THE FUTURE OF CAPITALISM

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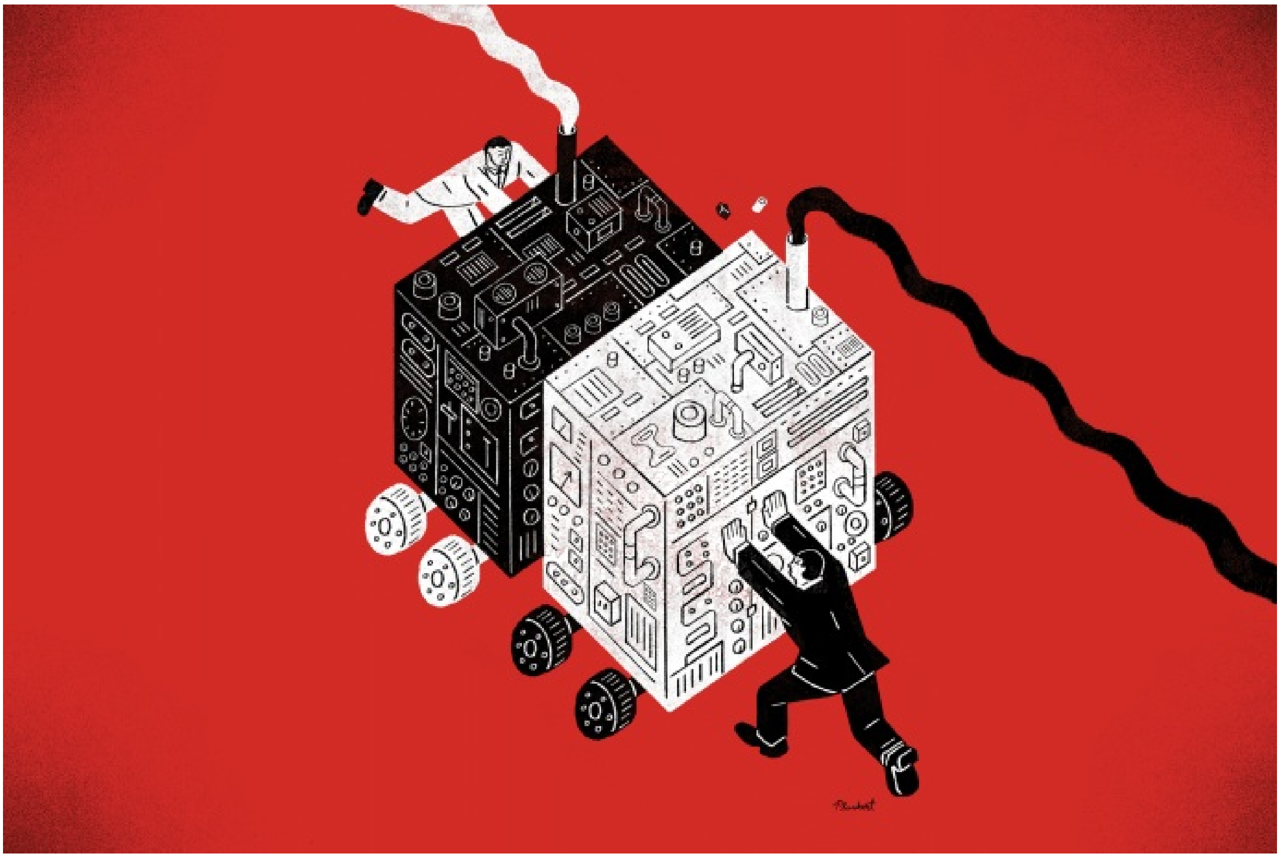

Capitalism rules the world. With only the most minor exceptions, the entire globe now organizes economic production the same way: labor is voluntary, capital is mostly in private hands, and production is coordinated in a decentralized way and motivated by profit.

There is no historical precedent for this triumph. In the past, capitalism—whether in Mesopotamia in the sixth century bc, the Roman Empire, Italian city-states in the Middle Ages, or the Low Countries in the early modern era—had to coexist with other ways of organizing production. These alternatives included hunting and gathering, small-scale farming by free peasants, serfdom, and slavery. Even as recently as 100 years ago, when the first form of globalized capitalism appeared with the advent of large-scale industrial production and global trade, many of these other modes of production still existed. Then, following the Russian Revolution in 1917, capitalism shared the world with communism, which reigned in countries that together contained about one-third of the human population. Now, however, capitalism is the sole remaining mode of production.

