Introduction

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Orientation of the Study

The original purpose of the fieldwork on which this study draws was to discern the political consequences of emerging markets for Communist states and societies. Decades of scholarship had developed a view of these societies as highly bureaucratized orders. Power and privilege were defined by bureaucratic rank, and the citizenry were highly dependent on local officialdom. I had tasted this during two years of residence in a North China work unit from 1980 to 1982, experiencing firsthand the pervasive mediation of daily necessities and activities by local state agents. In mid-1988, at the close of the first decade of Chinese market reform, I returned to study the link between emerging markets, social structure, and political change.

I focused on private business, widely viewed as the furthest commercial departure from the classical Communist order. My assumption was that private business was creating new resources and careers independent of the state apparatus that were lessening citizens' bureaucratic dependence. The expectation was that interviews with private business operators would illuminate changes in local interactions between state and society, letting me document the increasing autonomy of citizens from the state apparatus.

My expectations were considerably diminished when, upon entering the field, I was unable even to clearly distinguish private businesses from public ones. Some entrepreneurs introduced to me as "private" business operators insisted their firms were "public." Others introduced as the operators of "public" firms claimed they ran "private" ones. Yet others maintained that their firms were "half-public/half-private." A few even claimed different statuses from interview to interview, although the legal registration of their companies had not changed. This situation frustrated my attempts to classify the abundant data flow. I spent much time thinking about classificatory schemes while almost every new interview presented anomalies defying my pigeonholes.

A turning point in my research direction was a conversation in early 1989 with an entrepreneur nicknamed Boss Short Pants (*Duanku*

Laoban), who ran a business group with a mix of privately owned and public firms. The Boss had previously impressed me with his no-nonsense style, indicated by his trademark casual wearing of short pants in hot weather. I made an appointment to talk to him, hoping to clarify what was "private" about private business. I figured that the Boss must have some scheme for distinguishing it – how else could he manage his commercial empire? During our conversation, I kept turning the topic back to legal property rights whenever Boss Short Pants veered away from what I deemed the crucial issue. He became agitated, finally blurting out, "Read the damn government policy if you want to know about property rights. But if you want to know about the business situation here then listen to what I'm saying!" After my profuse apologies he continued, "Property rights give you only a legal existence. But your market activities depend on the social environment (*yao kao shehui huanjing*). If your connections (*guanxi*) with officialdom are good, then your business can develop, but if they are bad then officialdom squeezes you and you can't get anywhere."

Boss Short Pants insisted that my concern with legal property rights was misplaced. Later I would realize the importance I placed on the issue stemmed from an uncritical, indeed unwitting, acceptance of the ideal-typical market image of standard economic theory. But this realization would not come until later; the immediate upshot of our conversation was that I resolved to stop wasting time trying to square data with the public/private dichotomy of legal property rights and listen to what entrepreneurs were telling me about themselves and their business. During the next year and a half I cast my net wide and deep, meeting many people in Xiamen, entrepreneurs and others, while socializing intensively with some entrepreneurs with whom I developed rapport.

I began to pay closer attention to what people were saying and how they said it. The realization dawned on me that private business operated in networks of personal ties centered on the local government. Personal ties with state agents enhance access to profit opportunities located in the state's bureaucracy and protect subsequent wealth accumulations. Commercial rationality, therefore, also entails the social process of forging and cultivating the personal ties to local government through which business-enhancing resources flow.[1] Business strategies and competition are patterned by the different accumulations of personal ties through social background and skill in the "art of social relations" (*guanxixue*) of

[1] My use of the term "local government" corresponds to the *difang zhengfu* of Chinese official terminology, which denotes any level of government below the center (Huang 1996: 20–1); that is, it can refer to governments all the way from the provincial level down to urban subdistrict levels and rural villages and townships. When necessary I distinguish specific levels. The center is referred to as the central state or state elite, while the term "state" refers to the entire complex of central and local government.

specific firm operators. I also realized that the idiomatic ways in which entrepreneurs spoke of their business practices expressed continuities with as well as changes from the clientelist relations of the pre–market reform era.

