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China's Engagement with Neo-liberalism: Path Dependency, Geography and Party Self-Reinvention

LEONG H. LIEW

China's post-Mao market reform, even after the Asian crisis, does not conform to the standard IMF/World Bank model and the state continues to mediate market reform. Three principal factors have influenced how the state mediates China's market reform: path dependency, a result of China's communist and nationalist revolution; China's geography, which favours developmental-state-type industrialisation; and most important of all, the Chinese Communist Party's successful post-Mao self-reinvention that has enabled it to remain in power as a monopolistic party. These factors determine that China's engagement with neo-liberalism will be a loose hug rather than an intimate embrace.

I. INTRODUCTION

China's economic reform has been a resounding success. It has produced stellar economic growth that has made a huge dent in the numbers of Chinese people living in poverty. China's official estimates show that its economy grew at an annual rate of 9.7 per cent between 1978 and 1998 [*Lardy, 2002: 12*] and at an annual rate of 7.7 per cent between 1998 and 2002 [*NBSC, 2003: 27*].¹ In 1978, 60 per cent of China's population were below the international poverty standard [*World Bank, 1997a: 3*], but by 1996, the number of people living below the absolute poverty line had fallen to less than 6 per cent of the population [*World Bank, 1997b: 2*]. Some scholars like Stiglitz [*2002: 180–94*] saw China's economic reform as a policy challenge to the IMF/World Bank. China's approach to economic reform differs from

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the approach prescribed by the IMF/World Bank, but China's reform has produced outcomes better than outcomes of reform in countries in the Commonwealth of Independent States, which have followed more closely the IMF/World Bank prescription.²

The Asian financial crisis had a weaker impact on China than on many other countries in East Asia. The crisis initially appeared to increase the urgency among China's leaders to speed up liberal market reforms. But with China escaping relatively unscathed from the crisis, ironically due to its resistance to IMF pressure to open its capital account and allow free convertibility of the *yuan*, the earlier imperative has disappeared. Today it is 'business as usual'. In China 'business as usual' does not mean the status quo. Since the Chinese Communist Party (CCP) commenced market reform in 1978, China's economy has been transformed gradually from a centrally planned to a market economy. 'Business as usual' means that China's progression to a market economy has multiple contestable pathways and the form of market liberalism that is pursued continues to develop in ways that are contingent on China's history, geography and politics.

China's market reform programme contains elements of the two key pillars of the IMF/World Bank neo-liberal model – market liberalisation and privatisation.³ However, I argue in this article that China's market reform, while it contains these elements of the IMF/World Bank's market model, is mediated distinctly by the Party/State and modifies this model. The standard IMF/World Bank approach favours the free mobility of resources and use of 'undistorted' market prices, including wages, to allocate resources. According to this approach, a country's output is maximised when ownership of its resources is largely in private hands and the country allocates its resources according to its predetermined comparative advantage; public policy cannot alter a country's comparative advantage.⁴ Political interference with the market, state ownership and management of sectors of the economy and any form of strategic industry policy are incompatible with the model. Economic reform in China has created a market economy that departs sharply from this model.

One obvious departure is seen in the fact that state ownership remains significant in post-reform China. In 2001 state-owned and state-holding enterprises comprised 27.3 per cent of the total of industrial enterprises and produced 44.4 per cent of industrial output [*NBSC, 2002: 423*]. It is a market economy where the state continues to intervene actively to promote its political goals and where the state remains a strategist in industry policy. The state also remains tied to the CCP, limiting the scope of market reform to what is possible under prevailing Party ideology and requiring the state to protect the CCP's privileged market position so that the CCP can preserve its monopoly on political power.

I argue that three principal factors – China's history, China's geography and CCP self-reinvention – influence how the state mediates China's market reform. These factors are briefly outlined here, prior to a more detailed discussion of each. First, the CCP came to power through a communist and nationalist revolution. Although difficult, it is possible for a post-communist government to erase the legacy of communism. But it is impossible for any Chinese government, not least a CCP government, not to pay heed to Chinese nationalism and do whatever is necessary to preserve national unity – Xinjiang and Tibet are yet to be securely integrated within the PRC – and to prevent *de jure* independence for Taiwan. China's government also has to intervene heavily in the market because poor factor endowments – in Xinjiang and Tibet for example – that do not allow them to develop economically without state intervention and unequal economic development are considered likely to exacerbate ethnic tensions and are thus viewed as a serious threat to national unity.

The CCP, unlike the communist parties of Central and Eastern Europe (CEE), remains in power and therefore controls the process of transforming China from a centrally planned to a market economy. The path of liberal market reform in China is therefore very much restricted to what is possible given Party norms and beliefs. The CCP could never have contemplated the 'shock therapy' approach to marketisation adopted by the post-communist governments of CEE when it made the decision to reform China's economy in 1978. The post-communist governments of CEE knew their ultimate aim was to transform their planned economies to liberal market economies. This was not the case with the CCP in 1978; it never aimed to transform China's planned economy completely to a market economy. The market was to complement the plan, not to replace it (*jihua wei zhu, shichang wei bu*). It is the contradictions inherent in a plan–market system and the momentum of pent-up liberal forces when unleashed by reform that have gradually forced CCP's leaders to shift China's economy away from a plan towards a market economy.