It’s increasingly common to hear commentators in the West describe the current order as “late capitalism,” as if the economic system were on the verge of disappearing. Others suggest that capitalism is facing a revived threat from socialism. But the ineluctable truth is that capitalism is here to stay and has no competitor. Societies around the world have embraced the competitive and acquisitive spirit hardwired into capitalism, without which incomes decline, poverty increases, and technological progress slows. Instead, the real battle is within capitalism, between two models that jostle against each other.

Often in human history, the triumph of one system or religion is soon followed by a schism between different variants of the same credo. After Christianity spread across the Mediterranean and the Middle East, it was riven by ferocious ideological disputes, which eventually produced the first big fissure in the religion, between the Eastern and Western churches. So, too, with Islam, which after its dizzying expansion swiftly divided into Shiite and Sunni branches. And communism, capitalism’s twentieth-century rival, did not long remain a monolith, splitting into Soviet and Maoist versions. In this respect, capitalism is no different: two models now hold sway, differing in their political, economic, and social aspects.

In the states of western Europe and North America and a number of other countries, such as India, Indonesia, and Japan, a liberal meritocratic form of capitalism dominates: a system that concentrates the vast majority of production in the private sector, ostensibly allows talent to rise, and tries to guarantee opportunity for all through measures such as free schooling and inheritance taxes. Alongside that system stands the state-led, political model of capitalism, which is exemplified by China but also surfaces in other parts of Asia (Myanmar, Singapore, Vietnam), in Europe (Azerbaijan, Russia), and in Africa (Algeria, Ethiopia, Rwanda). This system privileges high economic growth and limits individual political and civic rights.

These two types of capitalism—with the United States and China, respectively, as their leading examples—invariably compete with each other because they are so intertwined. Asia, western Europe, and North America, which together are home to 70 percent of the world’s population and 80 percent of its economic output, are in constant contact through trade, investment, the movement of people, the transfer of technology, and the exchange of ideas. Those connections and collisions have bred a competition between the West and parts of Asia that is made more intense by the differences in their respective models of capitalism. And it is this competition—not a contest between capitalism and some alternative economic system—that will shape the future of the global economy.

In 1978, almost 100 percent of China's economic output came from the public sector; that figure has now dropped to less than 20 percent. In modern China, as in the more traditionally capitalist countries of the West, the means of production are mostly in private hands, the state doesn't impose decisions about production and pricing on companies, and most workers are wage laborers. China scores as positively capitalistic on all three counts.

Capitalism now has no rival, but these two models offer significantly different ways of structuring political and economic power in a society. Political capitalism gives greater autonomy to political elites while promising high growth rates to ordinary people. China's economic success undermines the West's claim that there is a necessary link between capitalism and liberal democracy.

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Liberal capitalism has many well-known advantages, the most important being democracy and the rule of law. These two features are virtues in themselves, and both can be credited with encouraging faster economic development by promoting innovation and social mobility. Yet this system faces an enormous challenge: the emergence of a self-perpetuating upper class coupled with growing inequality. This now represents the gravest threat to liberal capitalism's long-term viability.

At the same time, China's government and those of other political capitalist states need to constantly generate economic growth to legitimize their rule, a compulsion that might become harder and harder to fulfill. Political capitalist states must also try to limit corruption, which is inherent to the system, and its complement, galloping inequality. The test of their model will be its ability to restrain a growing capitalist class that often chafes against the overweening power of the state bureaucracy.

As other parts of the world (notably African countries) attempt to transform their economies and jump-start growth, the tensions between the two models will come into sharper focus. The rivalry between China and the United States is often presented in simply geopolitical terms, but at its core, it is like the grinding of two tectonic plates whose friction will define how capitalism evolves in this century.

LIBERAL CAPITALISM

The global dominance of capitalism is one of two epochal changes that the world is living through. The other is the rebalancing of economic power between the West and Asia. For the first time since the Industrial Revolution, incomes in Asia are edging closer to those in western Europe and North America. In 1970, the West produced 56 percent of world economic output and Asia (including Japan) produced only 19 percent. Today, only three generations later, those proportions have shifted to 37 percent and 43 percent—thanks in large part to the staggering economic growth of countries such as China and India.

