



Capitalism in China: A Centrally Managed Capitalism (CMC) and Its Future

Nan Lin

Duke University, USA

ABSTRACT While China continues to develop capitalistic capacities, the party-state has increasingly tightened control of the economy and synchronized political and economic stratification – a tendency towards a *centrally managed capitalism*. Under centrally managed capitalism, the party-state commands the economy by controlling personnel, organizations, and capital in both political and economic arenas. At the same time, it delegates fiscal and administrative authorities to multiple and diversely formed corporations to compete in the marketplace. I further speculate on future ideological alternatives: a western-style democracy, a mature-stage socialism, or an enlightened authoritarianism – *Xiaokang* (小康 – moderate prosperity or well-off society). After eliminating or casting doubt on the former two, I argue that a two-step transformation towards *Xiaokang* is under way. In the first step, the party-state leadership gradually decouples its position from Marxist ideology of communism and socialism, and moves towards the maintenance of economic growth and social order. The second step then allows the legitimacy of party rule to be based on indigenous Confucian ideology that emphasizes enlightened leaders, moral institutions, and social relations (i.e., *Xiaokang*). Finally, I explore the feasibility and paths towards an indigenous ideology of democracy (*Datong*: 大同 – universal harmony).

KEYWORDS capitalism, centrally managed capitalism, Chinese capitalism, ideological transformation

INTRODUCTION

The phenomenal and sustained economic growth of China over the past two decades has raised fundamental issues about whether the system is capitalistic. This issue is significant not only because it offers an opportunity to understand and appreciate the dynamics driving the economic growth of China, but it may also challenge existing theories about the nature and characteristics of capitalism and provide clues about the future evolution of China and capitalism itself. In an earlier essay (Lin, 2008) I proposed that a capitalistic society has emerged in China. Specifically, I made the following arguments. First, I defined capitalism as

a set of social institutions that sustain the production, accumulation, and reproduction of capital, and identified these institutions as calculating capitalists, free markets, wage labour, an expansive system, and a strong and supportive state. I explicated existing theories that explain capitalism, ranging from self-interest – the psychological motive (i.e., Smith) and exploitative reproduction – the socio-political motive (i.e., Marx), to institutional enticement – the cultural motive (i.e., Weber), and the networking imperative – the social motive (i.e., Braudel, 1977; Wallerstein, 1979). Each theory offers only a partial explanation of capitalism, but collectively they explain how these institutions are coordinated. Based on these conceptual and theoretical articulations, I drew on empirical evidence to support the contention that China today strongly meets these requirements as a capitalist state. This capitalist state, however, exhibits two relatively unique features not usually identified with capitalism, namely, the state itself acts as a capitalist, and economic activities are heavily embedded in social relations (*guanxi*). Each of these features, which are not unique to China, shows its full leverage and sustainability in a capitalistic system that is not transitioning to the liberal capitalism of the West, as some have wished or argued, but may instead be establishing an alternative paradigm of capitalism to be emulated by other state-run capitalistic countries.

In this essay I further elaborate on the feature of the state as a capitalist. The other feature – embedding economic activities in social relations, or socially embedded capitalism – will be deferred to comprehensive treatments in other essays. I point out that while China continues to develop capitalistic capacities, the party-state has increasingly tightened control of the economy and synchronized the political and economic stratification – a tendency towards a *centrally managed form of capitalism*. Mechanisms and features of China's centrally managed capitalism (CMC) will be articulated. Three principal mechanisms make this politically commanded capitalism feasible: (i) the control of personnel and the incentive and mobility for political attainment; (ii) the control and rewards for organizations, including economic corporations; and (iii) the control of capital.

I then speculate that an ideological transformation is underway. This transformation takes two steps. In the first step, the party-state leadership gradually decouples the justification of its dictatorial position from the Marxist ideology of communism and socialism, and couples with the maintenance of economic growth and social order. This shift relieves the party from the burden of proposing mechanisms by which China can move from the primary stage of socialism to the mature stage of socialism. The second step then allows the legitimacy of party rule to be based on indigenous Confucian ideology (i.e., *Xiaokang* and *Datong*) that emphasizes moral institutions, social relations, and eventually democracy. When fully realized, this transformation will have significant and substantive consequences for China and its paradigmatic position in world capitalism.

THE ROLE OF THE STATE IN CAPITALISM

Empirical modern-day capitalism can be traced to the seventeenth-century financial systems of the Netherlands in which the stock market was innovated, global trade was envisioned, and the banking system established. The British adopted and improved these systems and, along with its industrial innovations, created a world empire. The systems were subsequently transported to the U.S. Mead (2009) and others have called the Dutch system version 1.0 of capitalism in about 1620; the British introduced version 2.0 in about 1700; the Americans upgraded to version 3.0 in 1945. Thus the dominant model of capitalism for the past 300 years has been the Dutch-British-American model – liberal capitalism. Since Adam Smith, the theory of a perfect, frictionless market, including financing, has lent a strong ideological support to the superiority of this model (Krugman, 2009). Some scholars have maintained that capitalism only needs a governance system that monitors the ‘natural’ free market and allows it to function without interference or abuse. Rand (1966), for example, stated that the only function of the government should be the task of protecting citizens’ rights. In a capitalist system all human relationships should be voluntary. Variations of capitalism have always existed, including types of welfare capitalism in Europe (see Lin, 2008) where the state’s role in the market is recognized and duly exercised. But ideologically (or theoretically), the state has been treated as a supportive player in capitalism, even though the state has played a critical role in the development and maintenance of the Dutch-British-American systems.

Some scholars challenged this theoretical stance by pointing out that various institutions, including the state, played different roles in different phases of the industrializing process. Gerschenkron (1962) argued that historically when the industrialization process was launched in a backward country, the productive and organizational structures of industry that emerged from those processes were considerably different from those in more advanced or mature countries. These differences were largely attributable to the state’s application of institutional instruments for which there was little or no counterpart in an established industrial country. He therefore concluded that the extent to which these institutional instrumentations exhibited utility appeared to have varied directly with the degree of backwardness of the countries. The emergence of Japan as a capitalist country offered an important site, outside of Europe and North America, for intensive, close examination of the development process from early backwardness to an industrialized society. In his study of Japan’s capital formation during the period 1868–1940, Rosovsky (1961) shows that the state played a prominent role in the process.

It was probably Johnson (1995) who coined the term the ‘capitalist developmental state’. Focusing on the institutional arrangements in the development of Japan, he showed that economic development (growth, productivity, and competitiveness)

was the priority for state action. The state used a small-scale, elite economic bureaucracy staffed with the best managerial talent available to guide the privatization and marketization processes. The elite bureaucracy (the Ministry of International Trade and Industrialization) employed consultation and cooperation to forge consensus among corporations on goals and information exchange in their innovative development, manufacturing, and competition in the global market. This strong political system allows the bureaucracy to take initiatives and operate effectively. Thus, in the developmental state, the politicians 'reign' and the bureaucrats 'rule' (Onis, 1991). This seminal work confirmed the significance of the state in the early stage of industrialization or at the developmental phase, as discussed by previous scholars, and set the stage for voluminous studies on the developmental state as found in East Asia.

Subsequent studies in Korea (e.g., Amsden, 1992; Cumings, 1987; Lie, 1998) and elsewhere in East Asia (e.g., Taiwan, Singapore, see Deyo, 1987; Evans, 1995; Onis, 1991; Wade, 1990; Wong, 2004) amplified the role of the state in the development of these states and solidified the linkage of the term 'the developmental state' to the development of East Asia. Onis (1991) and Wong (2004) summarized the developmental state as one in which the state must be autonomous and capable. It employs a small elite bureaucracy to tightly coordinate corporations, provide resources, and set national productivity goals. Because of the economic crisis in Asia in the late 1990s, individual states in East Asia had to adapt and adjust their policies, but it is felt that the role of the state has remained largely unchanged (Wong, 2004).

While this rich literature highlights the significant role of the state in emerging capitalism, especially in East Asia, the literature by omission ignores the role of the state in the entire spectrum of capitalism. This omission can lead to an implicit and erroneous inference: the state is only important for emerging capitalism. As I discussed in a previous paper (Lin, 2008), the state has always played a critical role in capitalism historically. Capitalism requires a *state* – a governance institution – that is willing and capable of protecting, regulating, and promoting the coordination and functioning of capital accumulation, the markets, and wage labour. Historical evidence convincingly shows that in order to thrive, capitalism requires a strong national government – a *powerful state*. Analyses of broad historical data on capitalistic development have amply demonstrated that a strong and supportive state is an essential ingredient for all capitalistic systems. Braudel (1977) stressed that capitalism, differing from a mere market system, triumphs only when it becomes identified with a powerful state. He cites the Italian city-states, Holland, and England as examples. The state provides guarantees that players follow the rules of the game. It ensures that capitalists produce and reproduce commodities with acceptable practices of acquiring material resources and compensating labour. Commodities are channelled through distribution and consumption markets transparently and without price fixing, hoarding, or dumping. Also impor-

tant is the state's role in arbitrating disputes over production, distribution, and consumption markets. While it attempts to be even-handed, the state is ultimately responsible for protecting capitalists so that capital accumulation can proceed (Johnson, 1995).