Second, China's geography bestows upon the Chinese state certain advantages and disadvantages in its approach to and links with the global economy. These incline the Chinese economy away from the standard IMF/World Bank liberalisation model. Market reform in China has propelled the size of China's economy to number three or two, if purchasing power calculations are used, in the world's rankings [UNDP, 2002]. Its huge domestic market is attractive to other countries to sell to and invest in, but it also enables China's industries to exploit significant production economies of scale just by selling at home. Small market economies have to export to gain production economies of scale, but this is not so for China. This asymmetry gives China enormous advantages in bilateral and even multilateral

bargaining over industry support and market access. Thus, in a globalising world, China is in a good position to implement developmental state-type industry policies and selectively adopt features of neo-liberal economic policy to engage with the global economy on terms of its own choosing.

China's geography endows sub-national governments and local actors with power to mediate the central government's market reform and strategic industry policy. China's physical size and large population have enabled its sub-national governments to enjoy a large degree of autonomy from the centre throughout its long history and this has posed enormous challenges to national governance. China's central government has often found it difficult to enforce national policies at the local level without the cooperation of sub-national governments. Post-Mao, Beijing finds that its liberal market reforms and strategic industry policies require active cooperation from sub-national governments but local economic interests often lead sub-national governments to oppose or moderate national policies [*Baum and Shevchenko, 1999; Breslin, 1996; Dougan 2002*].

Finally, in the midst of market reforms, CCP self-reinvention so far has enabled it to remain in power as a monopolistic party. For some, a monopolistic party state with an IMF/World Bank-type market economy is an oxymoron. A monopolistic party in power that functions exclusively and continuously as 'the state' has to prevent the emergence of external groups that can challenge its monopoly on political power and this requires it to have overwhelmingly superior economic power. The party and its supporters can ill-afford to allow other groups to compete equally with it for economic resources on a level playing field.

This article now turns to a more detailed analysis of each of these factors.

II. PATH DEPENDENCY

China's market reform has been gradual compared to the 'big bang' approach to market reform in the post-communist countries of CEE, which follow relatively closely the standard IMF/World Bank reform prescription. A key reason for the difference was the collapse of communist party rule in CEE. This allowed the IMF and World Bank to exert their considerable influence on the reform programmes in these countries and inspired the determination of the non-communist parties there to break up the core centres of the communist parties' influence, which were concentrated in the central planning bureaucracies and state-owned enterprises (SOEs) [*see for example, Steele, 1994: 291–310*]. In China, without the collapse of Communist Party rule, there was no similar rush to replace central planning with the market and to privatise industry. Instead, the market and private enterprise were only to complement the plan and state ownership. Collapse of communist party rule

produced discontinuous institutional change in CEE, but with continuing Party rule in China, the presence of increasing returns to institutions ensures that market reform in China is path dependent. Policy-makers remain constrained by existing theories and ideologies, informal constraints and entrenched interests [North, 1990].

Elsewhere [Liew, 2000], I have explored the trajectory of China's market reform from when it was first introduced in 1978 to the late 1990s. China's approach to market reform, as would be predicted by North's theory, was gradual and can be described in two phrases: '*momo shitou guo he*' (groping for the stones while crossing the river) and 'Pareto-improving'. The former phrase refers to the Party's emphasis on experimentation and the latter refers to the Party's stated policy to, as far as possible, make no Chinese worse off because of economic reform. As I explained in that article and elsewhere, the endeavour not to make any Chinese worse off was designed to build a constituency within the Party/State in favour of economic reform. I believe the policy also reflected a genuine desire of the Party, at least until 1992, to prevent the emergence of significant income differentials and to avoid social conflict. The Party's revolutionary history helps to explain this desire. In his article, *Building Socialism with Chinese Characteristics*, the architect of China's market reform programme, Deng Xiaoping [1984: 36] wrote:

If we take the capitalist road, we can enable less than 1 per cent of the people of China to become prosperous, but we definitely cannot resolve the problem of how to make 90 odd per cent of the Chinese people prosperous. Therefore, we have to persist with socialism. According to the socialist principle of distribution according to labour, there will not be a large gap between the rich and the poor. After another 20, 30 years, after developing our forces of production, there will not be a two-class differentiation.

The CCP believed that persisting with state ownership could prevent significant income differentials. Following Marxist ideology, the CCP believed that incomes earned only from labour could not lead to large income differentials. Until 1993, mandatory planning and state ownership were inviolable principles of the Party; the market was introduced only to support the plan. The reforming post-communist regimes of CEE were freed from restrictions imposed by Marxist ideology and the need to establish a pro-market reform constituency in the Party/State bureaucracy and therefore never sought a 'Pareto-improving' outcome.

The plan-market system that the Party wanted to adopt was clearly far from the usual IMF/World Bank model of free markets and private ownership. In any case, the plan-market system became unsustainable

because of economic and political developments. The plan–market system was unable adequately to protect SOEs from market competition as corrupt officials diverted massive amounts of critical supplies from the plan to the market. A result of the plan–market system was the 1989 Beijing tragedy when troops fired on demonstrators who were protesting against official corruption and its negative impact on the standard of living of urban residents, who had previously enjoyed access to subsidised goods distributed through the plan.

