



## A New Agenda for Research on the Trajectory of Chinese Capitalism

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**ABSTRACT** This article sets a new agenda for research on the trajectory of Chinese capitalism. We first critically review the conflicting views on the causes of China's economic development. Then we suggest that insights from the comparative capitalism and economic sociology literatures can provide theoretical tools to understand the critical features of Chinese capitalism in a more systematic manner. The comparative capitalism literature can help us understand how Chinese capitalism resembles or differs from other varieties of capitalism in terms of the relationships between government, firms, and workers. The literature on economic sociology provides insights about how particular markets have evolved and become stabilized. We use these perspectives to suggest a set of possible research agendas for studying Chinese capitalism.

**KEYWORDS** Chinese development, comparative capitalism, economic sociology, research agenda

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### INTRODUCTION

The growth of the Chinese economy and its dramatic effects on reducing poverty in China is perhaps the most important change in the world economy in the past 30 years. Understanding these changes and China's complex economy has become the work of a small army of scholars both outside and inside of China (for overviews, see Chow, 2007; Lin, Cai, & Li, 1999; Naughton, 1995, 2007; Qin, 2008; Tsui, Bian, & Cheng, 2006). Academic theories of market development have frequently been based on the Western European and American experiences. This is in spite of the fact that the Chinese experience seems to defy the basic principles of many of those theories. Most obvious are the huge and continuing role the Chinese government has played in economic development, the lack of the creation of effective legal institutions to govern transactions of all kinds, and the apparent lack of bottom-up countervailing political forces to ensure that the gains of economic growth are not siphoned by the people who control either corporations or the government (i.e., what economists call rent seeking). This

paper is thus motivated to provide a conceptual framework to understand the nature of Chinese capitalism.

The debate over what has happened in China is not only an empirical debate but a normative one as well. For example, economists (and some sociologists, such as Nee, 1989; Nee, Opper, & Wong, 2007) are generally sceptical of the role of government and *guanxi* (Chinese social networks) in Chinese development. From their perspective, whatever China got 'right' was the result of using price signals and clearer property rights to unleash entrepreneurial activity (e.g., Tian, 2001). To the degree that China is now being held back, it is because social and political forces continue to operate as opportunities for rent seeking (Qin, 2005). Such scholars recommend that the Chinese government do all it can to remove itself from the economy and ensure that local networks of entrepreneurs do not use their social connections to limit market entry and obstruct fair competition.

A second group views the government as a positive developmental state that will need to continue to nurture the Chinese economy (Oi, 1992; So, 2003; Wang, 2009). From this perspective, government officials in concert with economic actors operate to produce the right conditions for economic growth. These scholars applaud the efforts of government to pick winning and losing industries and to aid China in moving up the 'value' chain. Two main explanations have been put forward for why Chinese (local) governments are so development oriented. The first, termed 'market-preserving federalism', argues that the policy of fiscal decentralization and intergovernmental fiscal-sharing contracts, which started in the early 1980s, allowed local governments to benefit from local economic growth, thus generating their unprecedented enthusiasm for economic development (Li & Zhou, 2005; Montinola, Qian, & Weingast, 1995; Oi, 1992; Weingast, 1995). The second explanation highlights the impact of political incentives or career concerns for local officials. This view argues that the incentive provided by 'the Chinese central government to reward and punish local officials on the basis of their economic performance motivates them to promote the local economy' (Li & Zhou, 2005: 1744; see also Blanchard & Shleifer, 2001; Whiting, 2001; Zhang, 2008).

A third group of scholars focus on the role of social networks called *guanxi* as pivotal to the success of local economies and, particularly, to the newly emerged private sector (Peng & Heath, 1996; Peng & Luo, 2000; Wank, 1999; Xin & Pearce, 1996). Here, scholars argue that under the environment characterized by a poor legal infrastructure, weak property rights protection, deficient capital market structures, and high institutional uncertainty during China's transition, it is the social network ties that fill in these institutional voids (Peng & Heath, 1996; Xin & Pearce, 1996). Social network ties between firms and ties between entrepreneurs and government officials allow firms to successfully alleviate the barriers of the old command system, get access to critical resources, and find and exploit market opportunities (Krug & Hendrichske, 2008; Wank, 1999; Zhou, 1996).

Social networks also offer greater capacities for generating and transmitting new information (Boisot & Child, 1999). These scholars maintain the idea that social networks will continue to play important roles in China's economic development.

This paper first lays out these arguments in some more detail. The main theoretical problem is that the factors that are supposed to have led to Chinese economic growth are also held to have made that growth less than it could be, or the factors that had driven economic growth at one time period became barriers later. Given there is some empirical support for all these positions, this implies that the empirical work is probably based on a non-random or narrow sample. Part of this reflects the size of the country and the heterogeneity of the development projects. But more importantly, this reflects the limits of empirical study and the lack of systematic, overarching theoretical thinking about what is happening.

We propose that one way out of this morass is not to expect to discover what is going on in China through a bottom-up empiricist approach. Instead, it is necessary to pursue a more theoretical and conceptual agenda. To push forward such an agenda, we consider the literature from comparative capitalism and economic sociology that have so far been ignored. We use these conceptual apparatuses to suggest empirical projects that might lead to a better understanding about the nature of the Chinese economy.

Discussion about the Chinese economy usually compares it either to the former Soviet Union or the United States (or some stylized version of the US model). But the study of national capitalisms has revealed a great deal of variation across societies in their linkages between governments, markets, and labour. Close scrutiny will find that the current Chinese economy resembles some of the European economies and East Asian developmental states in this regard, and we explore how these other forms of capitalist systems offer insight into how one might do research on China's present and future. The literature from economic sociology offers ways to study the social structuring of markets. These tools allow us to clarify how market competitors actually produce products and ties to their suppliers and customers.