Polanyi (1944; see also Polanyi, Arensberg, & Pearson, 1957) made the essence of the state explicit. He identified the state and the market as the two central pillars of modern capitalism. For Polanyi, these two institutions are interconnected. The state plays a central role in determining the structure of property rights, the quality of financial institutions, and the incentives for capital accumulation, investments, and entrepreneurship (see Heilbroner, 1985 for elaboration). Of particular interest is the arbitration of disputes between capitalists and labour. While in some capitalist states unions are advocates of labour, the state is the ultimate arbitrator. It ensures that labourers never challenge capitalists for rights to the products of their labour and the means of production. A strong state promotes (domestic) capitalism by providing internal production forces with a protective shell from external challenges, and at the same time insists on a free market elsewhere for domestic corporations to secure markets for resources, labour, and consumption globally.

Many sociologists and political scientists have rightly stressed the significance of the state in modern industrialized societies, among them Wallerstein (1979), Evans (1995), Skocpal (1996), Hobson (1997), Weiss (1998), and Evans, Rueschemeyer, and Skocpal (2002). Historically, the U.S. government has not shied away from interfering with the market system to protect or save firms and industries. Some examples include its long-term farm protection policies; rescues of automobile, steel, and airline corporations; international tariffs; and the recent massive bailout of financial institutions. Examining the recent history of the U.S., Fligstein (2005) pointed out that in the U.S. entrepreneurship and competition matter to the creation of new markets and industry but that they cannot occur without governments and stable social structures to support them. He shows that the U.S. government has directly affected market activities with laws and rules that determine tax policies, govern the use of equity and debt by corporations, regulate employment relations, enforce patents and property rights, and regulate competition or antitrust policy. The government can act as a buyer of products and a provider of research and development funds to firms. It also makes rules that can directly favour certain firms in particular industries, often at the behest of the most powerful actors in those industries. The government, Fligstein points out, has also built up public and private infrastructures that opened up the possibility for new firms and industries to emerge.

This clarification has important implications for understanding the role of the state in economic development. First, the association of the state with a backward or emerging capitalism is unattainable. Theoretically it has been shown that the state remains important beyond the developmental stage, even though its role also varies for different states embedded in differential historical and institutional

arrangements. Empirically, many East Asian countries have long been industrialized and yet the state continues to play critical roles in economic development. Second, the role of the state needs re-conceptualization as we study its role in all types of capitalism.

Historically, the varying presence or absence of various institutions (e.g., the relative powerfulness of the monarch, the nobility, the landowners, the merchants, or the peasants) in different societies has contributed to differential roles that the state has played in different capitalist societies (Lachmann, 2000). But at a minimum, a powerful and supportive state is an essential element in a capitalist state. The significance of the state in a capitalist system is prominently displayed when capitalism inevitably brings the economy to the brink of total collapse, due to the ever-present greed and continued desire for expansion and accumulation of capital. Minsky (2008) theorized that in the normal cycle of an economy, when cash flow rises beyond debt, a speculative euphoria develops and borrowing through hedging, speculation, and Ponzi schemes ensue. These speculations eventually bring about a 'Minsky moment' when an accumulation of debt pushes the economy towards a crisis. This inevitable financial fragility and instability can only be avoided if the government steps in to control it through regulation, central bank action, and other mechanisms. The Panic of 1907, the Great Depression, the oil crisis of the late 1970s, and the current world and European financial crises attest to the danger of this instability and the need for intervention from the state(s).

Yet the conventional wisdom of economists and those espousing the developmental state perspective remain: once the crisis is overcome or the development is attained, the state recedes to the background and allows capitalists to resume their expansive activities and accelerating accumulation of capital. The vision of a perfect, frictionless market system soon regains traction when the debt is dealt with (Krugman, 2009). Calls for deregulation soon appear when the crisis is averted and the cycle resumes. Thus we can hypothesize that in 'Western' capitalism (i.e., the liberal capitalist tradition of the Dutch-British-American model), this cycle of stability and crisis, and the up-and-down role of the state are a routine process. Gaining an advantage over other actors in the marketplace supersedes all other considerations. Driven by greed and forever seeking gaps in regulations and normative trade practices to gain advantage, capitalists will inevitably move the system towards another crisis when the state emerges from its 'invisible' role to its role of blatant and outright intervention.^[1]

FORMS OF STATE CAPITALISM

The term 'state capitalism' has been widely used to characterize capitalism in which the state plays a significant and visible role. However, its usage is diffuse, ranging from characterizing state socialism to fascism, to state-firm-union coordination. In the Marxist tradition, state socialism is a system in which the state owns

and controls the means of production while wage labour and limited markets function. Thus the state is the sole capitalist. The fascist variety, characterized by Italian Fascism, identifies the authoritarian role of the state in intervention and supervision of big businesses and the economy. In still a third variation of state capitalism, the state manages strategic resources and coordinates closely with large private firms and unions to guide economic growth and development. Thus the degree or variation of state capitalism can be characterized by two dimensions: (i) the extent to which the state owns the means of production; and (ii) the extent to which the state dictates or coordinates with big firms (national champions) and unions in the marketplace. When the state is the sole owner of all means of production it is a dictatorial system, exemplified in state socialism (e.g., Cuba, North Korea). For the purpose of this essay I rule out further discussion on systems where capitalism, if it exists at all, is clearly subsumed under the authoritarian state and serves the pleasure of the dictators. Most state capitalistic countries, however, show that the state owns only some but not all means of production. In fact, it is hard to find any state that does not control or supervise certain industrial sectors and valued resources deemed central to the survival of the state. Most states retain control of all or portions of the defence industry, water (rivers, dams, etc.), environmentally essential resources (pollution control and environmental safeties), taxation, mining, and vital infrastructure (major roads, harbours, airports, communications), and so on. Schmidt (2002) identifies three types of capitalism in modern-day Europe: market, managed, and state. She puts modern-day France and, to a lesser extent, Italy in the third category. Even in the market capitalism category (i.e., Britain), however, the state plays a significant role and controls certain resources.

Some scholars have argued that the saliency of state capitalism as a counter-paradigm to liberal capitalism has been a recent development. For more than a century, liberal capitalism (i.e., Britain and the U.S.) assumed the political, military, and economic high ground in international markets, exploiting vital resources (e.g., oil) through its powerful corporations from other and less industrialized countries. Only during the second half of the twentieth century did states holding vital resources learn to mount a challenge. Bremmer (2009), for example, argues that state capitalism first took shape during the 1973 oil crisis when the Organization of the Petroleum Exporting Countries (OPEC) countries agreed to cut oil production in response to the U.S. support of Israel in the Yom Kippur War. The world's most important commodity became a geopolitical weapon, giving OPEC governments unprecedented international clout. The oil crisis gave birth to modern oil corporations, which have since been imitated and extended. Today, governments, not private shareholders, own all of the world's largest oil companies and control three-quarters of the world's oil reserves. The 13 largest oil companies in the world, measured by their reserves, are owned and operated by governments – companies such as Saudi Arabia's Saudi Aramco; the National Iranian Oil

Company; Petróleos de Venezuela, S.A.; Russia's Gazprom and Rosneft; the China National Petroleum Corporation; Malaysia's Petronas; and Brazil's Petrobras. State-owned companies such as these control more than 75 percent of global oil reserves and production. According to Bremmer, a second wave of state capitalism began during the 1980s, with the emerging countries controlled by governments with state-centric values and traditions, and newly reformed countries liberated from state socialism. Examples are the rapidly growing economies of the 1990s, including Brazil, China, India, Mexico, Russia, and Turkey. Finally, a third wave of state capitalism resulted from the fast growth of trade surpluses and was marked by the rise of sovereign wealth funds (SWFs). Most of these SWFs are run by government officials and compete and challenge in the global capital market. I will return to the issue of capital accumulation and reproduction by these states later.

These waves cited by Bremmer (2009) are rather arbitrary as many of the features he identifies had been evolving over longer periods of time and across different political and economic regimes. Nevertheless, they unfailingly point to growing state capitalism as a viable alternative form of capitalism capable of challenging liberal capitalism today. Yet within the diverse range of state capitalism, China stands out and is perhaps alone in its peculiar alignment and synchronization of a party-government-military-economy regime. The nature of this type of state capitalism will be discussed next.

CENTRALLY MANAGED CAPITALISM

The type of state capitalism I wish to discuss here is one in which the state plays an active role as a capitalist (see Lin, 2008). In this system the state exercises much freedom in creating and maintaining enterprises through ownership, holding majority of the shareholdings, and direct control over critical personnel decisions and supply of capital. I call this type of state capitalism *centrally managed capitalism*. It differs from liberal capitalism (e.g., the Dutch-British-American model), welfare capitalism in which the state controls welfare systems and otherwise supports but does not own large firms (e.g., most European states), or coordinated capitalism where the state works closely with large firms but does not own any directly (e.g., Singapore, Japan, and Korea). The developmental states, for example, are characterized by separation of the state and the economic corporations in personnel, stratification and mobility, and control of capital. They are also characterized by the role of a small, elite bureaucracy. China, on the other hand, shows a total involvement of the state in the economy and complete synchronization of a party-government-military-economy regime.

