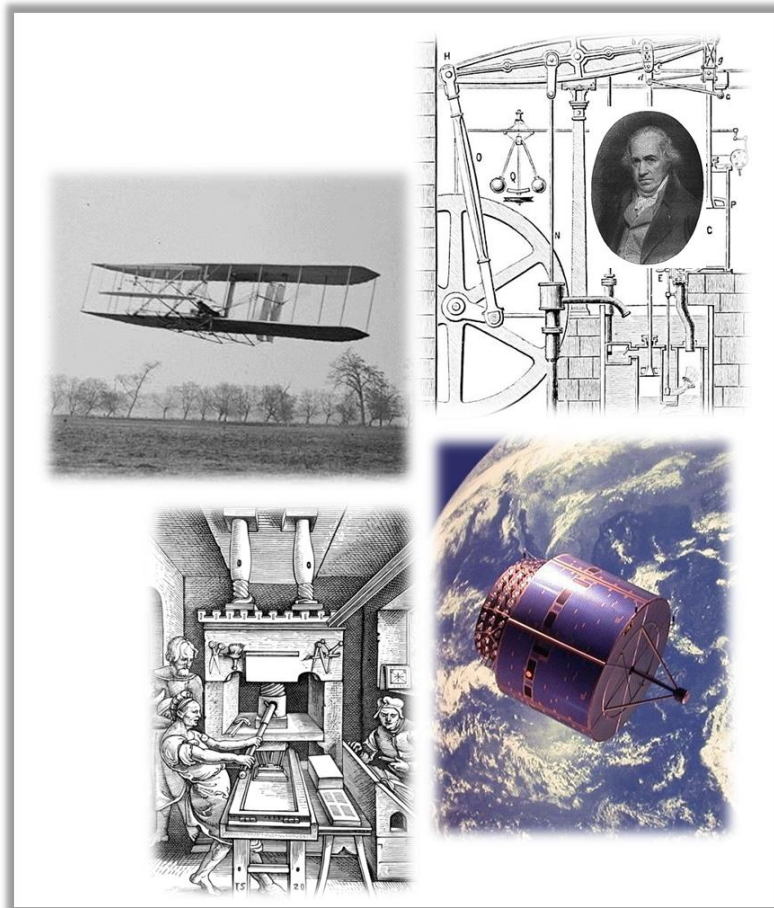


China vs. the West

“What makes the economy tick” series

Understanding our economic future through history



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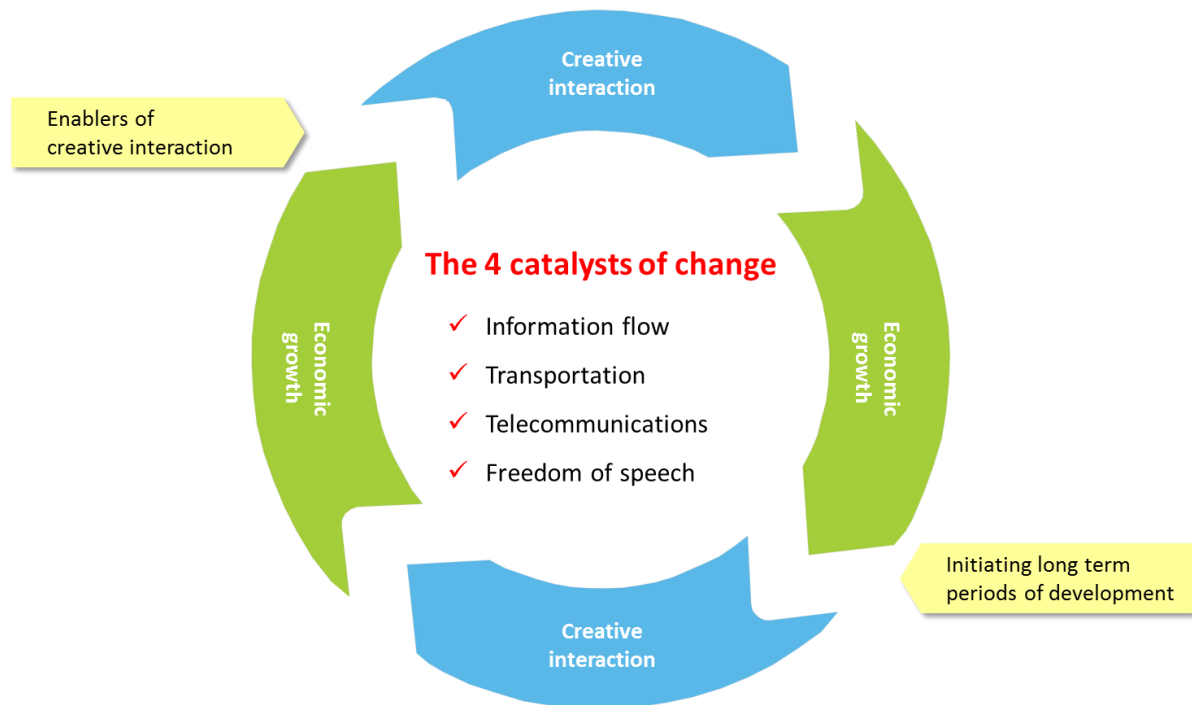
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*“Creativity is just connecting things. When you ask creative people how they did something, they feel a little guilty because they didn’t really do it, they just saw something. It seemed obvious to them after a while”, **Steve Jobs***