Capitalism in the West generated the information and communications technologies that enabled a new wave of globalization in the late twentieth century, the period when Asia began to narrow the gap with the "global North." Anchored initially in the wealth of Western economies, globalization led to an overhaul of moribund structures and huge growth in many Asian countries. Global income inequality has dropped significantly from what it was in the 1990s, when the global Gini coefficient (a measure of income distribution, with zero representing perfect equality and one representing perfect inequality) was 0.70; today, it is roughly 0.60. It will drop further as incomes continue to rise in Asia.

Although inequality between countries has lessened, inequality within countries—especially those in the West—has grown. The United States' Gini coefficient has risen from 0.35 in 1979 to about 0.45 today. This increase in inequality within countries is in large part a product of globalization and its effects on the more developed economies in the West: the weakening of trade unions, the flight of manufacturing jobs, and wage stagnation.

Liberal meritocratic capitalism came into being in the last 40 years. It can be best understood in comparison to two other variants: classical capitalism, which was predominant in the nineteenth and early twentieth centuries, and social democratic capitalism, which defined the welfare states in western Europe and North America from World War II to the early 1980s.

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Unlike in the classical capitalism of the nineteenth century, when fortunes were to be made from owning, not working, rich individuals in the present system tend to be both capital rich and labor rich—that is, they generate their income both from investments and from work. They also tend to marry and make families with partners of similar educational and financial backgrounds, a phenomenon sociologists call "assortative mating." Whereas the people at the top of the income distribution under classical capitalism were often financiers, today many of those at the top are highly paid managers, Web designers, physicians, investment bankers, and other elite professionals. These people work in order to earn their large salaries, but whether through an inheritance or their own savings, they also draw a great deal of income from their financial assets.

In liberal meritocratic capitalism, societies are more equal than they were during the phase of classical capitalism, women and ethnic minorities are more empowered to enter the workforce, and welfare provisions and social transfers (paid out of taxes) are employed in an attempt to mitigate the worst ravages of acute concentrations of wealth and privilege. Liberal meritocratic capitalism inherited those last measures from its direct predecessor, social democratic capitalism.

That model was structured around industrial labor and featured the strong presence of unions, which played a huge role in shrinking inequality. Social democratic capitalism presided over an era that saw measures such as the gi Bill and the 1950 Treaty of Detroit (a sweeping, union-negotiated contract for autoworkers) in the United States and economic booms in France and Germany, where incomes rose. Growth was distributed fairly evenly; populations benefited from better access to health care, housing, and inexpensive education; and more families could climb up the economic ladder.

But the nature of work has changed significantly under globalization and liberal meritocratic capitalism, especially with the winnowing away of the industrial working class and the weakening of labor unions. Since the late twentieth century, the share of capital income in total income has been rising—that is, an increasing portion of GDP belongs to the profits made by big corporations and the already wealthy. This tendency has been quite strong in the United States, but it has also been documented in most other countries, whether developing or developed. A rising share of capital income in total income implies that capital and capitalists are becoming more important than labor and workers, and so they acquire more economic and political power. It also means an increase in inequality, because those who draw a large share of their income from capital tend to be rich.

MALAISE IN THE WEST

While the current system has produced a more diverse elite (in terms of both gender and race), the setup of liberal capitalism has the consequence of at once deepening inequality and screening that inequality behind the veil of merit. More plausibly than their predecessors in the Gilded Age, the wealthiest today can claim that their standing derives from the virtue of their work, obscuring the advantages they have gained from a system and from social trends that make economic mobility harder and harder. The last 40 years have seen the growth of a semipermanent upper class that is increasingly isolated from the rest of society. In the United States, the top ten percent of wealth holders own more than 90 percent of the financial assets. The ruling class is highly educated, many of its members work, and their income from that labor tends to be high. They tend to believe that they deserve their high standing.

These elites invest heavily both in their progeny and in establishing political control. By investing in their children's education, those at the top enable future generations of their kind to maintain high labor income and the elite status that is traditionally associated with knowledge and education. By investing in political influence—in elections, think tanks, universities, and so on—they ensure that they are the ones who determine the rules of inheritance, so that financial capital is easily transferred to the next generation. The two together (acquired education and transmitted capital) lead to the reproduction of the ruling class.

The formation of a durable upper class is impossible unless that class exerts political control. In the past, this happened naturally; the political class came mostly from the rich, and so there was a certain commonality of views and shared interests between politicians and the rest of the rich. That is no longer the case: politicians come from various social classes and backgrounds, and many of them share sociologically very little, if anything, with the rich. Presidents Bill Clinton and Barack Obama in the United States and Prime Ministers Margaret Thatcher and John Major in the United Kingdom all came from modest backgrounds but quite effectively supported the interests of the one percent.

