Emerging Chinese Capitalism and its Theoretical and Global Significance

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INTRODUCTION

In this essay I argue that China hosts an emerging capitalist society. Studying the nature of this capitalism will allow us to evaluate and reassess the definition and theories of capitalism – a pivotal notion in the contemporary explanation of economic growth and associated ideas such as freedom and democracy. It will also afford us a better understanding of how this capitalism could impact the world economically, politically, and socially. Finally, it may help to identify clues about the mechanisms that are guiding China into the future. Specifically I will make the following arguments. First, capitalism consists of a set of social institutions that sustain the production, accumulation and reproduction of capital and these institutions include: calculating capitalists, free markets, wage labor, an expansive system, and a strong and supportive state. Theories ranging from self-interest – the psychological motive, exploitative reproduction – the sociopolitical motive, to institutional enticement – the cultural motive, and the networking imperative – the social motive, and they collectively explain how these institutions are coordinated. Second, China today strongly meets these requirements as a capitalist state. Capitalism in China, further, exhibits two relatively unique features: the state as capitalists and social relations (guanxi) embedding economic activities. Finally, I will consider theoretical implications of these institutional features for conceptualizing and theorizing capitalism, and for understanding global and domestic developments.

THE RISE OF CHINA

In January 2007, Time Magazine proclaimed the dawn of the Chinese century. While this was seen as premature by some, the rise of China as an economic power was not unanticipated. For a few scholars who have examined longer historical trends (Wong 1997; Frank 1998), the rise of the West in the past two centuries was the abnormality: for more than ten millennia the East has been the leading world power. Due to a combination of circumstances that occurred in the East and in the West (for Frank, the
discovery of gold and silver in the Americas allowed Western economies to appropriate materials and wealth from China, the West took the lead in the world economy in the eighteenth century, but that will only be a temporary change. Yet even though this perspective has gained some empirical validity, the causes for the anticipated re-emergence of the East are unspecified or unclear.

The rise of China has also been anticipated by scholars who have analyzed Asian economic miracles for the past three decades. In the early 1990s, proponents of the “snowballing” or the “flying geese” process also projected that following the rise of Japan, and then the four tigers (Singapore, Hong Kong, South Korea, and Taiwan), China would inevitably join the Asian trend. But the process could hardly anticipate or explain the speed and velocity of China’s rise.

In less than two decades, China’s per capita GDP has risen from less than 200 constant 2000 U.S. dollars to over 1,500. The poverty rate has dropped from over 60 percent to about 10 percent. During this period China lifted 300 million of its people out of absolute poverty (based on the one U.S. dollar a day threshold, set in 1993), even though 200 million remain below the poverty line (BusinessWeek January 3, 2007). Xinhua reported that the number of impoverished people without adequate food and clothing declined from 250 million in 1978 to 23.6 million at the end of 2005. It claimed that the percentage of the population living in poverty had fallen from 30 percent to less than 3 percent.

According to the World Bank (2005) and the World Development Indicators, China consumes 29.7 percent of the world’s rice, 24.4 percent of its soy oil, 31 percent of its cotton, 33 percent of its tin, 29 percent of its zinc, 29 percent of its iron ore, 31.5 percent of its steel production, and 12.6 percent of its energy (coal and oil). Goldman Sachs (May 2007) has estimated that China will match the United States in GDP (in purchasing power parity terms) by 2020, and it may well become the largest economy in the world (in actual market exchange rates) by 2027 (The Economist 2007a)

During this short span of time, China has become a major manufacture, a major consumer in the global economy, a major polluter, a furious competitor for energy resources, and a significant exporter of
goods, services, and human power. These trends have obvious impacts and consequences for the rest of the world: intellectuals, politicians, businesses, and the media have all been busily contemplating them and finding responses to the challenges they pose.

Grave concerns about the rise of China go beyond its economic challenges. China does not seem to adhere to the ideals of freedom, democracy, and the free market that are considered central to economic development. As recently as ten years ago, some still hoped that the Chinese political regime would become unstable and either “transition” into a Western-style democracy or collapse altogether (Chang 2001). The new “superpower” has clearly shaken the ideals and social order, real or imagined, of most Western observers and scholars. A hierarchy based on any number of economic and political criteria is disrupted. Arrighi (2005) rightly pointed out that the rise of China is “a fundamental subversion of the very pyramidal structure of the hierarchy.”

The phenomenal and sustained economic growth of China over the past two decades has raised fundamental issues about whether the economy is properly capitalistic, and if so whether that capitalism poses ideological and theoretical challenges to the norms of Western economics. Hence, I will (1) outline the received and updated definition and theories of capitalism, (2) argue that what is going on in China meets those conditions, (3) delineate the specific features of Chinese capitalism and how they both help and hinder its development, (4) discuss the implications of these features for the received wisdom on capitalism, (5) point out the implications of Chinese capitalism for the global system, and (6) sort through the confusion about the nature of the mechanisms that will lead China into the future.

WHAT IS CAPITALISM?

The term “capitalism” may have first been mentioned by Marx when he questioned whether Russia could bypass the “capitalist” stage of development, but it is an intellectual invention of the twentieth century, as Sombart (1902) may have been the first to properly use the term. To understand capitalism
we first need to be clear about what capital is (see Lin 2001a, chapter 1). Marx identified it as part of the surplus value generated in the production, distribution, and marketing of commodities. Surplus value becomes possible because of the difference between the labor cost (use value) and the value of the good produced (exchange value). When part of this surplus value is reinvested in the production of the same or different commodities in anticipation of generating more surplus value, it is called capital. The process by which capital is invested, reinvested, and accumulated is called capitalism.

More specifically, capitalism can be defined as a set of arrangements of social institutions that sustains the production, reproduction, and accumulation of capital. It is intrinsically social in that it both describes a social process and implicates social elements (institutions). Much of the historical analysis of capitalism has focused on the transition from feudalism to capitalism as experienced in Europe and North America in the past four or five centuries and has identified coalition processes among urban elites (e.g., intellectuals, nobilities and merchants) and rural peasants, serfs and slaves in upending feudal systems and bringing in various capitalistic institutions (see Dobb, 1947; Walzer, 1965; Tilly and Tilly, 1971; Hill, 1972; North and Thomas, 1973; Brenner, 1976; Hilton, 1978; Kriedte, and Schlumbohm, 1981; Goldstone, 1987; Gould, 1987 Lachmann, 1987; 1989). The extensive discussion about the nature, logic, and history of capitalism has identified fundamental and nearly consensual, but incomplete, institutions as essential to capitalism (see examples in Williamson 1975; Meyer and Rowan 1977; Williamson 1985; Heilbroner 1985; Zucker 1988; March 1989; North 1990; DiMaggio and Powell 1991; Miller 2005;). Heilbroner (1985:34-35) argued that capitalism was “not a material thing but a process that uses material things as moments in its continuously dynamic existence. It is, moreover, a social process, not a physical one.” What, then, are the major institutions implicated? Integrating diverse and rich discussions, I identify the following institutions.

CALCULATING CAPITALISTS
First, there are the actors who engage in the generation and regeneration of capital – the capitalists. They are distinguished from waged labor. Laborers are mostly excluded from engagement in capital production and reproduction, primarily because when they claim a wage they forfeit their claim to the products and the means of production (property rights). Neither are wealthy actors automatically capitalists: there are many sources of wealth, such as inheritance or even work that does not involve reinvestment in production. As Adam Smith (1937) pointed out, it was the individual effort to pursue material benefit that promoted free enterprise and the market system, the foundations of the wealth of the entire community, or the nation. Even though Smith himself did not use the term “capitalism,” his theory of self-interest and rational choice laid the foundation for much discussion about capitalism in the twentieth century.

There is some paradox to being a capitalist. On the one hand, there is the drive to produce and reproduce wealth, part of which affords a certain lifestyle and leisure to enjoy. On the other hand, there is restraint from such use of wealth for pleasure, as part of it is reinvested in the capital production process. These dual characteristics, the drive for profit and asceticism, reflect in part the ever-calculating personality of the capitalist.

FREE MARKETS

Second, there are markets in which production, distribution, and consumption exchanges can take place. These markets form a circular network; each relies on and propels the others (see Lin 2001a, chapter 1). A production market requires an ample supply of material resources and human resources (the labor). The commodities produced must be distributed to consumers, and there must be markets where consumers can find the commodities. Efficient production markets generate commodities at a use value that can be sold at a higher exchange value (price) to produce surplus value in the distribution and consumption markets. Exchanges in these markets are further facilitated by financial markets which raise
capital, buffering risk and expediting trade (through loans, stocks, bonds, derivatives, hedge funds, etc.).

All three types of market are never entirely free in the sense that each is dictated by the negotiation of prices between sellers and buyers and involves control or manipulation by these or other actors. A pure free market would inevitably fail, as actors would deny other actors access to resources, control of information, and so on to serve their self-interests and maximize their relative advantages. Contracts, organizations, and informal networking, which always exist in markets, inevitably reduce the freedom of the market. Government regulations, such as taxation, to produce and protect public goods such as roads and a safe environment, and to prevent fraud, further reduce the freedom of the market. Nonetheless, in an ideal and efficient market system, such “restrictions” are assumed to be kept at a minimum, and entries and exits are entirely voluntary and transparent.

WAGE LABOR

A third necessary institution in capitalism is wage labor. Capitalism as a social system differs from other systems in that it cannot rely on free (or slave) labor; it allows the claim of “proper” compensation for labor: wages are paid to the labor force for work. However, this transaction favors the capitalist. Commodities tend to generate exchange values that exceed production costs. Laborers forfeit their claim to the means of production and produced commodities (Heilbroner 1985). The laborer has no property rights whatsoever in the production process, beyond wage and compensation for their labor time and effort. This peculiar transaction is, of course, essential for the production and accumulation of capital.

AN EXPANDING SYSTEM

Fourth, capital accumulation dictates an ever-expanding system. The drive for profit requires capitalists to seek and expand the production of commodities and to generate profits through extensive and extending distribution and consumption markets. The process of production – in which costs must be paid
for the labor and material – and profit generation in the distribution and consumption markets become a relentless and continuous circulation and form the basis for competition. Thus “capital itself introduces a form of social war “(Heilbroner 1985:57). Likewise, Schumpeter stated that “capitalism stands and falls with entrepreneurship: if capitalism continuously presents new opportunities for profit it will thrive, otherwise it will die out” ((1946) 1951:81-86).

Expansion can be achieved through commodity diversification, increased production resources including labor, extended distribution channels and chains, ever-stimulated desires for commodities, and new consumers. Therefore capitalism, by definition, must continue to expand. Technological innovations are a necessity, as is the containment of production costs. But ultimately, capitalism needs ever-larger markets for resources, including labor, for production on one end, and for consumers on the other. Heilbroner stated, “Without the organizing purpose of expansion, capital dissolves into material building blocks that are necessary but not sufficient to define its life purpose” (1985:26-37). Wallerstein (1979b) pointed out that the essence of capitalism is in the capitalist’s production of commodities for sale on the world market.