Centrally managed capitalism is a form of state capitalism that takes on the capitalistic form with the essential elements of capitalism: it promotes calculating capitalists, a free market, wage labour, and an expansive system. Yet the state plays

a critical role in every aspect of the economy. The state-owned or affiliated enterprises compete with other enterprises in the marketplace, and its elites enjoy the rewards and benefits largely consistent with other capitalists. However, the elites ultimately answer to the dictates of the state rather than boards of directors, shareholders, or stakeholders. The 'free' market is asymmetric in favour of state-owned and affiliated enterprises in accessing loans and resources (e.g., land, raw materials, and so on) and operating in both domestic and foreign markets. Labour in state-owned and affiliated enterprises has only limited bargaining rights while enjoying security similar to that offered to employees in the bureaucracy. Some state-owned and affiliated enterprises become 'national champions' as the state restricts their competitors and encourages their mergers and acquisitions. Having national champions does not necessarily indicate a monopoly of one dominant enterprise in an industry or a sector. For example, in China the government deliberately allows several (usually two or three) national champions in a single industry (e.g., automobiles, banks, telecommunications) in order to preserve and encourage competition in the marketplace. But how does the state control and manage firms while allowing them to compete in the marketplace? Specifically, how does the state control and manage the top managers of the firms beyond the usual market-oriented rewards and incentives? And how does it control enterprises while allowing them a free hand to compete with one another and with other enterprises both domestically and globally? A closer look at CMC in China reveals the incentive (and punitive) structure that motivates and propels the top managers as well as the enterprises to respond to the demands and commands of the state.

Over the past three decades China has undergone significant economic reforms, adapting to market mechanisms in alignment with global trends. In the early phase of the reform there was conjecture that this movement towards marketization might represent a transitional phase whereby China would gradually move away from the central command structure towards a market structure consistent with conventional understanding of how such a structure would operate (Nee, 1989; 1996). However, the evidence is that China has instead been 'experimenting' with a new model of capitalism. While understanding the utility of capitalism in building capital and creating wealth for the state and the people, the Chinese government is nevertheless determined to maintain its one-party political rule. The argument is that by uniting under the leadership of a responsible party and its apparatus, China is able to advance economically and socially with efficiency and stability. As such a mixed structure has never before existed in theory or practice, China and the party leadership follow the advice of its leader Deng Xiao-ping, who announced to the world in the early 1980s that China would be 'crossing the rivers by touching the stones'.^[2] The other side of the river is a wealthy nation; the way to get over the river is to take one step at a time and, once finding a stone to steady oneself, proceed to find another stone. What was left unsaid is that finding the next stone

and coordinating the next movement are commanded by the party, and not by free-market mechanisms.

This new form, capitalism under party-state leadership, is an evolving process. Privatization of the labour force, housing, household commodities, and services has gradually been implemented. Individuals, households, and many firms have been allowed to work for profit, accumulate surplus values, and make capital investments (e.g., investments in supplies, technology, education, jobs, real estate, the stock market, and so on) without blatant interference of the state (Nee, Sonja, & Sonia, 2007). Market forces have gradually been introduced into other spheres of society (e.g., travel, leisure, and recreation). Yet this marketization process is largely and carefully managed by the party-state. Through several mechanisms this management and control is strong and self-reinforcing. Here I highlight three principal mechanisms by which the party-state manages capitalism: a reward and control system for personnel; a reward and control system for organizations, including large corporations competing in the marketplace; and a control system of capital.

Reward and Control of Personnel

Party control of personnel. The Central Organization Department is one of the most powerful central party offices. Initially established in 1924 and directed by Mao Ze-dong himself, the department is in charge of recruiting, appointing, evaluating, promoting, and removing thousands of cadres in the party and government offices at the central, regional, and provincial-city levels. This department holds personnel files of cadres in all important organizations in the country, spanning the party, the government, state-controlled or state-affiliated corporations and enterprises, and judges, to mass media, universities, institutions, foundations, political consultative councils, and provincial and city leaders. Candidates of all major appointments are screened by the department. At lower levels, all the way to each agency, office, and corporation/enterprise, the Central Organization Department is represented and embedded in the party office. The office holds personnel files of all employees in the organization. Actual appointments are determined by the top leaders of the party, but candidates undergo careful and thorough screening by the Central Organization Department.

Corporations in the economic sphere are no exception. The party is embedded and occupies a central position in the organization. The 'organizations' extend beyond party-state controlled or affiliated organizations. In many 'private' enterprises (the term usually used is *min-ying* 民營 or 'people's enterprise', not 'private enterprise' 私營 (*si-ying*); the distinction is subtle but critical) there is a party secretary and a party office. Geely, for example, is a private automobile corporation that recently acquired Volvo. Li Shufu, its founder and CEO, is also reported to be the party secretary of the company. The secretary may nominally be a

member of the board of directors or a deputy CEO in the enterprise (or even chairman of the board or the CEO himself/herself) and centrally involved in all critical decisions. Furthermore, the secretary or an Organizational Department cadre supervises the personnel files (人事档案 *renshi dang-an*). In China every urban working adult has a personnel file that contains detailed family background; education, marriage, work, and party histories; reviews and evaluations by supervisors; as well as criticism or 'black mails' – anonymous accusations of bad behaviour or conduct (Sun, 1992). This confidential file, which is not available to the worker, is kept in the personnel office directly under the supervision of the party secretary. When a worker requests a transfer to another enterprise or work unit, both sending and receiving units must agree and the file is transferred to the other work unit's party office. A receiving work unit cannot accept the worker without the personnel file. Occasionally, though rarely, the personnel file may mysteriously disappear and the worker's career is in limbo (Hille, 2009). If someone is laid off and the personnel file is missing, he would essentially become a 'homeless' worker as no other work unit would hire him. For workers in private corporations, personnel files may not be as critical. For workers in state-owned, controlled, or affiliated corporations, personnel files assume paramount importance for promotion and mobility. For private or foreign corporations, the party either operates openly as an office or through a party-controlled apparatus such as a union.

Synchronized incentives and mobility in the political and economic arenas. In China, top-tier stratifications in politics and economics are synchronized. Personnel move freely from the political hierarchy to the state-controlled and state-affiliated economic hierarchy and back, at the command of the party-state. Incentives are of both types: political positions or political capital, and material rewards or economic capital. Ultimately, attainment of political positions supersedes the significance of that in the state-controlled and state-affiliated economic hierarchy. The party-state is ultimately in control of the political and economic spheres and therefore both the political and economic positions and resources. The motivation and goal of actions for elitists is therefore to strive to attain the highest positions in the political hierarchy. In this politically and economically synchronized stratification system positions in enterprises and the marketplace, while having their own rewards, are means or stepping-stones towards the end goal – political attainment.

It should be noted that the political hierarchy runs vertically from the central apparatus in Beijing to local party and government offices. While local government and party officials are agents of the principles of the central party-state and sometimes take advantage of their positions to serve their own interests, it would be a serious mistake to conceive of the local officials as possible counterweights in a gaming situation. The party-state can and does swiftly remove local officials who are deemed disloyal, incompetent, or corrupt. The local governments are given the opportunity to control and manage their owned and controlled enterprises (to be

elaborated in a subsequent section). Identical stratifications and reward structures operate at regional and local levels – the political hierarchy is in command of the controlled and affiliated enterprises and elites compete for the top positions in the local party-state. Vertically, local political elites are under the command of the central party-state. Elites at the local level compete for mobility to the central-level political and economic positions.

In this synchronized stratification system, performance in the marketplace is one of the criteria for mobility in the political hierarchy as well. The firm's performance is an important credential for its leading managers to be promoted to positions in the political hierarchy. The top leaders in the political hierarchy are also evaluated and judged by the overall performance of the economy. In this feedback loop, CMC couples politics and economics. The goals for the elites are consistent across the political and economic spheres: to compete and perform well in the marketplace.

Leading personnel in state organizations and institutions and in the state-owned or affiliated corporations are transferred back and forth between the central government and local and regional governments with ease, as well as between the government bureaucracies and corporations, as such personnel mobility is largely in the hands of the party-state. One example is Guo Shengkun, who in 1998 was moved from serving as vice CEO of the China Colored Metal Industry Corporation, a State Council-owned enterprise, to deputy chief and member of the party executive committee of the National Bureau of Colored Metal Industry, another state-controlled organization. In 2001 Guo was transferred to the corporate world as the CEO and party secretary of China Aluminum Corporation and the chair of the board of directors and CEO of the China Aluminum Share-holding Company Limited. In 2004 he was transferred back to the government side to become the deputy secretary of the party of the Guanguangxi Zhuang Autonomous Region and elevated to party secretary of the region in 2007. Recently Xiao Ye-qing, party secretary and CEO of the China Aluminum Corporation and chairman of the board of directors of the China Aluminum Shareholding Company, was promoted to deputy secretary of the State Department and member of the party committee. Another example is Yun Gongmin, who was moved from his post as deputy secretary of Shanxi Province to vice chairman of the board and deputy party secretary of Shenghua Corporation in 2006, and then transferred to become the CEO and deputy party secretary of China Huadian Corporation in 2008 (*Xinhua Net*, 2009).

The interpenetration of personnel extends to 'private' corporations as well. Recently a private (*ming-ying*) company, Mengniu Dairy, China's largest milk producer, was involved in a scandal for selling contaminated milk. Its founder and owner, Niu Gensheng, and the company had previously been held up as a shining example of outstanding private enterprise. In 2002 it was hailed by the state as number one among the fastest-growing enterprises ('not on the stock market and

not controlled by the state') in the country. In the wake of the scandal, in July 2009 Mengniu was forced to sell a 20 percent stake to a consortium led by state-owned China National Oils, Foodstuffs and Cereals Corp (Cofco), China's largest importer and exporter of food. Thus the state became the single largest shareholder of the company. Cofco declared that it would not interfere with the management of the company. Two months later, in September 2009, a senior Cofco executive replaced Niu as chairman of Inner Mongolia Mengniu, the main operating subsidiary of the company (Anderlini, 2009).