In a modern democracy, the rich use their political contributions and the funding or direct ownership of think tanks and media outlets to purchase economic policies that benefit them: lower taxes on high incomes, bigger tax deductions, higher capital gains through tax cuts to the corporate sector, fewer regulations, and so on. These policies, in turn, increase the likelihood that the rich will stay on top, and they form the ultimate link in the chain that runs from the higher share of capital in a country's net income to the creation of a self-serving upper class. If the upper class did not try to co-opt politics, it would still enjoy a very strong position; when it spends on electoral processes and builds its own civil society institutions, the position of the upper class becomes all but unassailable.

As the elites in liberal meritocratic capitalist systems become more cordoned off, the rest of society grows resentful. Malaise in the West about globalization is largely caused by the gap between the small number of elites and the masses, who have seen little benefit from globalization and, accurately or not, regard global trade and immigration as the cause of their ills. This situation eerily resembles what used to be called the "disarticulation" of Third World societies in the 1970s, such as was seen in Brazil, Nigeria, and Turkey. As their bourgeoisies were plugged into the global economic system, most of the hinterland was left behind. The disease that was supposed to affect only developing countries seems to have hit the global North.

Workers at a steel production plant in Jilin Province, China, 2006
Ian Teh / Panos Pictures / Redux

CHINA'S POLITICAL CAPITALISM

In Asia, globalization doesn't have that same reputation: according to polls, 91 percent of people in Vietnam, for instance, think globalization is a force for good. Ironically, it was communism in countries such as China and Vietnam that laid the groundwork for their eventual capitalist transformation. The Chinese Communist Party came to power in 1949 by prosecuting both a national revolution (against foreign domination) and a social revolution (against feudalism), which allowed it to sweep away all ideologies and customs that were seen as slowing economic development and creating artificial class divisions. (The much less radical Indian independence struggle, in contrast, never succeeded in erasing the caste system.) These two simultaneous revolutions were a precondition, over the long term, for the creation of an indigenous capitalist class that would pull the economy forward. The communist revolutions in China and Vietnam played functionally the same role as the rise of the bourgeoisie in nineteenth-century Europe.

In China, the transformation from quasi feudalism to capitalism took place swiftly, under the control of an extremely powerful state. In Europe, where feudal structures were eradicated slowly over centuries, the state played a far less important role in the shift to capitalism. Given this history, then, it is no surprise that capitalism in China, Vietnam, and elsewhere in the region has so often had an authoritarian edge.

The system of political capitalism has three defining features. First, the state is run by a technocratic bureaucracy, which owes its legitimacy to economic growth. Second, although the state has laws, these are applied arbitrarily, much to the benefit of elites, who can decline to apply the law when it is inconvenient or apply it with full force to punish opponents. The arbitrariness of the rule of law in these societies feeds into political capitalism's third defining feature: the necessary autonomy of the state. In order for the state to act decisively, it needs to be free from legal constraints. The tension between the first and second principles—between technocratic bureaucracy and the loose application of the law—produces corruption, which is an integral part of the way the political capitalist system is set up, not an anomaly.

The flip side of China's astronomic growth has been its massive increase in inequality.

Since the end of the Cold War, these characteristics have helped supercharge the growth of ostensibly communist countries in Asia. Over a 27-year period ending in 2017, China's growth rate averaged about eight percent and Vietnam's averaged around six percent, compared with just two percent in the United States.

The flip side of China's astronomic growth has been its massive increase in inequality. From 1985 to 2010, the country's Gini coefficient leapt from 0.30 to around 0.50—higher than that of the United States and closer to the levels found in Latin America. Inequality in China has risen starkly within both rural and urban areas, and it has risen even more so in the country as a whole because of the increasing gap between those areas. That growing inequality is evident in every divide—between rich and poor provinces, high-skilled workers and low-skilled workers, men and women, and the private sector and the state sector.

Notably, there has also been an increase in China in the share of income from privately owned capital, which seems to be as concentrated there as in the advanced market economies of the West. A new capitalist elite has formed in China. In 1988, skilled and unskilled industrial workers, clerical staff, and government officials accounted for 80 percent of those in the top five percent of income earners. By 2013, their share had fallen by almost half, and business owners (20 percent) and professionals (33 percent) had become dominant.