An expanding system presumably also overcomes the possible concern about a zero-sum game. By continuously expanding, collective wealth and therefore capital are increased. But the fact is that this expanding system creates an economic paradox. There has been continuing debate among economists as to whether economic growth or economic inequality should be a primary concern. By the expansion criterion described here, then, economic growth should have the priority. There is not necessarily any association (either positive or negative) between economic growth and income inequality, either theoretically or empirically. However, once economic growth becomes the priority, income inequality may persist or even increase. As will be seen later when looking at the historical data from China and other capitalist countries such as the United States, economic growth has been negatively associated with income equality over the last two decades.
A STRONG AND SUPPORTIVE STATE

Finally, there must be a state – a governance institution that is willing and capable of protecting, regulating, and promoting the coordination and functioning of capital accumulation, the markets, and wage labor. None of the institutions mentioned previously constitute a capitalist system by themselves, and there is no guarantee that they will simultaneously coordinate with one another. Some scholars have maintained that capitalism only needs a governance system that monitors the “natural” free market and allows it to function without interference or abuse. Rand (1946) 1966), for example, stated that the only function of the government should be the task of protecting man’s rights. In a capitalist system all human relationships should be voluntary.

Historical evidence, however, convincingly shows that to thrive, capitalism requires a strong governance system, and thus a powerful state. Some economists have admitted that the state intervention may be necessary for a backward economy to catch up and become a capitalist system (see, for example, Rosovsky 1961 on France, Germany and Russia; and Gerschenkron 1962 on Japan). However, analysis of broad historical data on capitalistic development demonstrates that a strong and supportive state is an essential ingredient for all capitalistic systems. Braudel (1977) stressed that capitalism, differing from a mere market system, triumphs only when it becomes identified with a powerful state. He cited the Italian city-states, Holland, and England as examples. The state provides guarantees that players follow the rules of the game. It ensures that the capitalists produce and reproduce commodities with acceptable practices of acquiring material resources and compensating labor. Commodities are channeled through distribution and consumption markets transparently and without price fixing, hoarding, or dumping. Also important is the state’s role in arbitrating disputes over production, distribution, and consumption markets. While attempting to be evenhanded, the state is ultimately responsible for protecting the capitalists so that capital accumulation can proceed.

Polanyi (1944; Polanyi, Arensberg, Pearson1957) made the essence of the state explicit. He
identified the state and the market as the two central pillars of modern capitalism. To Polanyi, the two institutions are interconnected. The state plays a central role in determining the structure of property rights, the quality of financial institutions, and the incentives for capital accumulation, investments, and entrepreneurship (see Heilbroner 1985 for elaboration). Of particular interest is the arbitration of disputes between capitalists and the labor. While in some capitalist states unions are advocates of labor, the state is the ultimate arbitrator. It ensures that laborers never challenge capitalists for rights to the products of their labor and the means of production.

Many sociologists and political scientists have rightly stressed the significance of the state in modern industrialized societies, among them Wallerstein (1979a), Evans (1995), Skocpal (1996), and Hobson (1997), Weiss (1998), Evans, Rueschemeyer, and Skocpal (2002). Historically, the United States government has not shied away from interfering with the market system to protect or save firms and industries. Some examples include its long-term farm protection policies, rescues of automobile, steel and airline corporations, and international tariffs.

Examining the recent history of the United States, Fligstein (2005) pointed out that entrepreneurship and competition matter for the creation of new markets and industry but that they cannot occur without governments and stable social structures to support them. He showed that the U.S. government has directly affected market activities with laws and rules that determine tax policies, govern the use of equity and debt by corporations, regulate employment relations, enforce patents and property rights, and regulate competition or antitrust policy. It can act as a buyer of products and a provider of research and development funds to firms. It also makes rules that can directly favor certain firms in particular industries, often at the behest of the most powerful actors in those industries. The government, he pointed out, also built up public and private infrastructure that opened up the possibility for new firms and industries to emerge. Heilbroner made this point clear:

The state, both as defender and promoter of the economic realm, has played so prominent a role that even the most abstract scenarios of the system unwittingly assign it a central and
A strong state will protect a domestic market, protect capitalists, assure the supply of wage labor, create and implement rules of law and individual rights, secure networks and chains of trade, and advocate globalization for the benefit of the domestic market and capitalists. It is a core element of capitalism. Yet, and interestingly, the role of the state is largely absent or in the background in many economic analyses of capitalism.

CONTENDING INSTITUTIONS: PRIVATE PROPERTY RIGHTS AND DEMOCRACY

Two other institutions have also been associated with capitalism in the scholarly literature: the private ownership of property, and political freedom or democracy. The argument for the private ownership of property and its link to political development can be traced back to John Locke ((1764)1952). In the wake of the parliamentary struggle against the monarchy, Locke heralded the significance of the social contract whereby property rights must be spelled out and protected. Subsequent discussions extended this historically based argument into a broad argument for private ownership in a free or democratic society. Rand (1946; 1966), for example, defined capitalism as a social system based on the recognition of individual rights, including property rights, in which all property is privately owned.

However, the nature of property rights and its association with capitalism have remained equivocal. Property rights refer to a bundle of rights (Alchian and Demsetz 1973), including the ownership, use rights, rights to transfer, and rights to exclude use by others (Heilbroner 1985). Some
have argued that use rights rather than ownership are the central feature of property rights (Alchian 1965). Other scholars have argued that the exclusion of others from use rights rather than claims to property is more important. Still others question the validity of private property rights in capitalism and suggest that public property rights (e.g., eminent domains) are essential for the production of public goods and infrastructure to benefit all.

Recently, De Soto (2000) directly linked private property rights (ownership) to capitalism or democracy. But evidence that private property rights produce more capitalist behavior such as borrowing capital for investment remains unproven (The Economist 2006). Historically, capitalism has thrived with the ownership of means of production but without the ownership of other properties such as land. Although Friedman (1962) hailed Hong Kong as a shining example of capitalism, the government owns all land and only grants allotments for private ownership in the New Territories under the Small House Policy.

The linking of political freedom or democracy to capitalism is also a rather recent intellectual formulation. Friedman probably made the first link, proclaiming “the role of competitive capitalism … as a system of economic freedom and a necessary condition for political freedom” (1962:13). But he also cautioned that “it is clearly possible to have economic arrangements that are fundamentally capitalist and political arrangements that are not free (1962:10). Subsequent discussions tend to forget this causal conjecture and even reverse the sequence so that, for some, democracy is now seen as a precedent or necessary ingredient of capitalism. There is little theoretical foundation or historical evidence that democracy leads to capitalism and, according to Heibroner (1985: 126-129), “capital itself has no inherent dependence on or affinity to political freedom. … It is an elemental proposition of democracy that every voting citizen has the right to cast but one vote, whereas it is an equally elemental proposition of capitalism that every market participant may rightly cast as many votes as his or her wealth permits”. Differential voting weights, as practiced in shareholding rights among different types of shareholders,
illustrate this distortion of democracy well (*The Economist* 2007b). The dual- or multiple-class share system allows capitalists to exercise much greater power in corporate decisions. In fact, recent evidence suggests that “savvy autocrats have learned how to cut the cord between growth and freedom, enjoying the benefits of the former without the risks of the latter (Mesquita and Downs 2005).

Nevertheless, there is some evidence that capitalism promotes democracy. In Britain, voting rights were granted to all male citizens in urban areas in 1867, and extended to all male citizens in rural areas in 1928. It was not until 1928 that women were allowed to vote, long after the industrial revolution was over and capitalism reached maturity. In the United States, white males passing certain property and religious tests could cast votes in the years 1810-1820, and the tests were abolished in 1830. After the Civil War, the Fifth Amendment granted African Americans the right to vote in 1870. Women were not granted suffrage until the Nineteenth Amendment was passed in 1920. It is thus important to remember that it is capitalism that may lead to democracy, rather than the other way around. One possible reason why capitalism enhances the likelihood of democracy is that it brings about a middle class that has collective resources and challenges the prevailing authority (Rueschemeyer et al. 1992).

THEORIES OF CAPITALISM

What mechanism brings the social institutions of capitalism together and coordinates them in an orderly fashion? No single theory that can explain how they coordinate, but there are four “general theories”, each of which explains an important part or component of capitalism: self-interest – the psychological motive; exploitative reproduction – the sociopolitical motive; institutional enticement – the cultural motive; and the networking imperative – the social motive.

SELF-INTEREST. The dominant theory of capitalism focuses on individual behavior, with a historical base of Britain’s rise as an industrial power, and incorporates Adam Smith’s explanation that the pursuit of self-interest necessarily promotes the public good. When everyone has the opportunity to
pursue their own interests, exchanges are based on the supply of and demand for goods, and an optimal transaction based on the negotiated price will result. Without external influences, these transactions maximize the flow of production and consumption of goods, and create the optimal flow of goods and wealth for the entire society. While Smith did not employ the term “capitalism” to characterize the arrangements of social institutions, his argument laid the foundation for much subsequent discussion of capitalist development.

EXPLOITATIVE RELATIONS OF PRODUCTION. Karl Marx focused on the process by which production was accumulated – the rate of exploitation. Capitalists’ exploitative relations with labor, the extent to which they extracted surplus value from the use value of labor, determined how much capital could be reinvested in production. Capitalists not only controlled the means of production but also the arrangements of the institutions (wage labor, markets) that sustained and promoted the accumulation of capital, with the state serving the interest of the capitalists.

THE CULTURAL ENTICEMENT. Max Weber (1947) focused on the evolution of religious institutions in Western Europe, and argued that the Reformation resolved the tension between devotion to work and ascetics. The joining of the sacred (ascetics) and the secular (profit making) unleashed productive forces and channeled profits into further production rather than pleasure – thus developing the spirit of capitalism. Weber modified Marx’s theory by identifying a process in which surplus value could be generated by labor as well. By combining ascetics and profit making, it is at least conceivable that some laborers may generate surplus value and convert part of it into capital. In this consideration, it can even be argued that Weber preceded, even though he did not anticipate, the development of neo-capitalist theories such as human capital, cultural capital and social capital (see Lin 2001a, chapter 1).

NETWORKING AND CHAINS OF COMMODITIES. The networking motive joins the desire for profits with the practical necessity of locating resources and markets through chains of production (commodity chains), distribution, and consumption (value chains). Wallerstein’s (1979a,b) world system
exemplified the significance of chains in production and consumption. Braudel’s analysis of networks characterized the market system beyond local boundaries (1977). Castells (1996;1998) saw networking afforded by the new electronic media and the Internet as allowing capitalism to reach its summit. Such trust-based networks, more than anything else, ensure that the flow of resources and commodities transcends geographical limitations and imperfect information flows. Without these often informal relational configurations, capitalists would find it impossible to generate and accumulate capital. Even today, many regional alliances (e.g., the European Union) find it necessary to rely on networks to sustain their expansion to other parts of the global economy.

