

# COVID-19 PANDEMIC AND LONG-TERM DEVELOPMENT TRAJECTORIES OF EAST ASIAN AND WESTERN ECONOMIC MODELS

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**Abstract** The article examines the reasons for the superior performance of East Asia in containing the human and economic costs of the 2020 coronavirus pandemic. The East Asian model is based on solidarity and priority of collective interests over individual interests, whereas the Western model emphasizes competition and guarantees of individual rights. The quantifiable characteristics that allow to draw a distinction between the two models are income and wealth inequalities, property and control over corporations, institutional capacity of the state (measured as homicide rate and the size of shadow economy), and trust in the government. Because of the East Asian model's superiority in these respects, both the number of infections and the mortality rates from COVID-19 in China and other East Asian countries were lower than in Western countries by two orders of magnitude. Besides, the 2020 economic crisis associated with the pandemic was much deeper in the West than in East Asia. These developments give new arguments in support of the views that East Asian economic and social model is more viable than the Western model. Continued rise of East Asia and proliferation of East Asian model in the developing world will lead to profound changes in the world economic order.

**Keywords** models of capitalism, inequalities, state institutional capacity, health care system, coronavirus, structural crisis, adverse supply shock, conventional Keynesian counter-cyclical policy, industrial policy

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**Название статьи** Пандемия COVID-19 и долгосрочные траектории развития восточноазиатской и западной экономических моделей

**Аннотация** В статье рассматриваются причины лучшей социальной и экономической динамики Восточной Азии в ходе пандемии COVID-19 2020 г. – более низких смертности и заболеваемости и меньшего падения производства. Восточноазиатская модель основывается на солидарности и приоритете коллективных интересов над индивидуальными, тогда как западная делает акцент на конкуренции и гарантиях индивидуальных прав. Среди измеряемых характеристик, которые позволяют сопоставить две модели: неравенство в распределении доходов и богатства, концентрация собственности и контроля над корпорациями, институциональный потенциал государства (измеряемый уровнем убийств и масштабами теневой экономики) и уровень доверия к правительству. Благодаря превосходству восточноазиатской модели по этим

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параметрам, как число случаев заражения, так и уровень вызванной вирусом COVID-19 летальности в Китае и других восточноазиатских странах оказался на два порядка ниже, чем в западных странах. Кроме того, связанный с пандемией 2020 г. экономический кризис в западных странах был гораздо глубже, чем в Восточной Азии. Такое развитие событий дает новые аргументы в пользу точки зрения о том, что восточноазиатская экономическая и социальная модель более жизнеспособна, чем западная. Продолжение подъема Восточной Азии и распространение восточноазиатской модели в развивающихся странах приведет к глубоким изменениям глобального экономического порядка.

**Ключевые слова** модели капитализма, неравенство, институциональный потенциал государства, система здравоохранения, коронавирус, структурный кризис, неблагоприятный шок предложения, традиционная кейнсианская антициклическая политика, промышленная политика

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## I. Introduction

Even prior to the COVID-19 pandemic, the superior performance of East Asia attracted the attention of economists and sociologists. The bridging of the gap between poor and rich countries that has been happening since 1950 largely is due to the rapid growth of East Asia.<sup>1</sup> Only five countries or territories form the Global South – Hong Kong, Japan, Singapore, South Korea, Taiwan – managed to join the rich country club due to their high economic growth rates.<sup>2</sup> In recent decades South East Asia and China were catching up with the developed countries as well.<sup>3</sup>

The 2008–2009 economic recession, called the Great Recession at a time, affected advanced economies more heavily affected than the Global South. In China, there was no recession at all, but only a mild slowdown of growth (from 14% in 2007 to 9–10% in 2008–2009). In 2020, China and other East Asian countries handled the coronavirus pandemics way better than most Western countries: numbers of contaminations and deaths per one million of inhabitants in East Asia were by two (!) orders of magnitude lower than in the West (Figure 1).

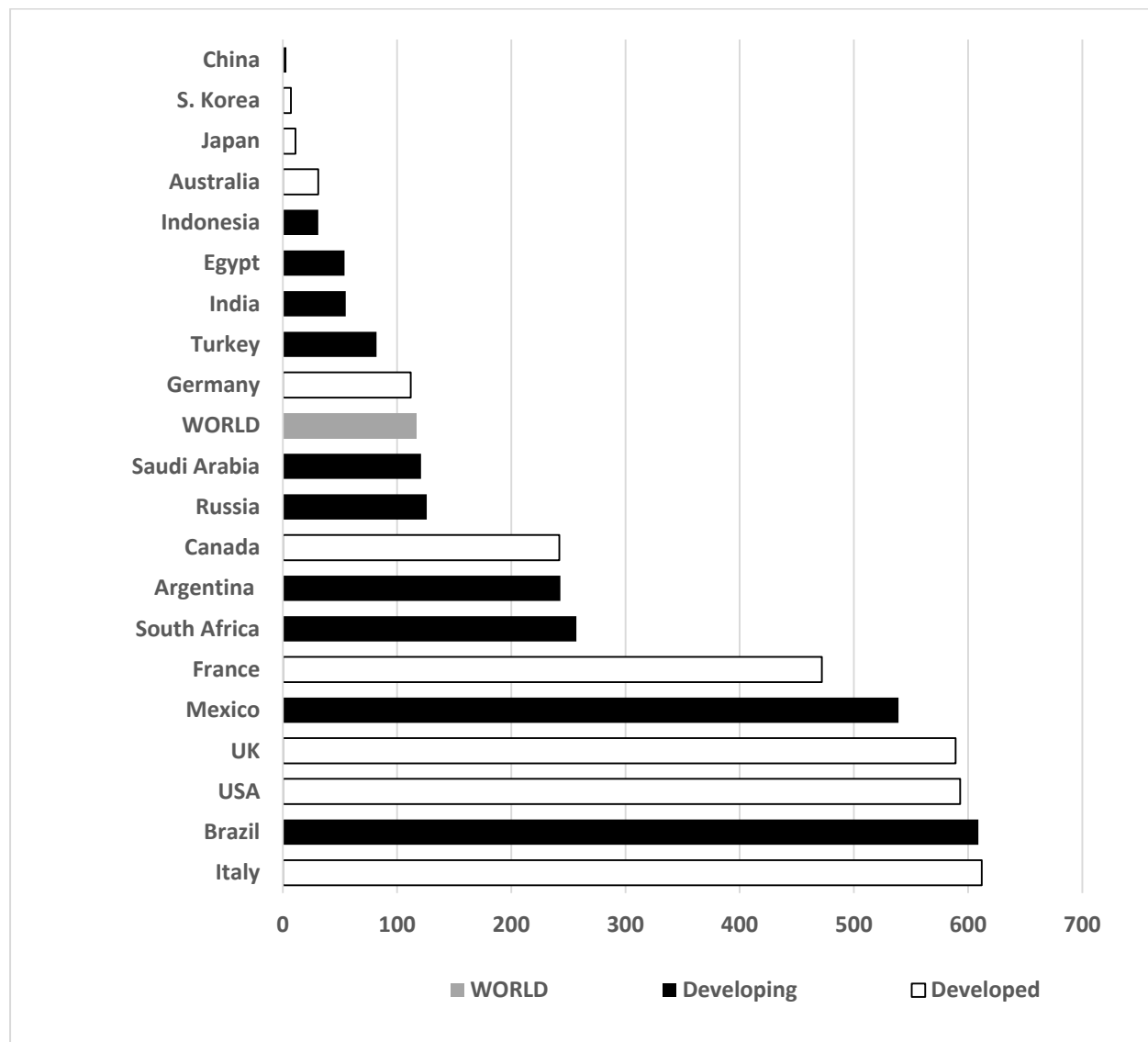
Partly the differences between developed and developing countries are explained by statistical deficiencies: higher numbers of tests, infections, and deaths attributed to coronavirus. Thus, developed countries have higher corona death rates than developing countries on average. Full analysis will be possible when the information on annual death rates by countries is available, so that the pandemic period (2020–?) rates could be compared with the rates for the previous years to compute excess deaths.<sup>4</sup>

Another likely explanation is the ability to carry out symptomatic tracking (even without testing) and isolation – in this respect, East Asian countries and the Middle East and North Africa (MENA) countries performed way better than most developed countries, where strict tracing, isolation, and lock down quarantine measures were often regarded as violation of human rights.

Besides, the recession associated with the restrictions imposed to fight COVID-19 has been much deeper in the West than in East Asia. The only country, whose economy totally recovered in the second quarter of 2020 after the coronavirus recession, is China: its second quarter gross domestic product (GDP) in 2020 was 3% higher than in the same

quarter of 2019, whereas in all other G-20 countries it was lower, mostly by 10 to 20%, i. e. recession not only continued, but has been getting worse (Table 1).

