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978-1-107-12341-0 - The Advance of the State in Contemporary China: State–Market Relations in the Reform Era

Sarah Eaton

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## The Advance of the State in Contemporary China

Since the Global Financial Crisis in 2008–2009, central-level, state-owned enterprises in China have extended their reach into the Chinese economy. Some have interpreted this development as a turning point in Chinese economic development; a decision for state capitalism and a stand against slow but steady marketization. In *The Advance of the State in Contemporary China*, Sarah Eaton suggests that the shift is a much slower-moving process and that this particular aspect of state sector reform can be seen to predate the financial crisis. She argues that the ‘advance of the state’ has in fact developed incrementally from an eclectic set of ideas regarding the political and economic significance of large and profitable state-controlled enterprise groups.

Drawing from case studies of China’s telecommunication services and airline reforms, this fascinating new study offers illuminating insight into China’s much-vaunted, but poorly understood, brand of state capitalism.

SARAH EATON is Professor of Modern Chinese Society and Economy at the Institute for Sociology and Department of East Asian Studies, University of Göttingen.

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# The Advance of the State in Contemporary China

*State–Market Relations in the Reform Era*

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Sarah Eaton  
*University of Göttingen*



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To my parents, Diane and Curtis Eaton

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## Preface

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It is not every day that one hears a senior American policymaker admit that ideology has tainted his or her policy choices. In American political discourse, the word ‘ideology’ is typically reserved to describe the false beliefs held by the opposing team. One’s own views do not sit on such unsteady foundations but rather stand firmly on the ground of Truth.

It was surreal, then, to see Alan Greenspan, Chair of the Federal Reserve from 1987 to 2006 – the man once known as ‘The Oracle’ to financiers – own up to an ‘ideology’ that he admitted had contributed to the Global Financial Crisis of 2008. In a congressional hearing during the darkest days of the crisis, Greenspan admitted he was in a ‘shocked state of disbelief’ because of the ‘collapse’ of an ‘intellectual edifice’ of risk management models (US Congress 2008: 13). Greenspan’s *mea culpa*, however, did not satisfy the committee’s chair, Democrat Henry Waxman, who pushed Greenspan to make a broader denunciation of his beliefs. He began by quoting Greenspan as having said ‘I do have an ideology. My judgment is that free, competitive markets are by far the unrivaled way to organize economies. We have tried regulation, none meaningfully worked.’ Waxman then asked whether Greenspan felt that his ideology had driven him ‘to make decisions that you wish you had not made?’ Greenspan replied that ‘Yes, I found a flaw, I don’t know how significant or permanent it is, but I have been very distressed by that fact’ (ibid. 46).

This and other scenes in the dark days of the Global Financial Crisis pulled back the curtain on Anglo-American capitalism. Long held up by champions of the Washington Consensus as the endpoint of history, the crisis revealed that the intellectual edifice of financial capitalism in the twenty-first century is, like the shoddy ‘tofu buildings’ (*doufu lou* 豆腐楼) that litter China’s urban landscapes, shaky to the core. It was an ungentle reminder of John Maynard Keynes’ famous insight about the immense power of ideas ‘for good or evil’, gleaned in the blackness of the Great Depression (Keynes [1936] 1997: 384).

However, as Greenspan rightly pointed out during his congressional testimony, we all ‘need an ideology’ – what he defined as a ‘conceptual framework ... [to] deal with reality’. The collapse of one dominant ideology

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simply triggers a search for the next. Since 2008, this quest has drawn many of the disenchanted to China's shores, where praise for the 'China Model' and the 'Beijing Consensus' has been warmly received by a leadership eager to be seen as offering something to fill the void. A few weeks before the Greenspan hearing, then-Premier Wen Jiabao declared in an interview with CNN's Fareed Zakaria that the secret to China's economic success was a rejection of the neoliberal injunction to enforce a rigid separation between state and market. 'Socialism can also practice market economy', Wen declared, when 'both the visible hand and the invisible hand are given full play in regulating the market forces' (CNN 2008).

