



China's Not the Big Trade Cheat Harming America's Domestic Economy

Romney expresses a widely held belief that China cheats its way to competitive advantage and harms the U.S. economy in the process, but that's wrong. It may be that our system has simply reached an impasse.

by Zachary Karabell | March 19, 2012 4:45 AM EDT

As in 2008, China has again emerged as a central campaign issue. On the stump, Mitt Romney has emphasized that if he is president, China will no longer run roughshod over the United States as he contends it has during the Obama administration. "On day one," he thunders, "I will declare China a currency manipulator, allowing me to put tariffs on products where they are stealing American jobs unfairly. We can compete when there's a level playing field, and we'd win."

Judging from the increasingly hard stance of the Obama administration—which last week filed several charges against China with the World Trade Organization—there is a widespread belief in the United States that China has taken advantage of generous U.S. trade policies to cheat its way to competitive advantage, harming the domestic American economy in the process. While popular, this belief rests on flimsy foundations. Much of what China now makes stopped being made in America long before China made it, or wouldn't be made in America without a sharp increase in the cost of the finished good. Anyone willing to pay a few hundred more dollars for that washing machine, cellphone, or iPad?

The belief that China's economic ascension is due primarily to cheating is even more wrong. That view allows Americans to maintain the illusion that our form of capitalism is unequivocally superior and has unquestionable competitive advantages, which would be readily apparent were it not for the fact that China's government has secret subsidies, steals American intellectual property, keeps its currency undervalued, and props up housing and industry.

But what if America's current form of capitalism isn't superior? What if the reason for China's ascension is that it's doing a better job moving forward and deploying capital with urgency and efficiency? What if the United States is feeling anxiety and fear not because of China, but rather because our system has reached an impasse?

Last week *Intelligence Squared* hosted a debate on whether China does capitalism better than the United States does. The result was a resounding no, and a strong audience endorsement of the notion that China is more paper tiger than dragon on the rise. The only capitalism China does

better than the U.S., said noted scholar Minxin Pei, is “crony capitalism.” His debating partner, Ian Bremmer of the Eurasia Group, hammered the point even further, asserting that on no scale is China a more conducive place to start a business, be an entrepreneur, or be a citizen. The audience agreed.

But this question is not answered simply because more Americans agree. At that debate, Orville Schell forcefully argued that China has significant advantages. Yes, it is a system rife with inefficiencies, nascent housing bubbles, corruption, and more unacknowledged debt and wasteful spending than shows up in official figures. Both the World Bank and the International Monetary Fund in the past week have highlighted the potential pitfalls of the Chinese system, which relies heavily on state spending to power its growth. Yet, the presence of manifold problems doesn’t prove that China’s system is second rate. It proves only that it is a normal human society, rife with opportunities and challenges.

While the American system in theory may be preferable, the Chinese system in practice appears to be doing a better job planning for the next decade. Both countries funnel a large portion of the economy through government, but it is hard to argue that the U.S. government—federal, state, and local—does a better job allocating capital for productive use than the Chinese do. That may feed Republican critiques that government shouldn’t be doing much of what it does, yet the Chinese government actually allocates capital to great effect, as well as great waste and with substantial corruption.

Much of American government spending goes to consumption, safety nets, and the military; much of Chinese spending goes to investment in infrastructure and urbanization, which is the very investment spending that the United States has been so unable to manifest. Even with waste, the new transportation networks, power grids, alternate energy, urban infrastructure, and housing will yield long-term benefits for the Chinese economy for decades to come. It is impossible to make the same claims for the nearly \$4 trillion that the U.S. government spends each year.

The lack of health-care spending or any real safety net in China does lead to insecurity and a high savings rate, which keeps domestic consumer activity more muted. That is an issue that China must address. But in terms of pure competitive advantage, all of the many American freedoms and cultural incentives to be innovative, be entrepreneurial, build a business, or go to college to create a career do not change one iota the sclerotic inability of government to urgently and productively invest for the common future. American government did that for the middle years of the 20th century to great effect, and even in smaller ways in the 19th century. No longer.

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The free-market answer is, well, there you go: government should get out of the way of the economy and stop gumming up the works and saddling the system with debt. But the Chinese example of state-sponsored capitalism highlights a key weakness of that argument: government is a necessary element for investment in common needs—including education—that demand far more money than any one company would or could spend and hope to see a return on investment.

The United States doesn't need to copy the Chinese example of state-mandated capitalism; we could emulate the Canadians and their public-private partnership model. But Americans do need to shake themselves out of a stupor that says China excels because they cheat while America is only held back because of Chinese cheating, evil banks, too much Washington meddling, or not enough. No. China excels because for now it has found a formula that allows it to invest for the future and rapidly transform the material landscape for hundreds of millions of people for the better, with all the attendant messiness and weaknesses. It also has found a formula that activates and energizes hundreds of millions of people to believe in a better future. The United States—still much richer per capita, still more productive, and still generating wealth and succoring dreams—is meandering economically and at odds with itself because its form of capitalism has ceased to fulfill the hopes, dreams, and needs of far too many people.

These are all snapshots of the moment. China may face a crisis in the next few years that makes its current success seem hollow; the U.S. may regain more footing and so make current questioning seem excessive. We don't know. China may also make the transition to a domestic consumer economy more fluidly than any would have thought, while the U.S. may continue to see a fractured system of tens of millions left out while tens of millions thrive.

We do know that the current American system is falling short of generating a competitive model and a compelling one, and that our political system is consuming vast resources and using them badly. If you are Republican, that is cause to cut what government spends; if Democratic, it's cause to spend more wisely and for the future. Those are the only debates we should be having, and in that scheme, China matters far less than how Americans address America in the years ahead.