None of the abovementioned theories can explain capitalism by itself, but they each describe a sub-process of capitalism. Self-interest explains the effort, action, and choices of actors in the drive for profit and wealth. Exploitative production characterizes the mechanism by which capital is retained and regenerated. The cultural and institutional mechanisms allow for the masses to participate in the capitalist processes. The networking mechanism explains the linkage from the production process to the distribution and consumption processes in the ever-expanding system. It is, in fact, the combination of these psychological, political, cultural, and social mechanisms that bring the actors together and submit their forms of behavior and practices to a set of rules and arrangements expected in capitalism. It is not surprising that more recent observers have noted the multifaceted nature of capitalism. For example, after analyzing economic development in East Asia, Hamilton and Biggart (1988) argued that it could best be understood in terms of a combination of market, culture, and authority.

MULTIPLE MODELS OF CAPITALISM

Similar to the multiple theories that describe the mechanisms of capitalism, empirical studies of capitalist societies have also uncovered diversity and differentiation in the actual institutional arrangements (see Esping-Anderson 1990). In fact, if rigorous criteria are used, no single society throughout history fulfills
all of the requirements of capitalism as defined and theorized. Each society molds and transforms but never revolutionizes available institutions to promote capitalism.

The initial models of capitalism formed around Marx and Smith’s observations of British economic development in the seventeenth and eighteenth centuries. That development was organized by medium and large firms, backed by industrialization with the invention of the textile mill and the steam engine, and the subsequent development of more advanced transportation, communication, and military technologies, coordinated by a powerful state with a military force that reached around the globe. The subsequent emergence of the United States, with its British institutional legacy, allowed the development of an Anglo-Saxon model of capital, characterized by an emphasis on entrepreneurship, less restrictive government regulations, and free trade; this has been labeled as liberal market-driven capitalism. There is also a continental European model of Germany, France, and others, as well as Japan, which has been labeled coordinated capitalism and is characterized by coordination between the state and large corporations.

Capitalistic states can also be grouped by certain theoretical or practical criterion. Esping-Anderson (1990) has used the term “welfare regime” to classify three types of capitalism, depending on the degree of state welfare provision or the decommodification of labor. A liberal regime, as exemplified by the United States, offers minimal policy intervention; a conservative regime, as exemplified by Germany, provides selective welfare services to stratified groups; and a social democratic regime, as exemplified by the Scandinavian countries, exercises a broad welfare policy. The extent and nature of state intervention has also been used by Monsen and Walters (1983) to characterize command capitalism, planned capitalism, regulated capitalism, democratic socialism, and pure market capitalism, with states capable of moving from one type to another.

Within each model or classification of capitalism, more refined capitalist states have been identified, such as the East Asian model of Japan and South Korea (see Albert 1991/1993; Arrighi
Finer analyses would further reveal that each society within a category shows certain different or unique features.

Other models have been based on the historical reconstruction of economies such as those of the Italian city-states. Venice has been described as a type of capitalist city-state where merchants traded over oceans with chains of exchanges for resources, backed by a powerful navy. Portugal, Spain, and Holland represented more extensive powerful colonial capitalist states where naval forces in conjunction with merchants extended trade and colonialism to several continents, including the newly “discovered” America.

Because of the close association of a scholar with the empirical system under observation, it is no surprise that each scholar has a favorite model of capitalism. Smith highly valued the British system of the eighteenth century. Likewise, Weber favored the Western European model. Even today, scholars freely express their preferences for a particular model. Baumol, Schramm, and Litan (2007) thought a combination of the American (entrepreneurial) and European-Japan (big-firm) models was the best. Most Western scholars tend to agree. Favoritism aside, historical and theoretical discussions lead to the inevitable conclusion – capitalism is an ideal that undergoes constant modifications as variations of systems emerge and evolve. Each capitalistic society is an evolving system. As timely opportunities and constraints appear and path dynamics evolve in interactions with the world, a society changes the institutional elements or their coordination to survive and persist. Thus, there is no ideal or “typical” capitalist society.

However, this absence of an ideal society does not erase the more universal underpinnings of capitalism. Each capitalist society must exhibit the presence of capitalists who seek to produce and reproduce capital, the presence of markets for production, distribution, and consumption, the availability of wage labor, and the presence of a state that maintains, protects, and promotes the institutional arrangements, the interests of the capitalists, and the expansiveness of the system. Thus, determination of
whether a particular society is capitalist or not should be based on the extent to which that society has met the fundamental definition and essential elements or the consensual features described above. Only then is it necessary to identify its unique features and speculate on how those features may be projected into the multiple configurations of capitalism.

IS CHINA A CAPITALIST SOCIETY?
In accordance with the institutional arrangements already outlined, China is an emerging capitalist system, with characteristics that are nevertheless different from those of other capitalist societies.

CALCULATING CAPITALISTS. There are several indications that capitalists are emerging in China. The first is that the amount of wealth held by the top executives in corporations is approaching the level generally associated with capitalists in the West. The top fifty executives in China were worth 50 billion yuan (5.1 billion U.S. dollars) by the end of 2006, thanks largely to the booming stock market (Xinhua, January 2, 2007). None of the top fifty was worth less than 200 million yuan, and half of them were worth more than 500 million yuan each.

The number of large corporations is also increasing, and the capital and assets of those corporations are growing. Huawei now employs over 25,000 workers, sells technical equipment in over seventy countries, and generated revenue of 5 billion dollars in 2004. Other internationally known corporations such as Haier, a white goods company, and Baosteel, the country’s top steelmaker, are already listed among the top 500 global companies by Fortune.

By 2007 China had become the largest automobile producer in the world. Shanghai Automotive Industry Corp (SAIC) aims to be among the world's top six car companies by 2020. Chery and Geely, two semi-government automakers, are planning to export automobiles to the United States in three to five years. GM and Volkswagen are producing more cars in China than anywhere else in the world except the United States and Germany respectively, and making more money there. It is certain that much of the
present production relies on low-cost labor and low-level technology. China has a long way to go before catching up with the advanced countries in the mass of capital and dynamics of corporations. Further, in many areas, foreign or foreign-invested companies take the lead. However, this may auger well for China’s future as skill levels improve and the level of technological innovation gradually catches up.

Another clear indication of capitalism in China is the rise of the middle class, a class of individuals who have accumulated sufficient wealth to enjoy leisure and luxury. According to the National Bureau of Statistics of China (China Statistical Yearbook 2005), in 2004, 95.9 percent of urban household owned washing machines (37.3 percent of rural households), 90 percent owned refrigerators (17.8 percent of rural households), 133 percent owned color televisions (75.1 percent of rural households), 47 percent owned cameras (3.7 percent of rural households), 11 percent owned mobile phones (34.7 percent of rural households), and 2.2 percent owned automobiles. McKinsey & Co. (2006) estimated that the ranks of the lower middle class (defined as earning an annual income of 25,000-40,000 yuan) will reach 290 million in 2011, and 520 million by 2025. It also estimated that 100,000 yuan would buy a lifestyle in China equivalent to 40,000 U.S. dollars in the United States in 2005.

Yet another indicator is the structural shift of the economic sectors. Between 2001 and 2005, the state sector decreased by 48.2 percent, currently claiming fewer than 190,000 enterprises. The collective sector has likewise experienced a decrease of 46.9 percent, with less than 450,000 enterprises remaining. In contrast, stockholding companies have increased 35.2 percent, private companies 49.7 percent (now more than 2 million), foreign companies 9.6 percent (more than 150,000), and other types of companies 66.5 percent (more than 75,000). The state intends to trim state-owned corporations and concentrate on building thirty to fifty state firms into globally competitive multinationals by 2010. The top three oil companies, PetroChina, Sinopec, and CNOOC, are buying oil and oil fields and building pipelines around the world, often in competition with each other. Boasteel plans to become the third largest steelmaker in the world by 2010.
FREE MARKETS. China has established substantial free markets for production, distribution, and consumption of commodities over the past two decades. According to a recent World Bank report (Winters and Yusuf 2007), exports from China of goods and services in 2004 accounted for 5.7 percent of the world total, behind only the United States (11.2 percent) and Germany (9.1 percent). By 2006 China had become the second largest exporter in the world, next to the European Union and surpassing the United States, according to a World Trade Organization report. Between 2005 and 2020 its share of growth is expected to be 15.4 percent of the world’s total growth, surpassing all other nations including the United States at 9.9 percent. However, it should be noted that about 60 percent of China’s exports are goods produced or assembled in China by multinational companies (International Herald Tribune February 9, 2006).

Export industries have also shown significant shifting patterns in the past decade (United Nations Commodity Trade Statistics, accessed via the World Bank’s World Integrated Trade Solution software). Twenty-six percent of China’s exports in 1995 were textiles, but by 2004 textiles exports only accounted for 16 percent of the total. Iron and steel also decreased from 3.5 percent to 2.3 percent. On the other hand, electrical equipment rose from 5.9 percent to 10 percent. Vehicles accounted for 1.8 percent in 1995 and 2.8 percent in 2004. Thus, the shift has been away from labor-intensive products and raw resources to more technologically advanced products. As of 2004, exports of goods and nonfactor services accounted for close to 45 percent of GDP (World Bank, World Development Indicators database).

China’s domestic market continues to grow as well. By October 2006, its retail sales amounted to 199.8 billion yuan, a surge of 14.3 percent from the previous year. In 2004 its imports of goods and services accounted for 4.8 percent of the world total, trailing only the United States (16.5 percent) and Germany (8.2 percent). The World Bank estimates that China’s share of growth between 2005 and 2020 will be around 11.0 percent, trailing only the United States (at 15.4 percent). In
2006 alone, China received 63 billion U.S. dollars in foreign direct investment (FDI) \((Xinhua\ January\ 14,\ 2007)\). Imports of capital (in terms of foreign direct investment), firms, technical and other personnel, and energy resources have also been remarkable. Currently China ranks second only to the United States in the amount of annual FDI. In 2005, 70 percent of the top 200 enterprises in the world had made investments in China. Recently, China also did away with tax advantages for foreign firms and investments; foreign and domestic firms can now compete on an equal footing.

China became the factory of the world by the early 2000s. In the past decade it has emerged as the consumer market of the world. Joining WTO has continued to affect the openness of the Chinese market. Foreign banks have been encouraged to invest in Chinese banks. More recently, foreign banks have been allowed to register locally. It is only a matter of time before China’s financial sector and stock market will be as open as many other capitalist states in the world. Some have argued that China’s market is more open today than those in Japan and South Korea in terms of the extent of relaxation of tariffs and commodity protection. For example, the United States has recently demanded that South Korea open its market to American automobiles – a non-issue in China.