This intertwining between the political and economic spheres also facilitates intergenerational inheritance among the leading cadres at the central and local governments. Instead of escorting their children through government bureaucracies and being accused of nepotism, they can now see their children promoted through corporations. This is especially convenient if the children are talented. Levin Zhu, son of Zhu Rongji, who received a Ph.D. from Wisconsin-Madison, heads the China International Capital Corporation. China Development Bank is run by Chen Yuan, son of Chen Yun, one of the eight pioneering Communists. Jiang Mianheng, son of former president Jiang Zemin, who holds a Ph.D. from Drexel, controls Shanghai Alliance Investment Limited, a government-owned investment company freely competing as a private equity firm. Wen Yunsong (Winston), the son of Wen Jiabao, who holds an MBA from Northwestern, is the founding CEO of New Horizon Capital, one of the most influential private equity firms in China (*Financial Times*, 2010). Hu Haifeng, son of Hu Jintao, graduated with a bachelor's degree from Northern China Jiatong University and an EMBA degree from Tsinghua University. He chose to develop his career in the corporate world, joining Nuetech, an offshoot corporation from Tsinghua, after graduation. Nuetech claims to be the world's leading company in 'the research and development of X-ray inspection technology'. Hu started his career in the company as assistant to the general manager and, through a series of promotions, quickly became the executive vice president and then the president by 2006 at the age of 35. Later that year Nuetech was awarded the contract to supply securities scanners for all 147 airports in China, earning the company hundreds of millions of Yuan (Chen, 2006). In awarding the contract, China's aviation authority made it clear that Nuetech won the contract strictly due to its superior technology. Its Container/Vehicle Inspection System has been put into operation by Chinese Customs in customs, ports, and railway stations. In 2008, at the age of 37, Hu became the party secretary of Tsinghua Holding Company, which controls more than 30 Tsinghua-affiliated enterprises (*Dwnews*, 2009). In 2009 Hu left the corporate world and became the Deputy Secretary at Tsinghua University. The intergenerational transfer is not unique to China; most political and economic elites in major (and minor) capitalist countries show such transfer. What is rather unique in China is that this transfer traverses freely between the public and private sectors and between political and economic hierarchies.

Reward and Control of Organizations

Control and stratification of organizations. Political control extends from personnel to the organization itself. Each state-owned, controlled, or affiliated organization carries a rank in the hierarchy of all public organizations. Following the Soviet Union's wartime socialism tradition and continuing from the state socialism era (1949–1978), all state work units have ranks similar and parallel to military units. For example, a top national university carries the rank of a 'division' and a local university a 'regiment'. To a lesser extent, calculable rankings apply to corporations as well, depending on the scope, size, and other criteria. Positions in corporations are likewise assigned ranks. Synchronization of organizations and positions makes it possible to transfer personnel across corporations with ease. CEOs of banks and oil companies are regularly 'rotated' (similar to regional military commanders), not only between organizations in the same sector but also across sectors. Furthermore, transfers occur that cross political and economic boundaries. A manager with a rank of regimental commander in a corporation may thus be promoted to a divisional commander position in the state or local government or institute. The transferability of personnel serves important functions. For one, the ultimate promotions and rewards are the top positions and ranks in the party and the state in Beijing. Therefore, even for corporate CEOs a promotion may mean not only a position of higher rank but also to an organization of higher rank (preferably in the central party or state bureaucracy in Beijing). The loyalty of the corporate executives is ultimately to the party and the state, not the board of directors, shareholders, or stakeholders. Of course, one significant criterion for being promoted is performance in the marketplace. In this manner capitalism is linked to rewards in the political realm as well.

Control of national champions and large corporations. The party-state manages a reward-and-control system over large and important corporations in the economy. The party-state maintains strong control of the top-ranked corporations in most sectors. These corporations include state-owned (e.g., oil companies, banks, steel); state-controlled (e.g., most large automobile, telecommunication, and transportation industries); and corporations/enterprises that are affiliated with central and/or local governments through capital, personnel, and other relations. While the private sector has grown rapidly in the number of enterprises and individuals employed, the leading corporations (national champions) in most sectors are public. (Some have argued that retailing may be the only sector that so far has minimal central state participation, Anderlini, 2010). According to a rating of the '500 strongest' enterprises in 2009 voted on by the China Enterprise Confederation and the Chinese Enterprise Directors Association, the top enterprises are all national enterprises. The leading 'private' enterprise, Jiangsu Shagong Corp., ranks thirty-fifth.^[3] Furthermore, many of the so-called public and nongovernmental enterprises (e.g., Huawei, Lenovo, Haier, Chery) are in fact closely related to

state institutions (universities, academies, or local governments). For example, Tengzhong Heavy Industrial Machinery Corporation, a little-known Chendu company, recently bid to buy Hummer from GM (but eventually failed to receive government approval and support). Tengzhong is listed since 2006 as a private enterprise. Tracing its background, it turns out to be a merged corporation from several state-owned (Sichuan Changdian Power) and provincial-owned (Sichuan Huatong Auditing) companies (*Financial Times*, 2010). The majority shareholder of Legend (the holding company of Lenovo) used to be the Chinese Academy of Sciences. It was recently announced that the CAS has reduced its shares from over 65 percent to 36 percent. Legend itself retains 35 percent of the shares and a new partner, China Oceanwide (a private enterprise, registered in Beijing), took over 29 percent. Thus Legend has nominally become a private majority holding corporation (Anderlini, 2009). These direct and indirect linkages allow the state and the party to exert control or influence on the strategies and execution of many private as well as public corporations' activities in the marketplace.

Control of Capital and Trade

State control of economic capital. Another important mechanism of political control of the economic sphere is the party-state's command of the capital. The party-state has direct control of vital economic capital as it controls all the major financial institutions. All major banks are under the control of a vice premier at the State Council. According to a recent report in the *Economist* (2010), about four-fifths of the assets in the banking system are controlled by 17 institutions, whose leaders are all appointed, ranging from the more visible, such as Zhou Xiaochuan of the People's Bank of China, to the vast and powerful China Development Bank, under Chen Yuan (son of Chen Yun, one of the pioneering Communists). Bank chiefs are readily shifted around (e.g., in 2006 Zhang Jianguo, the president of Bank of Communication, became the president of China Construction Bank, ostensibly one of its competitors). As mentioned earlier, the China International Capital Corporation, the most important domestic underwriter, is under the leadership of Levin Zhu, son of Zhu Rongji, a former prime minister. His two former lieutenants, Wu Shangzhi and Fan Fenglei, are now in charge of CDH Investments and Hopu Investment Management, two of the top private-equity firms in China.

China is expanding its SWFs. From an experimental beginning in 2007 with the establishment of the China Investment Corporation with assets of \$200 billion, China now has at least three (not including one in Hong Kong: Hong Kong Monetary Authority, with \$140 billion in assets) SWFs: The State Administration of Foreign Exchange (with assets of \$347 billion), China Investment Corporation (\$289 billion), and the National Social Security Fund (\$147 billion). Jointly they hold capital assets of \$783 billion, far exceeding the top three SWFs in the world (UAE – Abu Dhabi – with \$627; Norway with \$445; and Saudi Arabia with \$432

billion). As Western countries continue to deal with substantial debts, the unimaginable has happened – top Western debt managers travel to China to seek investment, primarily from its SWFs, in their government bonds. Carl Heinz Daube, the head of the debt management agency of Germany, probably the strongest economy in the West, travelled to China and Singapore in March 2010 to seek such investments.

Transferability of capital. With control of personnel and organizations, there is little wonder that the financial institutions cooperate fully with the directives of the party-state. When China responded to the world financial crisis in 2007–2008, it asked the banks to substantially increase its loans; the banks responded in unison and were much credited for the swift economic recovery. The stimulation package launched by the Chinese government in November 2008 in response to the financial crisis provided an occasion to illustrate how capital is transferred from the state to state-owned, controlled, or affiliated corporations. More than 75 percent of the stimulation fund (\$586 billion) was allocated to infrastructure work, almost all of which was allocated to corporations owned, controlled, or affiliated with the state or local governments (Elegant & Ramzy, 2009). Another avenue of the stimulation package was bank loans. In the first half of 2009, loans amounted to 7.37 trillion Yuan since the government intended to ensure that it met its 8 percent economic growth target for 2009. State-owned, controlled, and affiliated corporations are again favoured for loans from the banks and the SWF. Such loans come in handy when corporations engage in acquisitions. This accounts in part for the recent rush of Chinese automobile corporations buying foreign companies. In the last 6 months, for example, both Beijing and Shanghai Automotives have bid on shares of Saab. Shanghai Automotive Industry Corporation has also bid on the GM factory in India. These state-owned corporations will continue to acquire more foreign companies. Even privately owned companies rely on state financial institutions for their acquisitions.

