CHAPTER 24

The Fallacy of the "China Collapse" and "China Threat" Theories

Keyu Jin

Dr. Keyu Jin is a tenured associate professor at the London School of Economics. Her research focuses on international macroeconomics and the Chinese economy. A Ph.D. from Harvard University, she was a former visiting professor at Yale University and UC Berkeley.

K. Jin (✉)
London School of Economics, London, UK

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All the Western dire predictions for the Chinese economy have come to naught so far. Since the 1990s, there have been voices prophesying the doom of China's economy and every five to 10 years, all kinds of "China collapse" theories resurface, as well as the "China threat" theory. Some pundits even make a living from it.

However, over the past 40 years of reform and opening up, China has not collapsed. On the contrary, its comprehensive national strength has increased and absolute poverty has been eliminated. In fact, it is the "China collapse" theory that has repeatedly collapsed.

Why do these two theories keep popping up again and again? Why do Western scholars and media fail to predict the state of China's economy correctly? Keyu Jin talks about these issues as well as what China's rise will bring to the rest of the world.

CNS: Before China's seventh national census data was released in 2021, some American and European media claimed that China was facing a demographic crisis. It was not the first time that the Western society tried to portray China in a negative light. Why does the "China's economy will collapse" theory keep on recurring?

Keyu Jin: I'm not worried about China's population aging. Too much emphasis is placed on the number of old people, young people and labor force in China. We should focus on efficiency, because the efficiency is improving very quickly from generation to generation. The education level, training and overall environment of the one-child generation enable them to support the elderly.

Why does the "China's economy will collapse" theory recur?

First of all, China's growth model is different from the Western market economy model in textbooks. The outside world has never seen such a growth rate and development model outside China. Some Westerners think that if it doesn't conform to conventions, there must be problems, and even link the Chinese economic model with that of the Soviet Union. These perceptions are wrong.

Second, most of their knowledge of China's growth model is superficial. They only know that both the government and the market play a role, with the government playing the main role. Western mainstream media believe that as long as there is government participation, unless public facilities are provided, there must be problems, such as low efficiency, or high asset mismatches, which will lead to risks in the financial system.

They seldom know the more subtle mechanisms, systems and structures in the Chinese economy, and the relationships among the participants in the economy.

In recent years, many foreign experts consider China to be the biggest source of risk for the international financial system. For example, at the World Economic Forum in Davos, Switzerland, the problems and risks of China's financial system were repeatedly mentioned. They didn't expect that China's financial risks would be resolved gradually and considerably through policy adjustment although China had accumulated high debts due to its rapid development.

The Chinese government, with its great strength and resources, can introduce a series of policies to control financial risks. In Western countries, including the United States, however, the governments are not so powerful. They are aware of the financial risks, but the measures they can really take are far fewer than in China.

CNS: What are the differences between China's economic system and growth model and those of Western countries?

Keyu Jin: In China, the relationship between the government and the market is unique. The resources, strength and mobilization ability of the government are unprecedented.

According to China's State Administration for Market Regulation, there were 21.79 million new market entities in China in 2019. Western scholars are mostly confused why so many new enterprises appeared in such a short time. The government played a very important role, especially local governments. They are willing to support private enterprises with high efficiency, which is difficult for economists with mainstream views to understand.

In China's system, politics and the economy are closely linked. The governments have a series of performance indicators to consider: development, investment attraction, environmental protection and innovation, so they are more willing to select enterprises with ability and potential.

If you look at the relationship between state-owned and private enterprises, in China, it's very close, and some state-owned enterprises (SOEs) directly or indirectly become shareholders of private ones. Data shows the private enterprises most closely connected with SOEs grow the fastest with the highest efficiency.

This close connection between state-owned and private enterprises is unique to China. Some people think that if a large amount of state-owned capital is involved, the efficiency will definitely be very low, but in fact it is not. The resources of state-owned and private enterprises are complementary. Private enterprises boast good corporate culture and product innovation; SOEs have advantages such as financing. Just like the *yin-yang* diagram, both black and white, or two different entities can co-exist, which is beyond the understanding of the West.

The relationship between the Chinese government and the market is very complicated, but there is a clear economic logic and relationship. Most Western scholars have only a superficial understanding of this.

CNS: If the Chinese economy is measured by Western systems and standards, what will be the errors?

Keyu Jin: The West measures China's economy very inaccurately. They always measure China by their own standards, systems and models. They believe that China's savings rate and investment rate are too high, and its economic structure is biased toward exports and industry.

However, if we observe China only from some macro data, we won't understand the growth pattern of the Chinese economy. Although the investment rate is higher than that of many other countries, China is undergoing urbanization and needs a lot of investment, including in new and old infrastructure. So what is "too high"? The situation in China is different from Japan's and the United States'.

The same goes for the savings rate. In foreign countries, a high savings rate means weak consumption, so we must reduce it to stimulate the economy. China's savings rate is indeed high, but it has its advantages. It avoids the trap that many developing countries have stepped into; that is, they need to borrow a lot of money from abroad to develop. And foreign debt has finally triggered economic and financial crisis in many developing countries.

Another misunderstanding is that China's savings rate and investment are very high, and the economic growth is entirely driven by capital accumulation. Once investment is reduced, the economic growth will definitely slow down or even go into a downturn.

