Polanyi’s Curse and the Second Great Transformation in China

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Abstract: A rapid marketization could cause social movements of self-protection yet populist disorder, as Karl Polanyi warned in his classic *The Great Transformation*. The Chinese economy sits at a strategic yet worrying turning point from the high speed booming to a slower growth, which is conceptualized by the government as the ‘New Normal’. As a result, the Chinese government urges a “Supply-side Structural Reform” to conquer this economic challenge. At the same time, the ongoing anti-corruption campaign is reshaping the fundamental rules of Chinese politics and business. The government-business relationship is transforming to a ‘New Type’, and it also provides unprecedented challenges and opportunities for new social forces. This talk aims to reveal how to understand those elusive yet vital jargons by the Chinese government and its underlying implications to China and the World.

Introduction: The New Era?

Inspired by Karl Polanyi’s the *Great Transformation*(Polanyi, 1944), Michael Burawoy labeled the socioeconomic and political changes in the post-communist world as a “second great transformation”(Burawoy, 2000). He and his advocates argue that this wave of marketization actually provides us not only a fertile ground to collect more data and test theories that were developed in other geographical contexts, but also a historical-making invitation to rebuild a revolutionary social science that reconfigures what we already know from existing classical and contemporary theories (Eyal&Szelényi et al., 2003; Eyal&Szélényi et al., 2001; Outhwaite&Ray, 2005).

So far the major story in the post-communist China is about rapid economic growth driven by market-oriented reforms. However, commentators and observers have been keeping warning that a growth without balancing interests of disadvantaged social groups could cause serious socio-political consequences. Particularly, when liberalizing reform of social welfare system was blocked in Central and Eastern Europe during the 1990s, marketization and de-centralization was undertaking in both rural and urban China(Ho, 1995; Huang, 2002)—the reform of healthcare system was so radical that was portrayed as a “Great Reversal”(Chen, 2001). For some moments, it looked like that crises driven by social self-protection movements have been jeopardizing the legitimacy of the regime. However, the Chinese party-state responded. For example, as European postcommunist countries started to abandon their inherited public health system, the financially strong Chinese party-state was in

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the process of establishing a universal healthcare system, proposing to spend $124 billion by 2011 to subsidize basic medical coverage and overhaul hospitals (Rösner 2004; Wong 2009). Chinese paramount leaders promised a “bigger government role in public health, with a goal for everyone to enjoy basic health care service” to respond to the fierce complain about the commercialized and marketized healthcare system. Overall, at either historical phrase of reforming social welfare system, China was on an opposite trajectory to most Central and Eastern European countries: in the 1990s, it was weak market in Europe but strong commercialization in China; in the 2000s, the state is retreating in Europe while the big government comes back in China.

These responses yet do not mean that the double movements argued by Karl Polanyi disappeared. His “curse” is still on the air: if marketization dominated all spheres of our life, a counter force would emerge to protect the society. So, what is new for today’s China?

In March 2016, the Chinese President Xi on a conference urges a “new type of government-business relationship”: sincerity and honesty. As he defines, sincerity means that government officials must keep magnanimous exchanges with private enterprises to help them solve practical problems, while the honesty refers that government officials need to be aboveboard and ethical to stamp out greed for money. Meanwhile, private entrepreneurs should tell the truth, offer their counsels, and run businesses with law-abiding principles. The calling for this “new type of government-business relationship” has been a landmark event given the fact that at that moment the market was concerning about the ongoing anti-corruption campaign’s impact on their business. It also becomes the first time the paramount leader of China elaborates to the public about his idea on how to balance the tension between the state and the business. Xi’s talk provoked a fierce feedback from both the market and the public media. For scholars of the study of state-business relations (SBR), this calling implies that the Chinese government is aiming to transform the government-business relationship from “old” to “new”. So, what is the “old”?

The Old Story

Despite the pessimism about Chinese political elite the global business community and a large number of political scientists abroad share the optimistic view that encouraging private sector would eventually bring on a democratic transition in China. Currently private economy is already strong in China: it contributes more than 60% of China's GDP, provides cities with more than 85% of all jobs and accounts for more than 90% of migrant worker jobs. It is expected that private entrepreneurs will play the role their European counterparts did in the past and will become “a class with teeth” in the spirit of “no taxation without representation”.

