taken – Singapore’s and Switzerland’s, China’s and Japan’s, the United States’ and Nigeria’s, Sweden’s and North Korea’s – saying, “Here they are: choose which you want.” A country’s state at a given time, along with its historical route to the present, considerably narrows the set of routes it can follow, although the route to be followed is not determined by that either. There remains for decision-makers significant freedom of choice, and the historical responsibility that goes with it.

Let us compare the attributes of China and Hungary from this point of view:

- China is a vast country. Many of its provinces are maritime. It spans a number of climatic zones, which allows a wide range of agricultural goods to be produced. It has several rich natural resources. Leaving aside whether it would benefit China to turn inward, it is

certainly true that it would be *capable* of so doing to a large extent. Inland Hungary, poor in natural resources, would be *incapable* of isolating itself in that way. Openness is thrust upon it by its natural and geographical features.

- Hungary's investment ratio is about one third of China's, and it could not rise to China's level even if the government wanted. For that depends only partly on government will. To a large extent it depends on citizens, individuals, households, families, private firms, and at least partly on autonomous bodies and smaller communities. The state can attempt to influence their decisions with rhetoric and financial incentives, but such a decentralized process does not operate on a state command. It depends on separate decision-makers, who save and invest, on how much the trust in the future and in the safety of their investments and wealth.
- Hungary's competitiveness is not improving. Would it be possible to improve it radically by pushing Hungarian wages down to Chinese levels? Should state spending on health care, education and pensions (in per cent, per capita) be depressed likewise? Here I am not asking whether this would be desirable according to some system of values. I am just talking about feasibility. Would it be *possible* to follow China's example? It can definitely be said it would *not*.
- An important criterion is the so-called economies of scale. Hungary has a population the size of some larger Chinese city. China has a domestic market of 1.5 billion, offering enormous scope for saving and profitability to Chinese and foreign investors alike. That scope is not available to the Hungarian central will.

Summary of the positive analysis

The lines from the Tusnádfürdő (Băile Tușnad) speech do not present a clear cause-and-effect relationship, just point to two simultaneous phenomena: "star" economic performance – in the sense of very rapid GDP growth – and a non-democratic, autocratic/dictatorial form of government. Nonetheless, mentioning them together does create an impression of causality, at least in the narrower sense of autocracy/dictatorship being a necessary condition for such growth. To put it precisely, the purported relation is: autocracy/dictatorship → rapid growth.

This contention will not stand. It is not true under any conditions. I do not even try a general refutation of it in this discussion; limitations of the length of the paper are sufficient reason to prevent me from doing so. I do not attempt a refusal with real examples from all the five countries cited in the speech. I hope that I can back my refutation referring to the case of China: the causal relations are far more complex than the assertion cited above. On the one hand, the "cause" side of the relation includes a large number of explanatory factors, not just one or two. On the other, the "consequence" side does not include a single result – a high rate of GDP growth – but many, ranging from livelihood developments through income distribution to environmental damage.³ The two sides of the proposition are interactive, i.e. mutually influence each other. Repression, infringement of human rights, can be placed on the "cause" side (for it is used in the institutional system to curb expression of discontent), but it belongs on the "consequences" side as well, because it is part of the embittering side-effects of the forced acceleration of growth.

Let me also stress that it is inadequate to take a snapshot of the relation between the system of political and economic institutions and economic growth. There must be an understanding of the dynamics of the processes: which speeds up or slows down when, and why.

Would it be desirable for Hungary to follow China's example?

Let us discount for a moment one of the conclusions from the earlier line of thought – that it is *not possible* for Hungary to follow China's example. Were it not possible in total or in its main traits, there could still be many parts of it that might be adopted.

³ Economists and economic statisticians have underlined for decades that a distorted, misleading picture of economic development is gained by focusing on the single indicator of GDP growth rate.

I am not ducking the question; this is no value-free, “purely economic” problem. The response depends on the respondent’s value system. Firm believers in democracy (like me) will answer the question in the subtitle with a decided *no*. Democracy – and the respect for human rights and legal security inseparable from it – is not just one of many values. It is not just a good that can be traded, at least in part, for other values like faster growth or greater prosperity.

Let me express that in the language of economic theory. Some talk of a trade-off between democracy, human rights, and legal security on one side and growth and related material welfare on the other. To them it is worth putting a few excitable people away or if need be shooting into protesting crowds, if that opens the way to increasing the growth rate by one or two percentage points. Here I have stated in economists’ jargon and in plain speech the idea about China’s growth on many people’s minds: “So there is no democracy in China and human rights are routinely trampled on, which is despicable, but a price worth paying now and in the future for a giddy speed of growth in production which will spare many people penury in the end and improve the population’s material welfare.”

That trade-off is repugnant to democracy’s committed believers. Democracy, respect for human rights, and legal security cannot be sacrificed on the altar of other values.⁴ Earlier I rejected the formula “autocracy/dictatorship → rapid growth” in the frame of a positive analysis, for not explaining China’s growth adequately. Now I will turn against it again, this time in a normative analysis, because in my set of values democracy must not be forsaken even if the result would be to speed up growth.

My line of argument will raise at least as many new questions in readers’ minds as it tries to resolve. Is there a line of development in which the governmental form is liberal democracy and lasting growth and the associated material welfare can be maintained? Can Hungary follow this route? If I were to try to answer these questions I would far exceed the maximum length allowed me by the editors, which I have already outstripped in any case.

Is there sense in discussing this?

Not for sure. At a scientific conference, one speaker will express his or her point of view, backing it with data and logical arguments, while the other debates with him/her on a basis of *rational reasoning*. But the Tusnádfürdő speech was not given at a scientific conference.

I am no cloistered scholar. I have had first-hand experience of life and read a great deal about the theory of rational decision-making and the psychology of political activity.

There is no convincing fanatics with rational arguments.

A politician considering basic issues does not choose between alternative pieces of advice. He/she has already a position suggested by his/her own convictions and selects an adviser who is ready to deliver advice supporting exactly that position. An adviser who is prepared to give advice which he/she likes, and who is willing to take up the cause of the politician.

Elections are not won, power is not obtained by the force of thought.

And yet, perhaps there may be sense in such discussions as this article offers. They may give a little help to those open to rational argument in finding their way through the complex interrelations between a form of government and economic growth.

⁴ This view can be described in the language of decision theory, using the first person plural, as follows. We are led in political and decision-making judgments by a “lexicographic” preference ordering. Criterion No. 1: we prefer democracy to non-democracy or all variants of tyranny. Only when this criterion is met can No. 2, No. 3, etc. ensue. Of course, we prefer faster growth to slow, a fairer division of income to a less equitable one, but only if the democracy criterion is met. To express it more strictly calls for a dynamic approach: we prefer the processes that promote the building of democracy to those that promote the building of autocracy/dictatorship. Of course, a full exposition of this argument will not fit into the footnote of an article.