A remarkable feature of the new capitalist class in China is that it has emerged from the soil, so to speak, as almost four-fifths of its members report having had fathers who were either farmers or manual laborers. This intergenerational mobility is not surprising in view of the nearly complete obliteration of the capitalist class after the Communists' victory in 1949 and then again during the Cultural Revolution in the 1960s. But that mobility may not continue in the future, when—given the concentration of ownership of capital, the rising costs of education, and the importance of family connections—the intergenerational transmission of wealth and power should begin to mirror what is observed in the West.

Compared with its Western counterparts, however, this new capitalist class in China may be more of a class by itself than a class for itself. China's many byzantine forms of ownership—which at the local and national levels blur the lines between public and private—allow the political elite to restrain the power of the new capitalist, economic elite.

For millennia, China has been home to strong, fairly centralized states that have always prevented the merchant class from becoming an independent center of power. According to the French scholar Jacques Gernet, wealthy merchants under the Song dynasty in the thirteenth century never succeeded in creating a self-conscious class with shared interests because the state was always there ready to check their power. Although merchants continued to prosper as individuals (as the new capitalists largely do nowadays in China), they never formed a coherent class with its own political and economic agenda or with interests that were forcefully defended and propagated. This scenario, according to Gernet, differed markedly from the situation around the same time in Italian merchant republics and the Low Countries. This pattern of capitalists enriching themselves without exercising political power will likely continue in China and in other political capitalist countries, as well.

A CLASH OF SYSTEMS

As China expands its role on the international stage, its form of capitalism is invariably coming into conflict with the liberal meritocratic capitalism of the West. Political capitalism might supplant the Western model in many countries around the world.

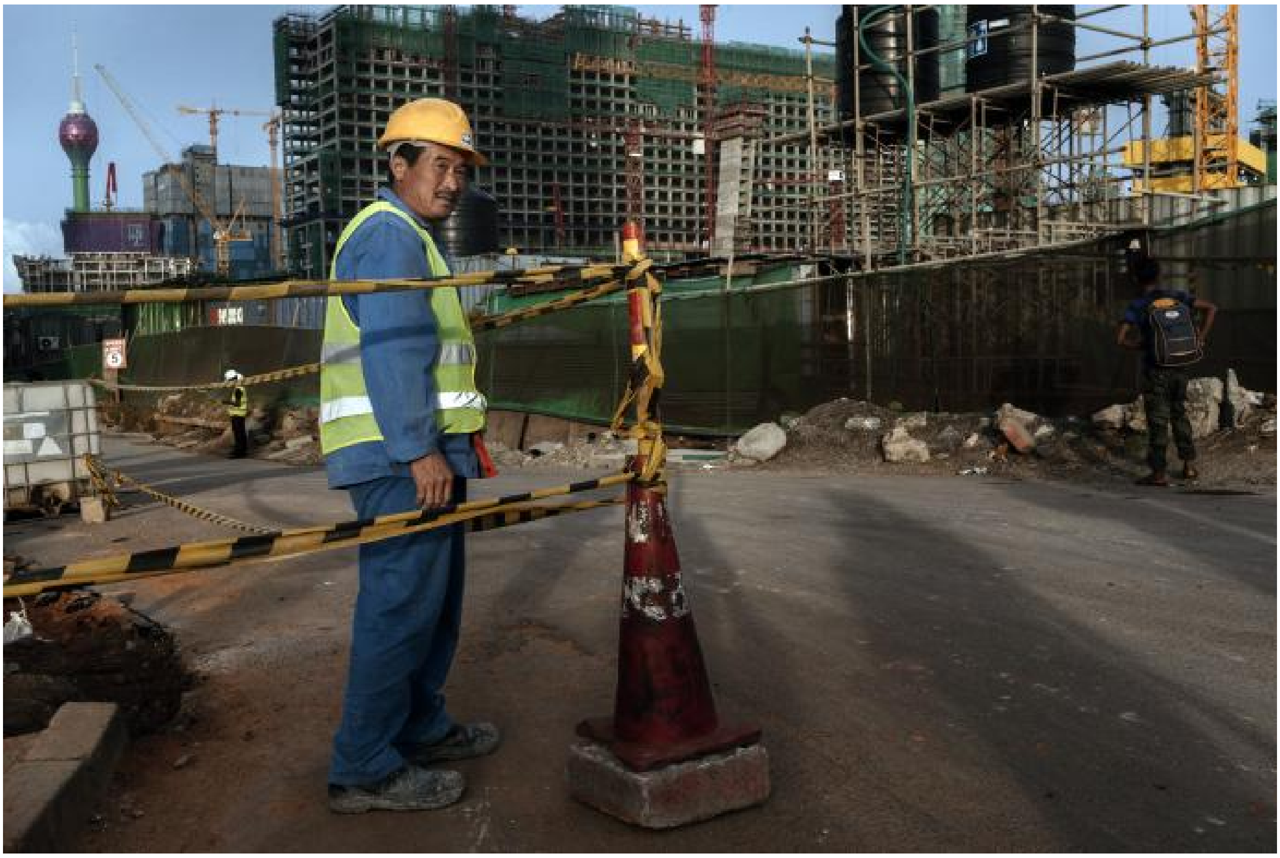
The advantage of liberal capitalism resides in its political system of democracy. Democracy is desirable in itself, of course, but it also has an instrumental advantage. By requiring constant consultation of the population, democracy provides a powerful corrective to economic and social trends that may be detrimental to the common good. Even if people’s decisions sometimes result in policies that reduce the rate of economic growth, increase pollution, or lower life expectancy, democratic decision-making should, within a relatively limited time period, correct such developments.

