A Tale of Two Capitalisms

democracyjournal.org/magazine/56/a-tale-of-two-capitalisms

Arthur Goldhammer, *Democracy* n° 56, Spring 2020

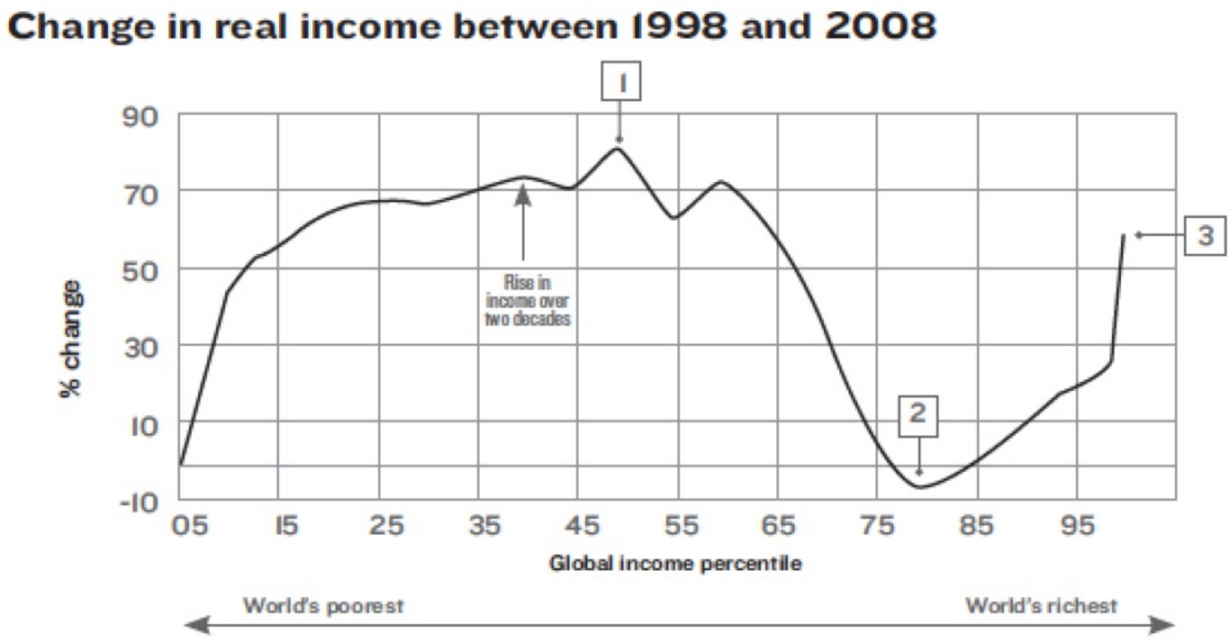
Hongyuan Outdoor Mall, in Shanghai. Photo by ctny, CC 3.0

Capitalism Alone: The Future of the System that Rules the World by Branko Milanovic • Harvard University Press • 2019 • 304 pages • $29.95

In certain quarters of the United States it is taken for granted nowadays that capitalism has failed or at the very least fallen into desperate crisis, which will soon result in its replacement by "democratic socialism." Branko Milanovic, who grew up under Tito's brand of socialism in Yugoslavia, is impervious to such romantic fantasies. For him, capitalism is without question "the system that rules the world." By this he means simply "that the entire globe now operates according to the same economic principle — production organized for profit using legally free wage labor and mostly privately owned capital, with decentralized coordination." These criteria are met not only by what used to be called the "advanced industrial economies" of the West (plus Japan) but also by China, India, Russia, Brazil, Vietnam, and many other countries, which, taken together, account for the lion's share of global production. This, says Milanovic, an economist who holds the Maddison Chair at the University of Groningen in the Netherlands in addition to being a senior scholar at LIS and former head of research at the World Bank, is a situation "without historical precedent."