The prospect, however, seems dim. The domination view by scholars on the state-business relations in China can be conceptualized as clientalism or prebendalism. Scholars argue that China's capitalists/private entrepreneurs may constitute a nascent civil society, but presently they are playing an unconventional role; rather than use their power to wield influence over the state, they become more closely integrated with the system as it already exists. In other words, entrepreneurs are not very supportive of democratic reform for fear of potential instability. They therefore are labeled as “ally of the state” and “red capitalist”, while the myth of China’s economic booming is often interpreted through terms like local growth coalition, corporatist state, and resilient authoritarianism.

In addition, business classes in China have more and more formal ways to express their interests. As a logical complement to selective repression, the Chinese party-state has created several avenues for linking itself with private business interests. There are various quasi-government business associations, such as the Industrial and Commercial Federation, which registered nearly 80% of private owners. In addition, the party-state is systematically co-opting “outstanding private entrepreneurs” into the People’s Congress (the Chinese parliament, PC) and the Chinese People’s Political Consultative Conferences (a political advisory body, CPPCC) at both local and national level. In those conditions it is hard to imagine that the economic elites would be inclined to risk a conflict with state authorities, at least in the short run.

This scenario, however, only provides us one side of the story. The B-side of clientalism should never be neglected. In short, the intimacy between power and private wealth cannot be taken for granted. For example, the full legitimacy of private property was not written into the Constitution of China until 2007, and the capitalists could not join the Chinese Communist Party until 2002 after a big ideological debate among the leadership. More importantly, the allegedly changed macro-economic environment since the early 2000s, a.k.a. “the state enhances and the market retreats”, has been tremendously influenced the rhetoric of the state and the feelings of the private investors. Some media even used a stronger tone. They asserted the Chinese government was launching a “(creeping) (re)nationalization” movement into such industries as airlines, petrochemicals, consumer goods and metals, which previously had a record of sustained privatization.

Following the Bourdieu’s term, the group of private entrepreneurs is still in general a dominated fraction of the dominant class, even for the super richest. One more fact is that though GDP of Private sector has been more than 60%, according to official data, most private entities are small and medium enterprises (SMEs) and self-employed households. Even for those giant private enterprises, either their number or their size is still smaller than those monopoly state-owned or controlled enterprises (SOEs). This fact can be easily revealed by the breakdown of numbers of Chinese firms listed in Top 500 of the Fortune magazine: SOEs surpasses private enterprises significantly.

Anti-corruption

The recent unprecedented anti-corruption campaign becomes an even more urgent cause for securing the expectation of Chinese private entrepreneurs. A report based on public-media spotlighted cases: more than 600 cases in 2015, compared to 426 cases in 2014. A typical scenario of this campaign is that when a corruptive official falls down, his or her ‘rich friends’ fall down, too. So far, most investigated entrepreneurs are business elites on the local economic stage, but the number of tycoons with national impact has been increasing. This has been causing some concerns among those super rich who actually had been shadowed under the so-called “The Forbes Curse” for decade. The rich list curse is believed as the people whose names appear on the top would be sent to jail or got into big troubles. Statistics show that only a small proportion of the riches are actually in prison: 24 people till 2011, 2.4%. Yet many people believe their wealth in China is of volatility. It brings about some remarkable results.

The first result is the emerging of a group of more reflexive entrepreneurs on their relations with the government. The most notable event was happened in 2013, when in a private gathering, Liu Chuanzhi, the leader of the world's second largest computer maker, cautioned his peers to "stay out of politics and talk only business“. Many famous business elites evolved and it became one of the most notable public events of Chinese business elites in 2013. Though some disagree with Liu's argument about staying away from politics, a common perception among Chinese private entrepreneurs, especially those giant tycoons, is that it has been much more risky to do business in the clientalist old way than before.