We use the theoretical tools of economic sociology and the comparative capitalism approach to evolve some hypotheses about what might be going on in China. One advantage of having a more refined conceptual apparatus is that it clarifies what kind of evidence is necessary in order to get a better handle on what firms are really doing. Much of this evidence is publicly available and does not rely on interpreting secretive (or non-transparent) governmental actors.

Our purpose is not only to look backward but to look forward as well. That is, we can get clues about the direction of the Chinese economy after 30 years of reform from the discussion and understanding of what happened in the past. As any development trajectory is path-dependent with its own logic, the future of Chinese capitalism can be informed by the past and present situations. Once one

understands the key institutions that are set in place, one can predict how those institutions will respond to new challenges and opportunities in the future.

## **CURRENT DEBATES OVER THE STRUCTURE OF CHINESE CAPITALISM**

One of the most important aspects of the debate over what has caused rapid economic growth in China is how people view the role of the state. One view suggests that China is transitioning towards some form of market economy (e.g., Nee, 1989). This economy will be based on the private ownership of firms, which will be embedded in networks of local and regional suppliers and customers, and the market allocation of resources. In this model, the state is seen as retreating from the economy and giving it over to the actions of private entrepreneurs. This perspective mainly views the government as an impediment to sustained economic growth.

The other vision is one of continued state-led development with the Chinese government continuing to play an important role. In this view, the government has altered its development strategy from top-down control to one where it will promote a mixed economy. The positive role of the Chinese government includes many aspects, such as choosing a suitable national development strategy that fits China's competitive advantage (Lin et al., 1999); creating institutional incentives that lead to 'market-preserving federalism', which has greatly motivated local governments to develop the economy (Blanchard & Shleifer, 2001; Montinola et al., 1995; Oi, 1992; Weingast, 1995); opening to the outside world and aggressively attracting foreign investment (Yang, 1996); rationalizing bureaucracy and government administration (Guthrie, 1999); and restructuring industries in order to create some national champions to meet worldwide competition (Wang, 2009). Here, the view is that the government will control certain strategic industries, own core firms and continue to manage the economy, labour relations, and the allocation of capital. It will allow private entrepreneurs to operate and individuals and families to amass private fortunes. The government will work to sustain its legitimacy by pushing forward programmes for economic growth, but it will continue not to tolerate political dissent.

Note that both of these perspectives contain a normative edge. For scholars who want to see the withdrawal of the state from the economy and the eventual takeover of the economy by private entrepreneurs, the triumph of what they view as US-style market capitalism is a good thing. The transition, from this perspective, will eventually become self-reinforcing because it will overwhelm the ability of state actors to control the economy. For scholars who view the Chinese state as adjusting its tactics slowly over time, this process will maintain a role for a developmental state that guarantees the basic industrial, financial, transportation, and energy

infrastructure while underwriting the ability of firms to make investments in new industries. This will allow those firms to move up the 'value' ladder by becoming able to produce products that do not simply rely on cheap labour but on the use of advanced technology.

A second dimension of the debate focuses on how the Chinese economy is organized. Here, there are two perspectives as well. One perspective studies the rise of a Chinese entrepreneurial class (e.g., Liu, 1992; Zhang, 2008). In this view, business people follow the call of the market, find new opportunities, raise capital, hire workers, and produce goods and services for the new Chinese economy. These 'self-made' entrepreneurs are the heroes of China's rapidly growing economy, who act to produce rapid economic growth (Zhou, 1996).

The other point of view sees these entrepreneurs as embedded in various kinds of social networks (Wank, 1999; Xin & Pearce, 1996). The social ties of Chinese entrepreneurs include business partners, supply chains, foreign firms, and of course, local and national government (Lyles, Flynn, & Frohlich, 2008; Peng & Luo, 2000). In this view, under the condition of insufficient market economy institutions, Chinese business works because of *guanxi*. This elaborate system of favours allows actors to exploit new opportunities. How these networks work and what role they have in contemporary Chinese business practices is the subject of a wide-ranging and stimulating theoretical and empirical debate (Gold, Guthrie, & Wank, 2002).

Here too, the arguments have a moral character. Economists and some sociologists are somewhat sceptical of the positive roles played by *guanxi* (Guthrie, 1998). They see the use of social networks as part of a process of rent seeking whereby firms with the right connections can produce abnormal gains for themselves (Zhang & Keh, 2010). At the margins, *guanxi* is about paying bribes in order to get good deals from transaction partners or to get the government to help control competitors. Indeed, *guanxi* is often seen as an impediment to economic growth because it stifles competition, does not allow for the efficient allocation of capital, prevents the right kinds of investments from being made, and leads to transaction breakdown due to opportunism (Luo, 2006). In the newly freed economy, *guanxi* may disappear or decline as entrepreneurs no longer need ties to the state to do what they want (Guthrie, 1998).

### Alternative Views of China's Economy

One can take these arguments and create a typology of current approaches to the Chinese economy. Figure 1 provides this typology with eight alternative ideal typical views of what is going on in China. This typology identifies factors that can explain Chinese economic growth and simultaneously can be considered detrimental to economic growth. The ideas in this figure encapsulate many of the debates over contemporary Chinese economic growth.