**Figure 1. Death rate from COVID-19 in G20 countries, per 1 million inhabitants (by September 10, 2020)**



Source: Worldometers. URL: <https://www.worldometers.info/coronavirus>.

For 2020 as a whole, the mid-year World Bank economic forecast envisaged a sharper decline in output in advanced economies (–7%) than in the developing world (–2.5%), but no decline in China (in fact, 1% growth instead), as compared to the 6% decline in the United States. The OECD September 2020 forecast predicted the reduction of output in all G20 countries except for China (Table 2). It looked like the East Asia could cope better with the 2020 world economic downturn than the West, as was already the case in the previous downturn – the Great Recession of 2008–2009.

**Table 1. Growth rates of GDP in major G-20 countries in the first half of 2020, compared to the same quarter of the previous year, seasonally adjusted**

Country // Growth rates of GDP compared to the same quarter of the previous year, %	Q1-2020	Q2-2020
United States	0.3	–9.1
European Union (all 27 member states)	–2.5	–14.2
Germany	–2.2	–11.3
France	–5.7	–18.9
Italy	–5.6	–17.7
United Kingdom	–1.7	–21.7
Canada	–0.9	–13.0
Australia	1.6	–6.3
Turkey	4.4	–9.0
Russia	1.8	–5.6
Mexico	–2.1	–18.7
Argentina	–5.3	–19.8
Brazil	–1.4	–11.4
Saudi Arabia	–1.0	–5.6
South Africa	–0.2	–17.2
India	3.3	–23.5
Indonesia	3.0	–5.4
Japan	–2.0	–10.0
Korea	1.4	–2.8
<b>China</b>	<b>–6.8</b>	<b>3.2</b>

Source: G20 – Quarterly Growth Rates of GDP in Volume. OECD Statistics.

URL: <https://stats.oecd.org/index.aspx?queryid=33940>.

Does this mean that East Asian economic and social model is really more viable than the Western one? In his recent article, Francis Fukuyama points out three crucial factors that determine the performance of countries during the pandemic. “It is not a matter of regime type”, he wrote. “Some democracies have performed well, but others have not, and the same is true for autocracies. The factors responsible for successful pandemic responses have been state capacity, social trust, and leadership. Countries with all three factors in place – a competent state apparatus, a government that citizens trust and listen to, and effective leaders – have performed impressively, limiting the damage they have suffered. Countries with dysfunctional states, polarized societies, or poor leadership have done badly, leaving their citizens and economies exposed and vulnerable”.<sup>5</sup>

**Table 2. OECD economic forecast, GDP growth rates, %  
(September 2020)**

<b>Country</b>	<b>2019</b>	<b>2020</b>	<b>2021</b>
Argentina	−2.1	−11.2	3.2
Australia	1.8	−4.1	2.5
Brazil	1.1	−6.5	3.6
Canada	1.7	−5.8	4.0
<b>China</b>	<b>6.1</b>	<b>1.8</b>	<b>8.0</b>
France	1.5	−9.5	5.8
Germany	0.6	−5.4	4.6
India	4.2	−10.2	10.7
Indonesia	5.0	−3.3	5.3
Italy	0.3	−10.5	5.4
Japan	0.7	−5.8	1.5
South Korea	2.0	−1.0	3.1
Mexico	−0.3	−10.2	3.0
Russia	1.4	−7.3	5.0
Saudi Arabia	0.4	−6.8	3.2
South Africa	0.1	−11.5	1.4
Turkey	0.9	−2.9	3.9
United Kingdom	1.5	−10.1	7.6
United States	2.2	−3.8	4.0
World	2.6	−4.5	5.0
Euro area	1.3	−7.9	5.1
G20	2.9	−4.1	5.7

Source: OECD Economic Outlook: Statistics and Projections. URL: [https://www.oecd-ilibrary.org/economics/data/oecd-economic-outlook-statistics-and-projections\\_eo-data-en](https://www.oecd-ilibrary.org/economics/data/oecd-economic-outlook-statistics-and-projections_eo-data-en).

It is easy to see that on all three counts East Asian countries look superior to the United State and, perhaps, even to Western Europe. The question, of course, is why some countries have this state capacity, social trust and leadership, whereas other countries do not. Also, the question is what it takes to acquire these qualities. “...The Covid crisis may be an opportunity to move towards a new model of capitalism in which both innovation and the protection of citizens are promoted,” – argues Philippe Aghion and co-authors.<sup>6</sup> Shall we use or lose this opportunity?

## **II. The East Asian model vs. the Western model**

“East Asian Miracle”, a much-discussed paper by the World Bank,<sup>7</sup> was a belated recognition that economic catch up is occurring in East Asia based on the indigenous not Western economic model. This paper drew attention to the industrial policy and the role of the state in engineering economic miracle, but subsequent research pointed out other important features of the East Asian model.

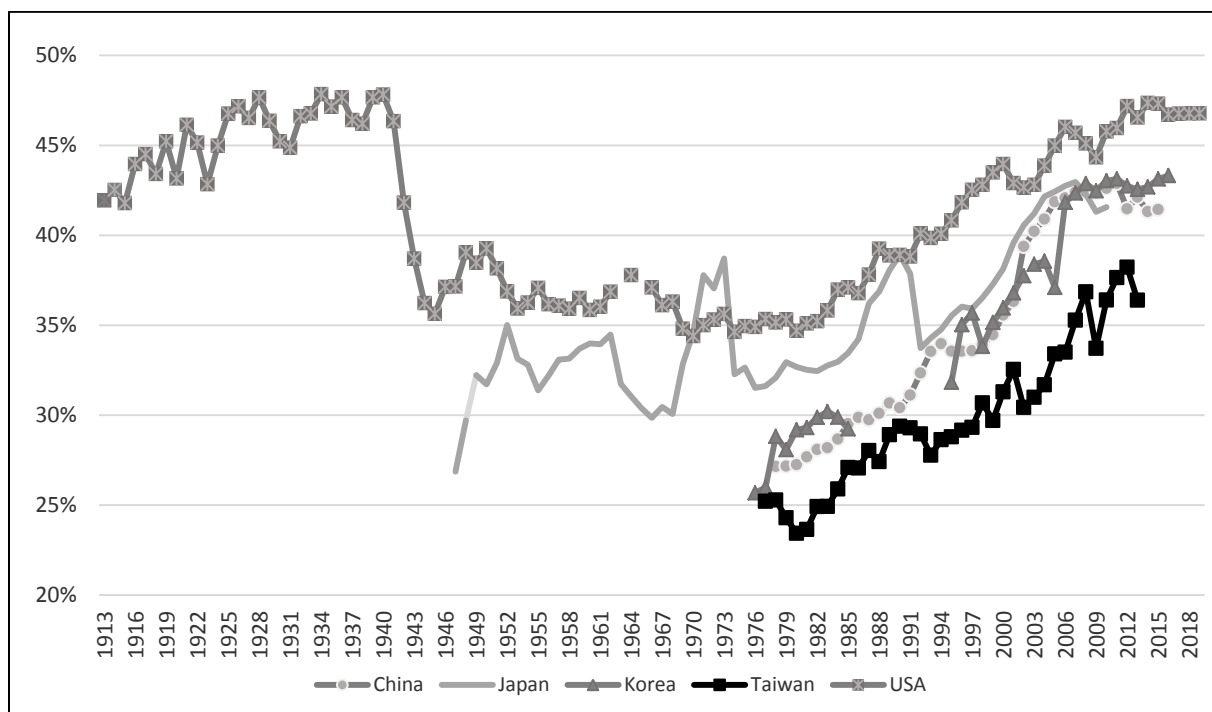
The largest difference between the two models probably lies in the so-called “Asian values”, especially the priority of collective interests over interests of the individual. Whereas

classic Western economics emphasize the Pareto optimality that can be achieved at any level of inequality, the East Asian model prioritizes solidarity, harmony, and social peace.<sup>8</sup>

The core feature of the East Asian model is a statistically measurable indicator of *low income and wealth inequalities*. It is argued that an economic model based on “Asian values” maybe the one that ensures greater social cohesion of societies and more successful catch up development.<sup>9</sup>

*Income and wealth inequalities in East Asia are lower than in Latin America (LA) and Sub-Sahara Africa (SSA).* Gini coefficients of income distribution in East Asian countries are usually below European levels (that stand at around 40%) and the share of the top 10% income group is lower than in the USA (Figure 2). In China, the Gini coefficient of income distribution is above 40%, but China is so large that it should be compared with Europe as a whole or at least with the United States.<sup>10</sup>