It would not have been possible to make this assertion before 1989 and the collapse of communism, which presented itself as a viable alternative to the capitalist organization of production. But if the economic system that has emerged since 1989 in much of the non-Western world can be described as capitalist, it is not capitalist in the same way as the West. For Milanovic, the cardinal fact about today's all-conquering capitalism is that it comes in two distinct forms: "liberal meritocratic" in the West, primarily the United States, and "state-led political or authoritarian" in Asia, primarily in China. Both are "capitalist" in the spirit of the definition set forth above, but in other respects they differ sharply. And crucially, both differ from the capitalism that prevailed in the West from the end of World War II until the fall of communism, which the author calls "social-democratic capitalism." He uses the term broadly to include not just the authentic social democracies of Europe but also the United States of the New Deal and Great Society, which similarly expanded the middle class and reduced inequality. But social-democratic capitalism has been in retreat everywhere for several decades now, with consequences for the distribution of wealth and income, as well as for democracy itself, that cannot be ignored.

Milanovic is best-known for his work on inequality, with a particular focus on *global* inequality—that is, inequality between countries and not just within countries. *Global Inequality* is in fact the title of one of his earlier books as well as of his consistently thought-provoking and compulsively readable blog. His pioneering work on the global income distribution is summed up in what has come to be known as the "elephant curve": If one plots the increase in real income over the past few decades versus percentile in the global income distribution, one ends up with a curve that resembles an elephant with its trunk raised.



Source: Branko Milanovic, Global Inequality: A New Approach for the Age of Globalization

What the graph shows is that real income increased significantly for all groups up to roughly the 70th percentile as well as for those at the very top of the distribution, especially the top 1 percent. The winners were thus the ultra rich in the West and the new middle classes in countries such as China, India, and Brazil. But income actually decreased for those who fell between the 75th and 85th percentile worldwide, which, when translated into sociological rather than economic terms, happens to correspond to the working and middle classes of the advanced industrial countries.

The elephant curve thus illustrates the widening income gap in wealthy countries between the working and middle classes, on the one hand, and those at the top of the income distribution on the other—the same gap highlighted by other researchers such as Emmanuel Saez and Thomas Piketty (full disclosure: the reviewer is the translator of several of Piketty's books into English). But it also shows something more encouraging: that the lot of many people living in the less developed world has begun to improve dramatically. In this momentous convergence of rich and poor, China of course led the way with its prodigious growth between 1980 and today, but other formerly poor countries such as Vietnam, India, and Brazil have also moved up in the global league tables. Since 1980, the global Gini coefficient has decreased from an all-time high of almost .75 to .65 (a higher Gini indicates greater inequality). China's economic revolution initiated this decrease in inequality, and rapid growth in other Asian economies continues to whittle away at the East-West gap. While inequality *within* each of the affected countries has increased, *global* inequality has decreased because formerly underdeveloped economies have outpaced the West in growth for several decades now. Billions of people no longer live in abject poverty, even if per capita income in Asia remains well below that of the West.

These dramatic political-economic changes form the backdrop for *Capitalism Alone*. The book sets out to answer the following questions: Why has inequality increased so much within countries? What has allowed the Asian economies to grow so rapidly that global inequality has decreased? And how stable is a global capitalist order comprising two distinct forms of capitalism competing not only for markets and resources but also for ideological preeminence? The Cold War between communism and capitalism is over, but a new conflict between liberal meritocratic capitalism and political state-led capitalism may be on the verge of taking its place.

To answer these questions, Milanovic dons his social theorist hat. These pages are littered with quotes from Adam Smith, Karl Marx, and Max Weber. The very categories within which the argument is framed are proposed as Weberian "ideal types." Indeed, "liberal meritocratic capitalism" as treated in this book is an abstraction that exactly mirrors conditions in the United States today, while state-led "political capitalism" is modeled entirely on China. The author is not overly concerned with the validity of these abstractions, and a critic might well ask how much China's state capitalist society has in common with Brazil or Indonesia or even Vietnam, or whether America really is the "ideal type" of Western capitalism. The total output of the European Union is greater than that of the United States, after all, and the "varieties of capitalism" that contribute to Europe's output have been much studied since the pioneering work of Peter Hall, David Soskice, and their collaborators, published some two decades ago but not mentioned here. In other words, Milanovic's ideal types mask a multitude of differences.