Political capitalism, for its part, promises much more efficient management of the economy and higher growth rates. The fact that China has been by far the most economically successful country in the past half century places it in a position to legitimately try to export its economic and political institutions. It is doing that most prominently through the Belt and Road Initiative, an ambitious project to link several continents through improved, Chinese-financed infrastructure. The initiative represents an ideological challenge to the way the West has been handling economic development around the world. Whereas the West focuses on building institutions, China is pouring money into building physical things. The BRI will link partnered countries into a Chinese sphere of influence. Beijing even has plans to handle future investment disputes under the jurisdiction of a Chinese-created court—quite a reversal for a country whose “century of humiliation” in the nineteenth century was capped by Americans and Europeans in China refusing to be subject to Chinese laws.

Many countries may welcome being part of the BRI. Chinese investment will bring roads, harbors, railways, and other badly needed infrastructure, and without the type of conditions that often accompany Western investment. China has no interest in the domestic policies of recipient nations; instead, it emphasizes equality in the treatment of all countries. This is an approach that many officials in smaller countries find particularly attractive. China is also seeking to build international institutions, such as the Asian Infrastructure Investment Bank, following the playbook of the United States after World War II, when Washington spearheaded the creation of the World Bank and the International Monetary Fund.

Beijing has another reason to be more active on the international stage. If China refused to advertise its own institutions while the West continued to advance the values of liberal capitalism in China, large swaths of the Chinese population could become more attracted to Western institutions. The current disturbances in Hong Kong have failed to spread anywhere else in China, but they do illustrate real discontent with the arbitrary application of the law, discontent that may not be confined to the former British colony. The blatant censorship of the Internet is also deeply unpopular among the young and educated.

By projecting the advantages of its political capitalism abroad, China will reduce the appeal of the Western liberal model to its own citizens. Its international activities are essentially matters of domestic survival. Whatever formal or informal arrangement Beijing reaches with states that embrace political capitalism, China is bound to exercise increasing influence on international institutions, which in the past two centuries have been built exclusively by Western states, to serve Western interests.



A Chinese construction worker in Colombo, Sri Lanka, June 2018
Adam Dean / The New York Times / Redux

John Rawls, the consummate philosopher of modern liberalism, argued that a good society ought to give absolute priority to basic liberties over wealth and income.

Experience shows, however, that many people are willing to trade democratic rights for greater income. One need simply observe that within companies, production is generally organized in the most hierarchical fashion, not the most democratic. Workers do not vote on the products they would like to produce or on how they would like to produce them. Hierarchy produces greater efficiency and higher wages. “Technique is the boundary of democracy,” the French philosopher Jacques Ellul wrote more than half a century ago. “What technique wins, democracy loses. If we had engineers who were popular with the workers, they would be ignorant of machinery.” The same analogy can be extended to society as a whole: democratic rights can be, and have been, given up willingly for higher incomes.

In today’s commercialized and hectic world, citizens rarely have the time, the knowledge, or the desire to get involved in civic matters unless the issues directly concern them. It is telling that in the United States, one of the oldest democracies in the world, the election of a president, who, in many respects in the American system, has the prerogatives of an elected king, is not judged of sufficient importance to bestir more than half the electorate to go to the polls. In this respect, political capitalism asserts its superiority.