**Figure 2. Share of top income group in total income in the United States and some East Asian countries, %**

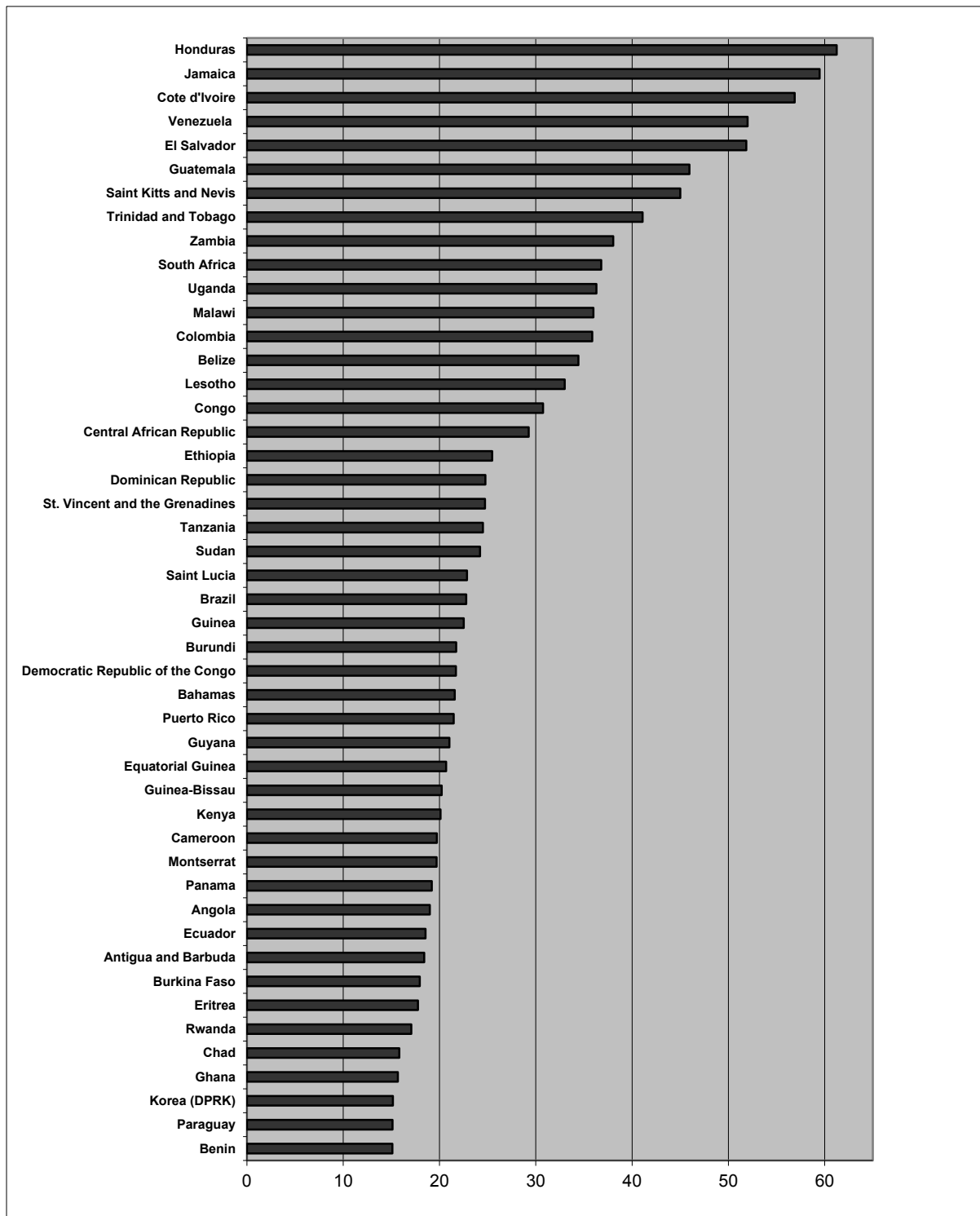


Source: World Inequality Database. URL: <https://wid.world/data>.

If the distinction is made between inequalities *within* countries/provinces and inequalities *between* countries/provinces, the results would be very telling. In China (with its 29 provinces), the general Gini coefficient of income inequality was over 40% with 24 p.p. (percentage points) coming from disparities between provinces. In the United States, the inequality coefficient was similar (over 40%), but only 6 p.p. came from disparities in income between states. In the EU (27 member states), the Gini coefficient in 2005 was about 40% with 23 p.p. coming from inequalities between members. If China manages to reduce the

income gap between its provinces to a level close to disparities between the U.S. states, its general inequality between citizens will fall to quite a low level.<sup>11</sup>

**Figure 3. Murder rate in countries with over 15 murders per 100,000 inhabitants (2008)**



Source: World Health Organization (WHO).

Lower income inequalities make societies less polarized and are usually associated with *stronger institutional capacity of the state*. The latter, according to a narrow definition, is the ability of a government to enforce laws and regulations. While there are a lot of subjective indices (corruption, rule of law, government effectiveness etc.) that are supposed to measure the state institutional capacity, many researchers do not think they help to explain economic performance and consider them biased.<sup>12</sup>

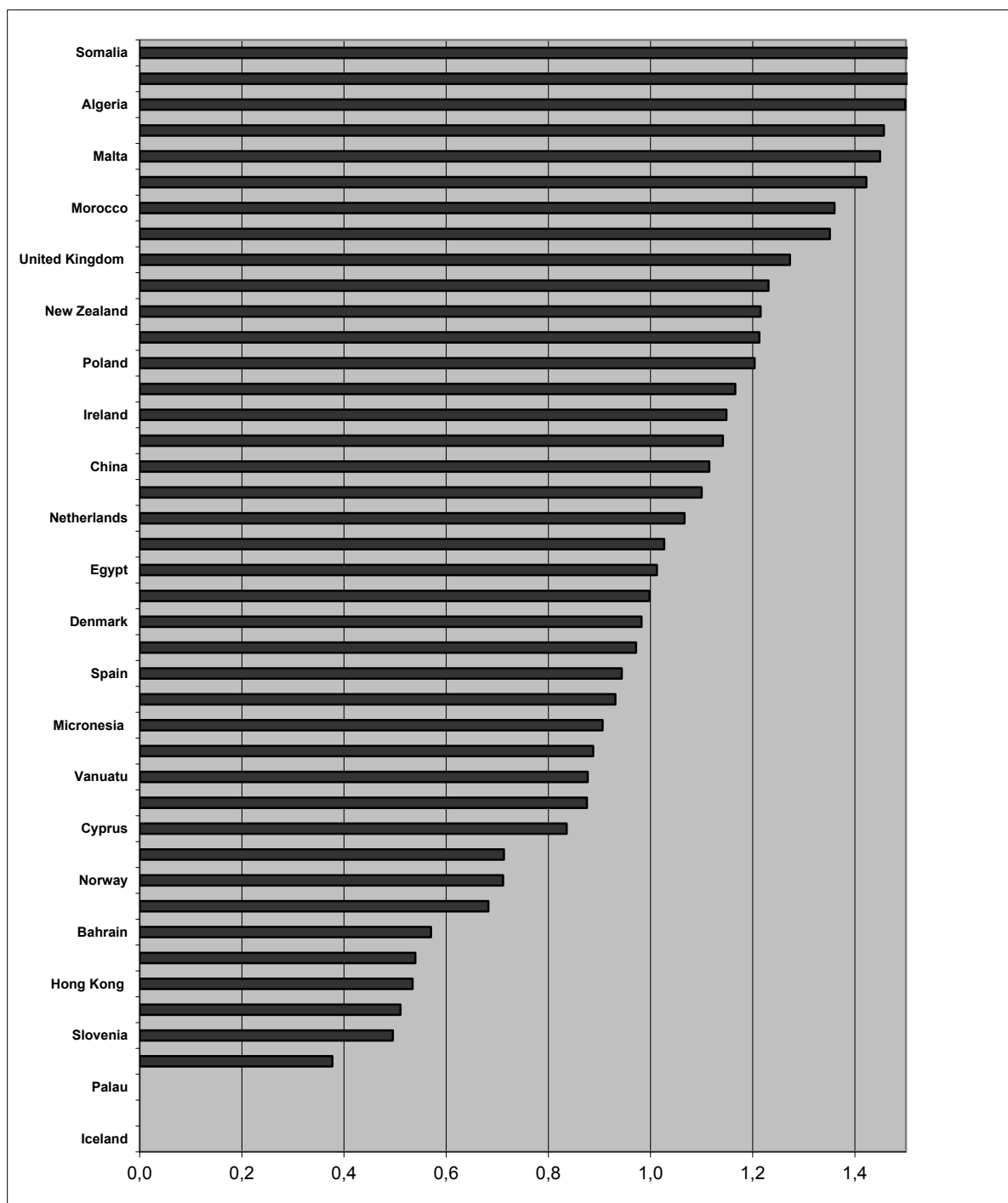
The natural objective measures of *the state institutional capacity* are the *homicide rate* – non-compliance with the state’s monopoly for violence,<sup>13</sup> and the *shadow economy* – non-compliance with the economic regulations. On both counts, Asia and MENA show very different picture from LA and SSA: they have one of the lowest indicators in the developing world if compared to that of developed countries (Figures 3, 4, 5). In China, for instance, there are only one-two murders per 100,000 inhabitants against one–two in Europe and Japan and five in the US. Only few developing countries, mostly in the MENA region, display such low homicide rates. They are normally higher by the order of magnitude, as it is observed in LA, SSA, and many post-Soviet states. The same applies to the shadow economy: it accounts for less than 17% of the Chinese GDP (a level that is lower than that in Belgium, Portugal, and Spain), whereas in developing countries the share typically amounts to 40%, sometimes even over 60% (Figure 5). Only few developing countries – in particular, Vietnam and some MENA countries (Iran, Jordan, Saudi Arabia, Syria) – have such a low share of shadow economy.