The Party's response to weaknesses in the plan–market system was to abolish the plan and instead, provide fiscal and banking subsidies to urban households and loss-making SOEs to maintain its Pareto-improving policy. However, these subsidies soon became a huge drain on state finances and impacted negatively on the financial sector. This forced the Party in 1993 to adopt a 'socialist market economy with Chinese characteristics', to officially replace mandatory planning and state ownership with the market and public ownership as core features of China's 'socialist' economy and as two of its central ideological pillars.⁵ This 'socialist market economy' recognises that private businesses make valuable contributions to the economy and so effectively sanctions the privatising of state assets. The CCP had to overcome intense objections among its regular members and even among its senior leaders to replace the two central ideological pillars. There was intense debate within the Party's senior hierarchy and in the winter of 1991–92 Deng Xiaoping had to go on a 'southern tour' to garner support from the coastal and southern provinces, which are the major beneficiaries of market reform, for the 'socialist market economy'.

The CCP's implementation of the 'socialist market economy' was grounded in the policy of 'grasping the large and releasing the small' (*zhuada fangxiao*). To 'release the small' is to privatise or contract out small SOEs or to let them go bankrupt.⁶ To 'grasp the large' is to turn into world-class businesses a select group of 300 out of a list of 1,000 already successful large enterprises and enterprise groups [Xie, 1998: 54]. This is a policy of the state picking and making winners and is encapsulated in the slogan 'support the excellent and the strong' [Lin, 1998: 183]. It is South Korean-style industrialisation in place of Soviet-style industrialisation and clearly runs counter to the post-Asian crisis prescriptions of the IMF and World Bank, which are against state-sponsored industry policy. There are, Hall and Soskice [2001] point out, many varieties of capitalism; China's variety is just one of the many and is clearly not a clean break from China's pre-reform economic model and the model's approach to industrialisation.

Even more critical than the retention of planning – in the form of state industry policy and support – are the strategic reasons for China not embracing wholeheartedly neo-liberal reforms. The CCP claims that it has

yet to complete its task of nationalist revolution. The CCP continues to face challenges to its rule in Tibet and Xinjiang and its declared historic mission to reunify Taiwan with the 'Motherland' remains unaccomplished. In its attempts to suppress separatist movements in Tibet and Xinjiang, the CCP seeks to win 'hearts and minds' with a policy of massive fiscal subsidies and market intervention to improve standards of living of national minorities in the two provinces [*Liew, 2004; Wang, 2004*]. The policy is designed also to support the livelihood of the large number of Han residents in the two provinces who have been encouraged to migrate there from other provinces to dilute the national minority population for national security reasons [*Becquelin, 2000*].⁷

A concrete example of this policy is official intervention in the cotton market in Xinjiang. Xinjiang's cotton is competitive against other domestic suppliers in price and quality, but is not competitive against overseas imports [*Du, 2000: 251*], and so is hit particularly hard by China's entry into the WTO. A study by China's Academy of Social Sciences forecasting developments in the cotton industry after China entered the WTO projected a nationwide 12.6 per cent fall in production, with a corresponding decline in employment of 22.6 per cent [*Li, Zhai and Xu 2000: 75*]. Safeguarding national unity and successful economic development are the two pillars that sustain the CCP's legitimacy. The state has made Xinjiang's economy highly dependent on cotton and, WTO or no WTO, it is highly unlikely that it will allow the fate of the cotton industry in Xinjiang to be determined solely by market forces, given that it perceives the cost of this outcome to be highly damaging to the national-unity pillar.

III. NEO-LIBERALISM AND GEOGRAPHY

Despite claims by supporters of the neo-liberal economic model of the positive impact of free trade on economic growth, the available empirical evidence to support this claim is inconclusive [*Rodriguez and Rodrik, 2000*]. There is no doubt that exports have contributed to China's phenomenal post-Mao economic growth, but it is less clear that China's gradual lifting of import barriers has had a similar positive effect on economic growth. The reason is China's large domestic market, which challenges neo-liberal prescriptions regarding free trade. The relative factor endowments model of trade that is behind much of the IMF and World Bank trade policy advice to countries assumes constant returns to scale production technology and the presence of competitive markets with many sellers. The negative economic outcome associated with trade intervention depends very much on these assumptions of the model. Changing these assumptions in a model such that they fit better with the realities of China's large domestic market and the

existence of oligopolies in world markets can produce the result where trade intervention is economically beneficial. Krugman [1984] showed in his theoretical model that with increasing returns technology and an oligopolistic market structure that import protection for a firm could lead to an increase in its exports. Although Krugman's model is technical, the basic idea behind his model is simple. Import protection for a firm can allow it to compete at home, enabling it to realise economies of scale and lowering its production costs, which makes it competitive in all markets at home and abroad.

Krugman's and other similar theoretical models provide a rigorous economic explanation of why certain countries can continue to implement developmental state-type industry policies in the current post-Asian crisis era. The key is the presence of a large domestic market, which is very attractive to trading partners and enables the domestic firm to exploit economies of scale in production from import protection alone without having to rely on exports. A large domestic market confers China advantages in international bargaining over market access and makes China less vulnerable to trade retaliation against its exports when it uses import barriers to exploit economies of scale in production.

