Lessons for the west from Asian capitalism

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Asian elites have always looked at the world differently from western elites. And after this crisis is over, the gap in perspectives will widen. Asians will naturally view with caution any western advice on economics, particularly because most Asians believe that the crisis has only vindicated the Asian approach to capitalism.

To be accurate, there is more than one Asian approach. China's economy is managed differently from India's. Yet neither China nor India has lost faith in capitalism, because both have elites who well remember living with the alternatives. The Chinese well remember the disasters that followed from the Maoist centrally planned economy. The Indians well remember the slow "Hindu rate of growth" under Nehruvian socialism.

The benefits of the free market to Asia have been enormous: increased labour productivity, efficient use and deployment of national resources, a tremendous increase in economic wealth and, most importantly, hundreds of millions have been lifted out of absolute poverty. Just look at Chinese history through Chinese eyes. From 1842 to 1979, the Chinese experienced foreign occupation, civil wars, a Japanese invasion, a cultural revolution. But after Deng Xiaoping gradually instituted free market reforms, the Chinese people experienced the fastest increase so far in their standard of living.

The desire for an orderly society is deeply ingrained in the psyche of all Asians, which helps explain why virtually all Asian states hesitated to copy America in deregulating their financial markets. Instinctively, they felt government supervision remained critical. This was equally true in India's democratic system and in China's Communist party system. It is telling that, while Y.V. Reddy, India's former central bank governor, was occasionally vilified by his country's media for holding back on deregulation, he has now become a national hero. His stance saved India from the worst effects of this crisis. China was equally wary of deregulation. Indeed the Chinese leaders may have understood earlier than most that America was building a house of cards with its reckless creation of derivatives. Gao Xiqing, an adviser to Zhu Rongji, then Chinese premier, said in 2000 that "if you look at every one of these [derivative] products, they make sense. But in aggregate, they are bullshit. They are crap. They serve to cheat people." Mr Gao said all this while Alan Greenspan, as chairman of the US Federal Reserve, was waxing eloquent about the economic value of derivatives.

Asian culture has been honed by centuries of hard experience, which explains why Asians save more. All Asian societies have memories of turbulent times. They know from experience the importance of preparing for the bad days that will follow the good. Most Asian friends of mine find it inconceivable that some Americans can live from pay cheque to pay cheque. "But what happens if you lose your job?" they ask.

The Asian financial crisis of 1997-98 may have been a blessing in disguise. The failure of the International Monetary Fund and western policies then confirmed in Asian minds that they had to create their own safety mechanisms for economic downturns. Thus began a decade-long exercise of accumulating foreign reserves. China's went up from nearly $145bn at the end of 1998 to almost $2,000bn (€1,520bn, £1,430bn) at the end of 2008. India's went up from $27.83bn in early 1998 to $315.6bn in June 2008. This enormous pool has helped to protect Asian societies as they hunker down for the storm.

And when this storm is over, we should not be surprised to discover that the greatest global believers in capitalism will be in Asia. But it will be an Asian mix of capitalism, not the western formula, that will become the dominant form of global capitalism, where the "invisible hand" of free markets will be balanced by the "visible hand" of good governance.

The Asian mix may have its own weaknesses. Asia is still underperforming in creativity and innovation. Corruption will remain a serious problem.

The Asian emphasis on the family unit may also be a mixed blessing. Many of Asia's most successful entrepreneurs are keen to retain family control of the business. This enables them to take a long-term view. But the downside is nepotism and the lack of a deep culture of meritocracy.

On balance, the strengths of Asian capitalism are greater than the weaknesses. Within a decade Asians will have some of the largest free trade areas, including those between China and the Association of South East Asian Nations, the Japan-ASEAN FTA, and the Indian-ASEAN FTA that is likely to be set up. Recent history has taught Asians a valuable lesson: more trade leads to greater prosperity. In the Asian way – two steps forward,
one step back – trade barriers will gradually come down. By the middle of the 21st century, intra-Asian trade will far surpass that of any other region.

Despite this, there will be no ideological trumpeting of the virtues of Asian capitalism. After their experiences of the past 100 years, Asians are wary of ideology. They prefer the simple, commonsense approach of learning from experience and they will heed the advice of Adam Smith, who said that prudence is “of all virtues that which is most useful to the individual”. It may also be helpful to nations.

The writer, dean of the Lee Kuan Yew School of Public Policy, National University of Singapore, has just published The New Asian Hemisphere: the Irresistible Shift of Global Power to the East. To join the debate, go to www.ft.com/capitalismblog

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