Finally, the *structure of property and control over business companies* in the West and in East Asia are different. Owners of firms in Asia are usually described as stakeholders, whereas in the United States or the UK the ownership is quite dispersed over a large number of individual investors (shareholders).<sup>14</sup> Financial systems in East Asia are similar to the ones in continental European countries: banking systems are highly concentrated (“big three” / “big five”), large companies more often than not are controlled by stakeholders (financial institutions such as banks), and external financing for companies comes from banks and bond issuing rather than from the stock market.<sup>15</sup>

These features of the Chinese/East Asian model have emerged due to the specifics in their long-term development trajectories. The extraordinary success of China before the Opium Wars (mid-nineteenth century) and after the 1949 Liberation was due to institutional continuity<sup>16</sup> – the ability to proceed along the evolutionary path without breaking up traditional collectivist structures (in line with “Asian values”). In a sense, Deng Xiaoping’s famous “feeling for the stones while crossing the river” reform strategy is deeply rooted in the millennium-old Chinese tradition and represents this institutional continuity. On the contrary, other developing countries (Latin America, Sub-Sahara Africa, the Russian empire) chose (sometimes non-voluntarily due to colonialism) to replicate the Western route and, among other things, destroyed agricultural communities and allowed the rise in inequality. This resulted in the increase in savings and investment rate that speeded up economic growth, but only at a price of weakened institutional capacity of the state and growing social tensions.<sup>17</sup>

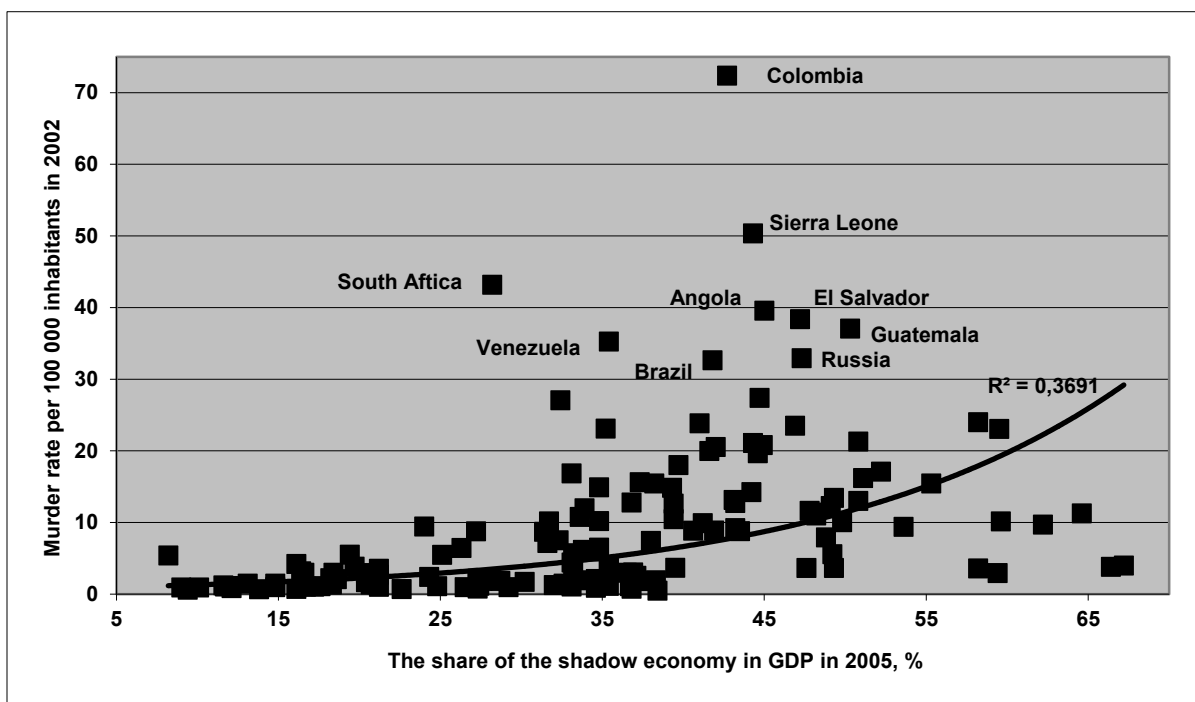


**Figure 4. Homicide rate in countries with less than 1.5 homicides per 100,000 inhabitants (2008)**



Source: WHO.

**Figure 5. Share of the shadow economy in GDP, % (2005)  
and the homicide rate per 100 000 inhabitants (2002)**



Sources: WHO; Schneider F. Shadow economies and corruption all over the world: new estimates for 145 countries // Economics: Open Access, Open Assessment E-Journal. № 9. 24 July 2007.

The argument is that East Asia and China in particular found another and more painless exit from the Malthusian trap. Western countries broke traditional collectivist institutions at a low level of development (in the sixteenth to eighteenth century) and experienced painful income redistribution in favor of the rich (rising income and wealth inequality). This allowed the share of savings and investment in income, capital/labor ratio, and productivity to rise, but only at the price of high income inequality associated with deteriorating quality of institutions and increased mortality coupled with low income levels. China retained traditional institutions and low income inequality for nearly five hundred years longer than the West, until technical progress allowed productivity and the share of investment in income to increase without causing mass deprivation of the population.<sup>18</sup>

The East Asian model is better suited to dealing with emergencies like natural disasters and pandemics. Such factors as universal health care systems, relatively low income inequalities, and readiness to sacrifice the interests of particular companies and individuals for the greater good of the society as a whole allowed East Asian countries to limit the damage from coronavirus pandemic and associated economic recession.

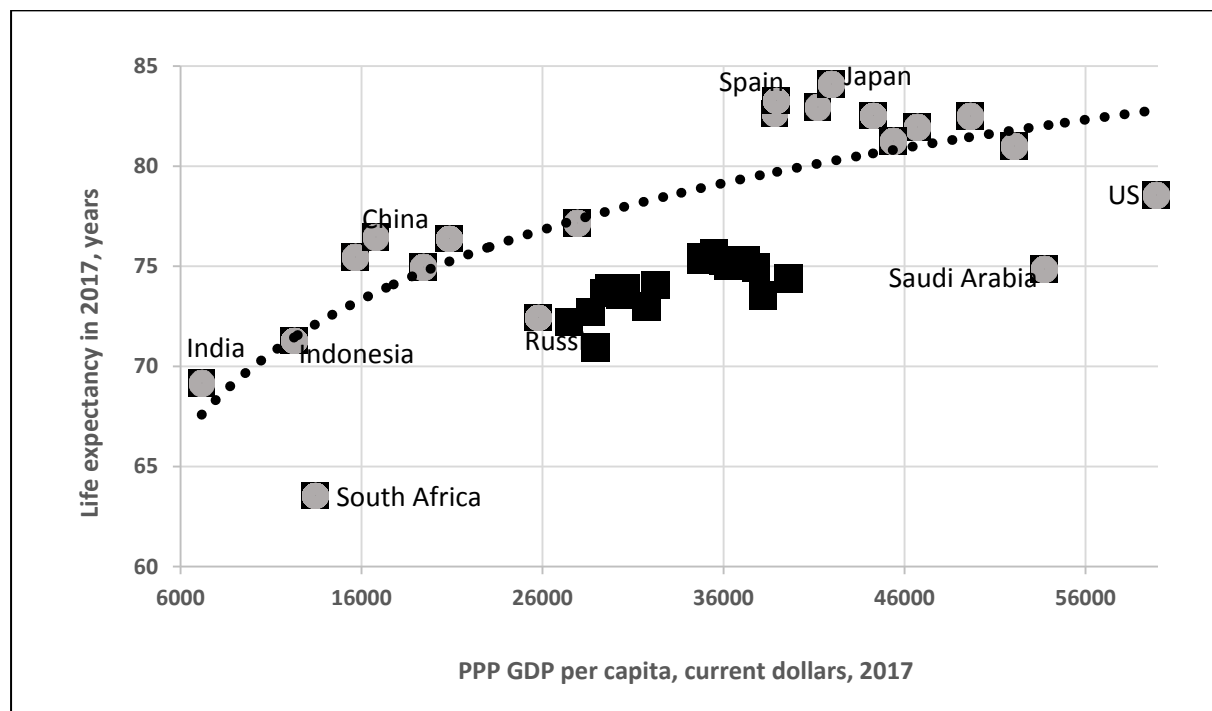
### **III. Keeping people healthy**

It is widely accepted by experts in public health economics that health care is an area with a lot of externalities: social returns from investments into health care are greater than

private returns and hence such investments should be financed by the state. The same applies to national spending on health care: global benefits from health care spending are greater than national benefits, whereas the costs of underinvestment into national health care system are borne not only by the country in question, but by the world as a whole. From this point of view, East Asian and European universal health care systems look much more efficient than those in the United States and in many developing countries.<sup>19</sup>