The second result is the so-called "sloth administration". For those officials who used to benefit personally from boosting private investment in their region, the political risk of rent setting or flexibility is becoming much higher: to be caught or investigated by the discipline organs of the Party-state. The less incentive to maintain the used-to-working local growth coalition between the power and wealth is believed a partial yet vital reason for the slowdown in private investment in this year: fixed-asset investment expanded by a weaker-than-expected annual clip of 9.6% in the first five months of the year, compared with 10.5% growth through April. Even worse, the private investment portion grew by a mere 3.9% in January-May, down from an already weak 5.2% in January-April.

Two caveats, however, should be emphasized about the impact of anti-corruption campaign. First, anti-corruption is overwhelmingly welcomed by the people (CSS data in 2014) and legitimates the current leadership significantly. Second, anti-corruption is not the essential reason for economic slowing down as some might argue; instead, it is providing new opportunities for China's economic restructuring. The current economic problems are more caused by those long term structural pathology.

A "New Normal" of China's economy and "Supply-side Structural Reform"

Anti-corruption is not the only momentum that has been changing the government-business relationship in China, not even the most fundamental one. The changing economic landscape is. China's economy has been experiencing rocky years: lower growth rate dragged by a housing slowdown, softening domestic demand and unsteady exports. "A new normal of China's economy has emerged with several notable features," Chinese president Xi defines in a Party document: (the Chinese economy is) from the previous high speed to a medium-to-high speed growth; the economic structure is being constantly improved and upgraded; the economy is increasingly driven by innovation instead of input and investment. Put this official rhetoric aside,

The Chinese government has realized the reality that China could not achieve two-digit growth rate anymore under the new normal. In an article published on *People's Daily* this May, the Communist Party's official newspaper, the author who named as "the authority people" claims that China's growth pattern would not be a V shape growth but a L shape growth, i.e., a long term relatively slow growth without rebound in the foreseeing future. It is largely interpreted as the officials have been prepared to make their policy based on a new expectation.

Other economic issues are also emerging in recent years. Housing bubble is huge. The Chinese government attempted to cool off the overheated housing economy by both financial and administrative means, but the aim so far is not achieved. Soared capital outflow has been jeopardizing China's foreign exchange reserve. Overcapacity of steel, coals, and cement should be reduced while this thorny task is largely delayed due to violation from local governments. Even if this reduction goes thoroughly, the potential risk of high unemployment of those workers will emerge and could be even more hazardous. In other words, the exogenous crisis forced the Chinese policy makers to sustain the dynamics that contributed to constant economic growth; they were well aware that a more sustainable development is demanded to be pursued for the sake of long-term prosperity.

With the combined pressures above mentioned, we can now focus on the third result of changing state-business relations: China needs a new wave of fundamental and comprehensive reform. This reform was called as “supply side structural reform” when it was finally official announced in the late Nov in 2015. This tricky term sounds like the “supply side economics’ endorsed by those economists favored in the Regan administration in the 1980s, but the Chinese officials denounce its connection. The essential issue, however, is not whether the Chinese government was inspired by the supply-side economics, but to understand what exactly they aim to achieve through this reform.

Every single word of the “supply side structural reform” matters for understanding its meaning. “Supply side” refers to the factors such as labor, capital, land, and even institution. Compared with previous policies emphasized more on “demand side” such as consumption, export, and investment, a shift of focus onto the supply side indicates a vital strategic move. For example, in order to boost domestic consumption, the demand side policy would be to stimulate individual’s consumption behavior. The supply side policy, by contrast, requires the government to reflect whether they have provided the right products (like good quality milk powder) or service (like low tax) for consumers to consume.

“Structural” means this reform aims to restructure China’s economy, which however is not a brand new idea. The highlight therefore should be on the “reform”. Though the Chinese government seldom put “supply side structural reform” and “the construction of new type of government-business relationship” together, these two new policy blueprints are essentially mutual beneficial: if the Chinese government is aiming to break those institutional barriers between the supply side and the demand side, they are overthrowing those obstacles in the way of a less corruptive and a more accountable state-business relationship.