The automobile industry provides a striking example of China becoming both an import and export market. China surpassed Japan to become the world’s second-biggest vehicle market in 2006, and sales rose 25 percent to 7.22 million units. China now has more than 100 automakers. Honda, DaimlerChrysler, GM, and Ford have all invested heavily in manufacturing and assembling cars in China, to the tune of 21 billion U.S. dollars. China is Volkswagen’s largest overseas market, and has made GM’s Asia-Pacific region its most profitable. The estimation is that the passenger car market, around 5.24 million in 2007, will grow by 40 percent to 7.3 million vehicles by 2010.

An ever-increasing, though still relatively small, portion of the cars produced in China will be made by Chinese firms rather than by joint ventures. Chinese automobile companies have bought foreign car companies wholesale, including the manufacturing plants for engines and transmissions. For
example, Nanjing bought MG Rover in 2005, transplanted the plants wholesale from England, and within a year started producing MG cars in China. Chongqing Changan Aotmobile Co. also began making its internally designed model, the Benben compact, in September 2006. Chery showed off thirty new models in April 2007 and Cheely showed fourteen new models at the same time. Chery outsold Shanghai-GM in March 2007, the first Chinese firm to overtake the Detroit flagship venture in monthly sales. By 2007 China was exporting more automobile parts to the United States than most other countries, passing Germany and trailing only Japan (*Herald Tribune International* June 6, 2007). Chery reached an agreement with Chrysler in July 2007 with the aim of supplying up to 100,000 subcompacts per year to the United States within three years.

Over the past decade China’s foreign trade surplus has been on the rise. By the end of March 2007, its foreign reserves had exceeded 1.2 trillion U.S. dollars. Since July 21, 2005, China has relaxed its currency peg to the U.S. dollar, shifting the yuan from 8.20 to 7.65 per dollar. It seems that China has decided to make slow adjustments over a period of time to limit the possible effects of hot money pouring into the country with a substantially devalued currency, which could render it a semi-colonial state as it was during the foreign economic, political and military domination of the late 19th and early 20th centuries.

The equity market has also been moving ahead at a measured pace. After some rules were relaxed, the stock market shot up in 2006 to a composite value of more than 1 trillion dollars, an annual increase of 130 percent. The market continued to surge in 2007, with the Shanghai market index reaching 4,000 in May, an increase of 85 percent over 2006. As of May 2007, an estimated 968 million Chinese are participating in the stock market. By April 2007, bank savings deposits had decreased to 17.37 trillion, while the stock market value exceeded 17.43 trillion by May 17. Although corrections are expected, the long-term perspective seems positive – more Chinese are becoming rich, and their wealth will partly be recycled to produce more capital.
China is also ambitious in the world market. In 1990 China’s exports amounted to 2.5 billion U.S. dollars. By 2002 its cumulative exports had increased to 35.5 billion dollars, and by 2005 to 57.2 billion. By late 2006 Chinese exports were the third largest in the world, behind only Germany and the United States (Financial Times March 23, 2007). In fact, China will become the largest exporter in the world by 2008.

WAGE LABOR. China is currently the most populous nation in the world and enjoys an ample supply of labor. While the distribution of education across the population is uneven, the general literacy and education level are good for a developing country. The relatively low wages also afford competitive advantage to manufacturers in producing commodities in the world market. The cheap labor has so far allowed products made in China to be extremely competitive in the world market. Despite a tightening labor supply in certain industries, the massive population in the interior and rural areas will keep wages in China low in comparison with labor in North America and Europe for many decades to come.

Eventually, some argue, China’s population and cheap labor advantage will be reduced. Within the next five years, India’s population will surpass that of China; from that point on, China’s population will be aging with increasing speed. The expectation is that if current trends and policies hold, the aged population will reach 400 million by 2040, bringing with it a reduction in labor supply. However, the current trends and policies need not remain unchanged. The one-child policy is likely to be reassessed and moderated in the near future. The retirement age may also be extended and become more flexible. Thus, the only real threat to wage labor relative to other countries is rising wages and benefits.

AN EXPANSIVE SYSTEM. China recognizes the vast and expansive domestic market, and is making systematic plans to build up infrastructure to facilitate its growth. Urbanization is taking place at a brisk pace of 0.8 percent per year, and economic development has been expanding to the interior regions and cities (The Economist November 18, 2004; New York Times November 21, 2006). Along the upper reaches of the Yang-tze and Pearl rivers, cities and industries are sprouting up. Wuhan is becoming
a major industrial, commercial and financial center. Chendu-Chongqing is emerging as another gigantic commercial center. An entirely new development zone is being developed in Northeast China to match the still growing Shanghai-Jiangsu region and the Pearl River delta. Dalian in the Northeast and Qingdou in Shangdong are fast emerging as high-tech centers, following the developments in Shanghai and Beijing regions.

In 2005 China announced that it would renovate or expand twenty regional airports with an investment of 5 billion yuan. It has also started developing large cargo and passenger airplanes with of the aim of competing with Boeing and Airbus for the Chinese market in ten to fifteen years, and with an eye toward the world market.

Existing harbors are being upgraded and new harbors built. From 2005 to 2010, China will invest over 400 billion yuan to improve its ports (Bloomberg News November 2, 2005) and highways. In 2006 China had seven of the world’s twenty busiest shipping terminals. A deep-water port is being built from scratch in Hangzhou Bay, Zhejiang, 27.5 km from Shanghai. In 2007, South Korea built 41 percent of all ships delivered, but Chinese yards signed 56.6 percent of the total number of new contracts in the first quarter of 2007, with the South Koreans accounting for only 26.1 percent. The projection is that China will overtake South Korea as the largest ship builder by 2015 (China National News, May 19, 2007).

China currently has a 45,400 km of express highway (Ministry of Communications, January 2007) at both national and local levels, the second longest in the world behind only the United States. It will build another 5,000 km in 2007 to complete the 36,700 km trunk lines of its national highway network. The national network will probably reach 50,000 – 55,000 km by 2010. In 2007 it will also upgrade up to 300,000 km of rural roads. China’s railroad construction is also expanding at a frantic pace. Currently, it has a network of 76,000 km and will reach 90,000 km by 2010, the longest mileage among all nations.

These infrastructure projects will continue to fuel the growth of domestic markets and the internal
capacity for manufacturing and service industries. But China has also aggressively sought out resources and markets globally. It has started exporting cars, vans and trucks to Africa, Latin America, and Iran. China-made Hondas have now been successfully launched in Europe. Many multinational automotive companies no longer see China as a sales market only, but are making it an important manufacturing, outsourcing, exporting, and regional research base.

To supply the increasing energy needs of its population and industry, China has ventured to Africa, the Middle East, Russia, and South America for oil exploration and purchases. Uganda, Sudan, Ethiopia, Iran, Russia, Azerbaijan, and Venezuela, among others, have all signed agreements with China for joint oil explorations and/or supply.

The strategies for China’s overseas expansion are two-pronged. On the one hand, China makes investments in resource exploration, refinement, and transportation, in cooperation with local governments and firms, sharing the benefits and profits. It also demands that local markets be opened to Chinese goods and services, and promises to allow local goods to be imported to China. On the other hand, China has extended foreign aid and technical support to many countries in the third world. With its ample foreign currency and state treasury, it is helping to build hospitals, schools, roads, railways, and technical and personnel assistance in Africa, Latin America and the Middle East. Chinese firms, almost all of them state enterprises, have been given the actual construction and assistance contracts along with Chinese managers, technicians, and workers. Also following are Chinese entrepreneurs who have set up shops and trading companies in these countries. Chinese-manufactured commodities are being supplied and in many instances saturate the local markets, with their relatively inexpensive price tags and reasonable quality. China also promises to not interfere with local politics or ideologies.

China’s expansion into Africa over the past decade illustrates these strategies well. There were 450 Chinese investment projects in Africa in 2004 (Winters and Yusuf 2007). In 2005, Africa exported goods valued at 20 billion dollars to China and imported goods valued at 15 billion dollars from China.
By 2006 there were more than 700 Chinese companies in Africa. China has become the continent’s third largest trading partner, after the EU and the United States, but closing in on the United States fast. It is buying copper and cobalt from Congo and Zambia, iron ore and platinum from South Africa, timber from Gabon, Cameroon, and Congo-Brazzaville, and oil from Nigeria and Angola, Sudan, Equatorial Guinea, Gabon, and Congo-Brazzaville. A Chinese firm is engaged in coal mining prospects in Algeria, and intends to export coal to Morocco and Spain.

About 70 percent of Sudan’s exports go to China. The biggest oil refinery in Sudan was expanded in 2006 to double its capacity with an investment of $341 million from China and construction by Chinese firms. Of Sudan’s $2 billion in oil exports, half was sent to China. In 2006 a Chinese state-owned company agreed to pump more than $2 billion into a major, loss-generating refinery in northern Nigeria, Africa’s leading oil producer, in exchange for drilling rights in four sought-after oil fields.

Similar strategies and initiatives, on a relatively smaller scale, are being undertaken in Southeast Asia, Latin America, the Middle East, and Central Asia. Venezuela has promised to substantially increase oil exports to China (from the current 150,000 barrels a day to 1/2 million a day in five years, and perhaps up to 1 million barrels a day by 2012). China has also signed a free trade agreement with Chile, with special interest in its copper mines. China wants natural gas from Bolivia and agricultural products from Brazil and Argentina. It has agreed to purchase mid-range airplanes from a Brazilian company. It will build a railroad for Cuba. China is now the second largest trading partner of Peru and Brazil, the third largest of Chile, and the fourth largest of Argentina. Trade with China now falls within the top ten for Paraguay and Uruguay (Mohan Malike, *Power and Interest News Report* 2006).

China is now the biggest trading partner for the EU, Southeast Asia, and East Asia (Japan, South Korea, Taiwan). Regional alliances are also being promoted by China. The ASEAN countries plus three (China, Japan, and South Korea) are discussing the establishment of a free-trade zone, parallel to the EU. The Shanghai Cooperation Organization Conference is an example in which China, Russia, and the
Central Asian states of Kazakhstan, Kyrgyzstan, Tajikistan, and Uzbekistan have formed an alliance of mutual assistance, resource exploration, and other exchanges. India, Pakistan, Iran, and Afghanistan have recently joined as observers with the potential for membership in the near future. China is actively befriending Japan and South Korea, in particular de-emphasizing Japan’s atrocities during the Second World War.

A STRONG AND LEADING STATE. China provides a clear example of how a strong government participates in the development and growth of capitalism. In fact, the state was responsible for initiating that development. In the early phase of reform (1978-1989), the state allowed the market mechanism to emerge in rural development, and followed with policies that gradually allowed public institutions and enterprises to be diversified into pseudo-independent enterprises. Other public enterprises were allowed to be truncated into public and “private” enterprises to contain public and bank debts. Collective enterprises in rural areas were allowed to pass into private (largely local cadre) hands (see, for example, Lin 1995a; Lin and Ye 1998). Urban housing was gradually released to private ownership. Job assignments were gradually replaced by a job market. At every step, the state watched the dynamic changes and implemented policies to encourage market mechanism.