Flexibility in investments. Capital transfer goes both ways. The state receives capital as the owner or shareholder from these corporations. In 2008, 26 percent of government revenues came from corporate taxes. It has the flexibility to increase or decrease its form of control or amount of shares as the state controls the board of directors and the top managers. In a crisis, when the state is in need of additional capital and other forms of aid, state-owned, controlled, and affiliated corporations are among the first to ‘volunteer’ contributions. Within 2 weeks after the earthquake that struck Sichuan in May 2008, these corporations had donated more than \$US645 million in cash and goods (McGinnis, Pellegrin, Shum, Teo, & Wu, 2009). Employees in these corporations were asked to donate their share of contributions ‘voluntarily’.

The state has little difficulty in expecting cooperation and coordination with local government corporations in investments. When the state decides to make a certain

investment, it simply asks the local government to comply. One outstanding example of the 'good' investment is China's dramatic commitment to developing sustainable energy. Within the last 2 years China has become the leading country in the development of solar power. First Solar, the solar cell builder based in Tempe, Arizona, signed a 10 year agreement with China to build the largest solar field in the world in Inner Mongolia. The project will eventually blanket 25 square miles of Inner Mongolia – slightly larger than the size of Manhattan – with a sea of black, light-absorbing glass. The solar field will dwarf anything in operation in the USA or Europe. At 2 gigawatts, or 2 billion watts, the solar plant could pump as much energy into China's grid as two coal-fired plants, enough to light up three million homes. CEO Mike Ahearn told *The Associated Press* before the announcement: 'The Chinese government is further along in its thinking about solar than we've imagined'. It would be impossible to create such a large field in the U.S. since energy policies are made at the state level, Ahearn said. Solar First signed a 'memorandum of understanding' with Wu Bangguo, chairman of the Standing Committee of the Chinese National People's Congress. China has promised to guide First Solar through the approval process and make the project profitable (Kahn, 2009).

Applied Materials, an important U.S. manufacturer of microchips, has ventured into making solar panels. In the past 2 years it has become the world's largest solar panel manufacturer and has built 14 solar panel factories in the world: five in Germany, four in China, one in Spain, one in India, one in Italy, one in Taiwan, and even one in Abu Dhabi. None is located in the U.S. Uncertainty of price and lack of connectivity and regulation on a national basis has made such investment costly and slow. As a result, 'our federal and state subsidies for installing solar systems are largely paying for the cost of importing solar panels made in China, by Chinese workers, using hi-tech manufacturing equipment invented in America', observed Thomas Friedman (Friedman, 2009). In October 2009, Applied Materials opened the world's largest solar research centre in Xian, China.

Coordination in diplomacy and foreign trade. The synchronization between the state and the state-owned, controlled, and affiliated enterprises and the national champions also operates well in foreign trade. Whenever and wherever the Chinese government signs a trade agreement with a foreign country in the developing world, China inevitably commits itself to providing infrastructure construction and natural resource (e.g., oil, gas, and other mines) explorations. Much of the work is then allocated to one or more Chinese enterprises without bidding. These enterprises selected by the Chinese government are inevitably state-owned, controlled, or affiliated or national champions. Some subcontracts may be extended to other local or Chinese enterprises at the discretion of the contracted enterprises (sometimes with the state's own choices). Most contracts stipulate the maximum number of Chinese workers so that some local workers are employed, but the majority of the managerial and technical personnel are Chinese.

This synchronicity has shown no sign of eroding or retreating in the past decade. Given the steady economic growth and accelerating accumulation of capital, China believes it is crossing the river nicely. China's fast and efficient response to the global financial crisis in 2007 and 2008 and results yielded thus far in its two-pronged state-directed approach (i.e., massive stimulations and investment in infrastructure, and massive bank loans) has only served to reinforce this form of CMC and the stone-feeling methodology.

The CMC in the Marketplace and Its Costs

The CMC of China, while exercising rigorous political control over personnel, organizations, and capital of economic entities, paradoxically offers extensive flexibility to the local governments and firms. Since the late 1970s when reform began, the Chinese government has implemented a decentralization process by which regional and local governments, first in rural areas and later in urban areas, have been delegated fiscal and administrative responsibilities to engage the market (Lin, 1995; Lin & Ye, 1998; Oi, 1992; Walder, 1994). Local governments in turn have sponsored firms, first as collectives and later as stockholding companies and other corporate forms, to compete in the marketplace. Oi (1992; 1995) recognized them as newly configured local-state-sponsored corporate entities (local-state corporatism).

Rather than as temporary or transitional entities, this pyramidal structure of a political authority at the top and market-oriented parts below has become typical in much of the country in the past two decades. In general, the central party-state delegates much fiscal and administrative authority to the regional and local governments (Zhang, 2006). Likewise, governments, central or local, delegate much fiscal and administrative authority to firms. The extent of such delegation varies widely from region to region and between governments and firms. It is pyramidal because the central political authority is largely invisible and seemingly far away in the marketplace where local governments and firms operate. But CMC in substance is more like an octopus; the central authority affords the local governments and firms the flexibility to reach every corner of the market locally, domestically, and globally and expects the firms to be nimble, efficient, and competitive. The firms, as capitalistic entities, secure and accumulate resources, organize resources in the production process, recruit cheap labour, and explore and exploit markets where they can compete advantageously.

We may describe the relationships between the centre and the local and the local and the market as 'fuzzy relationships'. Some of the fuzziness is unintended, as rules of the game have not been developed (Che & Qian, 1998). However, much of the fuzziness is intended so that governments and firms can maintain their flexibility to compete in the marketplace. Also, partly due to the delegation of authority and the fuzziness of relationships, firms show tremendous variations in

their organization, 'ownership', shareholders, involvement of foreign companies, etc. Nee and Yang (1999) observed a hybrid form of firms and thought it might be a sign of a transitional economy. But as Meyer and Lu (2005) and others show there may be indefinite forms and boundaries of Chinese firms as the economy in China advances. As a firm grows, it tends to create other firms, to gain leverage in multiple markets (domestic and overseas). Such reproduction of firms may be both lateral – to different markets, and vertical – taking aim at specific sub-markets. These firms can vary in organizational forms, the structure of ownerships, types of stakeholders, etc. Such conglomerated forms and institutions, however, are not unique to China; similar corporate entities can be found in Korea, Taiwan, and the Middle East. Rather than family-led as in those regions, Chinese entities (including state-affiliated business groups, see White, Hoskisson, Yiu, & Bruton, 2008) are guided by the political apparatus from the top down and yet organized as dynamic economic firms in the marketplace. This political-top and market-bottom corporate form offers two types of incentives for the local governments and firms. It offers fiscal incentives to the local entities (Jin, Qian, & Weingast, 2005; Meyer, Lu, Lan, & Lu, 2002), as profit-making guides the formation and operation of firms. Just as importantly, performance in the marketplace is an important criterion for political promotions for the executives (Li & Zhou, 2005; Zhou, 2007).

The loose coupling and fuzziness of the fiscal and administrative link between the centre and the local governments create opportunities for the local governments to mimic the central party-state hierarchy and its managed capitalism. They also act like capitalists. These local governments organize their own party-state capitalism – locally managed capitalism. Governments and bureaucratic branches seek sources of revenues (e.g., land development) and establish their sponsored or affiliated firms in the marketplace. Firms compete and seek profits and governments extract or share the profits. Firms, likewise, are allowed to establish more firms in multiple markets or sub-markets. Firm executives are evaluated for their economic performances and afforded opportunities to move up to the local party and government's hierarchy of positions. Ultimately and theoretically, the local governments and firms are all part of CMC, under the political command of the central party-state. In reality, the local governments and firms gain a degree of administration and fiscal autonomy and siphon off surplus values or profits to fulfil their own needs and interests.

CHALLENGES TO CMC

In addition to the potential problems detailed above, CMC faces other serious challenges both endogenous to the political-economy system and exogenous to the system. Synchronicity of the state and corporate interests makes it much harder to control and flush out corruption and nepotism. Corruption has become a deep and pervasive problem, penetrating the bureaucracy from the top

to the bottom. Recent cases against top party cadres in Guangdong, Zhejiang, and Chongqing as well as various ministries of the central government have demonstrated the seriousness of the matter and the determination of the party to root out corruption. However, revelations regarding the top leaders in the party's Central Disciplinary Investigation Commission as well as top cadres in both the central government and several regional and local governments and parties suggest that the problem has worsened and has penetrated to the core of the party in recent years.

It is widely known that many corporate and government cadres siphoned off money and fled abroad. Take the capital city, Beijing, as an example. Beijing Municipal People's Procuratorate's Office announced in 2008 that the number of party officials fleeing China had reached between 16,000 and 18,000 since the mid-1990s, taking over 800 billion Yuan overseas. The money was misappropriated primarily from major projects such as land development, tax revenue, loans from financial institutions, funds allocated for government expenditures, and national economic programmes. In the past 30 years Beijing Municipal People's Procuratorate prosecuted over 16,000 cases of corruption and bribery (*Xinhua Net*, 2009). In Chongqing, the newly appointed party secretary, Bao Xilai, initiated a massive campaign against corruption in the municipal government and found deep-rooted corruption and crime even in the core agencies such as the police force.