Figure 1. Alternative views of China's new capitalism

		State capacity for economic intervention			
		Low		High	
		Positive	Negative	Positive	Negative
Network capacity for economic creation	Low	<i>Cell A</i> Liberal capitalism, economists' dream	<i>Cell B</i> Social chaos	<i>Cell C</i> Developmental state (airplanes, cars)	<i>Cell D</i> Overly strong state, diffused rent seeking, and official corruption
	High	<i>Cell E</i> Supply chains, industrial districts, small- and medium-sized family businesses (Wenzhou)	<i>Cell F</i> Cartels, local corruption	<i>Cell G</i> Flexible state, strong firms (Yiwu)	<i>Cell H</i> Crony capitalism (real estate)

For some scholars, the real source of economic growth in China is its movement towards cell A in the upper left hand of Figure 1 (Nee, 1989; and to a certain extent, Naughton, 1995). Here, as the government removes itself from the economy and the social networks that sustained the planned economy are removed, entrepreneurs rush in to organize new firms to produce economic growth. This cell is supposed to be the end point of Chinese capitalism and, to the degree that Chinese development has occurred, it is this movement that produces good outcomes.

The upper left hand section of the figure (cell B) represents the idea that social chaos has been created in China by the government exiting business and by social actors being left on their own to create their own forms of livelihood (this view is frequently held by ideological leftists or Maoists in China). An example here is the release of millions of workers from farms and state-owned enterprises, a movement that has forced workers to become their own 'bosses'. They either participate in a 'third economy' where they try to peddle goods on street corners or markets or else become 'illegal' workers in a sweat shop economy that works to exploit them. This view of Chinese development may be considered a Marxist perspective on the ills of the new China.

Moving right in Figure 1 to cell C, we have a version of the developmental state (for a version of this argument, see Gao, 2008). Here, the government maintains control over the direction of the private economy and directs investments. The



private economy responds not through social connections but instead because they are given capital and various benefits to make new investments in government-sponsored initiatives. Two places to see this are the growth of the Chinese automobile industry and the current attempts to produce an airplane manufacturing capacity in China to compete with Boeing and Airbus. The Chinese automobile industry has proceeded mainly through joint ventures between state-owned enterprises and foreign auto producers. The airplane industry is being similarly supported by government investment as well as encouraging foreign participation, particularly by Boeing. Again, to the degree that economic growth is happening, it reflects government intervention into the economy.

Contrary to the view of the developmental state, some scholars find evidence that the strong state becomes the source of problems (cell D). Here, the government's ability to control the economy remains while there exists no 'civil society' to block the actions of government officials (Qin, 2008). This tends to produce local corruption and rent seeking on the part of officials who can demand that local business people and workers pay bribes for what they were previously guaranteed (Ding, 2000a,b; Lu, 1999). The Chinese press is full of stories of corrupt government officials who use their positions to enrich themselves and their families. Instead of a developmental state, scholars and the population see a corrupt government bureaucracy being used to feather the nests of those lucky enough to have the right social positions (Lu, 1999). Besides corruption, scholars have found that state involvement contributed negatively to the economic performance of incorporated firms (Nee et al., 2007), created higher economic inequality, and impeded economic development (Zhang, 2008). Huang (2008) argues that the heavy involvement of the Chinese state in the economy is not developmental but is detrimental to further development; it reflects more the interests of the party state in power.

At the bottom left of Figure 1 (cell E), we have the model proposed by those who view the role of local *guanxi* as critical in the creation of the Chinese market (e.g., Zhou, 1996). In this case, the government has withdrawn from the economy. It has left behind local organizations of supply chains and industrial districts. These create small- and medium-sized businesses mostly owned by families (Whyte, 1995). These networks of *guanxi* are the glue that propels forth local economic growth. Groups formed around such networks work together to make investments, deal with market turmoil, and shift market strategies. The examples that demonstrate this are Wenzhou, Zhejiang province, and some places in Fujian province (Liu, 1992; Tsai, 2002; Whiting, 2001; Zhang, 2008).

We can also observe the negative impact of local *guanxi* when government has removed itself from control over the economy (cell F). Local businesses use their social connections to coordinate their activities, fix prices and wages, and generally rent seek for themselves and their families. We note that the main difference between cell F and cell B is who is getting the opportunity to rent seek, the newly

rich among the entrepreneurs or the members of the cartel or social network who can use their positions to collect rents.

The bottom right side of the figure takes the perspectives that both high levels of *guanxi* and the state are positive or negative for economic development. Scholars who consider *guanxi* and the state positive (cell G) maintain that the state provides favourable policy, infrastructure, money, even rule of law to promote local development projects, while business networks facilitate development. Gao's discussion on Yiwu is an example of how the government aided already existing networks of firms to help grow the market (Gao, 2008). In Yiwu, the local government has been working with local businesses for the past 15 years to create the world's largest small commodities market. The market started as a farmer's market that mainly served local customers. It evolved over time to small commodities manufacturing, and this development process now produces a multi-billion dollar market place. Government has built the infrastructure of the market and loaned money to entrepreneurs. Local networks of firms have sprung up to take advantage of the market and to organize to produce goods that are now shipped all over the world.

The opponents of this perspective make the case that both government officials and local networks work together to collect rents (Wank, 1999). In other contexts, this might be called 'crony capitalism' (cell H). The best example of this cell of the figure might be contemporary real estate development in many cities. After the 1993 tax reforms, local governments lost much of their tax base (Naughton, 2007). This caused them to look for new sources of revenue. The main source they discovered was to sell land to real estate developers. It has been estimated that as much as one-third of the cost of real estate development is paid out in bribes to local officials. In spite of the high price of doing such business, local developers work together to divide up the business and share the wealth. They often build shabby buildings that have substantial problems but are immune to lawsuits and government sanctioning because of the cosy relationships to local governments. It is not surprising that seven of the ten richest people in China were involved in real estate development (*Forbes*, 2008).

