Why the West Got Rich, Why China is Catching Up, and Why Russia is Not

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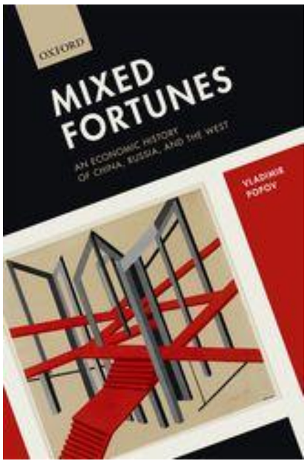
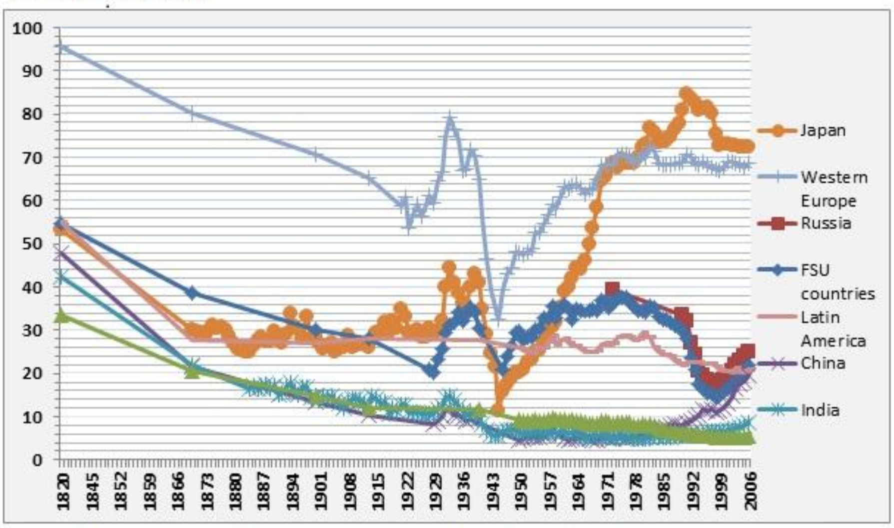


The goal of this book is to provide a non-technical interpretation of the "Great Divergence" and "Great Convergence" stories – the widening of the gap in per capita income between developed and developing countries in 1500-1950, and the narrowing of this gap afterwards (see fig. 1).

The usual explanation is that countries that we now call "developed", or the "West", acquired in the 16th century and afterwards some features that were absent in more traditional societies. The list of these features ranges from the abolition of serfdom and protestant ethics, to the protection of property rights and free universities. The problem with this reasoning is that it is assumed that these features emerged initially only in North-Western Europe and only in the 16th-18th century. However, in fact, there were many countries before the 16th century with social structures that possessed or were conducive to many of these same features, but they never experienced productivity growth comparable to the one that started in Britain and the Netherlands in the 16th century and later – in the rest of Europe (0.2-0.3% a year in 1500-1800 and 1% and more a year afterwards).

Fig. 1. PPP GDP per capita (in 1990 International Geary-Khamis dollars) as a % of the US level