Several brave reforms have been undertaking in recent years. For example, the Chinese government has been calling for “Administration Streamlined and Power delegated” as “a self-revolution to the government”. They simplify and streamline the procedure for establishing a firm by lowering and even abandoning some requirements for registration. They encourage entrepreneurship and innovation. In addition to reduction of tax for certain enterprises, the central government announced this year to comprehensively replace business tax with value-added tax (VAT), which could be a huge tax reduction if fully implemented. They have canceled or exempted more than 400 administrative fees or approval. In order to reduce cost for enterprises, the government would gradually reduce social insurance premium rate and consider amending controversial Labor Law.

Corporatism from the bottom

Economy is not the only aspect that would be reshaped by the “supply side structural reform”. Another important field is society. The logic is clear: when the Chinese leaders vow to build a “smaller government”, they need to cultivate a “large society” to shoulder some responsibilities that the Party-state used to do. Some notable steps have been undertaken. For example, the Charity Law was passed this March, setting basic rules on some very important issues for growth of charity organizations. The government also issued a new regulation to boost the growth of state-endorsed grass-root business associations, private think-tanks, and other social organs. Consequently, the enragement of institutionalized channel of dialoging made it possible for the party-state to have real bodies to talk prior to the unexpected exogenous crisis.

For private business elite, context analysis of proposals by private entrepreneurs also shows increasing intention and ability for influencing policy. Political leaders repeatedly deny that the government is implementing a policy of re-nationalizing parts of the economy and most analysts agree there is no formal policy. But still, private entrepreneurs and their representatives express their anxiety and anger via business groups, parliament and other political adversary bodies such as the CPPCC. They do not, of course, dare to criticize the party-state; instead their blusters are directed against the colossal “Central Enterprises”, that is, the 136 large-scale SOEs controlled directly by the central government. Since government officials and the SOE tycoons usually compare giant state corporations to “the eldest son of the People’s Republic”, private entrepreneurs call themselves the “step-children” or “servant girls” of the state. This can be viewed as increasing lobbying forces among private owners, though the “eldest son/step-child” metaphor reminds us of a competition between children striving for the favors of the patriarch. The question is: has lobbying - or babyish tears and petulance- worked?

On the one hand, a realistic businessman must be aware that complaining is one thing but acting smart is another thing. The government is hoping a new wave a “hybrid ownership” or PPP projects can be a new momentum for balancing interests of monopolistic central-state enterprises, provincial-state enterprises, local governments, and private investment. The old story of previous PPP however reveals that it is extremely difficult for private capital without political connection to cut a slice of the cake from monopolistic enterprises of the central government, while certain slices are apportioned to state-owned corporations and local governments by means of sub-contracting or outsourcing. No substantial analysis can be conducted yet to demonstrate to what extent private companies lose or benefit from the calling of hybrid ownership. The one way to gain access to bigger deals and finance has been for private firms to hook up with the state-owned firms’ patronage system because state-owned firms not only have the upper hand in bidding for stimulus-related projects but they also hold the power to decide which businesses to patronage for supplies and sub-contracting jobs, particularly in the massive infrastructure construction projects. It was reported that this strategy was acknowledged and even encouraged by the Chinese political leadership.

On the other hand, the state also responds to request of private investors. Under the pressure of declining of real economy sector, the Chinese central government released a document called for a more blunt reduction of cost for enterprises in the real economy. This document contains 56 clauses, a follow-up to the government’s policy released years earlier. Some policy watchers believe that these regulations are meant to be an answer to the complaints of private entrepreneurs by encouraging further liberalization of transportation, tele-communications, energy, access to large areas of specific industry. In addition, local governments have strong motivations to keep a “local growth coalition” to let private capital take of financial pipeline of the state, because local officials need investment from private owners.

Yet, seen from a political perspective the imperative of the party-state was not to allow workers to rise as a national force of change. The slowdown of economy was a big challenge to Chinese policy makers and political leaders became keen to learn what might happen if an unprecedented depression actually did take place. It was disclosed that the All-China Federation of Labor, the government-controlled and the only legitimate trade union in China, sent several teams along with officials from other government branches to major coastline and inner cities to investigate how serious the situation was because none of them had any idea what was going on. The bottom line yet is to restrict the growth of labor NGOs, though NGOs fro-business can be encouraged.