Japan, South Korea and Taiwan, with much smaller populations than China, have successfully carried out strategic industrialisation. But the pinnacle of their success was during the Cold War when the US was willing to allow its strategically important allies to industrialise through trade subsidies. The US kept open its domestic market to subsidised exports from its strategically important allies and acquiesced to their protection of their domestic industries. Now the US no longer has any need to help these countries economically for strategic reasons and often sees them more as economic competitors than as strategic partners. Moreover, there is now a backlash in industrialised countries against globalisation [Rodrik, 1997]. Increasing domestic opposition in the US, EU and other industrialised countries to the loss of jobs due to unrestricted imports into these countries has made it much more difficult for industrialising countries, unless they have strong bargaining power, to implement strategic industry policies. Industrialised countries are likely to act against any industrialising country perceived to be supporting its exporting or import-competing industries. The White House in 2004 lifted trade restrictions against steel imports into the US from the EU not because of a ruling from the WTO, but because the EU threatened to impose restrictions on imports from states of the US where President Bush is vulnerable politically. A similar threat from a small country would not carry any weight.

To govern a country with China's physical size and population is a challenging task. State power in China is decentralised by necessity. China has a population of about 1.3 billion and many cities and provinces are as

large as a typical European country. Shanghai has a population of over 16 million and Sichuan over 86 million.⁸ It is impossible for any government in Beijing to govern a country the size of China without cooperation from local authorities. Localities in the PRC enjoyed a fair amount of autonomy even at the height of central planning and there was continuous tension between the centre and sub-national governments. Conflicts between the centre and sub-national governments in China, especially over public finance, have a long history that predates the PRC. In traditional China and the PRC until 1994 there was no central tax collection agency. Sub-national governments collected taxes and the centre depended on them to deliver to it its share of the taxes collected. The historic dependence of the centre on tax collection efforts of sub-national governments made rich provinces powerful political actors in the PRC's political system. The political influence of provinces is formalised in the PRC political system where 'province' is a rank in the national political administrative hierarchy that is equal in rank to a national ministry [*Lieberthal, 1995: 164–66*] and although not stated formally, richer provinces rank higher than poorer provinces.

Under Mao, provincial cooperation was necessary to draw up and implement the central plan and provinces were required to have had their own plans, which complemented and supported the central plan. Mao, while he advocated central planning and harangued against localism (*difangzhuyi*), was also a firm believer in self-reliance and local initiative. Post-Mao, the localities have become even more difficult for the centre to control.⁹ The post-Mao central government had to intervene directly and forcefully on numerous occasions in the localities to regain macroeconomic control [*Liew, 1995*]. Sub-national governments in China have utilised their large degree of autonomy to become major players, often as shareholders, in local industrialisation, promoting the development of various industries – from those involved in the production of consumer durables, to those involved in high technology production like civil aviation manufacturing [*Dougan, 2002*]. Local industrialisation efforts are not limited to producing globally competitive industries. Sub-national governments also promote local industrialisation to create local employment and to maximise tax revenues. In promoting local economic interests, sub-national governments have even erected trade barriers against domestic products made in other localities [*Gilley, 2001b; Watson et al., 1989*]. The disposition of China's powerful provinces towards strategic industry policies and the desire of sub-national governments to create local employment and raise local tax revenues have led many specialists to argue that sub-national governments and local economic interests, not the central government, are the major impediments to China's WTO compliance [*Johnston, 2003: 15*].

There is no guarantee that China's strategic industry policy, which is pushed by its national and sub-national governments, will be able to duplicate the success of the post-War industry policies of Japan, South Korea and Taiwan. Steinfeld's [1998] and Beeson's and Liew's [2002: 147–54] studies on SOE reform and Moore's [2002] study of China's textile and shipbuilding industries cast doubts on the policy's likely success. State–industry ties date from the days of central planning and remain largely 'particularistic ties of industrial paternalism rather than the universalistic ties of rational–legal authority' [Moore, 2002: 305] and competition among sub-national governments weakens further the effectiveness of China's industry policy. However, weakness in strategic industry policy does not translate into strength in market reform. Competition among sub-national governments weakens both market reform and industry policy. In sum, China's geography gives the PRC strong international bargaining power and has produced powerful sub-national governments in China, which together with the PRC's earlier embrace of central planning and continued quest for national unity are producing a form of market liberalism that is situated between the plan and IMF/World Bank neo-liberal models.

IV. NEO-LIBERALISM AND PARTY SELF-REINVENTION

Post-Mao, the CCP has adopted a more liberal approach to managing the national economy. Here there is an inherent ideological contradiction with communist orthodoxy. Therefore, although the CCP remains in power as a monopolistic party, it has had to reinvent itself to do so. The CCP so far appears to be able to successfully reinvent itself by reconfiguring its support base through co-opting the new social strata that have been empowered by market reform. This has been a critical factor in enabling the CCP to remain in power as a monopolistic party. It also ensures that China's market reforms will continue to depart from the standard neo-liberal model. In China, financial resources are required to sustain political power in an increasingly market-oriented economy. This is the key reason why the CCP, as a monopolistic party, will not allow a full and free market; free market competition would serve to erode the party's continuous and dominant control of the economy's financial resources, which is essential if the party is to preserve its political power.