Such claims have been met in the West with both thunderous applause from the left and anxious hand-wringing from the right. To long-time opponents of neoliberalism, like Martin Jacques, a prominent journalist and former editor of the British Communist Party's *Marxism Today* journal, China's extraordinary rise has served to expose the poverty of neoliberal development strategies (Jacques 2009). Jacques characterizes the coming 'age of China' as one in which the Chinese principles of policy pragmatism and gradualism will supplant the practice of development as the delivery of one-size-fits-all reform packages from Washington to all corners of the world. On the right, worried guardians of the American-led world order have also conceded that China's rise poses a deep challenge to the existing rules of the game. Political scientist Stefan Halper, a White House official under three Republican Presidents, argues in *The Beijing Consensus: How China's Authoritarian Model Will Dominate the Twenty-First Century* (2010), that there is a clear and present 'model threat' from China. He argues that China has now taken the lead in marketing its 'vision' of politics and economics to the rest of the world. But all is not lost, Halper tells us; if America were to commit itself to winning back the hearts and minds of the global public, the world could again be made safe for American supremacy.

The above illustrates an important point about distortions that have arisen in the post-crisis debates over ideology. As others have argued, 'the China case' – once the preserve of a small number of little-known economic historians – has now become a political football between left and right, and everyone in between, in rich capitalist countries (Ferchen 2013; Naughton 2010). How China-as-talking-point is characterized, however, is subject to the distorting lens of the particular commentator. It is an elusive, shape-shifting creature barely recognizable from one commentary to the next. Wherever it appears, though, it is a fearsome, clear-minded and patient animal.

Yet China does not see itself in nearly such certain terms. Indeed, what the China debaters have all too often overlooked is the extent to which China's self-understanding is a continually evolving and deeply contested subject (Ferchen 2013). Of course, certain features of the Chinese economy set it

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apart from the world's other major economies – the economic might of large state-owned enterprises (SOEs) in key industries, for example. But if we look more closely, we find this and other supposedly distinct features appear far less solidly outlined. We might expect, for example, that the extraordinarily rapid ascent of the Forbes Global 500 list by China's central-level SOEs – up from just ten in 2003 to fifty-one in 2014 – would be a source of national pride. And, indeed, for many Chinese, it is. But others within China view it grimly, as evidence not of the fruition of 'reform and opening' but instead as a betrayal of the reform pathway laid down by Deng Xiaoping. Indeed, at the time of writing, debate over the appropriate role and form of SOEs in the Chinese economy is arguably *the* economic issue in Beijing and a perennial topic of debate among policymakers, economists and the reading public.

This book puts under a microscope the question of how China's muscular state-owned national champions came into being. In much of the popular literature on China's brand of 'state capitalism', the role of large, centrally controlled SOEs in China's political economy is characterized as an almost inevitable consequence of China's gradual move towards a market economy within the structure of continuing Chinese Communist Party (CCP) authoritarian rule. As Ian Bremmer, an American political consultant, wrote in his popular *The End of the Free Market* (2010):

Certain that command economies are doomed to fail but fearful that truly free markets will spin beyond their control, authoritarians have invented something new: state capitalism. In this system, governments use various kinds of state-owned companies to manage the exploitation of resources that they consider the state's crown jewels and to create and maintain large numbers of jobs. They use select privately owned companies to dominate certain economic sectors. They also use so-called sovereign wealth funds to invest their extra cash in ways that maximize the state's profits . . . in all three cases, the ultimate motive is not economic (maximizing growth) but *political* (maximizing the state's power and the leadership's chances of survival). This is a form of state capitalism but one in which the state acts as the dominant economic player and uses markets primarily for political gain. (Bremmer 2010: 4–5)

However, the reality in China is much more complex. Bremmer is right to point out that political motives and not purely economic considerations have given shape to China's national champions strategy. But the reality he describes is not, in fact, the result of the methodical execution of a blueprint from on high but rather of a thoroughly contingent and incremental process.