### **A Critique of the Current Research**

One of the interesting things about our characterization of the nature of Chinese business networks and the role of the Chinese government in economic growth is that the empirical literature provides cases that appear to fit all of the alternative views (Krug & Hendrichske, 2008). For example, some of the social chaos produced by the government removing itself from the economy and the destruction of traditional Chinese networks of family is clearly a bad thing because it leaves people to fend for themselves and creates poverty and vulnerability. At the same time, in some industries, opening up local opportunities to produce goods and



services like beer and restaurants have clearly contributed to positive economic growth. Such diversity might reflect the decentralization of the state and the heterogeneity across regions and/or across industries. As some scholars maintain, the role of government ranges from arm's length state to developmental state to pre-corporatist state across China's regions (Krug & Hendriscake, 2008). In terms of developmental stage, some provinces (e.g., south-east coastal provinces) are more developmental than other provinces, which is why some scholars differentiate interior from coastal areas in their analyses (e.g., Peng & Luo, 2000).

Our two main theories produce four possible arguments for why the Chinese economy is growing and why it is being held back at the same time. Given there is empirical evidence for all of the scenarios affecting economic growth in both positive and negative ways, this suggests that our theories are not getting much leverage. Moreover, like many debates in social science, partisans of one scenario over another disregard alternative evidence and continue to act as if their explanation of Chinese economic growth were sufficient to account for what is occurring. For example, scholars enamoured of *guanxi* explanations and Chinese 'exceptionalism' accounts ignore evidence for the continued role of the state in economic development and case studies that show how social connections produce corruption.

This analysis suggests that we need to invoke other theoretical perspectives or a grand conceptual framework to develop a more coherent understanding of the complexity of Chinese capitalism. Such a theoretical perspective should take into account that every transition to capitalism has produced a new variety of capitalism, and in each transition, a set of common problems have had to be resolved. Using theory to understand the problems and the Chinese solutions may open up a research agenda on state-firm relationships that is likely to prove fruitful going forward.

Another problem of the current research is that most studies of China's development largely follow a bottom-up approach. Scholars begin by studying some region or industry or by focusing on state/private/foreign firms. They then assume that whatever they find has somehow given them insight into the whole picture. The problem of this piecemeal bottom-up approach is that it does not allow us to sufficiently understand the big picture. Some scholars maintain that the Chinese model of development is unlike any other in the world. While every transition to capitalism on a national basis is unique, we also think that comparing Chinese development processes to the experiences of other societies will help us understand what is unique about China and what might very well reflect common processes.

Therefore, we propose to make more explicit comparisons between the Chinese case and other cases of capitalist development. By doing so, we can generate hypotheses on the basis of those models about the nature of Chinese capitalism. Then we can compare those predictions to our empirical observations and relevant

data from China. Through this process, we may discover whether China is a hybrid model or an entirely different model.

There are two obvious intellectual sources for this kind of theoretical orientation: the literature on comparative capitalism (sometimes called the ‘varieties of capitalism’, see Albert, 1993; Amable, 2003; Hall & Soskice, 2001) and the literature from the new economic sociology (Fligstein, 2001). We will begin with a discussion of comparative capitalism, followed by a discussion of the economic sociology framework. In both discussions, we will draw research implications from the framework for China’s developmental journey.

## **INSIGHTS FROM COMPARATIVE CAPITALISM FOR THE STUDY OF CHINESE DEVELOPMENT**

The comparative capitalism literature begins with the observation that most systems of national capitalism are uniquely organized. This organization reflects the history of firms’ development, the labour movement, and the government in each society, which makes such systems both path-dependent and heavily institutionalized. So, as new opportunities and crises occur within a national system, the actors in the national system respond using the institutions they have. This can cause them to modify those institutions and adapt to changing circumstances. It can also necessitate clean breaks with the past if events are sufficiently tumultuous.

At the core of the comparative capitalism approach are two ideas. First, such systems exist because they work to produce positive economic outcomes for the stakeholders in a given economic system. If systems cease to be able to provide these outcomes, then the main players in the systems (firms, government, and organized workers) will seek out new ways to organize themselves. Second, the main dimension that distinguishes national systems can be identified as ‘liberal’ versus ‘organized’ (or, in some versions, ‘illiberal’) systems (Hall & Soskice, 2001).

### **Liberal Capitalism**

Liberal systems refer to ideal typical relationships between government, firms, and workers that focus on governments staying out of direct market governance. Here, the price mechanism in particular markets determines the allocation of capital. Such systems are frequently characterized as having weak labour organization. Share ownership in publicly held corporations is diffuse, and financial markets are important sources of equity funding and debt. Managers have to maximize shareholder value and please stock markets, or they will risk having their stock prices plunge and their access to credit dry up. While governments can help firms and workers in crises, they will usually do so either by providing a social safety net or aiding the reorganization of failing market actors. Govern-

ments stay out of picking winning and losing industries and allow the market process of creative destruction to work unimpeded. In the literature, the USA, Great Britain, Canada, New Zealand, and Australia are supposed to be the countries with liberal systems.