A new way of understanding growth

Ever wondered what triggered [China's remarkable economic turnaround](#) during the last three decades, out of the ruins of the previous century?

Based on the methodology presented in a recent post, titled "[What makes our world and the economy tick?](#)", in order to understand periods of great development, we should seek for significant progress in the following key areas: information flow, transportation, telecommunications, and freedom of speech.



These advancements, apart from being important on their own, act as a **catalyst** for future growth by boosting effective communication, thus facilitating business and economic transactions, free exchange of ideas, and other types of **creative interaction**, therefore, resulting in the initiation of a virtuous cycle of more innovation and economic activity.

The theory was tested in the three most recent periods of the modern western civilization, the Renaissance, the Industrial Revolution, and the Globalization Era, and it turned out to work fine.

In this post, we will use the same framework to explain China's recent economic rise and also ascertain its future potential.

China vs. the West: a “game of thrones”

From a historical perspective, China’s growth should not be a surprise. China’s economy has been one of the largest in the world in the last two thousand years. During the first millennium, its economy accounted for almost [one fourth](#) of the global economy. At the same time, the combined economy of the western countries, including Europe and North America, was almost [half the size](#) of the Chinese economy due to the diminishing power of the Roman Empire and the coming of the Middle Ages. During the second millennium, and until the 18th century, China continued to outperform the West in terms of contribution to global GDP. However, the West, especially after the Renaissance, started to grow at much higher rates, quickly closing the gap. At its peak, near the beginning of the 19th century, China accounted for almost [one third](#) of the global economy. If you lived in the early 19th century, you would have thought that the prospects of China were brilliant, and indeed they were. It had the largest economy in the world, and was still growing, despite West’s advancements during the Renaissance and the start of the Industrial Revolution.

So, what went wrong?

Key in understanding these economic cycles is the level of interaction of the Chinese economy, both inside and outside the country. The Chinese empire prospered during the largest part of the last two millennia, albeit largely isolated from the rest of the world. This isolation had a side effect though, as China completely missed the opportunity of the Renaissance and the Industrial Revolution. The decisive hit came with the defeat from the British, during the two Opium Wars, in 1839 and 1856 respectively. By the mid-20th century the Chinese Empire and its economy collapsed to a mere [5% contribution to global GDP](#) and it remained near this level until the late 1970s. The turning point for the economy came after Deng Xiaoping assumed power in 1977, following Mao’s death. The new leader immediately started a series of economic and other reforms that had a [great impact](#) on China and the global economy. He liberalized the economy, encouraged free trading and entrepreneurship, and opened up the country for knowledge sharing and business to other destinations. His single most important accomplishment was that he put to an end China’s infamous isolation and xenophobia (or at least he helped lower the barriers). Indeed, this opening of the economy, increased the level of China’s interaction with the world, and helped the country to develop significantly in many key areas. Now [China’s contribution to global GDP exceeds 17%](#), a level similar to the one it had in 1870, indicating the closure of an economic cycle after more than a century. In the following, we will try to interpret these growth dynamics, by examining how each of the four key catalysts of change, *Information flow*, *Transportation*, *Telecommunications*, and *Freedom of speech* evolved through China’s history from the 15th century up to the late 1970s (Mao’s death) and then after 1980.

Information flow

During the successive periods of the Renaissance, the Industrial Revolution and the Globalization Era, the West based its growth on a series of important discoveries that facilitated the easier and more cost-effective flow of information, the best examples being the invention of the Printing Press by Gutenberg and the introduction of the modern computer systems from the mid-20th century onwards. No need to describe the numerous ways that these advancements helped to shape the future of the Western civilization as we know it today. So, where was China during that time? The simple answer is, isolated from the rest of the world.