The party's Central Disciplinary Investigation Commission holds the primary responsibility for upholding party members' behaviour and discipline, and counteracting their corruption. Confronting the problem of cadre corruption, in 2006 it issued regulations 'regarding leading cadres' reporting of their personal significant events' (*News Release*, 2009). The regular report includes events such as marriages, going abroad for private purposes, spouse and children living abroad, and spouse and children engaging in business abroad. Realizing that there were some serious gaps, the Commission reissued the regulations in September 2009 and added houses owned, investments, and spouse and children's job situations. Furthermore, the Commission focuses on cases of cadres involved in corruption, business and commercial bribing, implications in 'group or collective accidents', and in activities damaging public interests. Such anticorruption measures seem to follow the 'feeling stones to cross the river' approach as well – installing measures as corruption is discovered.

Social stability has also been problematic. The country responded well to the natural disaster of the Sichuan earthquake, but the violent ethnic protests and clashes in Tibet and Xingjian indicate deep-seated ethnic and religious problems that place the party and the state in an awkward position. Following the Stalinist model, China designated Tibet and Xingjian (along with Ningxia, Inner Mongolia, and Guanxi) as autonomous ethnic regions rather than conventional provinces. The ostensible purpose was to respect and sustain the linguistic, cultural, religious,

and other values of the dominant minorities. However, the political leadership (party secretary) has always been in the hands of Han cadres (the only exception was a brief stint of Seypidin Eziz in Xinjiang 1973–1978). Ethnic Uighur and Tibetan officials have served as chairmen of the regional governments, a secondary nominal leadership. The Dalai Lama's escape and the exile government in India have allowed international connections for the local resistance. Likewise, Uighur's connections to Uighurstan communities in Kazakhstan, Kyrgyzstan, Mongolia, Uzbekistan, Turkey, and other central Asian countries occasionally evoke the call for an East Turkistan state.

These historical institutions seem difficult to reverse. It would be dangerous for these autonomous regions to revert back to provincial status as the minorities would surely and strongly oppose. Yet to date the party has shown little confidence in yielding party leadership to minority cadres. In the meantime, massive immigration of Han people into these regions has further aggravated ethnic tensions as the minorities see them as non-natives who intend to infringe on their land and natural resources and take over better jobs and the economy. These Hans, having achieved critical mass, have also become more aggressive in their confrontations with the minorities. It is becoming increasingly difficult to seal off these regions from the outside world as the Internet, camera phones, and other devices record and transmit news of confrontations swiftly and effectively through security to reach the outside world. Protests and violent clashes with authority are not limited to the border regions. Unemployment, land disputes, complaints about local officials' corruption and injustice, ruthless handling of appeals and protests, and numerous other issues have fanned hundreds of thousands of such protests and clashes throughout the country each year.

LEGITIMIZING CMC: FROM MARXISM TO ECONOMIC GROWTH AND SOCIAL STABILITY

Confronting these serious challenges, the Communist Party is reaching a fork in the road where it must make choices. A critical and fundamental element in the choices is the ideological basis on which the party legitimizes its dictatorial rule and demands for mass support. From its inception, the ideological guide of the Chinese party-state has been the Marx-Lenin-Mao doctrine of communism and socialism. In the early period of the People's Republic, the Marxist-Leninist Soviet Union ideology guided institutional creation and development. The Soviet model guided every phase of society, ranging from urban–rural segregation and an emphasis on building heavy industry, to rearrangements of educational systems from nursery school to higher education, the work unit as the core in society and for all urban residents, and, most of all, the supremacy of the party. The ideology focused on class struggle in China, rooting out all bourgeois classes and individuals, and on reducing private properties and inequality to the minimum.

This ideology and its implementation culminated in the ultimate societal struggle and catastrophe of the Cultural Revolution in which the ideology became a pretence for all factions who were desperately trying to preserve their survival by reducing and eliminating their (and the peoples') enemies. Deng Xiaoping's initiatives in rural reform were the beginning of pragmatically moving away from this ideology. Deng understood that it would be impossible to do away with the ideology as it would shake the foundation of all institutions and bring a vacancy that invites chaos and disorder. He chose to redirect the ideology, not to another ideology but rather to pragmatism – seeking truth from practice. His famous saying ('crossing the river by touching stones') reflected not only his approach of pulling away from the prevailing but failing ideology, but also his philosophical stance: let us not argue ideologically and let us be guided by what works. What he wanted was a modern China ('the four modernizations') – a China that was rich, self-sustaining, stable, and orderly. Steps in reform slowly did away with the Stalinist institutions (e.g., reforms in schools and higher education, unequal pay, increasing private property and ownership, and democratic attempts – the big-letter wall newspapers, although this failed because it went too far). Even when the reforms were *too extreme and the society was on the verge of challenging the official ideology* (e.g., the June 4 Tiananmen struggle in 1989), Deng continued to push his pragmatic approach of reform by giving his blessing to the economic developments in the South.

Avoiding confrontation with the official ideology, his successors have continued the pragmatic approach in economic reforms. Institutional reforms have brought about enormous strides in eliminating large portions of inefficient state enterprises. Instead of vacating the economic sphere to a private sector, the party leaders took steps to rebuild public corporations that could compete in the world market, while retaining and strengthening the party's control of the government and the economy. With favourable foreign trade, cheap and massive labour, and an influx of investments and manufacturing factories from Taiwan and Hong Kong, the government devised policies of protecting domestic enterprises by blocking off certain key sectors from foreign corporations and opening up joint ventures where state-controlled and affiliated enterprises could take advantage of foreign capital and learn from foreign management and technology. China survived the Southeast Asian financial crisis of the late 1990s and weathered the world financial crisis of 2007–2008. While other countries suffered, China gained by comparison. The 'trade rather than aid' foreign policy allows China to avoid any political and ideological traps and apply Deng's pragmatism to dealing with other countries.

By all measures, this subtle but important pushing away from the Marxist ideology towards a centrally managed capitalistic programme has been a success. Coupled with the call for social stability ('harmonious society'), the party-state has used these two pillars to justify its centralized authority. Giving the people a share of the growing wealth and a sense of social security, the party-state hopes to gain

their approval and support for this party-state dictatorship. Yet these two pillars, economic growth and social security, represent pragmatic programmes – they are operating mechanisms. Their associations with the party-state dictatorship are ideological rather than theoretical or logical derivations. Many countries have attained both economic growth and social stability without a party-state dictatorship. Parting ways with Marxist ideology is historically subversive and organizationally disruptive, yet a transformation of ideology is needed to keep the two pillars on solid theoretical ground and provide justification for the authority of the party-state in CMC without rupturing the party's roots in Marxism. In the following, I identify three ideological paths and speculate that China is exploring one ideology – the indigenous Confucian ideology.

TRANSFORMING IDEOLOGY: TOWARDS *XIAOKANG* AND *DATONG*?

China, it seems to me, or CMC, is faced with three possible ideological alternatives: subscribing to the western or the Dutch-British-American capitalism, committing a transition towards the mature stage of socialism, or moving towards an indigenous-based enlightened authoritarianism – *Xiaokang* and *Datong*. The first alternative is risky not only because it is deemed as likely to bring about instability and slow and inefficient responses to changes and opportunities, but it might fatally up-end the one-party state. It would have to come about through violent revolution.

Both the second and third alternatives are viable ideologies in China. In fact, there has been a tendency in official pronouncements and documents to mix the two: the primary stage of socialism, describing the present era, is a stage where productive forces are unleashed to achieve national wealth and prosperity for all and where a harmonious society with fairness and justice is obtained – *Xiaokang*. The following will explore these two ideological alternatives and assess their relative viability.

While the party leadership continues to claim Marxism as its ideological guide and add some indigenous idioms (Deng's pragmatism, Jiang's 'three principles', and an insistence that this is the primary stage of socialism), a new evolution of the ideology has begun to emerge (Lin, 2008). This was first mentioned by Deng in 1979 when he indicated that for China modernization meant *Xiaokang* (see a recent narrative linking *Xiaokang* and *Datong* to Deng Xiaoping's thoughts: Wang, 2003). Over two millennia ago, Confucian scholars compiled and narrated two visions of societal development in the *Book of Rites*. These two visionary societies both purportedly existed in ancient times. In fact, they were both idealistic societies. In the earliest of times, it was claimed, there was a world of great harmony, *Datong*. In *Datong*, the ultimate way, the world (authority) belongs to the public, where the wise and able are elected, trust and harmony prevail, and men care not only for their kin

but for all. After *Datong* vanished, it was purportedly replaced by a more modest society, a society of good living and wealth, *Xiaokang*. In *Xiaokang* the world belongs to the family (authority became inherited), society achieves moderate prosperity by following moral principles (propriety and justice) regulated by institutions, with all individuals claiming their rightful places in the hierarchical society (e.g., emperor–official, father–son, among brothers, and husband–wife relations) and performing their rightful duties for their own benefits. The state defends the society. Wise men, who follow moral principles, are trustworthy, and exercise legal authority are in charge of the state. Those in authority who do not follow these principles can be removed and are viewed by the people as pariahs.

It is clear that in Deng's conception the primary stage of socialism substantially overlaps with *Xiaokang*, where the principal goal is achieving a certain level of overall prosperity while society maintains stability and harmony under the leadership of the party-state (Lin, 2008; Wang, 2003). The significance of this indigenizing socialist ideology cannot be overlooked. *Xiaokang* stresses order, harmony, and respect for authority and concern for all. These principles are consistent with the visions outlined for the primary stage of socialism. At the macro level, they legitimate the authority of the state and the party based not so much on political ideology as on their wise and competent management of society's well-being and peoples' desire for better lives. At the micro level they expect that indigenously valued social relations and morality will promote and sustain harmony.

