

China: The Quiet Revolution

The Emergence of Capitalism

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When Deng Xiaoping unveiled his vision of economic reform to the Third Plenum of the 11th Central Committee of the Chinese Communist Party in December 1978, the Chinese economy was faltering. Reeling from a decade of stagnation during the Cultural Revolution and already falling short of the projections set forth in the 1976 10-year plan, China needed more than a new plan and the Soviet-style economic vision of Deng's political rival, Hua Guofeng, to improve the economy. Deng's plan was to lead the country down a road of gradual and incremental economic reform, leaving the state apparatus intact, while slowly unleashing market forces. Since that time, the most common image of China, promulgated by members of the US Congress and media, is of an unbending authoritarian regime that has grown economically but seen little substantive change.

There is often a sense that China remains an entrenched and decaying authoritarian government run by corrupt Party officials; extreme accounts depict it as an economy on the verge of collapse. However, this vision simply does not square with reality. While it is true that China remains an authoritarian one-party system, it is also the most successful case of economic reform among communist planned economy in the 20th century. Today, it is fast emerging as one of the most dynamic market economies and has grown to be the world's sixth largest. Understanding how this change has come about requires an examination of three broad changes that have come together to shape China's transition to capitalism: the state's gradual recession from control over the economy, which caused a shift in economic control without privatization; the steady growth of foreign investment; and the gradual emergence of a legal-rational system to support these economic changes.

Reform Without Privatization

During the 1980s and 1990s, economists and institutional advisors from the West advocated a rapid transition to

market institutions as the necessary medicine for transforming communist societies. Scholars argued that private property provides the institutional foundation of a market economy and that, therefore, communist societies making the transition to a market economy must first create industry and other public institutions. This school of thought argued that rapid privatization, often called "shock therapy" or "big bang" approach to economic reforms—was the only way to avoid costly abuses in these transitional systems.

The Chinese path has been very different. While countries like Russia have followed Western advice, such as rapidly constructing market institutions, immediately removing the state from control over the economy, and hastily privatizing property, China has taken its time in implementing institutional change. The state has gradually receded from control over the economy, cautiously experimenting with new institutions and implementing them incrementally within existing institutional arrangements. Through this gradual process of reform, China has achieved in 20 years what many developing states have taken over 50 to accomplish.

The success of gradual reform in China can be attributed to two factors. First, the gradual reforms allowed the government to retain its role as a stabilizing force in the midst of the turbulence accompanying the transition from a planned to a market economy. Institutions such as the "dual-track" system kept large state-owned enterprises partially on the plan and gave them incentives to generate extra income by selling what they could produce above the plan in China's nascent markets. Over time, as market economic practices became more successful, the "plan" part of an enterprise's portfolio was reduced and the "market" part grew. Enterprises were thus given the stability of a continued but gradually diminishing planned economy system as well as the time to learn to set prices, compete for contracts, and produce efficiently. Second, the government has gradually promoted ownership-like control down the government administrative hierarchy to

the localities. As a result, the central government was able to give economic control to local administrators without privatization. But with economic control came accountability, and local administrators became very invested in the successful economic reform of the villages, townships, and municipalities under their jurisdictions. In a sense, as Professor Andrew Walder of Stanford University has argued, pushing economic responsibilities onto local administrators created an incentive structure much like those experienced by managers of large industrial firms.

Change from Above

Even as economic reform has proceeded gradually, the cumulative changes over two decades have been nothing short of radical. These reforms have proceeded on four levels: institutional changes instigated by the highest levels of government; firm-level institutions that reflect the legal-rational system emerging at the state level; a budding legal system that allows workers institutional backing outside of the factory and is heavily influenced by relationships with foreign investors; and the emergence of new labor markets, which allow workers the freedom and mobility to find new employment when necessary. The result of these changes has been the emergence of a legal-rational regime of labor, where the economy increasingly rests upon an infrastructure of ordered laws that workers can invoke when necessary.

Under Deng Xiaoping, Zhao Ziyang brought about radical change in China by pushing the country toward constitutionality and the rule of law to create rational economic processes. These changes, set forth ideologically as a package of reforms necessary for economic development, fundamentally altered the role of politics and the Communist Party in Chinese society. The early years of reform not only gave a great deal of autonomy to enterprise managers and small-scale entrepreneurs, but also emphasized the legal reforms that would undergird this process of change. However, by creating a body of civil and economic law, such as the 1994 Labor Law and Company Law and the 1995 National Compensation Law upon which the transforming economy would be based, the Party elites held themselves to the standards of these legal changes. Thus the rationalization of the economy led to a decline in the Party's ability to rule over the working population.

In recent years, this process has been continued by global integration and the tendency to adopt the norms of the international community. While championing global integration and the Rule of Law, Zhu Rongji also brought about broader political and social change, just as Zhao Ziyang did in China's first decade of economic reform. Zhu's strategy

has been to ignore questions of political reform and concentrate instead on the need to adopt economic and legal systems that will allow the country to integrate smoothly into the international community. From rhetoric on "linking up with the international community" to laws such as the 2000 Patent Law to institutions such as the State Intellectual Property Office and the Chinese International Economic Trade and Arbitration Commission, this phase of reform has been oriented toward enforcing the standards and norms of the international investment community. Thus, Zhu's objective is to deepen all of the reforms that have been discussed above, while holding these changes to the standards of the international community.