When I left the field in the summer of 1990, I knew that my observations not only falsified my original hypothesis but raised entirely new concerns. My original question – What are the political consequences of an emerging market economy in a Communist order? – had been displaced by a new one – How does a market economy emerge from a Communist order? My dissertation, submitted in 1993, described the embeddedness of private business in social networks and political power as I came to understand it in 1988–90 after a decade of market reform. This present study, a more analytically sustained reflection on the field data, pays more attention to explaining the institutional process by which a Communist system transforms into a market economy. Why and how does private business operate through clientelist networks? What are the outcomes for economic performance? What are the outcomes for the polity? How does this differ from other post-Communist market economies and emerging market economies in general?

In this chapter I do four things. First, I give an overview of the classical Communist orders and the commercial departures from them. Second, I summarize this study's central thesis that the revival of private business gives rise to commercialized clientelist networks. Third, I describe the research strategy of the study. Fourth, I give a historical sketch of the fieldsite.

Communist States and Economic Reform

Observers of Communist orders have long pointed out that economic organization and political power are defined by the party-state's bureaucratic control of resources.[2] Central planning places allocation in the hands of Communist Party officials, while suppression of household and small-scale private enterprise and retail and wholesale markets creates a monopoly over the production and distribution of goods. This results in a lack of consumer items, the rise of in-kind distribution centered on workplaces, and the rationing of foodstuffs, housing, and other daily necessities. Andrew Walder observes that "all of this further served, for a considerable historical period, to reduce alternatives and reinforce dependence upon superiors for the satisfaction of needs" (Walder 1994a: 301). Access to daily necessities and career opportunities

[2] Classic statements of this point are Djilas (1957); Feher, Heller, and Markus (1983); Rizzi ([1939] 1967); and Trotsky ([1937] 1972).

was a function of one's power and influence in bureaucratic allocation procedures.

Much economic allocation and political power came to be embedded in clientelist networks.[3] At the local borders of state and society, officials' discretionary allocation of goods and opportunities created patron–client ties. These ties not only allocated resources but also facilitated local governance as clients took the lead in demonstrating compliance with state initiatives and providing officials with information on societal resistance. Patron–client ties also created cross-cutting cleavages in society that reduced the likelihood of organized popular resistance to the state and local officialdom. Within the bureaucracy, clientelist networks between superiors and subordinates buttressed central authority by enhancing the compliance of lower officials. Promotions depended on the recommendations of one's immediate superiors, inducing the responsiveness of subordinates. The institutionalization of clientelist networks was idiomatically expressed as *guanxi* in China (Walder 1986: 170–85), *protekcio* in Hungary (Róna-tas 1990: 119), *dosjcie* in Poland (Wedel 1986: 79), and *blat* in the Soviet Union (Grossman 1983: 105–8).

For some time social scientists have speculated on the political implications of the introduction and expansion of markets in Communist systems. In 1978 the sociologist Ivan Szelenyi wrote that "the interests of the powerless and disprivileged can be best served with increasingly transactive (and consequently *market-like*) relationships in the economic system" (Szelenyi 1978: 63). He speculated that increased market allocation of resources would reduce the party-state monopoly on power and privilege that was maintained by bureaucratic redistribution. Analysts saw commercial departures from bureaucratic redistribution through popular activities like worker moonlighting and state initiatives like private agricultural plots as enhancing individuals' autonomy from the system. However, these activities were deemed incapable of changing the system. Some analysts considered them so petty as to be marginal to the main arenas of political struggle; others saw them as safety valves that helped to maintain the system by channeling popular discontent into individualized strategies of material gain.[4]

In the 1980s Communist states shifted to more comprehensive market reform programs to counter stagnating production, obsolescing technology, declining living standards, and labor problems. This stimulated scholarly reassessment of the political implications of emerging markets

[3] Key studies in this vein include Baker (1982); Ionescu (1977); Oi (1985, 1989); Tarkowski (1983); Walder (1986); and Willerton (1979).