Is China's a liberal form of capitalism or is it moving in that direction? It is pretty easy to dismiss this hypothesis. Market activity has certainly increased across the Chinese economy, but the enormous continuing presence of the Chinese government in every market as regulator, financier, developmental state, and owner of the means of production suggests that, while the government's role in the economy has been dramatically altered in the past 30 years, it remains enormously influential. Chinese labour is relatively disorganized and independent unions are not allowed. But even here, the government has to manage the underlying political and economic unrest and worry about its own overall legitimacy, which it does in a paternalistic way. For example, in the economic crisis of the 2008–2009 period, the government has engaged in a massive economic stimulus package and worked to create a universal health care system. Top Chinese leaders openly embrace the view that government should actively regulate the economy in many settings. We can safely reject the idea that China's economic transition is about the removal of the government from markets.

### **Organized Capitalism**

The idea of organized or illiberal capitalism is more diffuse. Hall and Soskice (2001), for example, see the key features of organized capitalism as a close connection between workers and firms and sometimes extensive social relationships between firms. In organized capitalism, workers are viewed as having more power. They are more difficult to fire, and certain kinds of job security (including lifetime employment) are guaranteed. They are made partners in big changes that might occur in firms. In an economic downturn, hardships are partitioned between managers and workers, and firms operate to try to solve their problems by making new investments that will likely pay off down the road. Hall and Soskice (2001) and Albert (1993) argue that this feature (which captures the main characteristic of large German corporations) is responsible for the stability of these firms. A second feature of organized capitalism is groups of firms that have share ownership dispersed across them. Frequently at the centre of such groups are banks, which act both as holders of equity and lenders to firms.

We find huge variation across national systems of capitalism in industrialized societies like France and Scandinavian countries, and in developing societies in Asia, such as Thailand, Malaysia, Singapore, Korea, Taiwan, and India (see Amsden, 1991; Berger & Dore, 1996; Evans, 1995; Wade, 1990). Indeed, what all of these other models seem to have in common is less German and, instead, more heterogeneous structures that reflect their national patterns of development.

Governments play active and differing roles across the varieties of illiberal capitalism. Authoritarian governments like those that started the development of Singapore and Korea acted very much as developmental states, directing investment, owning firms, and controlling labour conflicts. Family-centred capitalism is also the norm in a great many places, such as Singapore, Malaysia, and Taiwan (Fukuyama, 1995). German (and, for that matter, Japanese) intercorporate shareholding patterns do not subsist across much of the world where families continue to dominate the largest corporations.

One might wonder, if the literature shows such diffuse agreement about how organized capitalism works, how can it be useful to the study of China? We argue that this framework offers some insights that can help us make sense of China. The comparative capitalism literature causes us to focus on three main actors in society: the government, firms, and workers. It may not tell us what that relationship will be, but it does argue that all economic development projects have produced stable institutions built around those relationships. This offers more conceptual leverage in understanding China than the bottom-up approach of most studies. For example, if we use the comparative capitalism framework to examine whether *guanxi* or social connections ‘matter’ in China, the real issue is not whether or not there are social relationships in markets. Rather, the issue is what the nature of those relationships is, how they have evolved over time, and what the current linkages are between firms, the government, and the labour force.

### **Research Implications for China**

The comparative capitalism literature suggests a set of research agendas and questions for studying Chinese economic development. What are the ownership relationships between Chinese firms? Are Chinese capital markets really operating to allocate capital in society, or does the government still control the financial system? What are the relationships between publicly owned firms and private firms? How do county, city, provincial, and national governments intervene into investment decisions? What is the role of government in adjudicating the relationships between firms and workers? What are the relationships between firms with various ownership structures (state firms, private firms, and foreign-invested firms) and their workers? To understand the trajectory of Chinese capitalism, we must operate at this institutional level to view how these relationships have evolved over time.

It is possible to try to look at the varieties of capitalism in the world to see if processes that have occurred elsewhere help explain what is currently going on in China. It is clear, for example, that the German model, with its strongly organized working class, is not going to be very useful to understand what is happening in China. Chinese workers have lost their right to lifetime employment, and Chinese managers can fire workers with little retribution (O’Leary, 1998). Chinese workers do not sit on boards of directors as do German workers, even though worker

representatives sit on largely symbolic supervisory boards. Given the continued level of government ownership of firms and control over the financial system, it is also clear that the Japanese model is not relevant to understanding the Chinese situation.

The Chinese model shares more features with other Asian countries, especially those that pursued development projects set by authoritarian regimes. Korea and Singapore, for example, had strong governments that directed investment and suppressed working class development. We know that the Chinese government has deliberately learnt from these other cases. In the late 1990s, the Chinese government tried to reorganize state-owned enterprises to build big business groups, somewhat resembling business groups in Japan and Korea (White, Hoskisson, Yiu, & Bruton, 2008). When the State-owned Asset Supervision and Administration Commission (SASAC) tried to improve its administration of state-owned enterprises, it learned from the Singaporean model of a state owner (in Singapore, the Ministry of Finance; in China, SASAC/MOF), a state-owned assets manager (in Singapore, Temasek; in China, large business groups with numerous subsidiaries), and operating firms. But these models also fail to help us understand China because, in both Korea and Singapore, the private, large corporations started out and remained under the control of elite, wealthy families. In China, it has only been in the past 10 years that huge private wealth has emerged. Moreover, these families do not control firms in the core of the Chinese economy. Instead, their wealth is based on retail, real estate, construction, services, and light manufacturing.

