Michael Hudson v. George Soros on China's Rejection of "Market" Capitalism

Description

by Yves Smith via Naked Capitalism

Earlier this week, the Financial Times posted a comment by famed investor George Soros, Investors in Xi's China face a rude awakening. This article would have been very useful if it had stuck to its headline warning, which is more or less along the lines that Xi has made very clear that he's not going to allow investors, above all foreign investors, to exercise more influence in Chinese business and society.

However, Soros then goes on in a vein that the article subhead accurately summarizes: "The leader's crackdown on private enterprise shows he does not understand the market economy." Oh, contraire, China's success has been built on learning from the mistakes of other Asian countries that developed quickly but then fell prey to financialization, particularly Japan, and had difficulties making the transition from being export and investment led to consumption led.

In particularly, Soros is cheesed off at Xi restricting foreign investment, particularly in stocks. First, China is a capital exporter. It doesn't need foreign funds. Second, despite the Anglopshere idealization of public stock markets, China doesn't need one either, although getting rid of the one it has now would be messy and very disruptive.

As Amar Bhide pointed out in a landmark Harvard Business Review article, Efficient Markets, Deficient Governance, anonymous, freely traded shares inherently lead to poor governance. Public companies cannot share critical business information that investors need to make informed decisions. Transient shareholders also lack the motivation and means to improve the performance of the companies they've invested in. Bhide has pointed out in other venues that while all other types of investments, such as derivatives and venture capital, existed in pre-modern times, arms length share trading did not because stock is a legally vague and weak promise.

And despite the idealization of share ownership, it's almost entirely divorced from the funding of business. The most important source for new investment is retained earnings. Second is borrowing. Share sales are a distant third. The overwhelming majority of stock trading is shuffling paper among investors.

The most charitable interpretation of Soros' position is that he suffers from a China version of the saying attributed to Charles Wilson, "What's good for GM is good for America," which here becomes, "What's good for people like me of course is good for China." Except as Michael Hudson explains, it isn't.

Below are sections of the Soros article, with Hudson's remarks in bold italics:

> **Xi Jinping, China's leader, has collided with economic reality. His crackdown on private enterprise**

> [***what the classical economists called rent-seeking and unearned income***] **has been a significant drag on the economy** [***meaning the economy's polarization concentrating wealth and income in the hands of the richest One Percent***]. **The most vulnerable sector is real estate, particularly housing. China has enjoyed an extended property boom over the past two decades, but that is now coming to an end. Evergrande, the largest real estate company, is over-indebted and in danger of default. This could cause a crash.** [***That's just what is needed.*]**
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> **….One of the reasons why middle-class families are unwilling to have more than one child is that they want to make sure that their children will have a bright future.** [***This is true of every advanced nation today. It is most extreme in the neoliberalized countries, e.g., the Baltics and Ukraine – Soros's poster countries.***]

We have skipped over Xi's crackdown on the private tutoring industry…as if tutoring is essential to providing for security and an adequate standard of living for the next generation. How about strong public education, including remedial and advanced tracks, and vocational/technical training for those not bound to universities?

Back to Soros and Hudson:

> **Xi does not understand how markets operate** ***[meaning that he rejects rapacious rent-seeking, exploitative free-for-all, and shapes markets to serve overall prosperity for China's 99 Percent*]. **As a consequence, the sell-off was allowed to go too far** [***by which he means, too far to maintain the dominance of the One Percent; it seeks to reverse economic polarization, not intensify it***]. **It began to hurt China's objectives in the world** [***meaning America's neoliberal objectives for how it had hoped to make money for itself off China***].
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> **Recognising this, Chinese financial authorities have gone out of their way to reassure foreign investors and markets have responded with a powerful rally. But that is a deception. Xi regards all Chinese companies as instruments of a one-party state…**
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> **Pension fund managers allocate their assets in ways that are closely aligned with the benchmarks against which their performance is measured.** [***The tragedy of financializing pensions is that fund managers are rated on making money financially – in ways that hurt the industrial economy by promoting financial engineering instead of industrial engineering.***]
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> **Almost all of them claim that they factor environmental, social and corporate governance (ESG) standards into their investment decisions.** [***At least, that's what their public relations advisors advertise. Exxon claims to be cleaning up the environment by expanding offshore oil drilling in Guyana, etc. As for "social standards," the neoliberal mantra is trickle-down economics: by making our stock prices rise, by stock buybacks and higher dividend payouts, we are helping wage-earners earn a pension, even though we are offshoring and de-industrializing the economy, de-unionizing it and "freeing" the economy from consumer and workplace protection laws.***

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….The US Congress should pass a bipartisan bill explicitly requiring that asset managers invest only in companies where actual governance structures are both transparent and aligned with stakeholders. [*Wow. Such a bill would block Americans from investing in many American companies whose behavior is not at all aligned with stakeholders. What proportion: 50%? 75%? More?*] **This rule should obviously apply to the performance benchmarks selected by pensions and other retirement portfolios.**

If Congress were to enact these measures, it would give the Securities and Exchange Commission the tools it needs to protect American investors, including those who are unaware of owning Chinese stocks and Chinese shell companies. That would also serve the interests of the US and the wider international community of democracies. [***So Mr. Soros wants to block the US from investing in China. That is President Xi's objective also: China doesn't need U.S. dollars, and is in fact de-dollarizing.***]

There are a lot of reasons to criticize Xi and the Chinese regimes, but combatting foreign influence and a bit late in the game pushing back against high levels of inequality are not among them.

And Soros presents himself as having superior insight into China, and then acts as if an American strike on Chinese public companies would dent them. Good luck with that.