The problem, however, is that in order to prove its superiority and ward off a liberal challenge, political capitalism needs to constantly deliver high rates of growth. So while liberal capitalism’s advantages are natural, in that they are built into the setup of the system, the advantages of political capitalism are instrumental: they must be constantly demonstrated. Political capitalism starts with the handicap of needing to prove its superiority empirically. It faces two further problems, as well. Relative to liberal capitalism, political capitalism has a greater tendency to generate bad policies and bad social outcomes that are difficult to reverse because those in power do not have an incentive to change course. It can also easily engender popular dissatisfaction because of its systemic corruption in the absence of a clear rule of law.

Unlike liberal capitalism, political capitalism must be permanently on its toes.

Political capitalism needs to sell itself on the grounds of providing better societal management, higher rates of growth, and more efficient administration (including the administration of justice). Unlike liberal capitalism, which can take a more relaxed attitude toward temporary problems, political capitalism must be permanently on its toes. This may, however, be seen as an advantage from a social Darwinist point of view: because of the constant pressure to deliver more to its constituents, political capitalism might hone its ability to manage the economic sphere and to keep on delivering, year in, year out, more goods and services than its liberal counterpart. What appears at first as a defect may prove to be an advantage.

But will China’s new capitalists forever acquiesce to a status quo in which their formal rights can be limited or revoked at any moment and in which they are under the constant tutelage of the state? Or, as they become stronger and more numerous, will they organize, influence the state, and, finally, take it over, as happened in the United States and Europe? The Western path as sketched by Karl Marx seems to have an ironclad logic: economic power tends to emancipate itself and to look after, or impose, its own interests. But the track record of nearly 2,000 years of an unequal partnership between the Chinese state and Chinese business presents a major obstacle to China's following the same path as the West.

The key question is whether China's capitalists will come to control the state and if, in order to do so, they will use representative democracy. In the United States and Europe, capitalists used that cure very carefully, administering it in homeopathic doses as the franchise slowly expanded and withholding it whenever there was a potential threat to the property-owning classes (as in Great Britain after the French Revolution, when the right to vote became even more tightly restricted). Chinese democracy, if it comes, will likely resemble democracy in the rest of the world today, in the legal sense of mandating one vote per person. Yet given the weight of history and the precarious nature and still limited size of China's propertied classes, it is not certain that rule by the middle class could be maintained in China. It failed in the first part of the twentieth century under the Republic of China (which held sway over much of the mainland from 1912 to 1949); only with great difficulty will it be reestablished with greater success 100 years later.

PLUTOCRATIC CONVERGENCE?

What does the future hold for Western capitalist societies? The answer hinges on whether liberal meritocratic capitalism will be able to move toward a more advanced stage, what might be called "people's capitalism," in which income from both factors of production, capital and labor, would be more equally distributed. This would require broadening meaningful capital ownership way beyond the current top ten percent of the population and making access to the top schools and the best-paying jobs independent of one's family background.

To achieve greater equality, countries should develop tax incentives to encourage the middle class to hold more financial assets, implement higher inheritance taxes for the very rich, improve free public education, and establish publicly funded electoral campaigns. The cumulative effect of these measures would be to make more diffuse the ownership of capital and skills in society. People's capitalism would be similar to social democratic capitalism in its concern with inequality, but it would aspire to a different kind of equality; instead of focusing on redistributing income, this model would seek greater equality in assets, both financial and in terms of skills. Unlike social democratic capitalism, it would require only modest redistributive policies (such as food stamps and housing benefits) because it would have already achieved a greater baseline of equality.

If they fail to address the problem of growing inequality, liberal meritocratic capitalist systems risk journeying down another path—not toward socialism but toward a convergence with political capitalism. The economic elite in the West will become more insulated, wielding more untrammeled power over ostensibly democratic societies, much in the same way that the political elite in China lords over that country. The more that economic and political power in liberal capitalist systems become fused together, the more liberal capitalism will become plutocratic, taking on some features of political capitalism. In the latter model, politics is the way to win economic benefits; in plutocratic—formerly liberal meritocratic—capitalism, economic power will conquer politics. The endpoint of the two systems will be the same: the closing ranks of a privileged few and the reproduction of that elite indefinitely into the future.