But actually, in the past few decades, efficiency improvement, not investment, brought by reform has been the main driving force of China's economic growth. From 1990 to 2007, more than 50 percent of China's economic growth came from efficiency improvement, so it can't be said that China relies only on investment and savings, or only on exports to stimulate economic growth.

CNS: In recent years, while we hear less of the "China collapse" theory, we hear more about the "China threat" theory.

Keyu Jin: China is really a very powerful country. It is also the first time in nearly a hundred years that a developing country with such a population has become the second largest economy in the world. And the culture of China is very different from that of the West.

China's influence is not only reflected in its huge economy, but also in its science and technology, innovation efficiency and per capita income. The so-called threat theory may come from the fact that China is so strong.

After World War II, the United States acted as the world's boss, exporting so-called democratic ideas and American models. The United States believes that the whole world should follow the path it takes. However, China is very different. The political systems, values, cultures and economic development models of China and the West are very different.

Meanwhile, the outside world doesn't know much about China, or what its goal is. Therefore, many threat theories come from the differences and ignorance, which can easily breed fear or even demonization.

In addition, the "China threat" theory is also the political need of some countries.

Take the United States with its various problems as an example. There is a growing divide between the elite and ordinary people, which became an acute problem in the Donald Trump era. There are also racial issues, and human rights issues brought about by extreme liberalism, etc., which have accelerated the polarization of the U.S. It needs an external challenge to unite its domestic power, so hyping the "China threat" theory is also its political appeal.

China has every right to ensure its people live a better life, which is something all countries should agree with and encourage. Curbing China's growth will deprive the Chinese people of opportunities. From the perspective of human rights, it doesn't make sense either.

CNS: What does China's rise mean for the world?

Keyu Jin: Economically, it has many benefits for the world.

We live in the Internet age and also a "everybody's-a-winner" era. The leader of the Internet era has a completely different meaning from the "central country" of the previous stage. The "central country" in the Internet era should not contain the other participants but encourage, help and even support them. It should protect the network, internationalization and the entire economic system, so that everyone can win.

China can play its role mainly in three aspects:

First, China can act as the "anchor" of global financial stability. When a global economic or financial crisis occurs, it can serve as a cornerstone to stabilize the global financial market and industrial chain, together with the United States and other important economies.

Second, China's asset market gives many investors an opportunity to disperse their risks. Relatively speaking, China's stock market, bond market and other capital markets are much less related to those of developed countries. However, the proportion of Chinese assets held by international investors is still very small. If they increase the proportion of Chinese assets, the risks can be dispersed to a great extent.

Third, China can provide plenty of good trade opportunities. In the past 10 years, its contribution to global growth has remained at about one-third.

Although trade is win–win, some people can be negatively affected. Governments should take the lead in introducing some programs to help the vulnerable groups' re-employment, which the U.S. government has failed to do.

Therefore, when Chinese goods come to the American market, some vulnerable groups in the labor market lose their jobs or even have no chance to return to the labor market. Should Chinese goods be blamed for that or the U.S. government for not helping these people? For decades, the education level in the United States as a whole has declined. America should better solve its domestic problems.

CNS: Many people worry that once the U.S. central bank shrinks its balance sheet, we will have a repeat of the 2013 taper tantrum, when the U.S. Federal Reserve announced that it would taper bond purchases, triggering an economic crisis in developing countries. Can this be averted? What role can China play in this?

Keyu Jin: The Fed now faces two major challenges.

First, how to balance domestic goals and international influences.

The Fed acts as a cornerstone in the global financial system. Its interest rate changes as well as quantitative easing have a huge impact on the world. However, it does not consider the whole world when making decisions, but gives priority to the needs of the United States, ignoring policy spillovers.

But the policy spillovers are very large. When the Fed cuts interest rates, there is the issue of excessive credit expansion and bubbles appear in many countries, especially developing countries. When the Fed shrinks its balance sheet, developing countries are also negatively affected, and there could even be a financial crisis. This is a manifestation of globalization, and also a problem that globalization cannot solve.

As a core country, how to balance domestic goals and international influences? The United States has failed to strike such a balance. Some people say that the central bank of a second country, such as China, needs to play a role in stabilizing the market together with the Fed. The two central banks need to communicate with each other to control the situation together.

Second, the U.S. share of the global economy has decreased in recent years, and the safe assets and highly liquid assets that the United States can provide can't meet the global demand.

Other countries or economies need to fill the gap, especially in supporting emerging economies. Since 2009, China has played such a role. In the financial crisis of emerging markets, it provided liquidity support.

Many countries are opposed to the U.S. using the dollar as a political weapon to achieve its political goals. Many people support the birth of a new international currency. The euro can't do it. Europe is not economically stable, and it has not really become a big unified market. Although the European bond market is large, it is actually still separated because of the sovereignty issue of each country.

This is an opportunity for China. However, at this stage, China may not be able to do it, and it will take a long time for its financial system to be truly advanced. Money needs to be trusted. Although there is hard power behind an international currency, that is, its economic strength and overall stability, there is also soft power, including people's trust in a country's system, where China needs to do more.

(Interviewed by Pang Wuji)