Deng, however, interpreted *Xiaokang* narrowly, strictly in terms of economic growth and equality. His 1979 vision of *Xiaokang* was attaining a GDP of \$US1,000 per capita.^[4] In 1990 the 5 year plan added that 'the so-called *Xiaokang* level indicates the elevation of the quality of life from minimal requirement of food and shelter to sufficient comfort in clothing and food' (China.com.cn, 2002). By early 2000 most of the economic and social indicators that Deng had suggested in 1979 as goals for modernization, or *Xiaokang*, had been achieved, with the exception of income equality. Yet *Xiaokang* has remained a focal rhetoric, widely cited in all important official documents and in the 5 year plans. In 2002 Jiang Zemin outlined the plan for the construction of the *Xiaokang* society over the next 20 years: 'We should concentrate efforts to fully construct a still higher level of *Xiaokang* society, so that the economy will be further developed, democracy comprehensive and healthy, science and education more advanced, culture more prosperous, society more harmonious, and people's living richer' (China.com.cn, 2002). Thus *Xiaokang* was extended from mere economic goals to economic, political, sociocultural, and technological goals.

Left unsaid was the fact that the linkage of *Xiaokang* and the primary stage of socialism could imply that both are transformational stages towards the mature stage of socialism. Also left unsaid was the articulation or theorization of the operational mechanism whereby the present form of capitalism can be transformed into socialism in which most, if not all, capital belongs to the state or the public. To

justify the rhetorical silence, in February 2007 Wen Jiabao emphasized that China would remain at the primary stage of socialism for generations, perhaps for 100 years (Wen, 2007). The goals for socialism were not only to unleash productive forces, but also to create social fairness and justice in a 'prosperous, strong, democratic, civilized and harmonious modern socialist society' (*Xinhua Net*, 2007). Thus Deng's economic goals, the releasing of productive forces and the creation of wealth, have now been supplemented by the social and political goals of fairness and justice, and even democracy. With these expanded goals, *Xiaokang* will not be fully attained in 20 years as envisioned by Deng or another 20 years as advocated by Jiang, but rather not for another 100 years. In this long view, the articulation of the transformational mechanism from CMC to 'mature' socialism can likewise be postponed for generations. This postponement, I suggest, indicates more than reluctance on the part of the leadership to deal with a difficult theoretical issue. Rather, it represents a strategic decision to create space and time allowing for a possible ideological transformation. Would *Xiaokang* lead to *Datong* rather than mature socialism? We take a closer look at the political institutions depicted in these two narratives in order to gain some clues.

In *Datong*, 'all under the heaven are shared (authority is not inherited); the wise and the able are elected; and faith and harmony are advocated' (Wang, 2003). It is a system clearly based on democracy in order to achieve harmony. It is a society that is ruled by the wise and the able through elections, and where individuals care not only for their kin but for all; wealth is not hidden by individuals but shared; behaviour is not motivated by the self but by others as well; and all disadvantaged (the childless elderly, the widowed, the orphaned, the handicapped, and the sick) are taken care of. In other words, in this society democracy brings about wise and able leaders and harmonious social relations through generalized trust and norms of reciprocity.

In lieu of such a democratic, trusting, and reciprocal society, *Xiaokang* is a society where 'all under the heaven are for the self' (inheritance and succession rule) and everyone is expected to care for him/herself. Rites, rituals, and norms, however, are institutionalized: 'rituals (礼, or propriety) and justice (义) bind individuals'. Institutions define social relations (between the emperor and officials, between father and sons, among brothers, and between husband and wife), and property (land and communities). All resources and efforts are for oneself, the wise and the brave are esteemed, and the faithful are rewarded. Thus 'strategies are used and military confrontations arise' (Wang, 2003). *Xiaokang* offers six ancient wise emperors (all succeeded by sons) as exemplary because they followed rituals (propriety) and justice in rewarding and punishing their subjects. 'If any emperor does not follow rituals and justice, he can be removed and despised by the people' (*Xiaokang*). *Xiaokang* depicts a social system that is principally authoritarian but allows for the promotion of self-interest. It is a combination of authority and capitalism. Under wise and able leaders, the society is hierarchical and orderly.

We need to remember that these narratives were constructed over 2,000 years ago and are steeped and bound in Chinese history and culture. They are not theoretical in the contemporary and scientific sense. Nevertheless, they provide typologies and identify elements of theories. These narratives indeed suggest that CMC is closer to *Xiaokang* than *Datong*. Authority is recognized, but its legitimacy is based on its upholding of moral principles and institutions and its respect for self-interest. It is under these conditions that wealth is obtained and social order maintained. It is not far-fetched to view such an explication as legitimizing the authority of the Communist Party in Chinese society. Instead of insisting on the fundamental need to retain class struggle as the core principle, it can now be argued that only under the wise and able Communist Party's leadership can China strive for better economic and social well-being.

The Marxist rhetoric remains pervasive in official speeches and documents, but the increasing emphasis and attention paid to *Xiaokang* as a vision is subtle but important. *Xiaokang* is an indigenous ideology deeply engrained in the Chinese culture, universally admired by the Chinese, and espoused by Deng, a highly esteemed pioneering leader who heralded reform and brought new life to the party and state in China. An ultimate break from Marxism may not be necessary in the near future as the primary stage of socialism and therefore *Xiaokang* may last for generations. In the meantime, the ideological strategy has been to link *Xiaokang* to socialism. Deng was quoted as saying, 'Without socialism, *Xiaokang* cannot be realized in China'. Furthermore, constructing the *Xiaokang* society has been identified as the task of the 'historical mission' of the primary stage of socialism (Wang, 2003).

THE TRANSFORMING CMC: DEMOCRATIZATION?

Interestingly, China may have already attained the *Xiaokang* scenario. CMC represents a combination of authority and self-interest. A system is principally in place where occupants in most authority positions can be removed if they do not follow moral rules and institutions and if they are despised by the people. By the beginning of the twenty-first century, most of the economic indicators envisioned by Deng had been attained. The only goal yet to be attained is 'common prosperity' (共同富裕, or sharing of prosperity). 'Common prosperity' may be interpreted as the elimination of poverty, the elimination of the income gap, or the sharing of wealth by society. One path to common prosperity is to move from the primary to the mature stage of socialism in which private ownership of property is eliminated. Even if one ignores the impractical reality of appropriating the growing number of private properties and accepts that it would take 'one hundred years' to make the transition, what is the theory or proposed mechanisms guiding such a transition? So far there has been a total lack of substantive discussion on such a theory.

On the other hand, will the system follow the ideological path from *Xiaokang* to *Datong*, as conjectured in the ancient texts? This evolution depends on the development of democracy where authority is not inherited and instead is delegated to the wise and the able by election. It is obvious such a struggle for democracy and *Datong* is a path that is politically treacherous, arduous, and distant. Yet the movement in that direction may be already underway and detectable. Democracy may have been an indigenous notion in utopian societies. It also happens to be one salient element in contemporary capitalism. As articulated elsewhere, democracy is not a necessary causal element for the development of capitalism, but capitalism does enhance the development of democracy (Lin, 2008). Growing capitalism creates wealth among more and more individuals who desire that their voices be heard and demands be met. Markets benefit from moral principles and institutions. Income equality may be an unattainable goal, but reduction of income inequality and poverty is a key ideal for upholding the social order. All these features of capitalism increase the common peoples' desire for direct or indirect participation in deciding who occupies the authority positions. As managers of the CMC, the leadership of the Communist Party has increasingly been under pressure to recognize and meet these demands. It is therefore not surprising that calls for democratic processes can be heard at all levels.

The discussions and debates about democracy all carefully draw on the writings of Deng and link democracy to socialism. For example, in 2004 Hu Jintao pronounced that 'developing democratic socialism is always a goal of our struggle. We have clearly pointed out that if there is no democracy there is no socialism . . . Good institutions of democratic socialism guarantee people's rights in democratic elections, democratic decision making, and democratic supervision' (*Xinhua Net*, 2004). Note the causal implication that democracy is a necessary condition of socialism in this statement. Xie (2008), a former vice president of Renmin University, elaborated on democratic socialism. He stated that Deng's argument that one goal of *Xiaokang*, to have wealth shared by all, reflected the true merit of socialism – not to get rid of wealthy individuals but to elevate those who do not have wealth (i.e., the working class) so that they can attain wealth. Thus, rather than class struggle, which Xie felt deviated from the original and true intent of Marx, democratic socialism advocated eliminating inequality by elevating the wealth of the poor. In March 2008 Wen Jiabao suggested that the Chinese government was prepared to expand 'socialist democracy' under the leadership of the party: 'We will expand people's democracy, improve democratic institutions, diversify its forms and expand its channels and we will carry out democratic elections, decision making, administration, and oversight'. Such reforms would also include strengthening administrative oversight, fighting corruption, and creating a more efficient government that is ruled by law (*Associated Press*, 2008).

However, counterattacks came swiftly and emphatically. On February 9, 2009, the *People's Daily* published an editorial titled 'China Will Never Adopt the Multi-

party System' (*People's Daily*, 2009). It insisted that the multiparty system in the West is an institution of capitalism that allows capital and political power to be held by the ruling class. The system would also increase social fragmentation and disharmony, the author claimed. Wu Bangguo, chairman of the Standing Committee of the National People's Congress, stated in his report to the Congress meeting on March 9, 2009, that China will never copy 'tricks' from the West: multiple parties taking turns in holding power, separation of powers, or two separate legislative chambers (China.com.cn, 2009).