Domestically, the state has implemented rules and regulations consistent with international standards in the monitoring and regulation of economic transactions and trades, the stock market, financial and banking services, and property rights – rules largely developed by capitalist states for capitalist states. Since joining the WTO in December 2001, China has been trying to meet various deadlines for market access for goods and services. Among the key commitments to be undertaken by China are the following: (1) the provision of nondiscriminatory treatment to all WTO Members, (2) the elimination of dual pricing, (3) the removal of price controls, (4) the revision of existing domestic laws and the enactment of new legislation to comply with the WTO agreement, (5) the freedom of internal
trade three years of accession, and (6) the removal of all export subsidies on agricultural products.

China still lags significantly in meeting these commitments. However, fundamental steps have been taken. In early 2007 China allowed a number of foreign banks to register domestically without the requirement of allying with any Chinese bank. The first five such foreign applications were approved in early 2007. Foreign enterprises no longer enjoy any tax or tariff breaks, putting them on an equal footing in competing with domestic enterprises in the local markets. The stock market, still primitive by international standards, has also undergone changes. Foreigners can now purchase stocks previously reserved only for domestic parties. Significant, but still minor, shares of the public companies whose stocks are largely in the hands of public owners (the state or local governments) are now being released to the market.

UNIQUE FEATURES OF CHINESE CAPITALISM

Chinese capitalism is at an early stage of development. However, the trends over the past twenty years are clear and significant. By most of the universal criteria discussed earlier, China has the appropriate institutional arrangements to be labeled capitalist. Nevertheless, Chinese capitalism is different from other forms, with two institutions in particular making the difference.

STATE AS CAPITALIST. Given its past, it is not surprising that the state holds a commanding position in the political and economic arenas in China. As the country evolves toward capitalism, the state-economy synchronicity remains significant. Over the past decade the state has begun to separate itself from economic enterprises. The initial step was to segment state enterprises into the critical and non-critical sectors. The critical sector included industries and enterprises considered vital to the state, such as mining, defense, energy, transportation, and communication. The non-critical sector was further sorted into debt-laden and non-debt laden enterprises. Much effort was made to release debt-free
enterprises to non-state operators, and arrangements were made to reduce the obligations of debt-laden enterprises, either by reduction of work and employment or changes in management, production, and so forth to gradually reduce debt. So far, the strategies seem to be working in general; over the past four or five years the level of debt among state enterprises has been greatly reduced. By the end of 2005 the four state-controlled asset management companies had disposed of 839.75 billion yuan of nonperforming assets according to the China Banking Regulatory Commission. At that time the State-owned Assets Supervision and Administration Commission announced that it planned to complete payment on all bad debts within four years.

However, the state retains a significant presence in the manufacturing sector. As of 2004 state enterprises accounted for 36.7 percent of manufacturing enterprises (National Bureau of Statistics of China, China Statistical Yearbook 2005). These state-owned enterprises accounted for 47.8 percent of manufacturing sales revenue and 41.1 percent of employees in the sector.

The state has also invested in nominally non-state enterprises in significant industries such as automobile manufacturing. It is difficult to estimate the extent of this penetration because the control and investment in enterprises are not transparent. For example, all major banks in China are under state control, but this only became apparent to many foreign observers recently when the CEOs of three leading banks, all former state bureaucrats, were replaced with other state bureaucrats. Many known “private” brands such as Haier, Lenovo, and Chery are in fact backed by the central and/or a local government.

The state as capitalist has also directly or indirectly tried to invest in foreign companies. Lenovo is one example, with its large state share ownership and its purchase of IBM’s PC division. In 2005 CNOOC, a state-owned petroleum company, made an offer of 18.5 billion U.S. dollars to purchase Unocal, but the deal was blocked by the U.S. government. More recently, the Chinese government has moved into the global equity market. With its foreign exchange surplus exceeding 1 trillion U.S. dollars
and growing by about 20 billion dollars per month, the Chinese government established the State Foreign Exchange Investment Company in 2007, through which it purchased $3 billion worth of non-voting shares (or about 9 percent of total shares) of Blackstone, one of the largest private equity firms in the United States.

The state’s capitalistic nature cannot be appreciated by simply examining the behavior of the state-owned companies. Many more enterprises “lean” on state or collective institutions, meaning that although they have been “officially” separated from public institutions they are largely filled with former state employees and retain close relationships with their originating work unit, in terms of personnel, resources, capital, and networks of supply and distribution.

Further complicating the relationship between the state and the economy is the participation of the Party. It is extremely difficult to separate the Party from the state; the presence of one inevitably indicates the presence of the other. The presence of the state in an enterprise also indicates the presence of the Party apparatus in the enterprise. Most private firms of reasonable size incorporate the Party apparatus through the presence of a Party secretary and an office. More recently, the Party has used official unions as surrogates in foreign firms and joint ventures, most notably in Wal-Mart, which has resisted the presence of unions elsewhere in the world.

It should be noted that the state’s strong presence in China is not unique. In all capitalist societies, the state cooperates and coordinates with firms and capitalists. In many capitalist societies the state also operates enterprises considered critical or essential for national survival, and industrial sectors bearing on the development of military weapons, transportation and communication, energy exploration and development are either directly under the state’s jurisdiction or under close supervision and command of the state. As such, they are much less likely to be subject to market rules. However, seldom have we seen a state itself acting as a capitalist entity competing in the domestic and international markets, as we are witnessing in China.
What are the implications of this feature? On the positive side, it allows the fast accumulation of capital at the macro-level. The state has direct access to surplus value as long as its enterprises make profits. The surplus value further affords quick reinvestment in the production cycle. The direct participation of the state also reduces the opportunities for the enterprises to avoid taxes. In fact, tax revenue increased by 20 percent between 2004 and 2005, and by another 21.9 percent between 2005 and 2006. This “surplus” capital allows the state to make heavy investments in target areas that are vital for further development – infrastructure, education, communication, and the development of vital sectors such as high tech industries and the military industry.

More recently, the state has begun to address issues of inequality. In its current five-year plan, launched in 2006, more emphasis has been given to rural and regional development, the development of the service sector, and an energy-saving, environmentally friendly, and socially harmonious society focused on the quality of life, health, and public safety.

On the negative side, however, is the lack of checks and balances. The state presumably regulates and monitors the operations of the economy and the capitalists. Now it is both a referee and the player in the game. Despite efforts to discharge the responsibility of being the regulator by sending investigative teams to trouble spots and organizations, and initiating major investigations into the corruption at high levels of the government and state-owned businesses, the state finds itself in an awkward position – encouraging and tolerating regional and local government participation in capitalism and monitoring and regulating their activities. The state simply does not have the resources to conduct such independent work. This will remain a serious problem in the near future.

Another consequence of the joining of the Party, the state, and the economy is that nepotism often gets in the way of proper supervision and regulation. As of 2006, most of the top capitalists in China are children of high-level cadres. According to one unconfirmed report (Chinesenewsnet.com, September 3, 2006), citing a report on social and economic conditions produced by researchers at the State Council, the
Central Party School and the Chinese Academy of Social Sciences, 2,932 of the 3,200 richest persons were children of those cadres, and among the top executives, between 85 and 90 percent were children of the cadres. They held key positions in finance, foreign trade, land development, large construction projects, and the stock market.

Yet despite these problems, the population is by and large supportive of the present system. No doubt strong Party and state control account in part for the lack of resistance. Other factors may also explain why the public is willing to tolerate this odd linkage. For one, the state keeps reminding the population that it is all for the national interest and national development. The public is often reminded that China still faces severe international challenges, particularly from the United States, which is seen as the superpower that dominates, sometimes with force, in the global arena. The Chinese people are frequently reminded that Taiwan is an inalienable part of China and that the United States is the principal factor maintaining the continued separation of Taiwan from the mainland. Bilateral security treaties that the United States has established with Japan, Australia, and South Korea, and the intrinsic American sympathy for India, the largest democratic nation in the world, make China feel surrounded by the United States and its real and potential allies. The population is indoctrinated with patriotism and loyalty to the state. It is convinced that only a strong and united China can defend its own interests and ensure its ultimate survival.

The overall economic growth and its benefits to a majority of the population also contribute to this loyalty. Hunger and disease no longer threaten the great majority of the population. Rather, getting rich has become the focus. Ten years ago, laid-off workers from state firms seemed to be creating a potentially explosive threat to the stability of the country, but the rapid and continued economic growth and the emergence of many small firms has substantially increased permanent and temporary employment. It is impossible to find precise information about unemployment rates in China. Most official reports stated that by 2007 the urban unemployment rate was between 6 and 4 percent. Some
(e.g., Rand) estimated that the actual rate for the total labor force was about 23 percent (taking into account rural as well as urban rates and including “disguised” unemployment—those reported as employed but without income). So far, the economic opportunities seem to have contained possible discontent from the unemployed or underemployed. Ideologically and materially, the population has been convinced that strong state participation in the economy benefits the nation and its people.

SOCIAL RELATIONS (GUANXI). Guanxi is a reciprocal relationship that mixes utility and sentiment. For critical observers, it represents a transaction cost that reduces the efficiency of market exchanges. Guanxi, practiced universally in varying degrees, may induce corruption and fraud, and, to some scholars, need to be replaced by market and free trade practices. However, evidence has shown that in fact guanxi is used among Chinese even when the markets are quite open and competitive (Lin, 1989; Bian, 1994; Bian, 1995; Lai, 1995; Lin, 1995a; Bian, 1997; Bian, 2000; Lin, 2001; Lin, 2003; Bian et al., 2005). In Hong Kong, Singapore, Taiwan, and other communities where ethnic Chinese participate in local and global market competition, guanxi is often seen as offering a competitive advantage (King, 1985; 1982/1988; Hwang, 1987; Bian & Ang, 1997). Guanxi is a useful lubricant for buffering hard times and sharing profits. More importantly, social relations are the foundation for social capital—resources embedded in social networks that can be accessed and mobilized for instrumental or expressive returns (Lin, 2001b).

During the Asian financial crisis in the late 1990s and early 2000s, much of Southeast Asia and Northeast Asia suffered heavily and has only recently recovered. Yet Hong Kong, Singapore, and Taiwan were relatively less affected. One argument for this difference was that in these ethnic Chinese communities, corporate relationships were not abandoned. Instead, the cost of reduced work was shared by all and lay-offs were minimized. These overseas communities also benefited from their continued participation in the markets in China, which were relatively immune from the crisis because it managed its currency and financial institutions almost independently from the rest of the region. As China
continued to grow in its domestic and international trade, these communities participated and benefited from that growth. During the crisis many ethnic Chinese firms and entrepreneurs in much of the affected areas shifted their capital and investment to China through their ties.