[4] Key studies include Feher, Heller, and Markus (1983); Kemény (1982); Misztal (1981); and Sampson (1987). For China's second economy see Burns (1982); and Chan and Unger (1982).

in these systems. Such new commercial activities as foreign investment, expanded private business, and leasing of public enterprises were seen as transforming the system itself. In the words of sociologists David Stark and Victor Nee, market "reforms [are] redrawing the boundaries between the state and society and shaping new patterns of transaction, mediation, and bargaining across them" (Stark and Nee 1989: 16). The revival of private business is seen as one of the most consequential economic departures from orthodox central planning. The economist János Kornai concludes that "the rise of the private sector is the most important tendency in the economic sphere during the process of reform. It brings a deep change, since it affects the property relations and it does so in a radical way: private property appears alongside public property" (Kornai 1992: 433). In short, private business is widely considered the most far-reaching departure from the Communist order, with profound consequences for economy and polity.

The revival of private business reflects the growing concerns of Communist party-states to solve unemployment and provide more consumer goods, concerns that shifted their policies away from constricting private economic activity to a more tolerant stance. The reemergence of private economic activity varied in timing and pace by country. In regard to timing, the Hungarian private sector developed earliest, with policies expanding the scope of private farming and services in the late 1960s; this did not happen in the Soviet Union until the late 1980s. In regard to pace, the reemergence in China has been especially swift. On the eve of market reform in 1978 there were only 80,000 licensed private businesses nationally, mostly peddlers of farm produce and secondhand goods whose activities were an infinitesimal share of the national economy. A decade later there were at least 30 million private businesses of some sort, constituting the fastest-growing sector of the economy.

The revival of private business has followed a similar pattern in diverse Communist countries, although there has been considerable variation in pace and timing. Typically, it begins with the state's reduction of restrictions on self-employment in privately owned family businesses (Róna-tas 1994). However, the state restricts their size by limiting the number of employees, permitting only limited shareholding or banning it altogether, and stipulating that private businesses must buy raw materials on retail markets and sell goods and services to individual consumers (Aslund 1985). This keeps private businesses small and prevents public resources and personnel from flowing to the private sector (Gábor 1989: 40). The next step in the revival is state condonement of private endeavors in the collective and state sectors through leasing, work partnerships, and cooperatives. New policies encourage useful aspects of private economic capital in creating jobs and meeting consumer demand while maintaining public ownership of productive resources in accordance with socialist ideology. Again Hungary led in such innovations, while other countries such as China and the Soviet Union adopted similar policies later.[5] The third step is the expansion of the sector of licensed private business as when the myriad policy restrictions against them are reduced to permit incorporated and limited-liability private companies. These firms are the legal equals of public enterprises, can engage in capital-intensive manufacturing and service ventures, and can sell wholesale to public producers.

A similar sequence has occurred in China.[6] Policies from 1978 to 1983 encouraged small privately owned businesses – the so-called *getihu* (individual businesses) – to create jobs and meet consumer demands (Gold 1990a: 158–62).[7] Out of ideological concern to prevent a "capitalist restoration," shops were limited to seven employees,[8] could not issue receipts larger than ¥100, could not use mechanized production or transport, were denied access to bank loans, and could not pool capital.[9] Next, in order to expand the beneficial aspects of private business without challenging socialist ideology, the state permitted private management of collective and state sector firms and assets. Such arrangements spread in the mid-1980s through cooperative, leased, and contracted firms. This created jobs and met demand but caused administrative confusion; for example, it was difficult to distinguish a cooperative from a socialized collective firm in tax matters.[10] To further expand the role of private

[5] For cooperatives in Hungary see Rupp (1983); and Swain (1990). For China see Lockett (1988); and Sabin (1994: 948–54). For the Soviet Union see Jones and Moskoff (1991).

[6] Private business has waxed and waned since the founding of the People's Republic of China. After 1949, the party-state initially encouraged private business in order to revive the economy. The only businesses expropriated in the first years were so-called comprador firms connected to international capital and the state. In fact, many merchants prospered as inflation was checked and kidnappings of businessmen ceased. State tolerance evaporated during the Korean War, when competition between state agencies procuring war resources and private businesses caused inflation. The nationalization of private capitalist firms and the socialization of smaller shops into collectives in the mid-1950s led to the decline of private business. In 1950 private business accounted for 76.1 percent of wholesale trade and 71 percent of industrial output, but by 1955, only 4.4 percent and 18.3 percent respectively (Kuan 1960: 66–7). Private business flourished briefly in the early 1960s, when, because of economic disruption and famine following the Great Leap Forward and the halt of aid from the Soviet Union, the state permitted private stalls and shops.