Capitalism has not so much satisfied human needs as it has altered them to accommodate the needs of capitalism.

These are quibbles, however. The questions that Milanovic raises are good ones, and if the recourse to ideal types narrowly modeled on the United States and China is a ruthless simplification, it is nevertheless a justifiable one, and perhaps necessary to extract a usable signal from the ambient noise. What do we see when we look at liberal meritocratic capitalism through Milanovic's magnifying lens? First, a society in which capital's share of national income is rising compared to labor's share. Milanovic agrees with Nobel laureate economist Robert Solow that this is due largely to "a change in the relative bargaining power of labor and capital." Second, while capital ownership remains highly concentrated, as it has been throughout the history of capitalism, those who enjoy high income from capital are today also likely to enjoy high income from their labor—a marked change from capitalism's past, in which the wealthy did not work. Part of the reason for this change is that wealth affords access to more expensive and "better" education, and elite educational credentials afford access to more remunerative jobs. Individuals increasingly seek mates of similar educational attainment—what economists unromantically call "assortative mating"— and this coupling of high income with high income increases inequality between families even more.

The rich also tend to earn higher returns on their assets than the less wealthy, and they pass on more of what they accumulate during their lifetimes to their offspring. The upshot of all this is that inequality within liberal meritocratic society increases, social mobility decreases, and the wealthy increasingly exert control over the state. Those who own the most capital, attend the "best" schools, and earn the most from their jobs begin to think of themselves as *meriting* their good fortune by virtue of their superior talents and ideas. What was once a democracy comes more and more to resemble an oligarchy, which justifies its class structure through the ideology of *meritocracy*—that is, the belief that the rich are rich because they are also the best, brightest, and most industrious. Yet the real source of the political influence of the wealthy is not that they have better ideas about how to organize society but, quite simply, that they have more to spend on acquiring power: "Where does the influence of the rich come from?" Milanovic asks. "The answer is quite clear: through the funding of political parties and electoral campaigns. . . . In fact, the distribution of political contributions is even more concentrated than the distribution of wealth."

All this is reasonably familiar from any number of recent jeremiads lamenting rampant inequality and democracy's seeming inability to tame what used to be called The Money Power. Paradoxically, capitalism on this account can be said to have achieved communism's goal of abetting the withering away of the state, which has been reduced, in Milanovic's view, to "a committee for managing the common affairs of the whole bourgeoisie" (to borrow a phrase from Marx and Engels).

By contrast, in "state-led political, or authoritarian capitalism," the author's other "ideal type," the state's role is paramount. Its purpose (echoing Weber) is "the use of political power to achieve economic gains," as the Chinese state has done with such spectacular success since 1980. Its primary characteristic is the "highly efficient and technocratically savvy bureaucracy" that runs the system. Technocrats are free to interfere with the operation of the market in the national interest.

The bureaucracy is also "clearly the primary beneficiary of the system." It is legitimate only if it succeeds in producing economic growth, hence its recruits must be competent. In the absence of any binding rule of law, they enjoy considerable discretion, as they must in order to act decisively when necessary in order to deliver on the promise of uninterrupted growth. "Zones of lawlessness" are therefore an integral part of the system, despite the fact that the essence of bureaucracy is to bind individual behavior by rules. Thus "corruption is endemic to political capitalism." It must nevertheless be kept in check, lest the legitimacy of the system be undermined. This accounts for the periodic spectacular crackdowns on corrupt officials.