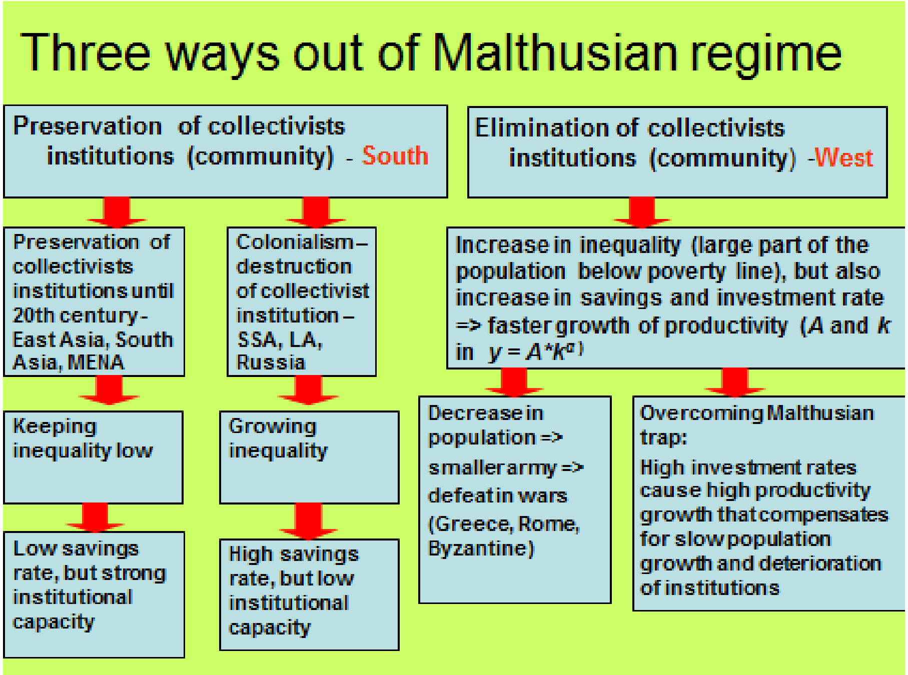


Source: Maddison, A. (2010). Statistics on World Population, GDP and Per Capita GDP, 1-2008 AD (http://www.ggdc.net/MADDISON/oriindex.htm)

The book presents a different interpretation of how the West got rich. Western countries exited the Malthusian trap by dismantling traditional collectivist institutions: this was associated with increased income inequality and even decreased life expectancy, but allowed the redistribution of income in favour of savings and investment at the expense of consumption (scheme). The elimination of collectivist (community) institutions was a risky experiment that put masses of population below the subsistence minimum and caused a reduction or slowdown of growth of the population – the foundation of the military might (number of people and the number of soldiers) in the Malthusian growth regime.

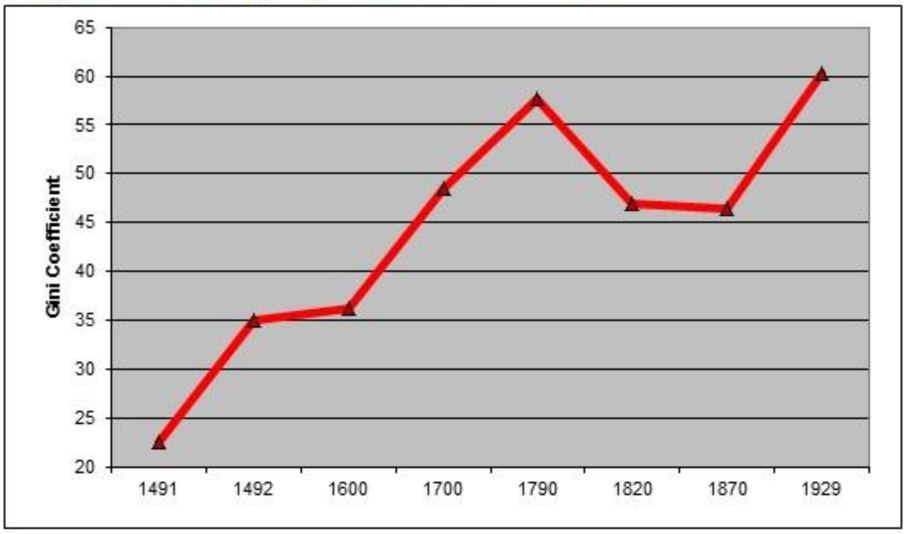
“A great civilization is not conquered from without until it has destroyed itself within" said Will Durant about the Roman Empire, but apparently this diagnoses could explain the collapse of many other ambitious civilizations. Early attempts to ensure the priority of the rights of individual over the rights of the community at the expense of collective interests and low inequality (Greece, Rome, Byzantine) led to the impoverishment of the masses, higher mortality rates and foreign conquest. Only in Northwest Europe in the 16-18th centuries this policy somehow succeeded for the first time in history.

It is not the abundance of competition or entrepreneurship, nor ideas for technological innovations that allowed the West to accelerate the growth rates of productivity by the order of magnitude. Instead, it is first and foremost the abundance of savings and investment that resulted from growing income inequalities that allowed an increase in the capital/labour ratio, and cast in iron the ideas for new products and technologies. To pit it differently, the West became rich not due to its inventiveness and entrepreneurial spirit, but due to the merciless dismantling of community that previously provided social guarantees to the poorest.