First, *life expectancy in East Asia and in some European countries is higher than it could have been predicted on the basis of per capita income*. As Figure 6 suggests, there is a strong correlation between per capita income and life expectancy, but some countries are doing better than others. China, Japan, and many EU member states have higher life expectancy than their income per capita suggests, whereas South Africa, Russia, Saudi Arabia, and the United State have lower life expectancy than could be predicted given their purchasing power parity (PPP) per capita GDP. This usually happens when national incomes are distributed unevenly and when the quality of access to the healthcare system is different for the rich and the poor. As Figure 7 demonstrates, there is an obvious negative relationship between life expectancy and income inequalities, as measured by the Gini coefficient of income distribution, even without control for the level of development.

**Figure 6. Life expectancy and PPP GDP per capita in G20 countries (2017)**

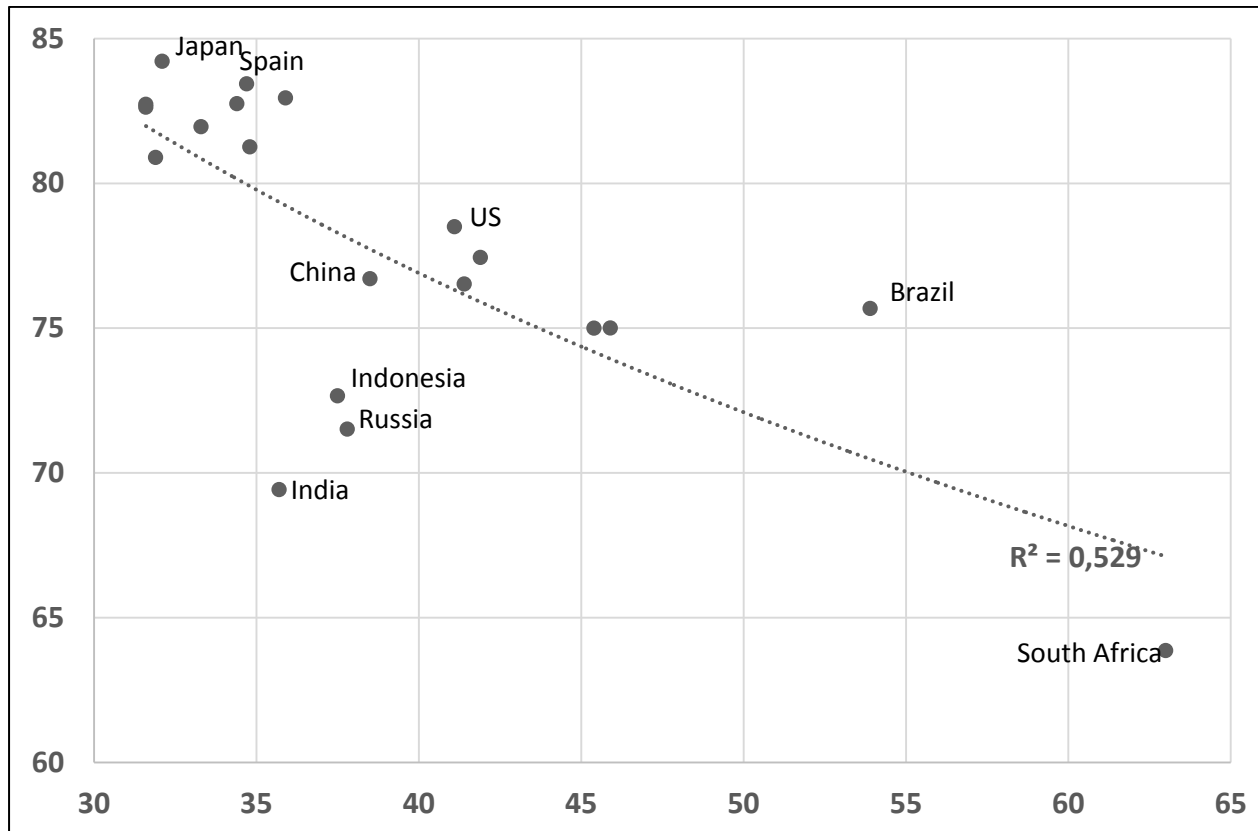


Source: World Development Indicators, World Bank

In general, in former communist countries income inequalities were low and the access to health care was free and generally universal. Even after the mortality crisis of the 1990s, life expectancy in former communist countries was on average five years higher than in other countries with the same level of development.<sup>20</sup> In China, universal access to health

care that existed before the 1979 market liberalization reforms was reduced in 1980–1990s, but was later strengthened again, with the creation of the national health care insurance system and especially following the 2002–2004 SARS epidemic. In the USSR in the 1960s, life expectancy reached 70 years (nearly the same as in much richer developed countries), but in the 1990s there was a mortality crisis associated with the transition to the market economy and life expectancy declined for over five years.<sup>21</sup>

**Figure 7. Life expectancy and the Gini coefficient of income distribution in G20 countries (2018 or last available year)**

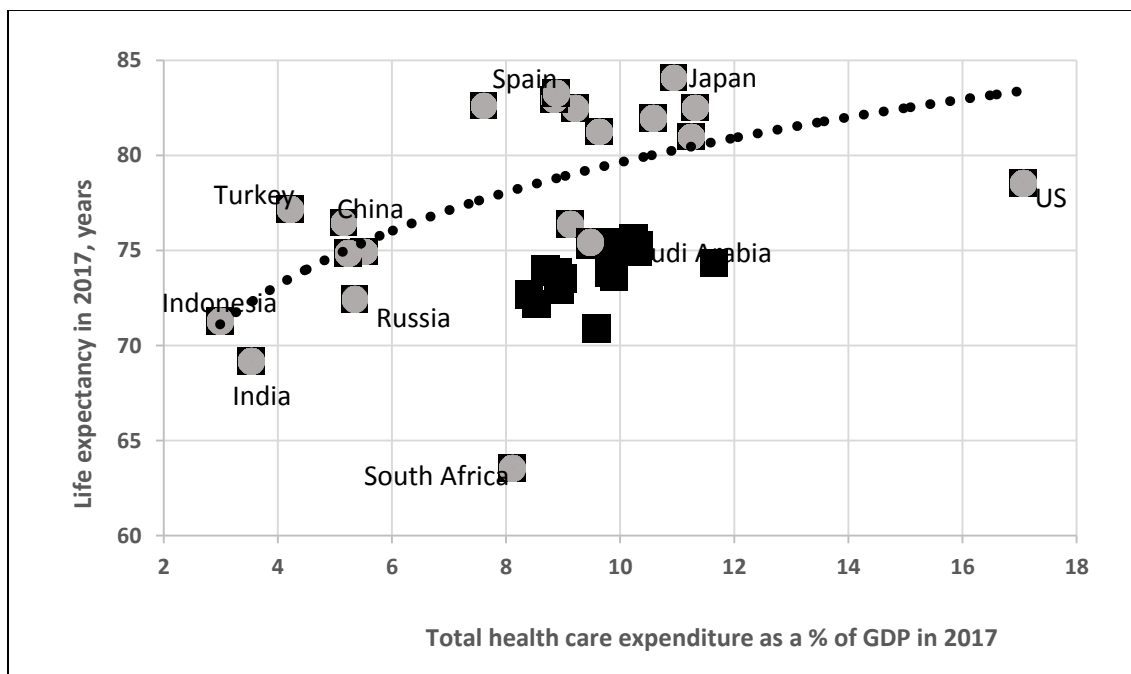


Source: World Development Indicators, World Bank.