[7] Urban unemployment had swollen by the late 1970s to between 8.5 percent and 18 percent of the labor force (Gold 1990a: 160).

[8] This figure is widely assumed to be derived from a hypothetical example in Marx's *Capital*.

[9] A 1983 policy revision eased restrictions and permitted joint ventures (*lianying*) with public enterprises, but the seven-employee limit remained.

[10] The actual number of cooperatives is not known, as they are aggregated with socialized collectives in collective sector statistics: a 1988 national figure claimed 50,000 cooperatives, while local statistics suggest a much greater number. For example, according to one

capital while avoiding administrative confusion, the 1988 Private Enterprise Interim Regulation legalized limited-liability privately owned companies. These firms have no restrictions on employee numbers and can issue large receipts.[11] Further policies in 1994 permitted the incorporation of private companies and the issuing of shares on stock markets.[12]

The revival of private business in China has been especially dramatic. By one estimate, private sector share of the gross value of industrial output rose from 0.2 percent in 1980 to 36.5 percent by 1991 (Pei 1994: 92–3) and the private sector share of the retail trade grew from 2.1 percent in 1978 to 33.1 percent in 1993 (State Statistical Bureau 1994: 497).[13] Yet private business also exhibited the generic characteristics of private business in the Communist world (Aslund 1985; Grossman 1987; Los 1990). While many restrictions had been removed, others still remained, most notably prohibitions against direct foreign trade and private ownership of real estate. The ideological legacy of hostility toward private business, sudden changes in policies and regulations by the state, and arbitrary regulation by local agencies created uncertainties. Much trade was dubious, consisting of activities that the state did not condemn outright nor explicitly condone. Legal property rights were ambiguous, and despite regulations against party officials conducting business on their own and working in private firms, many of the larger companies used personal ties with officials to gain access to business-enhancing public resources.

Overview of the Argument

The central thesis of this study is that the revival of private business does not lead to the decline of patron–client ties but rather to the emergence of new commercialized forms of clientelism. Thus rather than talk of the retreat of the state during the market reform era, I describe the

local survey published in 1989, 60 percent of all the collective enterprises in Fujian province are privately run (Lin 1989: 34). Given that there were 510,134 collective enterprises in Fujian province in the late 1980s, consisting of 446,694 village and township enterprises (1988 statistics, Fujian Province Statistical Bureau 1989: 43) and 63,440 trade and service enterprises (1985 statistics, Fujian Province Statistical Bureau 1992: 227), this would mean that the province alone had 306,081 cooperatives, a figure much larger than the national figure of 50,000 firms. According to a survey published in 1989, of 518 collective firms surveyed in Wenzhou municipality, 79.5 percent were cooperatives (Jia and Wang 1989). For problems of statistical measurement see Odgaard (1992: 234–50); Sabin (1994); Young (1995: 4–9).

11 The companies are single-investor, joint-investor, or limited-liability. By 1994, there were also 374,700 legally private companies nationally (*China Daily* 1994).

12 The petty private shops, cooperatives and leased firms, and private companies are described in greater detail in Chapter 3. Corporations are discussed in Chapter 9.

13 Pei's figures include legally private firms and rural village and township enterprises, which are often privately run.

commodification of its local bureaucratic power. Rather than speak of the declining role of *guanxi*, I show how entrepreneurs draw on preexisting ties and create new ones to influence local state agents. And rather than talk of enhanced entrepreneurial autonomy from the state, I describe new patterns of bargaining and alliance across the local boundaries of state and society.