When the same pattern was applied to developing countries (as a result of colonialism in Latin America, as well as Sub-Saharan Africa, or voluntary Westernization in an attempt to catch up, such as the Russian Empire), it resulted in the destruction of traditional institutions, an increase in income inequality, and a worsening of starting positions for catch-up development (fig. 2). This group of countries replicated the Western exit from the Malthusian trap and experienced immediate increases in income differentiation, the rise in savings and investment and in the growth of productivity, but at a price of rising social inequality and deterioration of institutional capacities, i.e. the ability of the state to enforce its own rules and regulations.

Fig. 2. Predicted inequality in Latin America 1491-1929

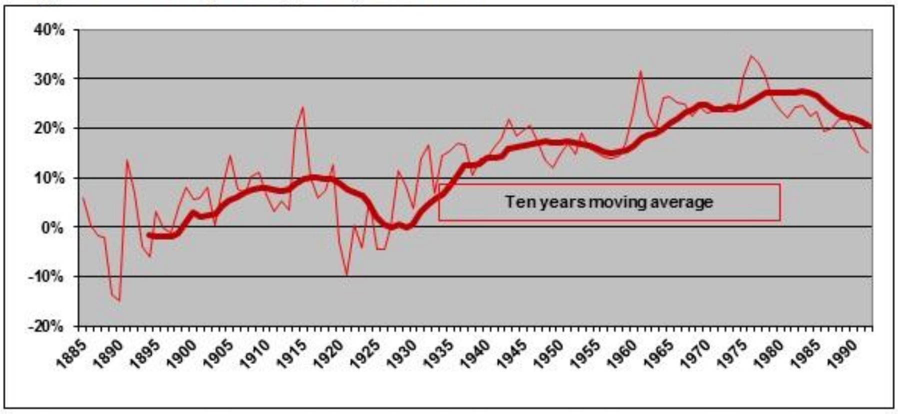


Source: Williamson, Jeffrey G. (2009). *History Without Evidence: Latin American Inequality since 1491*. Georg-August-Universität Göttingen. Discussion paper No. 3. (These are not the actual Ginis, but predicted Ginis reconstructed using regression equation for the more recent period).

Other developing countries (East Asia, South Asia, and Middle East and North Africa) were less affected by colonialism and managed to retain their traditional institutions. This delayed the transition to modern economic growth until the mid-20th century, but permitted them to preserve their low inequality and strong institutions – a beneficial starting position for future economic growth. Eventually they found another (and less painful) exit from the Malthusian trap: slow technical progress allowed a gradual increase of per capita income and a raise in the share of savings and investment in GDP without any major increase in income inequality, nor worsening the institutional capacity and decrease in life expectancy (see Malthusian scheme).

More Westernized countries of the global South (Latin America and the Russian Empire) raised their savings-investment rate (fig. 3) and exited Malthusian trap earlier than the rest in the 18th century, but at a price of undermining necessary conditions for future growth. So, in the end, Latin American and Russian growth was not enough to catch up with the West. Colonization of Sub-Saharan Africa (except for South Africa), unlike the colonization of Latin America and the Westernization of Russia, did not result in any considerable transfer of technology and human capital, and only increased inequalities and undermined institutions. As a result, these countries were disadvantaged on all counts and had the worst growth record in the world.

Fig. 3. Total savings in Argentina, % of GDP



Source: Taylor, Alan M. (1996). International Capital Mobility in History: The Saving-Investment Relationship, NBER Working Paper, No. 5743

On the contrary, most of the less-Westernized countries of East and South Asia, and the Middle East and North Africa, managed to preserve low inequality and efficient collectivist institutions. Their savings-investment ratios stayed at a level below 10% until the mid-20th century, so they virtually did not grow before that but, once saving increased, it transpired that they have all the preconditions for fast growth. Some of them became economic miracles, rapidly catching up with the West (East Asia), the development of others has increased in recent decades (South Asia), while others (Middle Eastern and North African countries) may well become the economic miracles of the future.

The examples of these two trajectories of the catch-up development of non-Western countries – Russian and Chinese routes – are examined in greater detail in *Mixed Fortunes*.

Discover more: the 'Introduction' in *Mixed Fortunes: An Economic History of China, Russia and the West* is now free and available to read until the end of July. Get access to all of this book, as well as over hundreds other Oxford's Economic and Finance titles, by recommending OSO to your librarian today.