Second, *efficiency of a health care system can be measured by comparing health care spending and life expectancy*. As Figure 8 shows, there is a correlation between total health care spending as percentage of GDP and life expectancy. However, South Africa, Saudi Arabia, and the United States are below the regression line, i. e. their health care spending produces worse results in increasing life expectancy than it is the case in other countries. The reason is usually the same – health care spending is not distributed evenly among the populations, so that the rich have better access to health care than the poor. Figure 9 shows the relationship between the share of government in total (public and private) health care spending and per capita income: generally, the share of the government increases with the rise in per capita income. There are some outliers though: in India, Brazil, South Korea, Saudi Arabia, and the United States, shares of private financing are higher than in countries

with similar levels of economic development. For countries with the relatively even income distribution (e. g. South Korea), this pattern cannot move the life expectancy below the trend (Figure 6), but for other countries it reduces the efficiency of health care spending and lowers life expectancy. South Africa, with one of the most uneven income distributions in the world (the Gini coefficient exceeds 60%), is a case in point: over half of its relatively high health care spending (8% of GDP) comes from the government (Figures 8 and 9). Even though this indicator is higher than in countries with similar income levels, it is not enough to raise South African population's life expectancy (just 64 years) to the level of countries with similar per capita incomes, such as Indonesia, with its life expectancy of 71 years (Figure 6).

**Figure 8. Life expectancy in years and total health care expenditure, % of GDP in G20 countries (2017)**



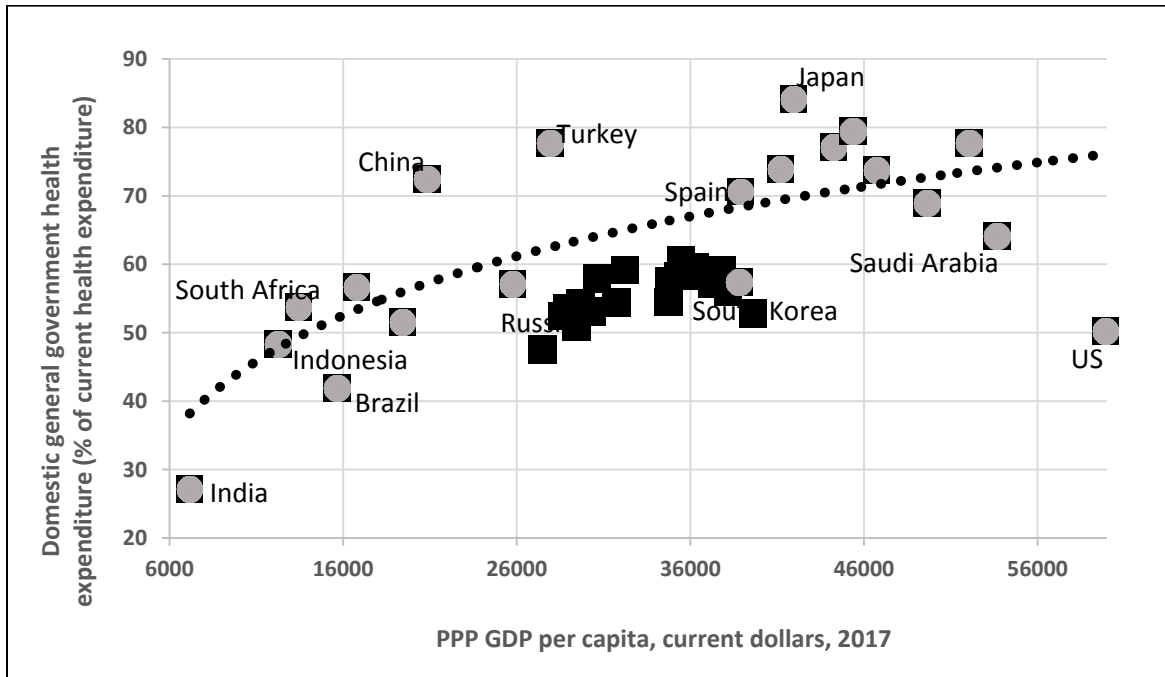
Source: World Development Indicators, World Bank.

Finally, *the capability of national governments to introduce quarantines and isolate infected individuals in case of an epidemic appears to be much greater in East Asia*. At the time of writing (September 2020), the coronavirus pandemic was not over and therefore the analysis of the relative performance of countries was yet to be completed and lessons to be derived. As preliminary statistical data suggests, the COVID-19 death rates by country differ by two orders of magnitude: from several to several hundred per one million of inhabitants (Figure 1).

China was first country to bring the pandemic to a nearly complete halt via strict, consistent and highly efficient measures of tracking, placing under quarantine, and treatment of infected persons. By September 2020, the total number of infected in China was only 80,000 (fewer than 60 per 1 million against 20,000 / million in the USA) and the total number of deaths was fewer than 5000 (fewer than 3 per 1 million against nearly

600 / million in the USA). After the new outbreak in the Xinfadi market in June 2020 (with only several dozen new cases), the community transmission was brought to a halt again. Since that time the daily numbers of new cases did not exceed several dozens, all of which were imported from abroad and immediately brought under control.<sup>22</sup>

**Figure 9. Government health expenditure (% of total health expenditure) and PPP GDP per capita in G20 countries (2017)**



Source: World Development Indicators, World Bank.

U.S. President Donald Trump and Secretary of State Mike Pompeo repeatedly blamed China for the damages caused by the COVID-19 pandemic, but in fact it is the United States, with its poor record of fighting the pandemic, that should be held responsible for not acting more efficiently. If the Responsibility to Protect (R2P) concept is extended to the public health domain, the performance of the country that spends more than other countries on health care as percentage of GDP (17%), but does not have a universal health care insurance system and lags behind in terms of life expectancy, would be considered substandard.<sup>23</sup>

If there is a global benevolent social planner or even if the international community (the UN, the WHO) adopts R2P principles with respect to health care systems, China would deserve praise, whereas the U.S. performance would be considered poor and detrimental to the global health status. At present, this kind of comparative / relative performance cannot have any legal consequences unless there are new international treaties and new powers are given to the UN and the WHO. But such comparisons can still impose important moral obligations on respective countries.

#### IV. Coping with economic recession

Many economists have already suggested that COVID-19 global crisis will give an additional push to the growing involvement of the state into economic and social life. In words of Dani Rodrik, “there is nothing like a pandemic to highlight markets’ inadequacy in the face of collective-action problems and the importance of state capacity to respond to crises and protect people”.<sup>24</sup>

One area where greater involvement of the state is both desirable and likely is the use of industrial policy as the counter-cyclical tool for fighting the downturns. The coronavirus recession is different from most previous postwar recessions. It is caused by the supply shock, not by the demand shock, and the policies to bring the economy back to the equilibrium with full employment should differ from traditional Keynesian fiscal and monetary stimuli.<sup>25</sup>

East Asian countries, especially China, seem to be doing better than others not only in fighting the pandemic, but also in overcoming economic recession. Their experience in economic policymaking may be no less valuable than that in the public health domain.

Economists distinguish between **demand driven recession** and **supply side recession**. The former is due to the shocks of demand. For instance, entrepreneurs decide to cut their investments on whatever reason or foreign countries stop purchases of national products, so exports go down, or households decide to postpone purchases of consumer durables. In this case the government can step in to stimulate effective demand through the expansionary fiscal and monetary policy – a standard recommendation in the framework of the Keynesian stabilization policy.

A supply side recession is usually associated with the increase in costs of production (wage increases, growing prices of imported materials, extra costs due to emergencies or calamities such as earthquakes, epidemics, wars, etc. creating bottlenecks in supplies and raising the costs of production and delivery). A specific case of the supply side recession is structural recession caused by the need to reallocate resources, labor and capital from one industry/region to another.<sup>26</sup>

In the process of economic development, structural shifts happen all the time. An example is the transition from producing musical records to cassette tapes and then to CDs, DVDs, iPods, and smartphones – all due to the introduction of new and better audio technologies. If these shifts are gradual and small-scale, they do not cause recession. But when there a need for a sudden large-scale structural shift emerges, this can lead to recession, because time and efforts are needed to reallocate resources from vanishing industries to emerging ones. Industrial output contraction in outgoing industries is not immediately compensated by production increase in newly emerging industries.