China pioneered in the information flow area, with at least [two inventions](#), paper making, even from ancient times, and printing, starting from the second half of the first millennium AD. However, due to its extreme isolation and xenophobia, China did not keep up with western developments. As a result, [it did not adopt Gutenberg's printing press until the 19th century](#), almost half a millennium after it was introduced in Europe.

The situation was even worse in the case of modern technology. For instance, [home computer ownership](#) in China was still very low even in the late 1990s, when electronic devices in the developed western countries were already considered a standard for the average household.

[Computer ownership in urban households](#) rose considerably in the 2000s from less than 10% to over 60%. However, the penetration is still very low in [rural households](#), indicating the big internal inequality problem in China.

Telecommunications

It's needless to remind us of all the great developments of the Globalization Era that boosted telecommunications in the West, such as the invention of the telephone, the radio, the television, and cellular phones. Most western countries made good use of these technologies during the largest part of the 20th century and still do today. Again, China's isolation deprived the country of the benefits coming from exploiting these great inventions. [Fixed telephone penetration](#), for instance, remained small (less than 10%) until the late 1990s. The same happened with [mobile phones' penetration](#) as well. [Fixed telephony's penetration rose rapidly after 2000](#) although its overall penetration still lags considerably against the other great economic powers of our times. Also [mobile phones' penetration rose after 2000](#); however, in this case, current levels of penetration are very close to those in the US, Japan, and Germany and, in absolute terms, [China has more mobile subscriptions](#) than all the other large economies combined.

Transportation

From ships, to railways, cars, and modern aviation, transportation is one of the key areas of development, especially during and after the Industrial Revolution. The benefit to the western society was huge, as it helped to increase travel speed and to lower costs for transferring both people and goods from one place to another. The investments made in relevant transportation technologies, but also in building the necessary infrastructure, such as bridges, roads, railways, ports, and airports, were enormous. That gave the West a competitive advantage against all other regions that helped its economy to grow with unprecedented rates and also to improve the average standards of living of its people. China, on the other hand, isolated as it was and lost in its internal problems, [didn't give any priority](#) to improve its transportation infrastructure until the second half of the 20th century.

This is of particular importance to modern China due to the logistics costs and delays incurred to the value chain by a poor transportation infrastructure and the need to move a huge population. Indeed, [China has invested a lot in modern transportation](#) thus facilitating the easier and more cost-effective transfer of goods and people in the recent years. However, there is a lot of ground to be covered as, even today, [logistic costs account for 20% of a product's price in China](#), at least twice as high compared to the US or other developed countries.

Freedom of speech

The path from Renaissance to modern western civilization is also a path of more respect for human rights and freedom of speech. Perhaps, the most significant landmarks in this development were the Declaration of Independence, establishing the United States as an independent Republic, and the outbreak of the French Revolution, paving the way for a more democratic Europe, in the late 18th century. Once more, China failed to follow this path. Not only due to its isolation, but also driven by its need to control a huge population scattered in all directions and great distances, China adopted a more authoritarian system of administration, which, to some extent, is still in place today.

For most of its history, China was an imperial state with dynasties succeeding one another. In the early 20th century, China was established, first, as the Republic of China and then as the People's Republic of China under Mao's reign. However, that was not a democratic state as we know it in the West, where Government officials get elected by the people, there is no censorship, and everyone has the right to their own opinion. Even today, although, in theory, China is a republic

and freedom of speech is a constitutional right, in practice, [the Communist Party abuses its power](#) to control mass media, the internet, and ban whichever opinion feels “uncomfortable”.

This is not an easy issue to handle. One of the most important problems, always haunting Chinese administrations, is the internal balance of the huge population, especially between the more and less developed parts of the country. Currently, there is a shift from using military force and an authoritarian administration to ensuring more economic benefits for the poor, in order to achieve this balance. However, giving away money has an important prerequisite, that of a continuously growing economy, something that, as history has taught us, is very difficult to maintain, even for the most successful economies in the world.

Conclusion

Overall, during the last five hundred years, China scored quite low, relative to the West, in all these “catalysts” of interaction and growth, namely *information flow*, *telecommunications*, *transportation*, and *freedom of speech* and eventually paid the price with a diminishing economy and social turbulence, especially after 1800.

After the many reforms of Deng Xiaoping, China opened up to the world, after 1980, thus improving its capacity for interaction both inside and outside the country, leading to one of the most impressive economic turnarounds for a country in only three decades.

Despite, its recent achievements, China, still lags today against the West in all these important development areas, perhaps with the exclusion of telecommunication infrastructure.

Instrumental to China’s potential for further growth will be the path it will choose to balance internal inequality, one of fear or one of motivation and creativity.

One thing is for sure: these choices will not only influence China’s economy and society, but the whole world as well.