After more than two decades of market reform, the private sector in China increasingly dominates the lives of ordinary citizens. As can be seen from Table 1, the growth of private enterprises in China in the 1990s was phenomenal. The growth of the private sector is occurring despite China's market reforms falling far short of the standard liberalising advice of the IMF and World Bank, but as Hall and Soskice [2001] have shown, resistance to

TABLE 1
DEVELOPMENT OF PRIVATE ENTERPRISES

Year	Number ('000)	Annual growth (%)	Employees (10,000)	Annual growth (%)	Registered capital (100 million yuan)	Annual growth (%)
1989	91		164		84	
1990	98	7.7	170	3.7	95	13.1
1991	108	10.2	184	8.2	123	29.5
1992	140	29.6	232	26.1	221	79.7
1993	238	70.0	373	60.8	681	208.1
1994	432	81.5	648	73.7	1448	112.6
1995	655	51.6	956	47.5	2622	81.1
1996	819	25.0	1171	22.5	3752	43.1
1997	961	17.3	1349	15.2	5140	37.0
1998	1201	25.0	1701	26.1	7000	36.2
Nov. 1999	1486	23.7	1901	11.8		

Source: Yan [2002: 194].

this advice does not mean that the government is anti-private ownership. On the contrary, the growth of private enterprises could not have been so rapid had it not been for state acquiescence and support.

Accompanying the growth in private enterprise is the shift in the national emphasis from 'politics in command' to 'economics in command', which switches the demand for political activists (cadres) to demand for skilled professionals, managers, and risk-taking entrepreneurs. This shift in national emphasis has weakened the coercive powers of the Party/State and its control over financial and human capital resources. While China's economic growth originating in market reform has been spectacular and has enabled substantial poverty reduction, this has come at a cost of rapid and significant increases in income inequality. China's Gini coefficient increased from 0.288 in the 1980s to 0.388 in the 1990s, transforming China from one of the world's most equal countries (in terms of income) before reform to one in the middle of world rankings [*World Bank, 1997: 2*].¹⁰ China's entry into the WTO is predicted to increase inequality further [*Zhai and Li, 2002*].

The significant change in income distribution and shift in national priority from 'making revolution' to 'making money' has produced a profound shift in popular perception of the relative status of social groups. Table 2 shows the outcome of a survey, conducted by China's Academy of Social Sciences in three cities (Shenzhen, Hefei and Hanchuan) and one county (Zhenning), of how members of different social strata evaluate their social standing [*Lu, 2002*]. Two observations from the data are particularly interesting. First, even casual and unemployed workers rank themselves higher than peasants rank

TABLE 2
SELF EVALUATION OF SOCIAL STANDING

Social stratum	Social standing (max 10 pts)			
	Shenzhen	Hefei	Hanchuan	Zhenning
Political and civic leaders	6.8	5.4	5.5	4.7
Managers	6.4	5.6	4.9	na
Private entrepreneurs	7.1	6.0	4.0	4.0
Professional and technical staff	6.2	5.7	5.1	5.4
Non-professional white-collar	5.6	5.5	4.7	4.3
Small business owners	5.8	4.7	4.4	4.2
Service workers	4.9	5.1	4.0	4.6
Production workers	5.3	4.8	4.4	3.8
Peasants	na	na	3.8	3.7
Casual workers/unemployed	5.7	5.2	4.1	4.3
Average	5.7	5.2	4.2	3.9

Source: Lu [2002: 32]

themselves. Second, private entrepreneurs rank themselves higher than do political and civic leaders in three of the four places surveyed. In Shenzhen, the city in China's southern Guangdong Province specially built as one of four special economic zones at the beginning of reform,¹¹ and Hefei, the capital of Anhui Province, private entrepreneurs rank themselves higher than political and civic leaders rank themselves. In Hefei, political and civic leaders rank themselves below the level that managers, professional and technical staff, and even non-professional white-collar staff rank themselves. In Zhenning, political and civic leaders rank themselves below the level that professional and technical staff rank themselves, but above the level selected by private entrepreneurs.

The CCP leadership have recognised that under these social and political conditions it cannot sustain its hold on power without the Party transforming itself. The change described here is so profound that we can describe it as the Party's self-reinvention. The CCP reinventing itself has meant changing the 'body and soul' of the Party. In practice this involves changing the characteristics of Party members ('body'), especially that of Party elites, and redefining the Party's ideology ('soul'). The Party is keen to co-opt the growing elite of skilled professionals, managers, and private entrepreneurs. Their bargaining power *vis-à-vis* the Party/State has continued to strengthen while marketisation gives professionals, managers and entrepreneurs wealth, leverage and space to pursue their interests within a political marketplace.¹²

How has the Party changed its soul? Jiang Zemin, the former Party general secretary who took over from the disgraced Zhao Ziyang in 1989, delivered an important speech at the 14th Party Congress in 1992, which called on the people not to debate whether certain reform methods are socialist or

capitalist, but to concentrate on production [*Jiang, 1992: 2*]. By shifting the attention to production, the CCP is able to justify the nation's ever widening income differentials. Instead of preventing widening income gaps, especially from large returns to private capital and skill, the CCP is defending income differentials and is resorting to appeals for those in front economically to lead those behind to achieve common prosperity [*CCP, 1993: 22*]:

It is necessary to introduce competitive mechanisms for rewarding individual labour and break away from egalitarianism, so as to implement the principle of more pay for more work and rationally widen the income gap. ... [T]hose who have become well off should be encouraged to lead forward and support those lagging behind, so as to achieve common prosperity.