The infamous “cotton famine” crisis of the 1860s in Britain is a clear example of such a structural recession. Due to the Union’s blockade of the Confederacy during the Civil War in the United States, raw cotton from the Southern states stopped flowing freely into Britain and prices of cotton went up by several hundred percent. Textile industry of Lancashire, the backbone of British industry at the time, faced increased costs and experienced sharp downturn, and total British GDP fell: in 1862 it was over 6% lower as compared to 1860.<sup>27</sup>

Another example is postwar recessions associated with the conversion of defense industries. They occurred when defense production after the war was curtailed, but defense

industries could not be quickly converted to production of civil goods. After the Second World War, the U.S. GDP was going down for three years (1945–1947) and in 1947 it was 13% lower than in 1944.<sup>28</sup>

Recent recessions in Western countries, associated with oil price peaks in 1973, 1979, and 2007, are examples of poorly managed structural shifts. In a market economy, the adjustment occurs through an increase in unemployment: industries that become unprofitable due to increased costs laid off workers, growing unemployment contributed to decline in wages, and only later cheap labor costs made it profitable to expand production in other industries.

One could imagine government policies designed to make domestic price changes for fuel and energy very gradual, so that energy consuming enterprises could adjust by switching to energy saving technologies without cutting output. Also, special subsidies can be given to companies to facilitate “green restructuring”. However, without government assistance in stretching the transition period and providing stimuli for new investment, structural shifts may be difficult, painful, and costly.

The transformational recession that occurred in post-communist economies in the 1990s is another example of poor management of structural shifts.<sup>29</sup> They involved the decline of agriculture and manufacturing, on the one hand, and the rise of services (trade and finance) and resource industries, on the other. In many of these countries, the reduction of output during this transition was larger than the one that occurred in the Great Depression of the 1930s.

In case of the structural recession, traditional Keynesian stimuli – fiscal and monetary expansion – may only be helpful to some extent. Increase in governmental purchases of particular goods and services should lead to increase in prices and, perhaps, in production. In theory, the slump in travel, tourism, public catering, and hotel businesses could be overcome by expansionary fiscal and monetary policy at the price of higher inflation. However, the necessary precondition for the multiplier process to unfold is the existence of unloaded production capacities and unemployment. The demand stimuli that are enacted simultaneously with the supply prohibitions for many businesses can only result in price increases. As Paul Romer and Alan Garber write, “loan guarantees and direct cash transfers will stave off bankruptcy and default on debt, but these measures cannot restore the output that is lost when social distancing keeps people from producing goods and services”.<sup>30</sup>

A quicker and more efficient solution to elimination of “bottlenecks” (supply constraints) is assisting and even carrying out mandatory reallocations of labor and capital. In case of the coronavirus pandemic this covers a wide range of facilities from ones affected by the epidemic prohibitions (travel, tourism, retail trade, sports events, restaurants, entertainment, etc.) to ones maintaining public health public, public order, and production of medical supplies.<sup>31</sup>

It is irrational to allow both unemployment and shortage of labor force (needed to produce medical protective equipment) and/or, like it happened in Europe, to combine unemployment with shortage of agricultural workers for seasonal activities.<sup>32</sup> In view of the future structure of the economy, the coronavirus crisis should be seen as an opportunity to make much needed investment into personnel retraining and capacity building in the health care systems making them truly universal and capable to prevent and cope with any epidemics and pandemics.



Quite a few successful examples of managing structural shifts can be found in East Asia, where collective interests are a high priority and governments are not afraid of resorting to market intervention and direct investment in times of crises. These interventions came in the form of the industrial policy, sometimes carried out through economic stimuli and sometimes even via heavy handed direct administrative orders. In China (including Hong Kong and Taiwan) and South East Asian countries, it was obviously facilitated by the lessons of the by September 2020 SARS epidemic and by restructuring health care systems that were carried out afterwards.

In China, the production of protective masks increased from 15 million a day in early February 2020 to over 100 million a day by the end of the same month. Over 3000 enterprises that previously had nothing to do with the supply of healthcare products began producing masks, protective suits, sanitizers, and other hygiene goods. Several major companies began to make masks at their enterprises: China Petroleum and Chemical Corporation, China National Machinery Industry Corporation, as well as major auto manufacturers Shanghai GM Wuling, Guangzhou Automobile Group, and BYD.

The South Korean Ministry of Food and Drug Safety gave emergency approval to company “Seegene” for mass production of a coronavirus test kit that it had developed in three weeks. All of 395 employees of the company dropped all other work and focused on making test kits, with even molecular biologists and senior scientists working at the assembly line.

The Vietnamese “Vingroup” was reported to be able to convert its automobile and smartphone factories into the production of 55,000 medical ventilators *per month* in a period of three months. In comparison, the *total* stock of the U.S. ventilators in March 2020 was estimated at 62,000 for new models and about 100,000 for old models. The total number of ventilators available in the UK at a time was just 21,000.

In Western countries, non-defense industries were converted into production of defense items in times of war. In most countries this happened with state support that facilitated and sped the transition. Before and during World War II, governments normally increased taxes and borrowings and used the proceeds to purchase weapons. In the United States, the increase in defense procurements following the 1937–38 recession caused a boom — economic growth that went from negative values in 1938 to the 17–20% growth annually in 1941–1943. Never before and never after the American economy was growing that fast.

Even better results were achieved by centrally planned economies that have advantages over market economies in mobilizing domestic savings, converting them into investment, and promoting structural shifts quickly and with full employment. In the 1930s–1940s, on the eve of and during the World War II, the USSR transferred huge resources from agriculture to industry, from light to heavy industry, and from non-defense to defense industries. In 1940, Germany produced two times more steel and more military output than the Soviet Union, but by 1943, the USSR had already surpassed Germany in producing tanks, aircraft, and artillery guns. This structural shift was the most crucial reason that changed the course of the war.

To summarize, the nature of coronavirus recession is a supply side shock requiring structural shifts to overcome it: transfer of capital and labor from temporary closed travel, hospitality, and other industries affected by administrative restrictions to other sectors, mostly to public health and safety. The ability of countries to move resources rapidly from

non-health to health-related industries is a crucial factor not only for fighting the epidemic, but also for fighting the recession.

If countries rely on market mechanisms alone (like most Western countries do), the increase in government orders for the ventilators should produce an increase in prices that is large enough to cover the costs of conversion and to ensure higher profitability to compensate for the risk. Only then one can expect that enterprises will introduce second and third shifts to expand their production of ventilators at the specialized plants and will make investment into conversion of non-profile capacities into production of ventilators. The faster and more efficient alternative used in East Asia is enactment of legislation (such as Defense Production Act) to force private enterprises to switch to the production of needed equipment, regardless of prices and costs.

An extreme example of forced reallocation of resources is the labor armies created by Soviet Russia during the Civil War in 1920 and often employed between battles. Such labor armies are hardly possible today, but public work programs are possible, whereas betting only on market forces to ensure equilibrium is a suboptimal approach.

The experience of East Asia has already proved that states' capacity to cope with the current coronavirus recession depends to a large extent on how governments are supporting markets in carrying out structural shifts. As the world economy entered the global recession in 2020, it may be prudent for policymakers to promote more active state-interventionist industrial policy based on past and present successful Asian cases. Encouraging and assisting the transfer of resources from recreation, travel, and hospitality industries to health care and epidemic prevention facilities may be good not only for overcoming the current recession, but also for building stable and resilient economies and social structures for the future.

## **V. Conclusion**

East Asian economic model is superior to other models in the Global South at least in terms of the catch-up development and possibly even in terms of innovations beyond the technological frontier. The East Asian model is based on solidarity and priority of collective interests over individual interests, whereas the Western model emphasizes competition and guarantees of individual rights. The crucial features of the East Asian economic model are relatively low income and wealth inequalities, strong state institutional capacity (as measured by homicide rates and share of shadow economy), high level of patriotism, and trust in the government institutions.

In the future, at least *three scenarios* are possible: convergence of the West with the Asian model, convergence of East Asia with the Western model, or the continuing divergence of the two models.

With the global proliferation of the Chinese model, the West and other developing countries can try to learn from the East Asian experience and to reform their models in the direction of greater solidarity and respect to collective interests. The world has a lot to gain from such a cooperation trajectory. The proliferation of East Asian model in the West and in the developing world would create better conditions for the catch-up development of the Global South and will lead to profound changes in the world economic order.

East Asia may transform itself in the direction of the Western model (in terms of marketization, privatization, and growing focus on individual rights at the expense of

collective interests). This, in contrast, will undermine the successful catch-up development and eliminate the East Asian model as the main alternative to the Western model. It may slow down the growth of the Global South and prevent reduction of the inequalities in the global economy.

If the Western strategy continues to significantly differ from, or oppose, the Asian solidarity model and to insist that the Western model is superior and should not be reformed, this could lead to the loss of the competitiveness by the West and may have potential for exacerbating tensions and conflicts between different social systems.

## ENDNOTES

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<sup>1</sup> Popov V., Jomo K. Are developing countries catching up? // Cambridge Journal of Economics. V. 42. № 1. 2018. P. 33–46.