This practice applies not only to individual capitalists, but also to the state itself. China is establishing economic transactions with other states around the globe, but at every step it wishes to maintain and promote friendly relationships and shared benefits. Thus China gives out aid when and wherever it is necessary. It expects reciprocity of relations and sentiment and sees such *guanxi* and economic cooperation as going hand-in-hand.

**IMPLICATIONS FOR THEORY**

What does a study of Chinese capitalism contribute to the theoretical analysis of capitalism in general? As discussed previously, two institutions that feature in Chinese capitalism deserve more attention: the state as capitalist and the utility of social relations.

**THE STATE MANAGING CAPITALISM**

The foregoing overview of Chinese capitalism suggests that the role of the state deserves greater attention in the analysis of capitalism. While many scholars have pointed to the role of the state in discussing economic development and capitalism, its centrality in the development and maintenance of capitalism deserves stronger emphasis in theoretical discussions. The dominant theories of capitalism have thus far either dismissed or deemphasized the role of the state. Yet capitalism depends on a strong state for its preservation and development. The British Empire enjoyed such a strong state, as does the United States. China is now enjoying it. But why did capitalism fail before in China?

**WHY CAPITALISM FAILED BEFORE IN CHINA.** It can be argued that various elements of the current institutional arrangements have been in place before in China. Chinese merchants throughout
history understood the need to reinvest surplus value in production to accumulate capital (Redding 1990; Arrighi 1996). What was missing was state legitimization of this ideology. Since the Han Dynasty, when the state established a national examination system and instituted Confucian ethics as the principal way of selecting and rewarding bureaucrats at all levels, society was stratified according to a moralistic ideology that downgraded profit making and placed merchants near the bottom of the social hierarchy. Even merchants were indoctrinated into this ideology, trading their wealth for bureaucratic positions and literate status and encouraging their sons to focus on training for examinations. Instead of business and commerce, capital was thus largely invested and re-invested in land ownership, but land accumulation was constrained by the rules of succession, which dictated the division of property among sons (Lin 1989; Hsu 2007).

Another major consequence of the state-commerce split in spirit and practice was the restraint placed on economic expansion. The state identified a geographic boundary for the center of the civilized world, beyond which the Chinese were not encouraged to go. Dynasties consistently constrained and even forbade economic expansion beyond its borders, and merchants were punished for venturing outside the boundaries (Wong 1997). Arrighi called this the “introverted” system of capitalism (2005). Faure (2006) showed that during the Ming and Qing dynasties (1368-1644, and 1644-1911) Chinese merchants had to rely on informal and private contracts to sustain trade and mobilize resources. Without the state’s participation and support, such informal institutions could not resist the onslaught of Western capitalists in the eighteenth and nineteenth centuries.

The centrifugal and contradictory ideology of the state and society has been sustained even into the twentieth century. Following Hong Kong and Singapore, both of which had developed state capitalism under British rule, and Taiwan which followed suit when the KMT abandoned the idea of “recovering” the mainland and began focusing on economic development and allowing capitalists to develop through special economic and technological zones, China finally decided to focus on
“modernization.” In the early 1980s, Deng Xiaoping proclaimed that “it does not matter whether it is a white cat or black cat as long it catches the mice,” and followed through with his southern inspections in 1992 that legitimated capitalistic developments in the special economic zones in the wake of the disastrous Tiananmen Incident that had deterred economic growth.

A second, and equally important, ramification of the state managing capitalism in China is that it acts as a capitalist itself. It is true that in capitalist countries most states are capitalists to varying degrees in that they manage or own certain corporations. State ownership of these corporations and enterprises is largely based on the premise that they hold vital resources for the survival of the state. As such, their operations tend to retreat from market competition. The Chinese state, in contrast, has shown a tendency to operate enterprises in the competitive market. Chinese state-capitalistic corporations show no sign of retreating from the market and every sign of aggressive competition. Chinese banks, largely owned by the state or local governments, are operating as typically private enterprises, listing in stock markets, entering into joint ventures with foreign banks, and entering into foreign markets. Ministries and local governments continue to incorporate local and private enterprises under their wings. This blurring of the demarcation between the public and the private and between the government and enterprises is at least a significant deviation from practices in other capitalist countries.

SOCIAL RELATIONS EMBEDDING CAPITALISM

The other interesting institution highlighted in the study of Chinese capitalism is guanxi, or social relations. Conventional wisdom, with exception of the recently developing behavioral economics, in the analysis of capitalism separates economic and social relations. Polanyi (1944) believed that capitalism was a historical anomaly because unlike previous economic arrangements, capitalism social relations were defined by economic relations (see Heilbroner 1985 for elaboration). Polanyi further thought that in the great transformation of human history, rules of reciprocity, redistribution, and
communal obligations were far more frequent than market relations. He did not contemplate the possibility that capitalism and social relations could be complementary rather than antagonistic, and his view was formed before the economic rise of East Asia. Much of East Asia, including China, has always valued social relations. Within the constraints and opportunities offered by the protection of the state and the operation of a free market, they consolidate reciprocity and mutual benefit with relational rules (Redding 1990) to accrue and reproduce capital. The cost of suboptimal profit in these socially based transactions is well compensated for by the benefit of long-term payoffs and the rewards of reputation and social standing (see Lin 2001a, chapter 9).

Even in other countries, social relations have not been replaced by capitalism, as Polanyi pessimistically forecasted. Indeed, with the advent of the Internet and other cyber-technologies, social relations and social networks are at the forefront of capitalistic development. Cybernetworks (Lin 2001a, chapter 12), or social relations and social networks in cyberspace, have become the foundation of entrepreneurship. AOL was probably the pioneering enterprise in this regard (Swisher 1999), when Steve Case focused on the development of online forums and beat out the more economically oriented competitors. Google established a network-based ranking system, again initially without regard to economics. MySpace and FaceBook carried it a giant step forward. Economic payoffs followed. Second Life, the online game in which real firms establish virtual presences to do real business, is another example. Thus, in this most modern and technologically innovative social system, cybernetworks are the primary goal of development and economic relations follow. Wikipedia is a shining example of collective and networking production, without regard, so far, for economic returns.

A major contribution of neo-economic sociology, as Granovetter (1985) pointed out, is that economic activities are all embedded in social relations. However, the centrality of guanxi in certain societies and the fact that social relations and networks precede economics in cybernetworks all point to a different theoretical proposition: that social relations serve as the foundation for economic activities.
Zelizer (2005) challenged the assumption that markets undercut solidarity-sustaining personal relations and described these “circuits of commerce” where intimate and interpersonal relations control and sustain transactions for communal benefits. In this view, guanxi represents generalized circuits of commerce as it transcends geographical and temporal boundaries. Guanxi can and must be maintained across time and space to allow its utilization as transactions demand.

This articulation about the importance of social relations does not deny the possibility of economic transactions with actors outside the circle. Actors within the circle continue to search for and establish relations with actors outside to seek and expand profits. However, the expectation is that such economic activities will be followed by the development of guanxi to maintain and expand future transactions. External partners are expected to become part of the guanxi network if transactions are to be maintained and expanded. Only when such relational commitment has been made will economic activity be continued. It is only with guanxi that economic activities afford the sharing of profits in good times and sharing of losses in bad times. Abandoning partners in times of crisis is seen as shameful and damaging to one’s reputation. Once one’s reputation is damaged, others treat future transactions with guarded suspicion and lower priority and choices. In this sense, guanxi adds value to economic transactions. The Economist, in describing how Western banks play the game of courting in seeking recognition and profit in China, quoted a seasoned British banker in Hong Kong, “in this part of the world relationship is everything” (The Economist, “The Art of Courtship,” May 19, 2007).

GLOBALIZATION FOR WHOM?

The world economic order is clearly going through a major transformation. According to The Economist (January 21, 2006), the thirty-two emerging economies are producing more than half of the world’s output measured in purchasing power parity terms, and they also account for more than half of the increase in the global GDP in current-dollar terms. All of these countries grew in both 2004 and 2005,
while in the previous three decades at least one of them suffered recession in a particular year. It took fifty years during the industrial revolution for Britain and the United States to double their real incomes per head; China has achieved that in a single decade. While this comparison must be contingent on market and technological constraints in different historical periods, China is quickly establishing itself as a major player in the global context, as the largest trading partner of the European Union, Southeast Asian countries, Japan, and South Korea.

There are two competing theories about what the new world order will be like. One theory espouses that any new economic power will simply increase global economic growth and bring global benefits. The other theory, much more prevailing among politicians and media in the West and gaining converts among scholars as well, is that China constitutes an economic, political, and technological threat to the existing world order and to the leadership of the United States. There is some evidence that the rise of a new economic power also increases global economic growth. A new economic power does not necessarily imply the demise of an older economic power. During the twentieth century, for example, Europe did not really suffer as a consequence of the emergence of American capitalism. Without World War One and World War Two, Europe would have enjoyed continued economic growth. In fact, after each of the two wars Europe recovered quickly, although with help from the United States, and assumed its growth. Thus, the assumption is that the emergence of Chinese capitalism, perhaps along with other developing economic powers such as India, Russia, and Brazil, will increase the economic pie and each may gain a share. This does not negate the fact that some of the current leading economic powers (e.g., United States, Britain, and the EU) may make room for China and others and even eventually cede their leadership. Nevertheless, there is no reason for them to suffer economically.

One variation of this theory even argues that the rich countries do not have to cede their leading positions. By upgrading their technologies and promoting innovations, these countries may cede the labor-intensive and low-skilled work to the emerging economic powers but will retain their comparative
competitiveness by moving on to manufacturing and producing high-value and high-skill work – the Ricardian school of thought. Further, the rise of new economic powers will have increased the labor pool, the talent pool, the sharing of resources, and the consumer demands. Presently rich economies could share these pools.

Others, especially those in developing countries, see China’s rise as a good counterbalance to the United States and the European Union, which are seen as imposing Western ideologies and other demands not necessarily consistent with local religions, cultures, and economic needs. In their eyes, China provides an alternative partner in development and, at a minimum, serves as a bargaining chip for soliciting and obtaining aid from other countries.

Yet the emergence of Chinese capitalism has created deep conceptual turmoil. Many theoreticians are confronted with the need to reassess and even revise their views about how the world evolves and will evolve. As most of these theories and theorists have used certain types of models and ideologies, the need for reassessment and reinvention will be uncomfortable at best and downright painful for others. What makes this phenomenon the more discomforting for most observers is the fact that China remains a socialist state after the world has proclaimed the triumph of Western liberal democracy following the collapse of the Soviet Union and most other forms of state socialism in the early 1990s, and has congratulated the United States not only for its supremacy as a world economic power but more importantly as the unchallenged world leader in ideology.