The message here is explicit. Egalitarianism is not the national ideal, income maximisation is. This requires 'those who have become well off' to lead from the front. In Jiang Zemin's report to the 16th Party Congress in 2002, he invoked the notion that whether a person is politically advanced (*xianjin*) or backward (*luohou*) does not depend on whether the person owns any personal property or how much personal property the person owns. What are important are the person's political thinking, his or her *biaoxian* ('compliant and supportive behaviour') towards the Party, how the property is acquired, how it is used and the person's contribution in 'building socialism with Chinese characteristics' [*Jiang, 2002b: 15*]. Thus, the working class is no longer necessarily considered the class that will lead from the front, and this paves the way for the Party to change its 'body'. In his speech to celebrate the 80th anniversary of the foundation of the CCP on 1 July 2001, Jiang Zemin [2001] made it clear that those who should lead are members of the new social strata such as private sector entrepreneurs, managers and professionals. These new rich can remain in the Party or are welcome to join because they are 'productive forces' and are therefore potential 'advanced elements of society'.

Indeed, the Party has to rely on what it considers to be 'advanced elements of the new social strata'. Their interests are more closely aligned with those of the Party than are the interests of workers and peasants. Members of the new strata are the major beneficiaries of the Party's policy on the economy and are therefore more likely to share the Party's vision of a socialist market economy and thereby support the Party. Moreover, money and political influence go together in a market economy and money increasingly buys political voice. Marketisation introduces a situation where money and competition commodify power and influence and tie the political marketplace to the market economy. This is the case even when there is no serious

electoral contest in China since power through regulation or influence does not require an electoral system and operates effectively through corruption and money politics. The new rich are in a position with their financial resources to buy influence, and perhaps power, and the Party recognises that it has to co-opt them lest they form an external threat. Furthermore, political mobilisation requires financial resources, to which the new wealthy strata have ever greater absolute and relative access and the old Party elites had ever less relative access. Here we see the reasons for the making and remaking of Party elites. In a widely publicised case of resistance by the new rich to the CCP, in 1992, villagers in China's richest village, Daqiu, south of the northern port city of Tianjin, challenged Party rule, which ended only with the intervention of para-military forces. The village rebel leaders were able to organise and mobilise against the Party only because they had the economic means to do so [Gilley, 2001a].¹³

The 16th Party Congress amended the Party's constitution and legitimised the previously illegitimate Party membership of many private entrepreneurs. The revision of the CCP constitution at this Congress symbolises the formal reinvention of the CCP. The former CCP constitution starts with a declaration that the CCP is the vanguard of the working class. In the revised constitution, the Party declares itself to be the vanguard not only of the working class but of Chinese peoples of all nationalities [CCP, 2002: 57]. Article One in Section One of the revised constitution states that Party membership is opened to workers, peasants, members of the armed forces, intellectuals and advanced elements of other social strata who are 18 years and above [CCP, 2002: 66]. Here recognition and legitimation of new social classes are made explicit as is their eligibility for Party membership. With the amendment to its constitution, the CCP formally embraces the new class structure and transforms itself from a revolutionary Party for the working class to a ruling Party, at least in theory, for the whole people irrespective of their class.

In sum, the Party changes its 'body' in two ways. First, is the reinvention of Party elites as many in the Party remake themselves into technocrats and entrepreneurs in the service of market reform in order to remain relevant to the Party and to maintain their power and influence in the Party. Second, it accepts into the Party a new category of members who are brought into the Party from the 'advanced elements of other social strata' to prevent the creation of power centres that are external to the Party.

Many Party members have in fact transformed themselves from Party activists into skilled professionals or even entrepreneurs when the state corporatises or privatises its enterprises. One Party member who has remade herself is Guo Fenglian, the well-known 'iron maiden' poster girl of the Cultural Revolution era who has become an icon of entrepreneurship. Guo comes from Dazhai, the village in the slogan, 'In agriculture learn from

Dazhai', coined by Mao Zedong to celebrate the ideology of 'self-reliance'. She joined the Party when she was 14. Now 56, she runs 12 enterprises, which had a combined output of 100 million yuan (about US\$12 million) and employed more than 1,000 workers [*South China Morning Post*, 2002: 4].

As an indication of their increasing influence in recent years, private entrepreneurs have been 'elected' to sub-national people's congresses in increasing numbers. A survey of private entrepreneur membership in the provincial parliament (*renda daibiao*) in the capital of Hebei province, Baoding, in the mid-1990s for example, found that 15.5 per cent (100 of 644) of members were private entrepreneurs [*Yan*, 2002: 203]. Furthermore, as indicated in Table 3, many private entrepreneurs were already members of the CCP before the 16th Party Congress. The Forbes team that drew up China's 2002 'rich list' estimated that 25 per cent of those in the list are Party members [*Hoogewerf*, 2002] and Dickson [2003: 108] estimated that about 20 per cent of private entrepreneurs are Party members.

Theorists like Diamond [2003] emphasise that economic development will create pressures for democratisation only if it is accompanied by rising levels of education, the growth of a diverse middle class that is independent of the state, and the creation of a 'pluralistic, active and resourceful civil society'. However, it is clear that the CCP's self-reinvention is designed to *prevent* the emergence of an autonomous civil society. At a time when it is seeking to recruit members from the newly economically empowered strata, the Party is actively denying autonomy to potentially influential civil organisations formed by members of these strata that choose to remain outside the Party.