The search for an analogy to China means that one needs to think about a system where government control is high, state ownership of firms remains central to the economy, workers are less organized, and a private sector has emerged but in the shadow of the state. We think that a provocative case bearing this kind of resemblance to China is France. While France is a democratic country (and this makes it in many ways incomparable as we will discuss below), the French government has created a system that the Chinese model greatly resembles. Labour in France is less organized than in much of the developed world. Less than 10 percent of the labour force belongs to unions (Visser, 2006). The French government is eager to arbitrate the relationship between firms and workers. The public sector is the largest employer in France, and the largest French firms are at least partially owned by the French government. The French system of education has produced an elite set of managers whose careers extend between government and posts in the largest firms. The French government has maintained control over transportation, communications, and utilities and owns shares in many core businesses like automobile and airframe manufacturing. For example, the French government owns a large share of Airbus and France Telecom. There is a thriving private sector in France, but much of it is centred on the production of luxury goods, tourism, construction, and retail. While the French government has adjusted its strategies

over time in response to economic crises, it has worked to create national champions that compete on a world scale. Overall, the French model can offer a plausible set of hypotheses about the direction and relationship between firms, workers, and the government.

Of course, Chinese capitalism also differs from French capitalism. First, political differences put differing constraints on government action. Democracy in France puts many limitations on government action. For example, it is difficult to push through liberalization reform in certain sectors (agriculture liberalization leads to farmers striking; employment and educational reforms lead to student upheavals). In China, the authoritarian state has relative autonomy in carrying out its will. Second, the role of the state differs. The French state's involvement in the economy is as much oriented towards social welfare and redistribution as the Chinese state's is embedded in the economy as owner, financier, and regulator. Third, the bargaining power of labour is different. In France, labourers can organize to bargain with the state; in China, workers can only wait for the paternalistic state to take care of their interests.

A comparative capitalism approach to Chinese economic development pushes a new research agenda for scholars. By seeing how other illiberal systems have evolved, scholars can identify features of Chinese development that will prove pivotal to understanding the nature of the Chinese model. As more adjustments (mostly by the government) are made over time, they ought to follow a predictable path. The Chinese model of development does have its uniqueness, but we think one can conclude that it looks more like French *dirigisme* than it does like American shareholder value liberal capitalism or the German stakeholder value organized capitalism. This conclusion already eliminates some possible outcomes for China's future. It also implies ways to understand the key dynamics of how the state will face economic challenges as they emerge.

## **INSIGHTS FROM ECONOMIC SOCIOLOGY FOR THE STUDY OF CHINESE DEVELOPMENT**

If the literature on comparative capitalism provides us insights on how to understand the nature of Chinese capitalism at a macro-level, then economic sociology is helpful for us to understand the formation and evolution of specific markets from the level of particular markets and industries. Our purpose here is to offer a research agenda and raise related research questions instead of giving tentative answers.

### **General Themes in Economic Sociology**

Beginning with seminal papers by White (1981) and Granovetter (1985), sociologists have proposed to study how markets are social structures created by actors



who have knowledge of one another and often long-standing ties and relationships. These actors take one another into account in their actions and position themselves vis-à-vis one another, depending on what the others do. White (1981: 517) characterizes these markets as a 'self-reproducing role structure'. Economic sociology contains a set of perspectives on how markets work as social structures that focus on the role of government, networks, and institutions (Dobbin & Dowd, 2000; Fligstein, 2001; see Fligstein & Dauter, 2006, for a review). In many ways, economic sociology is a complement to the comparative capitalism approach. By focusing more at the market level than on the entire economy, economic sociology can help make sense of the emergence, stabilization, and transformation of particular markets.

The study of particular markets ought to begin with the idea that the emergence of the market reflected an opportunity for economic gain. The critical issue is how do markets become reproducible role structures with a relatively fixed set of firms? Firms must have a particular set of products or services, but they also must have a way to control competition with one another. One of the most important ways in which business people produce and stabilize their markets is to create a common understanding of the market, what Fligstein (1990, 2001) has called 'conceptions of control'. The emergence and diffusion of a particular 'conception of control' is a result of the interaction between involved actors in a market. The model that eventually emerges to dominate that market will frequently reflect the outcome of the interaction/struggle between critical actors with different resources, interests, and visions in the market. It sometimes also mimics how firms from nearby markets come to organize a particular market.

While market projects often are unique and reflect the historical trajectory of particular economies, they have similar dynamics in that they involve firms, governments, and critical actors who operate as political, institutional, and economic entrepreneurs. We consider how this has worked recently in the USA to offer some idea about how it might be applied to China.

In the USA, large corporations have undergone periodic environmental upheavals, which control the firms. These have been driven by various shocks to their primary market, some of them from competitors, some due to new opportunities, but mostly due to large-scale macroeconomic downturns and active intervention by governments. Fligstein (1990) shows how, over the course of the 20th century, US firms were led by manufacturing executives who tried to create oligopolies in their markets, then were succeeded by sales and marketing executives who pursued marketing and product diversification strategies for their firms, and finally, financial executives who came to treat their firms as investment portfolios.

The shareholder value is the current guiding conception of the firm in the USA (see Davis, 1991; Davis, Diekmann, & Tinsley, 1994; Zorn, 2004; Zuckerman, 1999, 2000). The goal of the large corporation is to make money for its stockholders. Raising the stock price is the central goal of managers. This odd

goal can be understood in the following way. In the USA, there is a diffuse holding of stock ownership. In order for owners to exert control over the actions of managers, their main action is to sell their shares. If managers do not pay attention to shareholders, the stock price will plummet. Boards of directors are supposed to monitor managers for shareholders, and they set up systems of rewards that tie pay to performance.

