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BOOK REVIEW: 'How China Became Capitalist'

By Alberto Mingardi - Thursday, October 11, 2012

HOW CHINA BECAME CAPITALIST
By Ronald Coase and Ning Wang
Palgrave Macmillan, $100, 272 pages

A new book by Ronald Coase, age 101, is an event in itself. Mr. Coase, the 1991 Nobel laureate in economics, revolutionized the field by challenging conventional wisdom regarding the nature of business firms and how so-called public goods can be provided. One of his main contributions is the concept of "transaction costs," which are the costs individuals incur in making an economic exchange. In striking contrast to most contemporary economists, Mr. Coase did not choose the approach of complicated model-making, nor did he find delight in crunching numbers. Instead, Mr. Coase wanted to be a scholar of reality. He consistently studied markets for what they are, rather than for what they might be. In this sense, he is perhaps the most distinguished contemporary disciple of Adam Smith.

Mr. Coase was not among the most prolific economists of the 20th century — but he was certainly one of the most influential. His new book, coauthored with Ning Wang, assistant professor at Arizona State University, investigates the capitalist awakening of the Chinese economy. To understand "How China Became Capitalist," Mr. Coase and Mr. Wang take a deep look into the Chinese mind. The authors maintain that "China has always been a land of commerce and private entrepreneurship" but embraced the institutions of a modern capitalist economy only "after one century and a half of self-doubt and self-denial."

Mr. Coase and Mr. Wang emphasize how institutional change is not merely the outcome of the interplay of different interests. A common vignette of pro-market reforms in Deng China portrays a ruling class desperately seeking to stay afloat, even at the price of watering down its own ideology. Those who subscribe to this picture argue that such a drift toward pragmatism is best epitomized by Deng Xiaoping quoting an old Sichuan saying, "It doesn't matter if a cat is black or white, so long as it catches mice."

In this serious attempt to understand how market institutions are breaking through in China lie the hard facts of geography and demography. China was simply too big to be run as a centralized economy. "Centralization did exist once in Mao's China, but only briefly." However, the central government could never really cope with the size of the country, the wide variation in culture and customs and the difficulty in processing information at the needed speed. In a way, Chinese socialism has long been struggling with the fact that, as highlighted by Mao, the territory was so vast and the population was so large that China could not "follow the example of the Soviet Union in concentrating everything in the hands of the central authorities."

During the 1980s, the Chinese economy was transformed by "four marginal forces: private farming, township and village enterprises, individual entrepreneurship and the Special Economic Zones." These played a pivotal role in opening up China to the global market economy. Shenzen, in the southeast corner of the Guangdong province, was a poor town before becoming the frontline of China's economic integration. "China would probably have stayed on the intended path to socialism were it not for the marginal revolutions that reintroduced private entrepreneurship to the economy."

The change was as much institutional as cultural. On the institutional side, private ownership was restored. On the cultural side, the Chinese political discourse rediscovered the role of thrift, self-reliance and experimentation. Entrepreneurship requires risk-taking. The future is uncertain, therefore, the entrepreneur bets on his forecasts and intuitions.

It would be disingenuous to contrast Chinese "marginal revolutions" with the kind of "shock therapy" that made for a successful transition out of communism in places like Poland and the Czech Republic. However, these Chinese "marginal revolutions" were certainly no less "shocking" than "shock therapy" in Eastern Europe. Consider the opening of the stock exchange in Shanghai in 1990. One of the 20th century's greatest economists, Ludwig von Mises, remarked that there cannot be genuine private ownership of capital without a stock market and "there cannot be socialism if such a market is allowed to exist."

The authors do not assume that China has turned into a liberal democracy, nor they do naively believe that its economy can be considered a genuinely free one. They acknowledge the oligarchic nature of Chinese politics and point to a still depressed and censored "market for ideas" as a tragedy in itself and an obstacle to future development.

As the authors note, it's a work in progress. "Capitalism with Chinese characteristics is very much like traffic in Chinese cities, chaotic and intimidating for many Western tourists. Yet Chinese roads deliver more goods and transport more passengers than those in any other country." As China is sure to become a hotly debated focal point in the presidential election, this book, with its emphasis on markets and history, becomes of paramount importance.

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