Things certainly might have been otherwise. Indeed, the growing wealth and clout of China's large SOEs – referred to as the 'advance of the state' (*guojin* 国进) in common parlance – actually represent a puzzling break with the past. Until quite recently, the conventional wisdom among China watchers held that Chinese economic reform aimed at a gradual, minimally disruptive transition to a free market economy by slowly ushering the state-owned economy – long

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an albatross around policymakers' necks – into retirement while simultaneously nurturing development of the non-state sector. One prime proponent of this view, Nicholas Lardy, characterizes Chinese economic reform as the triumph of 'markets over Mao' (Lardy 2014). And, for many years, the state sector's lethargic performance leading finally to a massive retrenchment in the late 1990s supported the view that SOEs were increasingly being relegated to the margins of the Chinese economy. However, this conventional view is much less easily accommodated to the precipitous rise of the state sector since the beginning of the new century. Thus, we are faced with the question: what accounts for China's turn towards state capitalism?

The answer provided in this book brings us back to ideas and ideologies. A commonly held (though by no means universal) belief among China's intellectual and policymaking elite is that large centrally controlled, state-owned enterprise groups are an indispensable pillar of China's refurbished system of socialist market economy. The existence of this belief is something of a puzzle. It is out of step not only with the tenets of neoliberalism, the pre-eminent global economic ideology since the period of China's economic reform began in 1978, but also with Maoist economic doctrine which idealized small-scale industrial enterprises and bequeathed a highly fragmented industrial structure to reform-era China. The rise of large SOEs is not, then, a simple story of path dependency. Tracing back the development of this ideological commitment to nurturing large state-owned national champions, we find that it was the result of a process of ideational 'bricolage' (Carstensen 2011) whereby policy entrepreneurs grappling with pressing issues at different junctures framed the 'large enterprise strategy' as the solution to various problems, both political and economic. The effect, over time, was one of sedimentation in which the addition of new rationales gradually added firmness and stability and a veneer of permanence to the institutions.

But the institutionalization and implementation of this idea have not always been smooth. In fact, the decision to create SOE oligopolies in key industries has been hotly debated at every turn. This analysis traces not only the development of this triumphant idea, it also highlights the many critiques within Chinese policymaking circles that have emerged along the way. This book demonstrates, first, that the advance of the state is not, and has never been, as has sometimes been asserted, a matter of the 'Beijing Consensus'. At every point there has been a persistent counter-narrative pushing against the development of state capitalist institutions. Drawing attention to this persistent counter-narrative is also important because China's state capitalist dissenters have articulated a starkly different vision of what the Chinese economy ought to be. If state capitalism in China collapses under its own weight, as some think it might, this vision-in-waiting might well provide the ideational foundation for new rules of the game.

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In concentrating on the evolution of ideas and institutions regarding the role of large SOEs in the reform era, the analysis is necessarily drawn into the consideration of wider questions about state–market relations. The question of large SOEs is deeply entwined with – and ultimately inseparable from – a broad movement to recast the state economy in an era of almost unfathomable change characterized by torrid GDP growth, structural change, rural to urban migration on a massive scale and market liberalization. At the same time that policymakers wrestled with the extremely difficult question of what to do with SOEs, they were also confronted with a range of other equally thorny questions such as ‘What ought to be the sectoral boundaries of the state economy?’, ‘What is a strategic sector?’ and ‘What constitutes appropriate market intervention in China’s economy?’ At the centre of this book is an analysis of policymakers’ provisional answers to these thorny questions – answers that were very much the products of both contingency and contestation. The case studies of telecommunications services and airline reform, in particular, underscore the indeterminate and highly contested nature of the state sector’s great transformation.

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