The Ricardian theory of comparative advantage is under challenge, at least from proponents of outsourcing (see Samuelson 2004 and rebuttals by Bhagwati, Panagariy and Srinivasan 2004 and Amiti and Wei 2004). The underlying challenge from China and other emerging economic powers will be that they have no intention to simply carve out economic niches by making only labor-intensive and low-technological products. Both China and India now produce more engineers and high-tech scientists, and they are working on the forefront of science and technology. Increasingly Chinese and Indian
scientists and engineers are obtaining patents in the United States and elsewhere, and claim their share of publications in the top scientific and engineering journals around the world. In 2004 China ranked fifth in the world with 57,400 theses listed in the science citation index (SCI). Microsoft has established twenty (soon to be twenty-two) innovation centers (it has about 110 around the world) in cooperation with local universities and companies in China, where it has the most comprehensive research and development system outside of its headquarters in Seattle, with 1,200 engineers (China Daily April 21, 2007). On his visit to China in April 2007, Bill Gates proclaimed that the growth of the country’s software industry would stun the world. Zhang Yaqin, vice-president of Microsoft in charge of development activities in China, said that “a trend that is taking place is a shift from ‘made-in-China’ to ‘innovated-in-China,’” as the country builds up its innovation efforts.

Similar to the United States, China can count on its enormous domestic market to buffer any possible international trade disputes and problems. Currently, three-fourths of Chinese exports are assembled goods with components shipped in from abroad. Yet domestic consumption accounts for an ever-increasing portion of produced goods and commodities. Foreign investments and firms inevitably bring advanced technologies to China, so that reliance on imported components will be eased.

Instead of seeing China’s emergence as higher water that will carry all vessels, it is seen as a real threat to the Western economies and what they represent politically and ideologically. This superpower mentality and fear account for some of the currently arranged security pacts the United States has signed with Japan, South Korea, Australia, and many of the Southeast Asian countries and its stance on Taiwan. Johnson (2006), quoting official source, stated that the United States maintains 737 military bases around the world in 2005. It sees itself as the guardian of the free market and democracy that cannot be challenged. The terrorist attacks on New York and Washington on September 11, 2001 made this matter event more urgent. While the United States has had its hands full dealing with terrorists in the Middle
East and elsewhere, China, with its communist ideology, growing military prowess, and ever-expanding reach, is viewed as challenging the supremacy of the United States as a world leader. The fact that China often signs cooperative agreements with authoritarian states in Africa and Latin America, while the United States and the European Union has shied away from such aid or provides aid with many constraints and conditions is troubling to many in the West. Also, doubt has been cast as to whether the United States can upgrade its technologies and innovations to remain relatively competitive as China occupies the labor-intensive sectors (*Business Week* May 30, 2005). With China becoming more innovative and upgrading its technology, the United States is also worried about the significant trade and exchange imbalance and losing professional and technical jobs. The fact that China is building aircraft carriers is also seen as a threat to the United States’ supreme position in the Pacific, Northeast Asia, and Southeast Asia, and to the situation in the Taiwan Strait.

To a great extent, this perceived threat is exaggerated. From certain perspectives, China is far from a world power. Many indexes still place China comparable to England and United States in the late nineteenth century or early twentieth century (even in purchasing power parity terms). As *Time Magazine* (January 22, 2007) correctly pointed out, China is still a poor country (GDP per head in 2005 was 1,700 U.S. dollars, compared with 42,000 U.S. dollars in the United States) whose leaders face so many problems that it is reasonable to wonder how they ever sleep. The country's urban labor market recently exceeded by 20 percent the number of new jobs created. Its pension system is nonexistent. China is an environmental dystopia, with the air of is cities foul beyond imagination, and its clean water scarce. Corruption is endemic and growing. Protests and riots by rural workers are measured in the tens of thousands each year. The most immediate priority for China's leadership is less how to project itself internationally than how to maintain stability in a society that is going through the kinds of social and economic changes that have led to chaos and violence in the past.

At the same time, there is little evidence that developed economies have suffered as China’s
economy has grown. On the contrary, the United States and the European Union countries have continued to thrive economically. Despite recent housing slumps and concerns over energy costs, the United States continues to show economic growth, a relatively low unemployment rate, and low inflation rate (Reuters June 8, 2007). However, the newly gained benefit is largely unshared by workers (wages have not increased meaningfully in the United States for the past two decades). A recent report by the Congressional Research Service showed that CEOs make, on average, 179 times as much as rank-and-file workers. Seeking and maintaining skilled workers either through better education systems or immigration policies remains largely unresolved. Weakness in the manufacturing sector, unless corrected, will eventually harm economic growth. Most of these issues may not be corrected even with improved trade relations and demands with China and other developing economies. Interestingly, these problems may suggest the necessity of a stronger role for the state, not a weaker role (The Economist January 21, 2006). The question of how to encourage more saving, to reequip the labor force for the new economy, and to develop new industries and services demands national policies and plans for existing and potential economic powers alike.

FROM COMMAND CAPITALISM TO PLANNED CAPITALISM?

In a farsighted statement in 1984, Deng Xiao-ping laid down the conceptual and practical grounds for defending the reform that was unfolding at the time while insisting that China was still following the socialist path. He stated that in the advanced stage of socialism – communism – the principle of “from each according to his ability and to each according to his needs” would be applied. However, at the primary stage of socialism, Marxism as defined by Deng, the focus should be on the development of productive forces and the creation of an “overwhelming” abundance of material wealth. This two-stage formulation simultaneously defended the introduction of capitalist elements and remaining in the process of an evolving socialism. It fended off possible ideological reactions and even revolt from conservative
elements and pragmatically allowed the reform process to continue. It was a brilliant conceptual innovation.

During this primary stage, capitalist features were not only possible but perhaps necessary. At the time Deng envisioned it would take twenty to thirty years to attain a GDP per capita of 800 U.S. dollars and raise total GDP to one billion U.S. dollars. During this period, Deng also wanted to eliminate poverty and enrich 90 percent of the population instead of 10 percent. Zhao Ziyang, Jiang Zemin, and Hu Jintao, subsequent party general secretaries, have all reaffirmed these goals. But how long will China need to move to the advanced stage of socialism?

By all measures, the goals Deng set for the primary stage were attained by the late 1990s and early 2000s, except for one – equal distribution of wealth throughout the population. Should China take the next step to the advanced stage of socialism? Before his retirement as the party general secretary in 2002, Jiang Zemin proposed that China needed another twenty years to accomplish the goals set out by Deng. But in February 2007 Premier Wen Jia-bao emphasized that China would remain at the primary stage of socialism for generations, perhaps for 100 years. The goals for socialism were not only to unleash productive forces, but also to create social fairness and justice in a “prosperous, strong, democratic, civilized and harmonious modern socialist society.” Thus, Deng’s economic goals, the releasing of productive forces and the creation of wealth, have been now supplemented by the social and political goals of fairness and justice, and even democracy. The long-term vision is reinforced and goals are expanded.

If the current state of affairs lasts one hundred years, then the issue of identifying the mechanisms that will or will not bring the primary stage of socialism to the advanced stage of socialism will lose its urgency. But as an academic exercise, we should be curious about alternative courses for China that may extend from the current trends into the next decade or two. Two such trends can be identified: (1) ongoing and growing capitalistic development, and (2) the evolving nature of that capitalism – from
command capitalism to planned capitalism.

CAPITALIST TRENDS
Some recent developments have far-reaching implications for the growth of capitalism in China. The number of capitalists is increasing, as is their capital, and they have been welcomed into the Party. Likewise, the private sector is continuing to grow. Markets are also growing with strong state support. A new labor contract law was also approved for implementation in January 2008, requiring employers to provide written contracts for all employees. Part-time contracts can be renewed once and then those employees must become regular employees. At almost the same time, the state advised local (provincial) governments to implement minimum wage guidelines. These were seen as a major advance in protecting laborers in the increasingly free labor market. The financial market is also expanding. The stock market is growing in terms of capital, number of investors, and participation of Chinese corporations. Almost all of the giant corporations, including the three big banks, the petroleum companies, steel and other industrial corporations, have either listed or are on the verge of declaring IPOs. These companies are investing and reinvesting capital and intend to be global players. The projection is that China will host the most IPOs in 2007, with capital raised exceeding $52 billion, easily surpassing Hong Kong, London, and New York (Financial Times, July 4, 2007). Foreign banks are allowed to take minority, usually non-voting, shares in banks. They are also allowed to take majority shares or even ownership in some regional and local banks. Foreign banks and financial institutions are also gradually being permitted to issue credit cards and loans (including mortgages), either in conjunction with Chinese institutions or on their own in some localities.

To put the private and public sectors and domestic and foreign firms on equal footing, tax laws are also being revised and improved. The export tax waiver for Chinese firms has been lifted. Real estate will attract taxes, first for all corporate buildings and then apartment buildings. The tax advantage for foreign
firms will be eliminated on January 2008, raising the corporate tax rate from 15 percent to 25 percent.

A far-reaching new property law was accepted by the National People’s Congress and enacted into law in 2007. It gives protection to private as well as public (state and collective) properties and against unreasonable land seizures especially in rural areas, which are a major source of unrest and protest. The law stipulates that the state continues to own all mines, rivers and seabords, urban land, forests, mountain ranges, grasslands, uncultivated land and beaches, legally designated wild animals and plants, wireless wave channels, legally designated artifacts, defense resources, and infrastructures such as power, communication, and oil pipelines. Also, the collectives (local governments) continue to own legally designated land, forestry, mountain ranges, grasslands, uncultivated land, beaches, constructions, production equipment, irrigated lands and irrigation, infrastructure such as education, science, culture, health, and sports facilities, and other designated properties. Agricultural land is collectively owned and can be contracted to farmers for up to thirty years. Non-agricultural land used for buildings can be owned and used for profit by individuals. Land for housing can be owned and used by individuals for up to seventy years. Private individuals can own legally designated incomes, housing, daily life necessities, production tools, and raw materials, as well as savings, investment, and its profits. All property owners – the state, the collectives, and individual or private entities – enjoy equal protection under the law. This is a significant step toward permitting and protecting the private ownership of property.

Social reforms are also making progress. For example, recently the state, through its Patriotic Catholic Church, responded rather positively to the pope’s desire for a better relationship between it and underground churches. Civil society has received a surprising boost from the mushrooming of housing owners’ associations in cities around the country. As private ownership of housing grows, these associations allow apartment owners in residential buildings to form collectives that protect their property rights, negotiate for service contracts, and engage in dialogue with local government units. It is not farfetched to speculate that they may also exercise some power in local elections as blocks of voters in
the future.

Transparency in governance has also gained ground. Cadres are now subject to closer supervision, training, and evaluation. Major cadre training schools have been established around the country where cadres receive more up-to-date management training. As of 2006, all major administrators (from bureau and county-level up) in state and Party offices must include all sources of income in their individual annual reports.