These counteroffensives from authoritative sources did not suppress the voice for democracy. Within 2 months, in May 2009, Peng and Xin (2009), retired deputy editorial chief and deputy director of public relations of Xinhua, authored an article titled 'The Spirits of May Fourth and the Universal Values' that pointed out that the true spirit of the May Fourth Movement was that people are the masters and that practice follows the truth. Both principles, they observed, were imported. Past mistakes were made because these principles were not followed. They further noted, without identifying the source, that 'some individual' had made the statement about not adopting tricks from the West, but 'others' criticized this person and this statement for committing the same mistake of not allowing democracy and not understanding the truth. They further pointed out that these democratic and open discussions had not been reprimanded by the top leaders. The authors concluded that China may be turning away from the historical mistake of dictatorship and returning to the spirit of May Fourth.

In the latest party congress held in September 2009, the concluding statement advocated that the party must be close to the people 'by blood and flesh'. Among the important decisions made were: promotion of democracy within the party, consolidation of the party at the basic level, and insistence on rooting out corruption. These calls for democracy within the party and in general have seen modest but significant results. As mentioned earlier, the party now demands that all top cadres periodically report assets of all family members and accounts abroad. A web site has been created (<http://www.12388.gov.cn>) for reporting corruption at the central and local levels. The party is studying a new election procedure to select delegations to its congress – the number of delegations assigned to each province and city, for example, would be proportional to their membership size.

The media has gained leverage in reporting corruption cases and has demanded government transparency. An official truck driver in Shanghai was recently waved down by a person who sought a ride and offered the driver a fee. The driver was then arrested for accepting a bribe. As it turned out, the rider was an agent planted by a local government agency. The driver appealed to the media, which reported the story. The local government soon announced in a press conference that the rider was indeed part of a larger 'fishing' scheme and the incident should not have occurred. In the past, the government would have rarely retracted such a case, let

alone in a press conference. In the media this case is held up as a demonstration of governmental transparency.

Grass-roots democracy is reflected in various forms of civil society. For example, religious groups continue to grow in number and size. A recent estimate put the number of Christians (Protestants and Catholics) at 100–125 million (probably including household church members). The number of believers in Buddhism, Taoism, Islam, and other faiths has also seen modest to significant growth. In comparison, the Communist Party claims a membership of 74 million. Another rapidly developing grass-roots democratic movement is the rising number of homeowners associations in urban cities. Since most housing became privatized in 1994, the Ministry of Construction called for the formation of associations of residential neighbourhood's property owners and occupants; numerous associations have since been formed voluntarily. According to Read (2008), by the end of 2003 there were 4,756 homeowners committees in Shanghai. Many of the associations were inactive or passive; others are subject to the command of neighbourhood committees or property developers. Yet Li (2008) argued that homeowners associations are gradually learning to assert themselves, and the three parties (i.e., the homeowners associations, the neighbourhood committees, and property developers) now engage in power relations. As the homeowners associations gain their independence, learn how to form effective leadership and collectivity, and create networks with resourceful governmental and other agencies as well as other homeowners associations, they will likely become a uniquely powerful organized civil society in urban China.

Village head elections (with multiple candidates), another grass-roots democratic process, began some 20 years ago, probably in the Buyun township in Sichuan (O'Brien & Li, 2000). By now most villages have village committees and most committees elect their members (one estimate put the number at 95 percent). How the elections are conducted varies greatly. Whether and how the elections can be elevated to levels of townships and counties is still under debate and study within the Communist Party. One thing is clear: the electoral process for finding grass-roots leaders will slowly but surely proceed. Wen Jiabao proclaimed that China would 'resolutely advance in democracy, including direct elections', even though he did not mention possible elections beyond the village level (Fong, 2005).

In short, democratic demands and practices have emerged at all levels of Chinese society. They do meet resistance, either for ideological or self-preservation reasons, but for the past 2 years they have increased in volume and strength. Of particular interest is the increasing volume of discussion on democracy within the party. Some capitalistic and democratic societies (e.g., Japan) have a dominant political party in which multiple factions compete. These within-party factions do not differ substantially on ideology. Rather they may represent social demarcations (e.g., rural versus urban interests, religious groups, professional or occupational groups, regional interests, etc.). Becoming the major faction in a particular election

depends on both endogenous (e.g., charismatic leaders, demographic shifts, and mobility) and exogenous (economic conditions, external challenges, and natural or man-made disasters) factors. Given the nature of the party-state status, this process would seem less risky and more viable in the near future for China.

CONCLUSION: THE FUTURE OF CHINESE CAPITALISM

For the past three centuries industrialized states in North America and Western Europe have equipped themselves with political, military, and economic powers and organized large international corporations. Espousing the ideology of liberal capitalism – free markets and free competition – these states, through their international corporations, have been able to exploit and appropriate resources around the world and accumulate and reproduce capital. The emergence of state capitalism since the 1970s reflects the awareness of third-world countries of the need to preserve and protect their resources from being appropriated by first-world capitalist states. Using the state's control over valued resources, they have been able to resist such external appropriation and build their own large corporations (e.g., national champions). In the 1990s these self-preserving capitalistic states have been joined by post-socialistic states such as China and Russia. Now state capitalism not only affords these states the preservation of valued resources, but also the organization of large and capital-rich corporations (including the SWFs) competing in the world market.

In this essay I have placed China among these state capitalism countries and highlighted one sustaining trend in current Chinese capitalism: the continuing consolidation of state capitalism tightly managed by the party-state (the CMC). The CMC in part reflects the character of state socialism from the past – central command of the economy. But in contrast to the expectation that as China moves towards a capitalistic state the central command institutions will erode, for more than two decades we have witnessed further consolidation of state power over both politics and the economy.

Centrally managed capitalism is not set in stone. I have speculated in this essay that the Communist Party has increasingly justified its dictatorial leadership for the sake of maintaining economic growth and social stability. By arguing that China is at the primary stage of socialism and introducing the indigenous ideology of *Xiaokang*, the party attempts to convince the Chinese people that it is necessary to maintain party authority and to engage in capitalistic measures at the same time. I argue that the party is facing a choice of either articulating the mechanism by which the primary stage of socialism will transition into the mature stage of socialism – turning private capital into public capital – or allowing the process of democracy to unfold as anticipated by *Datong* and capitalism. Having noted the absence of proposals for such a transitional theory of socialism but more calls and enactment of democracy, I speculate a slow but firm infusion of democratic elements will occur at every level.

It is too early to tell how these transformations, indigenizing the ideology and incorporating democratic practices both inside the party and at the grass-roots level, may affect the viability of CMC. The ideal solution for the Communist Party and those in power is a CMC with a democratic character, just as it has acquired a capitalistic character. This may be a risky and treacherous process, but lacking an alternative (i.e., moving towards the mature stage of socialism and eliminating non-public capital), the party must try. If successful, this ultimately transformed CMC can reduce tension with liberal capitalism and provide a more stable paradigm of state capitalism. If it fails, it will bring chaos and upheaval 'under the heaven' (天下大乱), and turn the political and economic order of the world upside down. There is an urgent need for scholars and theoreticians to contemplate whether and how *Datong*, in its modern form, can mix with socialism. In the meantime, the Communist Party will carefully manage the transformation so that it will not bring about the worst scenario – its downfall from power. What we can thus expect is that the party will use its tried-and-true methodology of crossing the river by touching the stones.

NOTES

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- [1] Excluded from this discussion of the crisis-cycle thesis is the possibility that the state, due to debts, weakened military power and other deficiencies, cannot rescue the financial crisis. Ferguson (2010) argues that imperial collapse may come much more suddenly than many historians imagine and warns that a combination of fiscal deficits and military overstretch might bring about the sudden demise of the U.S. as an empire.
- [2] All Chinese names mentioned in the article are based on last name first.
- [3] The nature of Shagang Steel, like most large 'private' enterprises, is ambiguous. Typical among the Su-Nan model firms, the company was originally a collective enterprise under the jurisdiction of the city of Zhang-Jia-Gang. Shen Wen-rong was appointed as the CEO and party secretary in 1984. Through his able leadership the steel company expanded quickly, and in 2002 it reduced the shares of the city (the collective) to 25 percent while employees (30 percent) and leaders (45 percent, including Shen's own share of 17 percent) became the majority owners. Two years later, Shen further reduced the collective share and increased his own share to 30 percent. He remains the party secretary as well as the CEO of the company and was quoted as saying, 'Foreign reporters think I do not speak like an entrepreneur, and more like a party member. Well, I am a party member so I speak like a party member'.
- [4] In 1982 Deng also stated (Selective Works of Deng Xiaoping, vol. 3, p. 64) that 'the so-called goal of *Xiaokang* is to reach a GDP of \$US800 by the end of the century'.

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Nan Lin (nanlin@duke.edu) is the Oscar L. Tang Family Professor of Sociology at Duke University. His academic interests have focused on social networks, social support, and social capital. He has constructed theories, devised measurements (e.g., the position generator), and conducted empirical research in each research arena. Currently he is conducting national surveys in mainland China, Taiwan, and the USA on the production of and returns to social capital. He has authored or edited 11 books (including *Social Capital: A Theory of Social Structure and Action*, 2001, Cambridge University Press), and numerous journal articles and book chapters.

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