After two decades of transition, the architects of the reforms have established about 700 new national laws and more than 2,000 new local laws. These legal changes, added regulations, and experiments with new economic institutions have driven the reform process. A number of laws and policies in the 1980s laid the groundwork for a new set of policies that would redefine labor relations in fundamental ways. For example, the policies that set in motion the emergence of labor contracts in China were first introduced in an experimental way in 1983, further codified in 1986, and eventually institutionalized with the Labor Law in 1994. While there are economic incentives behind Chinese firms' willingness to embrace labor contracts, including the end of lifetime employment, these institutional changes have gradually rationalized the labor relationship, eventually providing a guarantee of due process in the event of unfair treatment and placing workers' rights at the center of the labor relationship. Incremental changes such as these have been crucial to the evolution of individual rights in China.

The obvious and most common response to these changes is that they are symbolic rather than substantive, that a changing legal and policy framework has little meaning when an authoritarian government still sits at the helm. Yet the scholarship that has looked extensively at the impact of these legal changes largely belies this view. Workers and managers take the new institutions seriously and recognize that the institutions have had a dramatic impact on the structure of authority relations and on the conception of rights within the workplace.

Other research shows that legal and policy changes that emphasize individual civil liberties are also significant. In the most systematic and exhaustive study to date of the prison system, research shows that changes in the treatment of prisoners have indeed resulted in the wake of the Prison Reform Law. And although no scholarship has been completed on the National Compensation Law, it is noteworthy that 97,569 suits were filed under this law against the government in 1999, a proportional increase

of over 12,000 percent since the beginning of the economic reforms. These institutions guarantee that, for the first time in the history of the People's Republic of China, individuals can have their day in court, even at the government's expense.

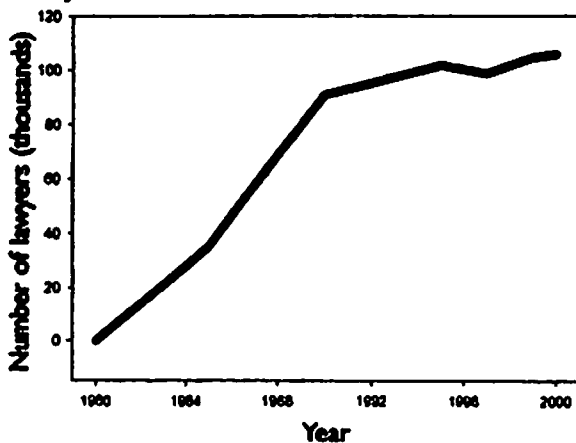
The 1994 Labor Law and the Labor Arbitration Commission (LAC), which has branches in every urban district, work hand-in-hand to guarantee workers their individual rights as laborers. Chapter 10 of the Labor Law, entitled "Labor Disputes," is specifically devoted to articulating due process, which laborers are legally guaranteed, should a dispute arise in the workplace. The law explicitly explains the rights of the worker to take disputes to outside arbitration (the district's LAC) should the resolution in the workplace be unsatisfactory to the worker. Further, many state-owned enterprises have placed all of their workers on fixed-term labor contracts, which significantly rationalize the labor relationships beyond the personalized labor relations of the past. This bundle of changes has fundamentally altered the nature of the labor relationship and the mechanisms through which authority can be challenged. For more than a decade, it has been possible for workers to file grievances against superiors and have those grievances heard at the LACs. In 1999, 52 percent of the 120,191 labor disputes settled by arbitration or mediation were decided wholly in favor of the workers filing the suits. These are official statistics from the Chinese government, and therefore should be viewed skeptically. However, even if the magnitude is incorrect, these numbers illuminate an important trend toward legal activity regarding workers' rights.

Many of these changes in labor practices were not originally adopted with workers' rights in mind, but the unintended consequence of the changes has been the construction of a regime of labor relations that emphasizes the rights of workers. For instance, extending the example of labor contracts that were being experimented with as early as 1983, these were originally intended as a form of economic protection for ailing enterprises, allowing a formal method of ending lifetime employment. However, workers began using the terms of employment codified in the contracts as the vehicle for filing grievances when contractual agreements were not honored. With the emergence of the LACs in the late 1980s and the further codification of these institutions in the Labor Law, the changes that were in progress became formalized in a set of institutions that ultimately benefited workers in the realm of rights. In a similar way, workers' representative committees were formed in the state's interest, but became an institution workers claimed as their own. These institutions, which many managers refer to as "consultative democracy," were adopted early in the reforms to curb the agitation for independent labor unions. These committees do not have the same power or status as independent labor unions in the West, but workers have made them much more significant in factories today than they were originally intended to be.