In the past 25 years, managers have discovered a set of tactics that they use to signal to financial markets. These include announcing layoffs, divesting product lines unrelated to the main business, and financial engineering of the balance sheet. The origins of this system are in the financial upheaval of the 1970s. In brief, the largest American firms today are being managed according to shareholder value.

### **Research Implications for China**

While there is a large literature documenting the existence of social ties between market actors and some literature on particular industries in China, there are still not many analyses of what firms and managers are actually doing to create and stabilize markets (though a few studies have appeared in recent years: Guthrie, 1999; Wang, 2009). Scholars are still struggling with trying to understand what will be the Chinese 'conception of control'.

Searching for that conception of control requires interviewing managers, but it also can be done by analysing corporate documents and managerial speeches, understanding the social structures of competition in particular markets, and making sense of their key dynamics. Again, the relationship between government and particular industries/firms is of paramount interest. For example, how do market actors together with state actors create order and the conception of control in a particular industry? What kind of formal or informal links between market actors and state actors serve such purposes? Who is taking initiatives in organizing the industry? How are actors with different interests accommodated during the process of creating new order?

Researchers could begin by investigating how the largest firms in China are owned and operated, how managers decide what kinds of products to produce and their relevant markets, and how governments are involved in investment decisions, personnel decisions, and firm direction. Are Chinese firms like Korean *Chaebol* during the 1960s and 1970s, which were essentially told by the government what kinds of investments they should make? Or is there really an independent set of managers who have been freed to make a profit any way they can, even when their major shareholders are the government? If so, in what directions have they taken their economic activities? What are their key strategies to compete? Understanding the dominant conceptions of control in Chinese business would be one way to clarify the developmental journey thus far and to determine whether it is focused on particular industrial sectors or more widespread.

A related research project could involve examining the 1,600 or so publicly listed Chinese corporations. About 500 of these are entirely in private hands and the rest are state owned (*Blue Book of Private Enterprises*, 2009). Many of the state-owned firms have their stock held by different levels of government: county, city, provincial, and national. Specifically, state firms or large government-owned investment funds hold these firms' stock. The national government owns about 140 firms, and these are the largest in the economy (SASAC, 2009). They are concentrated in important industries like infrastructure, utilities, material, telecommunications, and transportation as well as large-scale industries like oil, steel, and automobile (see Guthrie, Xiao, & Wang, 2008; Haveman, Calomiris, & Wang, 2008; Naughton, 2007).

What the government is trying to accomplish by listing these firms on the stock market is a fascinating place to begin to understand the trajectory of the Chinese economy. There is not total agreement about how to interpret the (partial) privatization of Chinese firms. Why has the government gradually sold off some shares? One interpretation is that many Chinese officials, particularly in the finance ministry, were trained in the USA, mostly as economists. These officials are making policy for China based on the US model. The privatization they have set in place are their attempts to build modern corporations and create US-style shareholder value capitalism. An alternative hypothesis is that the government is selling off part of the firm to get private investment to help expand the firm while, at the same time, intending to keep enough ownership in firms to maintain control. In essence, the government is moving to a model whereby the capital structure of the firm looks private or mixed, but the main owner is the government. This allows for the development of national champions who will do the bidding of the government.

How would we know if China were indeed developing shareholder value capitalism like the USA or if, instead, the Chinese government were evolving a French style *dirigisme* whereby they maintain control over firms? To understand these actions will require studying the firms and financial markets more closely. If firms were behaving more like those under the control of financial markets (i.e., managers trying to maximize shareholder value focused on the stock price), we ought to observe strategic behaviour in line with such a view. We would witness hostile takeovers, divestitures of parts of firms seen as not fitting into the overall strategy, and managers who engage in financial engineering to make their stock price rise. We also ought to observe independent boards of directors tying managerial pay to performance. The result is that managers would become the richest people in the society. If firms were behaving more like national champions (the French model), we ought to observe continued government direction of investment, access to government banks for financing, and personnel who shift jobs between working for government agencies and corporations. We also ought to observe managers who are reluctant to fire workers and close plants. Managerial pay would not be tied to

performance, and managerial salaries would not be the key driving force in creating income inequality in China.

All of these ideas suggest that we should be observing the dynamics of top-level managerial careers. If the government is working to maintain control over firms like the French model, then managers ought to have careers that reflect their passage from firm to firm with occasional stints in the government. We would also expect them to behave conservatively in terms of strategy by making sure the firm is solvent, making sure it grows, diversifying products to diversify risk, and continually employing many workers. In this model, the goal of managers is to get the next job and, in order to do that, they need to please their government owners. We would expect managers to change jobs if their firms were successful or unsuccessful. Managers of successful firms would be moved on to firms that needed help or moved on to government positions (as promotions), while managers of unsuccessful firms might be demoted. We would expect that the government would intervene in investment, employment, and choosing and firing top managers. A managerial elite could be created in China through this mechanism. By controlling their careers, the government would make managers satisfy the concerns of the party state.

If a Chinese managerial elite were more like the corporate elite in the USA, then we would expect their careers to be quite different. They would probably be more likely to make their way from within the ranks of the firm. Their backgrounds would be less related to politics and government connections and more related to the functional background in the firm. We would expect managers who were maximizing shareholder value to profit greatly from their positions both by drawing high salaries and by getting stock options and other forms of bonus pay.

The research projects suggested above can be done using publicly available data on firms. We already know that managers are not the richest people in the new China. We also know that Chinese firms rarely engage in mergers, and certainly, there is no history of hostile mergers. These facts suggest that the model of Chinese capitalism is less American and more French *dirigisme*. One could study what happens to a sample of corporate top managers and see what the role of the government is in their career trajectory.