While some argue that an active civil society is emerging in China [*He*, 2003; *Pei*, 1998], it remains true that the most influential civil organisations are not autonomous of the state [*Yu*, 2002: 216–20]. Although official regulations demand that civil organisations sever all official ties with the Party and government, the government is still the sponsor of most professional associations. According to official regulations, a civil organisation must first be affiliated to a Party or government organ before it can be registered. The civil organisation, once registered, is accountable to that organ. Furthermore, although official regulations state that Party and government officials above the division level (*zhichu*) cannot serve as leading officials of civic organisations, former senior Party and government officials continue to fill almost all the senior leadership positions in important civic associations. For example, a former minister of the State Economic Commission became president of the National Council of Industrial Economics [*Yu*, 2002: 218]. Retired village Party secretaries often serve as presidents of village senior citizens' association and the Party appoints the officials of chambers of commerce at both central and sub-national levels. Officials in many civic associations are like public servants, who rotate

TABLE 3
PROPORTION OF SOCIAL STRATA WHO ARE PARTY, OR FORMER OR CURRENT YOUTH LEAGUE MEMBERS 2001

Social stratum	Shenzhen (%)		Hefei (%)		Hanchuan (%)		Zhenning (%)	
	Party	Youth League	Party	Youth League	Party	Youth League	Party	Youth League
Political and civic leaders	100	100	77.5	95	100	90	100	93.3
Managers	35.7	76.8	58.8	97.1	53.8	61.5	na	na
Private entrepreneurs	22.2	85.2	24.4	72.1	9.1	45.5	0	0
Professional and technical	27.2	86.4	25.2	88.2	17.8	73.3	24	67.3
Non-professional white-collar	28.2	87.4	40.7	83.6	54.5	75.3	46.3	44.4
Small business owners	13.7	60.8	10.4	52.8	7.7	41	5.2	11.8
Service workers	10.4	59.5	7.6	68.3	10.6	55.3	3.9	28.8
Production workers	0	72.2	13.3	72.9	5.9	31.1	10.3	21.6
Peasants	na	na	na	na	4.3	23.9	5.2	10.2
Casual workers/unemployed	2	58.4	9.1	58.3	1.8	46.4	3.9	9
Average	17.5	73.1	23.4	74.1	12.1	40.3	6.7	12.9

Source: Lu [2002: 36]

between positions in Party–government and civic associations. Some Party members who are alarmed by endemic official corruption have called for an active civil society to supervise the Party [*see, for example, He, 2002*].

In a widely publicised article in the official newspaper of the Guangzhou Party committee, *Nanfang ribao* [*Ren, 2000*], Ren Zhongyi, a former Party Secretary for Guangdong Province, writing on the ‘Four Cardinal Principles’ (*si xiang jiben yuanze*), called for external supervision of the Party.¹⁴ According to Ren, for the Party to lead well, it must be supervised because ‘absolute power corrupts absolutely’ (*juedui de quanli hui dao zhi juedui de fubai*). As Ren claimed, ‘The Communist Party supervising itself is like using one’s left hand to supervise one’s right hand’. However, the official Party position is that only the Party should be allowed to supervise the Party [*Jiang, 2002a: 7*]. The Party’s desire to retain its monopoly power outweighs its concern with official corruption.

Nevertheless, endemic official corruption has forced the Party to introduce institutional reforms such as appointments based on merit as opposed to personal connections, and village elections to achieve greater accountability [*Li and O’Brien, 1999; Nathan, 2003*]. The increasing complexity of managing a market economy exposed to global economic forces is another reason for the CCP regime’s institutionalisation [*Shambaugh, 2001*]. The Party’s self-reinvention and pursuit of institutional reform are efforts at political renewal, which are intended to preserve its position as a monopolist of political power. That members of the middle and entrepreneurial classes, the new social strata that the Party wishes to co-opt, are lukewarm in their support for democracy, is helping the Party to preserve its monopoly political power.

The assertion of the existence of a causal relationship between the size of the middle class and successful democratic transition assumes members of the middle class demand democracy, which is not necessarily the case everywhere [*see Bellin, 2000*]. While the middle class is growing in China, only 15 per cent of the population are members of this class and they are not strong advocates for democracy [*Lu, 2002: 73*]. This pessimism about middle class support for democracy in China is supported by interviews of the middle class conducted by An Chen [*2002: 13*], who found them to have a ‘disposition against lower-class empowerment’. Similar elitist views against lower-class empowerment are held by most entrepreneurs in a survey on political beliefs of private entrepreneurs in China [*Dickson, 2003: 135*].

Several China specialists writing in a special issue of *Journal of Democracy* in January 2003 discussed the CCP’s post-Mao efforts at political renewal. As expected, there was disagreement among them on the success or otherwise of the CCP’s efforts. Minxin Pei neatly sums up the opposing conclusions of the specialists: ‘political renewal is still a work in

progress, while political decay has yet to reach a terminal stage' [*Pei, 2003: 80*]. One could speculate about China's political economy should the CCP's political decay not become terminal. But it is clear that as long as the CCP survives as a monopolistic party, which it has managed to do so far, it will never allow market competition on a level-playing field. Allowing the use of a level-playing field runs counter to the Party's imperative to secure dominant control over the country's financial resources lest social groups external to the Party obtain significant independent sources of finance that can provide them with the capability to pose a serious challenge to the Party's monopoly power.