This description of political capitalism does not explain its success, however. What does? The reader expects an account of key decisions made by the highly efficient but endemically corrupt bureaucracy but instead learns only that "the intrinsic advantages of political capitalism include autonomy for the rulers [and] the ability to cut through red tape and deliver faster economic growth. . . . The attractiveness of political capitalism depends on . . . economic success." The argument is strangely similar to the neoliberal complaint that regulation impedes growth by tying the hands of decision-makers with endless red tape. Why are bureaucratic autonomy and controlled corruption functional in China but dysfunctional elsewhere? Other countries—France, for example—have bureaucracies staffed with highly-trained and public minded officials who are afforded considerable autonomy in steering economic decisions yet have been conspicuously unsuccessful in stimulating growth. Other countries—Italy, for instance—have "pervasive corruption spread across all layers of society," as Milanovic himself notes, yet have failed to capitalize on the autonomy thus afforded to maneuver around constraining legal strictures.

In lieu of an account of the functional workings of Chinese bureaucracy, Milanovic gives us a meta-historical contrast between the "Western path of development" and the Chinese. Following the economist Giovanni Arrighi, he argues that Western capitalism, before it became liberal and meritocratic, "thrived in conditions of conquest, slavery, and colonialism," which "made the European path aggressive and warlike." European capitalists needed to "project power abroad and thus had to 'conquer' the state." By the late twentieth century, this path of development was no longer available to the countries of the developing world, which had long been dominated and exploited by the West, whose military superiority brooked no challenge. Meanwhile, an “authoritarian” state had developed in China, a state that “left rich merchants in peace as long as they did not threaten it.” Communism, on this view, played the historic role of sweeping away the archaic economic underpinnings while leaving the authoritarian state intact and in a position to midwife the birth of a novel form of capitalist economy. The Chinese state achieved this precisely by linking fledgling capitalist enterprise to the advanced capitalist economies of the West, in defiance of the *dependencia* theorists of the 1960s and ’70s, who had argued that the developing world would remain dependent on the advanced economies unless it cut its ties in order to foster development at home.

The dramatic success of political capitalism in Asia since 1980 might suggest that Milanovic believes that state-managed capitalism is more efficient in achieving growth and is potentially a more attractive model than liberal meritocracy, especially in view of the rejection of “neoliberalism” by many in the West. But he is lucid about the challenges that political capitalism is already facing in China, where private capitalists have begun to resent the autonomy of the state, as their counterparts in the West did before them. And he is also clear that the Chinese model may be difficult to export because its success depends in part on conditions and traditions unique to China.

Such is the thesis of *Capitalism Alone*: The capitalist system has become all but universal. Yet it has not so much satisfied human needs as it has altered them to accommodate the needs of capitalism. Milanovic’s portrait of humanity under capitalism is unsparingly bleak. The hierarchy of values is “based simply on monetary success.” Greed, he says, quoting Marx, is “a necessary concomitant of the increasing commodification of life.” Society has become amoral, because wealth is the only “glory” and the means used to acquire it “are largely immaterial—as long as one is not caught doing something illegal.” People have ceased to be political animals and no longer “value involvement in civic matters as a general principle.” In our hectic world, “citizens have neither the time nor the knowledge nor the desire to get involved in civic matters unless the issues directly concern them.” But they do not care as long as their material needs are met.

I’m not sure this is right. The standard of living in Vietnam is much lower than in France, yet 91 percent of the Vietnamese support globalization, which has improved their daily lives, compared with only 37 percent of the French, whose misgivings about the direction their society is moving have given rise to protest movements demanding greater citizen voice. People care enough about the ravages productivism has wrought on the environment to turn out in large numbers for protest marches. Yet it is true that they are loath to give up any of the creature comforts and conveniences that productivism has given them. What is lacking is not the desire to participate in civic life but clarity about how to reconcile capitalism’s relentless pressure for change —“everything solid melts into air,” as Marx put it—with the human need for a modicum of stability and tranquility. *Capitalism Alone* tells us a great deal about the former, but about the latter its only counsel—apart from a few modest policy recommendations such as taxing the rich, generously funding public schools, and banning all but limited government funding of political campaigns—is despair.