Political reforms are evolving slowly but surely, with remarkably open debates on certain issues. Over the past two years, a group of cadre-scholars at the Central Party School has been engaged in the formulation of political reforms. A draft statement supported the authority of the Party but raised issues on allowing religious freedom for Party members, reducing bureaucratic levels and the number of bureaucrats, developing more NGOs, and electing members to the national legislature. In October 2006, Yu Keping, former deputy director of the Central Translation Bureau and supposedly a protégé of Hu, wrote an article entitled “Democracy is a good thing.” He argued that while there were limitations to democracy and a price to be paid, under democracy officials should be elected and authority is constrained by the people. It was published in Beijing Daily on December 29 and widely reprinted, drawing severe criticism and counterattacks from doctrinal politicians and scholars. In a February 2007 interview with the Southern Metropolis Daily in Guangzhou, Zhou Ruijin, a retired editor of the People’s Daily, urged a faster democratic reform to overcome the serious social and economic problems of wealth inequality, waste of natural resources, deteriorating environments, a weakened social welfare net, and rampant corruption. He advocated expanded local elections and improved civil society. Xie Tao, a retired vice president of Renmin University, praised Sweden’s Social Democratic Party as a model for China’s Communist Party in a piece published in the liberal-leaning journal Yanhuang Chunqiu. Further debates ensued in the People’s Daily; rebuttal came in a statement on May 10, stating that “the democratic socialism is not suitable to China’s situation” and that democratic socialism was not authentic
Marxism. Subsequently, the paper published a statement on June 4 from Nie Yunling, a professor and authority on Western communism, who warned that China should not uniformly follow the changes and transformation in communist parties in Western democratic societies. Kao Fang, a senior professor from Renmin University, published a piece in Southern Weekend on the long history of changes in democratic socialism and scientific socialism in the West, and concluded that communism and social democracies shared origins, ideology, and politics. Others have joined in the discussion and debates. Cai Kuo, a political science professor from Nankai University, suggested that there were aspects of social democracy that China could learn from.

These debates could not possibly have taken place over such a protracted period and such a wide range of institutions and media without tacit permission and even encouragement from the senior political leadership. The debates reached a climax on June 25, 2007, when in his speech at the Central Party School Hu took a stand on the issue of political reforms. As expected, he took the middle ground. Declaring that he would follow the socialist path, he stated “four insistences”: liberating thoughts, reform, open and scientific development, and social harmony. He also suggested that political institutional reform would follow the principle of elevating and adjusting to people’s desire to participate in politics. This stand keeps the socialists at bay and yet leaves open discussion on political reform. The “elevation and adjustment” statement is the most intriguing. On the one hand, it keeps the Party in the leading role of elevating political participation among the populace. At the same time, it reminds Party cadres and thinkers to pay attention to what the people desire and adjust their positions accordingly. This stand will certainly be featured in the forthcoming congress of the Party scheduled for the latter part of 2007.

CAPITALISM WITH CHINESE CHARACTERISTICS

These trends and clues guide us in considering and evaluating alternative courses that China may undertake in the next decade or two and to assess their viability. One course is the process of moving
toward the advanced stage of socialism. While it is not clear what mechanisms will be required to facilitate this movement, we may assume that the fundamental requirement for the advanced stage of socialism is the public ownership of capital. Once capital is built up during the primary stage, then ownership of capital will revert to the public. The state is holding firm on certain economic sectors, either through outright ownership or owning the majority of the shares. But the larger trends have been the shrinking of the state sector and the expansion of the non-state sector. There is little evidence that any initiatives have been taken toward implementing the advanced stage of socialism in the next two decades.

Another course would be to segment the socialist and capitalist portions of society. One portion of society that can take advantage of capitalist development would be allowed to produce and reproduce capital on its own, while the state would focus on the remaining portion to ensure that social and economic justice and equality would be maintained. Essentially, this would be social capitalism, as exemplified in Scandinavian countries. Current trends cannot reject this alternative outright, but it would require significant evacuation of the state and the Party from much of society. The likelihood of this course for the next two decades is remote.

We can also rule out several other alternative courses. State capitalism typically implies that the state is the sole capitalist, which is no longer the case in China. Authoritarian capitalism conventionally refers to a dictatorial governmental rule over all economic development, such as in Nazi Germany. This does not fit the current trend in China. Instead, China is in the process of moving from command capitalism toward planned capitalism. In command capitalism, the central government dictates and guides industrial and economic practices. In planned capitalism, government, labor, and industry jointly plan long-range initiatives (Monsen & Walters 1983). In China, interactions among and joint efforts of the government, industry, and society seem to be emerging. Evans (Evans, 1995) uses the term, embedded autonomy, to describe an assertive developmental state which also networks with society. China showcases the nuance of such networking beyond corporate and individual entities and drives
home how planning and control dictate such networking.

The state and Party in China have always exercised their authority with adjustment and control (tiao-kung). Tiao-kung manages economic growth and social stability so that it will not overheat or subvert their authority, or reduce social stability and harmony. In other words, the state and the Party not only monitor and regulate developments, but they guide developments at a pace that maintains social and economic stability and justice. For example, while the state continues its general retreat from all economic sectors, it will continue to control sectors deemed critical, such as major energy resources; defense and security, and important research and development. It also intends to develop thirty to fifty major state-owned firms to compete in the world market. In the new labor contract law, a provision designates unions as the collective bargaining unit for negotiating salary and benefits for employees, yet all unions report to the All China Federation of Trade Unions, an organization with deep ties to the Party and the state. A certain degree of control is thus assured.

More importantly, adjustments and control allow the state to continue to invest and implement macro-projects to facilitate economic growth, social development, and societal safety and security. China has plans to build vital infrastructure such as highways, railways, airports, harbors, and communication lines. Rural and regional development is also receiving higher priority than before. Education received a larger budget in 2007, exceeding 3 percent of GDP, an annual growth rate of 8 percent. Financial assistance for colleges and vocational school students increased from 1.8 billion yuan in 2006 to 9.5 billion yuan in 2007, and over 20 billion yuan in 2008. Tuition and fees are waived for up to six years of education for all students in rural schools. Tuition is waived for all teacher training in the six national normal universities. There are more than ninety normal colleges and universities at the local and regional levels that are yet to benefit from this new policy.

Ambitious plans are being made to cover medical care in more than 80 percent of the rural counties. In 2007 the state invested more than 10 billion yuan to subsidize this plan. Plans are also
being made for aged care. This may entail a social security system based on individual accounts, along with contributions from firms and the government.

In response to the increasing emission of greenhouse gases, the state is launching a major environmental initiative in 2007 that will eventually close a massive section of old heavy industry (e.g., iron foundries and steel mills), ban the wasteful use of land, including the building of golf courses and free-standing homes, and implement energy-saving projects in various industries. It will also increase imports of energy, raw materials, and advanced technologies and build up the service sector.

Local governments are encouraged to take the initiative in economic and social development, but at the same time certain privileges and forms of authority have reverted back to the state. The new property laws set guidelines and limits on whether and how land, especially agricultural land, can be appropriated from peasants and properly compensated. Local governments have also been served notice that evaluations of their performances will now encompass social development and environmental protection. The state and the Party also maintain strict control over the appointment and removal of regional and provincial leaders.

Adjustment and control at the more macro-level are exercised through five-year plans that set the course of focus and development. A constant feature of the Chinese regime, five-year plans were originally adopted from the practice of the Soviet Union. For a while the planning aspect was de-emphasized, and in 1993 the term “planned economy” was deleted from China's Constitution, but it has come back in full force during the Hu-Wen era. It is an instrument with both policy and development directives. This middle-range strategy allows periodical investigation of the needs and demands of the people and society, and micro- and meso-level responses and adjustments in strategies and tactics in the formulation of policies and their implementation (Hsu 2007). The interaction and feedback between the state and society are effected in the planning process. The process also sometimes allows a gradual shift of macro-strategies and goals.
Such may be the case of the current five-year plan, which claims several firsts. It is the first time specific indicators and targets have been identified, and the first time that social development, rather than economic development, has assumed priority in the number of indicators and targets (fifteen versus seven). Employment, social security, poverty reduction, education, medical care, environmental protection, and safety are given priority. Chapters are devoted to rural development, development of the service sector, resource conservation, the development of science and human resources, institutional reforms (including finance, taxation and markets), further openness and foreign-trade and capital expansion, and the promotion of a harmonious society. Among the economic institutional indicators are the value added percentage of the service sector, the employment percentage in the service sector, research and development as a percentage of GDP, and the urbanization rate. It is clear that planning is taken seriously and that priority is currently given to social justice and welfare. Both the public and private sectors are to be mobilized to achieve these goals.

The focus of the current five-year plan is on the “construction of a Xiaokang society,” with the term Xiaokang ("moderate prosperity" or "well-off society") having historical significance. Over two millennia ago, Confucian scholars compiled and narrated two visions of societal development in the Book of Rites. In the long term, they envisioned a world of great harmony, Datong ("universal harmony"). In the short term, they pictured a society of good living and wealth, Xiaokang. In lieu of great harmony during Xiaokang, society achieves moderate prosperity by following moral principles (propriety and justice), with all individuals claiming their rightful positions and performing their rightful duties. The state defends society. Wise men, following moral principles, being trustworthy and exercising legal authority, are in charge of the state. Those in authority who do not follow these principles can be removed and viewed by the people as pariahs. In Datong, the ultimate way, the world belongs to the public, where the wise and able are elected, trust and harmony prevail, and men care for not only their kin, but for all, including the young, the old, the handicapped, the sick, and the isolated. Resources and properties are not
hidden by individuals; volunteerism is assumed. There is no trickery, corruption, or thievery. No doors ever need be closed.

Linking Xiaokang to development in China was another of Deng’s brilliant innovations. In 1979 he clarified that unlike what it might mean in the West, modernization in the case of China must refer to Xiaokang. It is clear that in Deng’s conception the primary stage of socialism substantially overlapped with Xiaokang, where the principal goal was to achieve a certain level of overall prosperity while society maintained stability and harmony under the leadership of the state. The goals identified for Xiaokang and Datong are strikingly similar to those identified for the two stages of socialism advocated by Deng, Hu, and Wen. The significance of this indigenizing socialist ideology cannot be overlooked. Xiaokang and Datong stress order, equality, and harmony, and teach respect for authority and concern for all. They are consistent with the visions outlined for the primary stage of socialism. At the macro-level, they legitimate the authority of the state and the Party, not so much based on political ideology as on their wise and competent management of society’s well-being and the people’s desire for better lives. At the micro level they expect that indigenously valued social relations will promote and sustain harmony. They offer an authentic Chinese justification for permitting greater political, economic, and social participation.

This course, from command capitalism to planned capitalism, offers a softer and indigenized version of ideology and projects harmonious social relations. As long as the state and the Party act on behalf of the well-being of all the people, protects China’s interests in the world, and adjusts itself to meet the people’s demands and desires, there is every reason to believe that they will remain supported by the people. This shift does not require abandoning any prevailing ideology. After all, the socialist and democratic ideals advocated are all embedded in Xiaokang and Datong, which predate Marx by more than two thousand years.
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