V. CONCLUSION

The Asian crisis has not altered fundamentally the form of China's engagement with neo-liberal economic policy. China has not embraced the IMF and World Bank neo-liberal model and the state continues to mediate and direct China's market reform. Three principal factors continue to influence how the state mediates China's neo-liberal engagement: path dependency, China's geography and the CCP's successful post-Mao self-reinvention that has enabled it to remain in power as a monopolistic party. The CCP cannot simply disown its history as a revolutionary and nationalist party. The CCP's mission to achieve national unity has special significance here. Safeguarding national unity is one of the two pillars of the CCP's legitimacy, alongside successful economic development. This severely limits the CCP's freedom to leave economic development in the restive provinces of Tibet and Xianjiang entirely to market forces.

China's geography is conducive to the implementation of developmental state-type policies because its large domestic market presents significant economies of scale in production and gives China bargaining power in international negotiations over industry support and market access in the current era of globalisation. Moreover, China's size and population bestows upon sub-national governments a significant degree of independence from the centre and they have utilised this independence to promote local industry even to the extent of erecting regional blockades against domestic goods from other localities. China's centre-local policy conflicts have a long history that predates the PRC and localities will contest China's WTO compliance with varying degrees of success.

Finally, the CCP has reinvented itself by co-opting wealthy and potentially powerful new groups of middle and entrepreneurial classes that its market reforms have created. These groups are lukewarm in their support for democracy and the CCP's reinvention has allowed the CCP to remain a monopolistic party in power. As a monopolistic party in a market economy,

where financial power has a huge bearing on political power, the CCP has to retain dominant financial power and keeps within the fold, or least on side, others who have financial power. This imperative determines that the Party cannot allow fair economic competition among market actors; the playing field has to be sloped to favour the Party and its supporters. Thus path dependence, geography and the Party's self-reinvention will ensure that China's engagement with economic liberalism will not conform to the neo-liberal model and will remain a loose hug rather than an intimate embrace.

NOTES

1. There are doubts over the reliability of China's official statistics. Annual growth rates may have been overestimated by up to 2 per cent, but even if growth rates are lower by 2 per cent, China's economic growth in the reform period remains very impressive and ranks comfortably among the world's ten fastest growing economies [*Lardy, 2002: 12; World Bank, 1997a: 3*].
2. However, Sachs and Woo [2000] argued that China's strategy is the result of conditions that are unique to China and therefore cannot always be adopted by other transition countries.
3. The remaining pillar of the IMF/World Bank model is monetary and fiscal austerity. It was a key feature of China's pre-reform model and China remains committed to it. CCP leaders are very afraid of inflation because hyperinflation in the late 1940s contributed to defeat of the Nationalists (*Guomindang*). For more details regarding the World Bank's and IMF's preferred model, see Beeson and Islam, this volume.
4. This is a clear implication of the Heckscher-Ohlin factor endowment theory of international trade, which is the intellectual foundation behind the IMF/World Bank push for free trade. The theory is taught in all university-level international trade courses and appears in all textbooks on international trade. See Appleyard and Field [2001: 117–39] for an excellent exposition of the theory.
5. Public ownership is group ownership where no one individual has a controlling interest and the major owners are primarily domestic institutions and the state, with the possibility of foreign participation.
6. Cao, Qian and Weingast [1999] argued implicitly that privatisation of small SOEs can be Pareto-improving in some instances because small SOEs are often privatised to employees at a discount and some former SOEs become profitable after a change in ownership. Hence retrenched workers are compensated ex-post with help from the local government to find new jobs or buy into the privatised SOE business at a discount that creates an ex-post environment, with workers having new sources of income. Workers then neither oppose privatisation nor demand subsidies.
7. The policy is part of a larger project to spur economic development in all the poor western provinces [*Gao et al., 2000*].
8. If one includes the population of its capital, Chongqing, which has provincial status and has a population of 30 million, the population of Sichuan is over 116 million [*NBSC, 2002: 94*].
9. The influence of the localities can be gauged by the crucial role some of them played in supporting the introduction of post-Mao reform in the late 1970s [*Shirk, 1993*] and, as I discussed earlier, in helping Deng to push through the 'socialist market economy' in the early 1990s.
10. Some studies give Gini estimates as high as 0.49. See for example Wang, Hu and Ding [2002].
11. The others are Zhuhai, Shantou and Xiamen.
12. Neo-liberals argue power operates in a kind of political marketplace.
13. At the beginning, the villagers of Daqiu rebelled against CCP economic policies. Later the villagers fought discrimination against the new rural rich. The CCP finally cracked down on

- the villagers when they directly challenged Party rule. The village Party secretary, Yu Zuomin had a slogan that said 'If you want to get rich, then abolish the party organisation' [cited in Gilley, 2001a: 156]
14. The Four Cardinal Principles are Party leadership, socialist road, dictatorship of the proletariat (people's democratic dictatorship), and Marxism–Leninism–Mao Zedong Thought.

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