Clientelist ties are a contractual transaction that reflects power asymmetries between exchange partners. Such ties are expressed in terms of personal identity and interpersonal sentiments and obligations; they intermingle potential coercion and exploitation with voluntary relations and mutual obligations, and they involve reciprocal and mutually beneficial exchanges that are labeled as dubious, illegal, and corrupt by the state (Eisenstadt and Roniger 1984: 49; Flap 1990: 237; Foster 1963: 1281; Schmidt 1977). The emergence of patron–client ties is linked to the organization of the state. Such ties are likely to flourish in a state that creates unequal distribution of resources through monopoly practices, has weakly developed standards of impersonal behavior, and has weakly developed class and occupational interest associations (Flap 1990; Scott 1972b: 42). In such a state clientelist ties do the following: they provide weaker parties with steadier access to resources, enabling them to manage their dependence on state agents; they enhance expectations on the likely behavior of others by embedding interactions in social norms and practices; and they provide parties with vertical ties that can be mobilized to meet diffuse challenges.[14]

The embeddedness of Chinese private business in clientelist ties reflects the evolving organization of the Communist party-state during market reform.[15] It also reflects new interests and possibilities for profit seeking in the vast resources accumulated by the party-state through the structures of centralized economic planning and redistribution. But clientelist ties also mean that fewer resources reach local levels of the state through central redistribution, inducing local governments to seek profit through the resources they control, thereby lining officials' pockets and filling local government coffers. Clientelist ties also reflect the failure of the state to institutionalize universal standards, as by fully enforcing legal private property rights, in the market economy. Local governments interpret central regulations as they see fit while entrepreneurs cut their own deals with local governments to increase profits and provide security for wealth accumulations. However, the clientelist ties through which pri-

[14] For general discussion of networks in economic life see Burt (1992); Granovetter (1973, 1985); Lazonick (1991); Powell (1987); Powell and Smith-Doerr (1994); and White (1992).

[15] For uses of the concept of clientelism in other areas of China's emerging market economy, see Oi (1985) for the rural economy, Pearson (1997) for foreign enterprises, and Paltiel (1989) for a suggestive comparison with Mexico.

vate business operates differ from pre-reform clientelism not only in new commercial calculations but also in changing dependence: citizens' dependence on officialdom is much reduced as officials and local governments are increasingly dependent on entrepreneurs and their firms for certain resources. The new ties are therefore symbiotic.

The argument can be sharpened by distinguishing the clientelism I observed from other manifestations of it in markets. First, it differs from clientelized ties between buyers and sellers found in many third world and informal economies that are indicated by such local names as *pratik* in Haiti, *suki* in the Philippines, *onibara* in Nigeria, *casera* in Peru, and *sedaqa* in Morocco.[16] These ties diffuse information and produce trust, processes that I too observed in China. But the key difference is that these other ties are horizontal ones of relative equality, whereas in China they involve asymmetries between those inside and those outside the state structure and are therefore more vertical. Furthermore, the entrepreneurs I observed view relations with officials as supportive and actively cultivate them; in contrast, third world traders see officials as predatory and seek to minimize contact with them through horizontal strategies.[17] Nor do the Chinese clientelist ties conform to Southeast Asian "crony capitalism," which is characterized by commercial advantage to an entrepreneur derived by personal association with the head of state, because the ties I document operate in much lower levels of the government.[18] Also, the concept of rent-seeking that undergirds crony capitalism is not particularly apt, as it presupposes a functioning market, whereas Communist orders lack markets; thus the analytic task is to explain the emergence of markets rather than their distortion. Finally, Chinese clientelist ties do not fit the East Asian model associated with Japan and Korea.[19] In this model, a strong central state maintains economic guidance of the market economy through particularistic flows of policy directives and economic capital to commercial firms. The situation I observed differs: the central Chinese state condemns many market practices and seeks to suppress them. China's emerging market contains many practices that deviate from central directives and that proceed in networks of local interests distinct from the center's. These local devia-

[16] See Granovetter (1993) for an overview of this kind of horizontal clientelism. Related terms in the Chinese context, such as *xinyong* (credit), refer to evaluations of honesty and dependability within the community of businesspersons (Barton 1983; DeGlopper 1972) and therefore also suggest horizontal relations.

[17] See, e.g., MacGaffey's (1991) account of Zaire.

[18] Kunio (1988) is the *locus classicus* for the concept of crony capitalism. The members of the so-called princes' party (*taizi dang*), the offspring of elite central officials, are more analogous to crony capitalists in the Chinese case. For the concept of rent see Bates (1981); Krueger (1974).

[19] The East Asian model draws on Gerschenkron's (1962) classic discussions of late development (Amsden 1989; Johnson 1982; Jones and Sakong 1980).