Besides looking at the structure and dynamics of the markets where government still has a strong presence, it is also valuable to study competitive markets that are mainly filled with private firms or marketized state firms, such as consumer product industries. It is interesting to analyse how conceptions of control emerge and evolve by observing the interaction of institutions and organizations, the role of institutional entrepreneurs, and the role of intermediary organizations such as trade associations. It is also interesting to examine the interaction between different forms of organizations, such as Chinese domestic firms and foreign firms. We would expect such competitive markets to somewhat resemble those in the West's early period of capitalist development in a sense that order is

fought out by critical actors. We would also expect those markets to share characteristics with overseas Chinese communities in terms of organization, governance, and network exchange, considering the impact of overseas Chinese investment and the similar cultural traditions. In some technology-intensive industries, such as IT, we would expect more western influence on the creation of the conception of control.

Economic sociology alerts us to another set of important issues in the Chinese economy. The problem of rent seeking on the part of governments is of real concern. Many of the societies in Africa are afflicted by governments who control so much of the economic assets that most people are suffering (Evans, 1995). One of the ways to prevent governments and capitalists from rent seeking is to have countervailing political and economic forces. Historically, organized political forces like political parties, unions, an active judicial system, and employers' associations have served these roles. In China, development has appeared to occur largely without these forces (Qin, 2008). There has been much talk of rent seeking and corruption in China, particularly at the lower levels of government (Lu, 1999), which is what one would expect without countervailing powers. Given the massive economic growth in China, the opportunities for a small number of government officials to enrich themselves are quite large. While there is a lot of anecdotal evidence about corruption, there also appear to be some countervailing powers, which prevent massive theft of government assets, such as took place in the former Soviet Union. This raises an important research question: is there evidence about a peculiarly Chinese form of countervailing powers to constrain rent seeking?

From a distance, one obvious candidate for creating countervailing powers to prevent rent seeking is competition between firms that are owned by varying levels of government as well as competition between regions. The competition between firms across the country makes it more difficult for one region or one level of government to control markets and rent seek, while competition between regions pushes the regions to adopt favourable policies to business (Yang, 1996) and contains official rent seeking, particularly given the federalist feature of Chinese development (Montinola et al., 1995). If there are new forms of countervailing power (e.g., the growth of a private entrepreneurial class or public opinion on the internet, especially after the Sichuan earthquake), they are worth considering. Instead of looking for the kinds of forces that have traditionally emerged in the west, scholars with local knowledge should consider how non-traditional forms of countervailing forces might exist.

One of the lessons of government intervention in many societies is that it appears to be less important exactly which economic institutions are in place and more important that some exist. In the west, social stability and predictability of government rules is the most important feature of property rights systems, governance structures, and rules of exchange. But there are other ways to get this predictability,

particularly by using local networks of firms who engage in repeated transactions. The relevance of this observation for China is that we need to study more adequately how this predictability has been put into place on the ground (for a recent example, see Zhou, Poppo, & Yang, 2008). While there are now lots of laws on the books in China, it is less clear how actors in the field perceive and use these laws. It may be the case that Chinese businesses have solved the problem of predictability in interorganizational transactions in novel ways. If so, it will be valuable to analyse what these are.

So, for example, it is clear that foreign investors are somewhat protected from violations of contracts by the existence of contract arbitration organizations like the Chinese International Trade and Arbitration Commission. But it is less clear how more local or regional producers get contracts and property rights enforced, even after the Property Law was implemented in 2007. When economic actors know one another and routinely interact, their ongoing personal relationships can create trust for these kinds of transactions. As the economy has grown bigger and firms are operating on a national or international level, enforcing property rights and contracts gets more difficult. One other obvious mechanism to enforce property rights is that many regional firms are either owned by their governments or else the people who run them have ties to their local governments. They can then rely on their local governments to ensure the enforcement of contracts through these ties. Or there might exist some *de facto* institutions that achieve this purpose. Understanding how these problems are now being solved will have implications for the continuation of rapid economic development.

## CONCLUSION

The Chinese economy has changed enormously in the past 30 years as the government has altered its mechanisms of control over the Chinese. The empirical work done thus far has been quite interesting and important. But understanding the Chinese economy is muddled by a wide variety of views about how the changes that have occurred have been positive and negative for Chinese economic development. Indeed, the same theoretical arguments can often support views that these factors have caused both good and bad outcomes. Given such contradictions, we propose that the comparative capitalism literature and the literature on the sociology of markets can provide conceptual clarity and hypotheses about the Chinese development model. By examining the characteristics of state, business, labour, and the relationships among them, we can better understand the nature of Chinese capitalism. The research projects suggested by this paper will also provide insights in predicting China's future.

We also argue that, in order to capture what are the essential features of China's path, scholars should be more conceptual, historical, and comparative in their analyses. To understand the Chinese developmental model, it is logical to



analyse how the Chinese model does and does not resemble those in the rest of the world.

To end, we suggest that China may be creating its own model of development. The Chinese government (at all levels) in concert with its largest corporations, labour force, and emerging private entrepreneurs is forging a new way to produce economic growth. The key feature of this Chinese model is the strong and continuing presence of the government as a dominant coordinating actor, as can be seen in China's response to the financial crisis of 2008. Even if the Chinese government had tried to mimic other capitalist models in the past, the current Chinese government is becoming more confident about its own way today. We have yet to observe whether this self-confidence will lead to a more 'Chinese' characteristic of development in the future.

## NOTE

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