<sup>2</sup> Some developing countries became rich not due to rapid economic growth, but because of improved terms of their trade as a result from increased relative prices for their export goods. The best known example is oil exporting states of the Persian Gulf: with the exception of Oman, these countries did not enjoy high growth rates of physical output, but their per capita income approached the level of developed countries due to increase in oil prices since 1973.

<sup>3</sup> In 1920s–1970s, the USSR and East European countries were catching up with the developed countries, but later they slowed down considerably and, in the 1990s, experienced transformational recession. In 1950–2020, high average growth rates (over 3% of per capita GDP annual growth) in developing world, in addition to East Asia, were observed in Botswana, Israel, and Oman.

<sup>4</sup> EUROMOMO Graphs and Maps. URL: <https://www.euromomo.eu/graphs-and-maps>.

<sup>5</sup> Fukuyama F. The Pandemic and political order: it takes a state // Foreign Affairs. July/August 2020. URL: <https://www.foreignaffairs.com/articles/world/2020-06-09/pandemic-and-political-order>.

<sup>6</sup> Aghion Ph., Maghin H., Sapir A. Covid and the nature of capitalism // VoxEU. 25.06.2020. URL: <https://voxeu.org/article/covid-and-nature-capitalism>; GDP and Other Major NIPA Series, 1929–2012: II. Bureau of Economic Analysis. August 2012. URL: [https://apps.bea.gov/scb/pdf/2012/08%20August/0812%20gdp-other%20nipa\\_series.pdf](https://apps.bea.gov/scb/pdf/2012/08%20August/0812%20gdp-other%20nipa_series.pdf).

<sup>7</sup> The East Asian Miracle: Economic Growth and Public Policy. World Bank Report. 26 September 1993. – Washington D.C.: World Bank, 1993. URL: <http://documents.worldbank.org/curated/en/975081468244550798/Main-report>.

<sup>8</sup> “The Western liberal approach to *inclusive capitalism* is the theory of the *welfare state* which has been developed by the mainstream economics in the tradition of Hobbes, Locke, Smith and J.S.Mill. However, there is another European tradition of the welfare state apart from Western liberalism, which may find a more appropriate way to connect to the Chinese economic model based on *tianxia*. Leibnitz, Rousseau, and Kant have conceived elements of an inclusive and hospitable political and economic world order which comes, at least partly, close to *tianxia*”. See Heller P. Entrepreneurship in the context of Western vs. East Asian economic models // The Dialogue of Civilizations (DOC) Research Institute. Berlin. 21.09.2020. URL: <https://doc-research.org/2020/09/entrepreneurship-context-western-vs-east-asian-economic-models>.

<sup>9</sup> Popov V. Mixed Fortunes: An Economic History of China, Russia and the West. – Oxford: Oxford University Press, 2014.

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- <sup>10</sup> The population of three Chinese provinces (Guangdong, Shandong, Henan) exceeds 95 million, and of another seven provinces – 50 million (that is bigger than populations of most countries). Thus, China should be compared with multistate regions, such as the European Union or ASEAN, rather than with particular states.
- <sup>11</sup> Milanovic B. Does Economic Inequality Set Limits to EU Expansion? Presentation at conference on “Sovereign Insolvency”, Jean Monnet Inter-University Centre of Excellence Opatija, Coratia, November 2012.
- <sup>12</sup> Popov V. Is the Chinese Variety of Capitalism Really Unique? Munich Personal RePEc Archive (MPRA) Paper № 28109. January 2011. URL: <https://ideas.repec.org/p/pra/mprapa/28109.html>; Popov V. Developing New Measurements of State Institutional Capacity. PONARS Eurasia Policy Memo № 158. May 2011. Program on New Approaches to Research and Security in Eurasia [Washington D.C., Elliott School of International Affairs, George Washington University]. URL: [https://www.ponarseurasia.org/sites/default/files/policy-memos-pdf/pepm\\_158.pdf](https://www.ponarseurasia.org/sites/default/files/policy-memos-pdf/pepm_158.pdf).
- <sup>13</sup> Crimes are registered differently in different countries: higher crime rates in developed countries seem to stem from better registration of crimes. Yet grave crimes, like homicides, appear to be registered quite accurately even in developing countries, so international comparison of homicide rates is well-warranted.
- <sup>14</sup> Lee K. Varieties of Capitalism and Re-thinking East Asian Model of Economic Growth after the COVID-19 Pandemic: Rebalancing Shareholder and Stakeholder Capitalism. DOC Research Institute. November 2020. URL: <https://doc-research.org/2020/09/varieties-capitalism-rethinking-east-asian-model>.
- <sup>15</sup> Popov V. The financial system in Russia as compared to other transition economies: the Anglo-American versus the German-Japanese model // *Comparative Economic Studies*. V. 41. № 1. 1999. P. 1–42.
- <sup>16</sup> Popov V. Mixed fortunes: An Economic History of China, Russia and the West.
- <sup>17</sup> Ibid.
- <sup>18</sup> Ibid.
- <sup>19</sup> Popov V. Global Health Care System after Coronavirus: Who Has Responsibility to Protect. 20 May 2020. URL: [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3606381](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3606381).
- <sup>20</sup> Popov V. Mortality crisis in Russia revisited: evidence from a cross-regional comparison // *When Life Expectancy Is Falling: Mortality Crises in Post-Communist Countries in a Global Context*. Ed. V. Popov. – Hauppauge (N.Y.): Nova Publishers, 2020.
- <sup>21</sup> Ibid.
- <sup>22</sup> COVID-19 coronavirus pandemic // Worldometer. URL: <https://www.worldometers.info/coronavirus/country>.
- <sup>23</sup> Popov V. Global Health Care System after Coronavirus.
- <sup>24</sup> Rodrik D. Making the best of a post-pandemic world // Project Syndicate. 12.05.2020. URL: <https://www.project-syndicate.org/commentary/three-trends-shaping-post-pandemic-global-economy-by-dani-rodrik-2020-05?barrier=accesspaylog>.
- <sup>25</sup> Popov V. Learning from Asia: How to Handle Coronavirus Economic Recessions. PONARS Eurasia Commentary. 28.04.2020. URL: <https://www.ponarseurasia.org/article/learning-asia-how-handle-coronavirus-economic-recessions>.

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<sup>26</sup> The theoretical framework is the AS-AD model (see, for instance: Mankiw N. Macroeconomics. 6th ed. – N.Y. Worth Publishers, 2006). The positively sloped AS curve characterizes positive relationship between output and prices (the higher the prices, the larger the supply of goods), whereas negatively sloped AD curve characterizes the negative relationship between the demand for goods and prices. The negative demand shock moves the AD curve to the left, but luckily, the government and the central bank can respond to the shock by expansionary fiscal and monetary policy and can return the AD curve back at its initial position. The negative supply shock moves the AS curve to the left (adverse supply shock). Increase in costs forces the entrepreneurs to increase prices to compensate for increased costs, but at higher prices they can sell less output (so the AS curve moves to the left). The government does not have the powers to affect the position of the supply curve in the short run. The only thing the authorities can do is to restore the output is to increase the aggregate demand (moving the AD curve to the right, restoring output at a cost of higher prices). This is called the absorption of the adverse supply shock. See Popov V. Learning from Asia: How to Handle Coronavirus Economic Recessions.

<sup>27</sup> Maddison Project Database. Version 2018 by J.Bolt, R.Inklaar, H. de Jong, and J. Luiten van Zanden. Groningen Growth and Development Centre, University of Groningen, The Netherlands.  
URL: <https://www.rug.nl/ggdc/historicaldevelopment/maddison/releases/maddison-project-database-2018?lang=en>.

<sup>28</sup> GDP and Other Major NIPA Series.

<sup>29</sup> Popov V. Shock therapy versus gradualism: the end of the debate (explaining the magnitude of the transformational recession) // Comparative Economic Studies. V. 42. № 1. 2000. P. 1–57; Popov V. Why shock therapy may lead to worse performance than gradual transition // Beyond Transition Newsletter. V. 17. № 1. 2006. URL: <https://carleton.ca/vpopov/wp-content/uploads/Shock-vs-grad-reconsidered-Beyond-TransitionEnglish-full.pdf>; Popov V. Shock therapy versus gradualism reconsidered: lessons from transition economies after 15 years of reforms // Comparative Economic Studies. V. 49. № 1. 2007. P. 1–31.

<sup>30</sup> Romer P., Garber A. Will our economy die from coronavirus // New York Times. 23 March 2020.

<sup>31</sup> Popov V. Learning from Asia: How to Handle Coronavirus Economic Recessions.

<sup>32</sup> Workers of this kind were previously coming to more developed West European countries from less developed East European countries, but encountered difficulties crossing national borders in the Spring of 2020.

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