Conditions for Success

So, what is the future scenario of China's state-business relationship? "Sincerity-honesty" is the official blueprint. In order to achieve it, the Party –state should obey its own manifesto on rule by the law by promoting judicial system reform and "putting the power into the cage". The anti-corruption campaign should insist to decrease rent-seeking/ rent-setting opportunities. On the economic side, the thorniest issue would be to break industrial monopoly of SOEs, because bureaucratic management of SOEs themselves has become a stubborn interest group who is able to manipulate policies for their own stake. More importantly, the government officials should respect relative autonomy of non-governmental commence and social organs.

What is also important is to examine the conditions which allowed the party-state to perform such a role with considerable success. What kind of state power do we witness in China today? Given the overwhelming importance of the role the party-state plays in the overall policy direction to be pursued, it is a pity that no serious debate has emerged in China to conceptualize the Chinese state in a manner acceptable to the international community of social science. We would like to fill in this gap starting with a preliminary sketch.

To begin with, the party-state of China differs significantly from both a 'totalitarian' state conventionally used in reference to Nazism, Fascism and Stalinism, and from a 'liberal-democratic' or a 'social-democratic' state in the Western sense. The Chinese party-state lies in-between these two opposite poles, and has the following general characteristics.

First, it shows the existence of an extensively developed bureaucratic apparatus with heavy networks of consultation and influence over the society as a whole. This condition is possible only when a country reaches a considerable degree of economic and social modernization.

Second, ambitious young people with recognised educational credentials both at home and abroad are recruited into state bureaucracy. In other words, they are protected by state power to act rather autonomously according to the rules of the state's activity. Insulated from external pressures they are more able to pursue developmental goals than they would be if they were subject to external pressures.

Third, the system of governance by this kind of bureaucracy entails a considerable degree of organizational discipline, which regulaties interactions. Although elements of corruption, factionalism, and clientalism exist, the party-state still maintains a discipline of meritocracy, an effective ability to formulate and evaluate national policies of development, rules of objective testing and competition as well as an emphasis on public good over private interests, public deliberation, and norms of general social welfare. Furthermore, the party-state is in a position to discipline private entrepreneurs as well as the workers.

Fourthly, there has emerged a considerable cohesion among the power elites, particularly between those who steer the economy and public security, that is, between socio-economic technocrats and the military. These two power groups are united in the belief that national wealth and military power ought to be increased through the state-led process of modernization. The internal cohesion makes it possible for the state apparatus to pursue economic policies consistently.

Consequently, political dissidents are effectively shut out of decision-making processes.

A salient aspect of the Chinese party-state is that rather than attempting to reach a compromise between government and enterprise, the state, often forcefully, attempts to induce enterprises to comply with its already established goals. The state uses various means to this end, among them financial inducement schemes as well as fiscal, and tax benefits. The secret lies in the state's control of capital supply to the private sector. The state also uses such devices as loans, industrial subsidies and other legally stipulated means by which it reduces or exempts duties, alleviates custom taxes and deferrs debt redemption.

In the prevailing order of things the state positions itself above the private sector. This position is deeply anchored in the Confucian norm of public service and has had an enormous influence on state policy over economic enterprises. While the state plays a large role in developing state-owned enterprises it also wants to play an important role in the private sector, which it tries to discipline, albeit not in the traditional way but in a capitalist way. It is therefore not accurate to describe the relations between the government and economic enterprises as symbiotic as is often done with Japanese capitalism. Rather, the concept of a "disciplinary" regime is more applicable. The state disciplines not only the workers but also the entrepreneurs. We may call this type a bureaucratic authoritarian state with built-in emphasis on economic growth.

However, this description involves idealization. The fact is that although the Chinese state turns out to be highly successful in accelerating economic growth it is undeniable that it also has serious limits and contradictions. This leads us to ask whether the Chinese ruling elite are aware of the possibility that the Chinese pattern of crisis management described above could in the long term store up problems, such as large amounts of bad loans. We would like to tease out how such a scenario would be likely to impact the future of China, particularly with regards to democratization. Since a sustainable democracy must come from within instead of being imposed from without we put a premium on domestic changes in China and pay close attention to attitudes and actions of the power elites and other social groups.

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