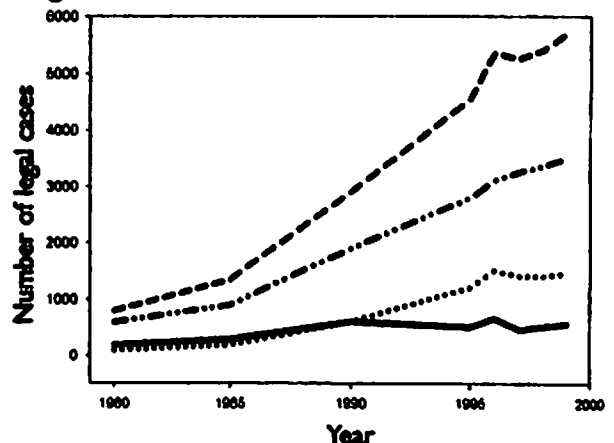
Foreign Investment's Impact

At the firm level, there is a process of rationalization in which firms are adopting a number of rational bureaucrat

Lawyers



Legal Cases



2002 Statistical Yearbook of China

Figure 1 An Age of Jurisprudence.

The above graphs depict two recent trends in China: a growing body of lawyers and an increasing number of legal cases. As the graph at left indicates, the number of lawyers in China has increased dramatically in the past 20 years, rising from fewer than 10,000 in 1980 to over 100,000 in 2000. The graph at right shows the growth in various types of legal cases over the same period. In particular, there have been significant increases in civil, economic, and first-trial cases.

systems, such as grievance filing procedures, mediation committees, and formal organizational processes, that are more often found in Western organizations. In my own work on these issues, I have found that joint venture relationships encourage foreign joint ventures to push their partner organizations to adopt stable legal-rational structures and systems in their organizations. These stable, legal-rational systems are adopted to attract foreign investors, but have radical implications for the structure of authority relations and the lives of individual Chinese citizens. Chinese factories that have formal relationships with foreign, and particularly Western, firms are significantly more likely to have institutionalized formal organizational rules, 20 times more likely to have formal grievance filing procedures, five times more likely to have worker representative committee meetings, and about two times more likely to have institutionalized formal hiring procedures. They also pay about 50 percent higher wages than other factories and are more likely to adopt China's new Company Law, which binds them to abide by the norms of the international community and to respect international legal institutions such as the Chinese International Economic Arbitration and Trade Commission. Many managers openly acknowledge that the changes they have set in place have little to do with their own ideas of efficient business practices and much more to do with pressure brought on them by their foreign partners. Thus, there is strong evidence that foreign investment matters for on-the-ground change in China.

Foreign investors and Chinese firms are not interested in human rights per se, but the negotiations in the marketplace lead to transformed workplaces, which affect millions of Chinese citizens on a daily basis.

Given the common image of multinational corporations seeking weak institutional environments to capitalize on cheap labor, why would joint venture relationships with Western multinationals have a more positive impact in the Chinese case? The answer has to do with the complex reasons for foreign investment there. Corporations are rarely the leading advocates of civil liberties and labor reform, but many foreign investors in China are more interested in long-term investments that position them to capture market share than they are in cheap labor. They generally seek Chinese partners that are predictable, stable, and knowledgeable about Western-style business practices and negotiations. Chinese factories desperately want to

land these partnerships and position themselves as suitable investment partners by adopting a number of the practices that Western partners will recognize as stable and reform-minded. Among the basic reforms they adopt to show their fitness for "linking up" with the international community are labor reforms. Thus, the signaling of a commitment to stable Western-style business practices through commitments to labor reform has led to fundamental changes in Chinese workplace labor relations. Foreign investors and Chinese firms are not interested in human rights per se, but the negotiations in the marketplace lead to transformed workplaces, which affect millions of Chinese citizens on a daily basis.

However, changes at the firm level are not meaningful if they lack the legal infrastructure upon which a legal-rational system of labor is built. The construction of a legal system is a process that takes time; it requires the training of lawyers and judges, and the emergence of a culture in which individuals who are part of the legal system come to process claims. This process of change is difficult to assess because it relies on soft variables about the reform process, such as, for example, how judges think about suits and whether a legal-rational culture is emerging. But we can look at some aspects of fundamental shifts in society. All of these changes, in turn, rest upon a legal-rational system that is slowly but surely emerging in China.

Finally, beyond the legal and institutional changes that have begun to transform Chinese society fundamentally, workers are no longer tied to workplaces in the way that they once were. In the pre-reform system, there was very little mobility of labor, because workers were generally bound to their "work units" for life. The system created a great deal of stability for workers, but it also became one of the primary means through which citizens were controlled. Individuals were members of their work units, which they were dependent on for a variety of fundamental goods and services.

This manufactured dependence was one of the basic ways that the Party exercised control over the population. Writing about the social uprisings that occurred in 1989, Walder points out that the erosion of this system is what allowed citizens to protest with impunity on a scale never before observed in communist China: "[W]hat changed in these regimes in the last decade was not their economic difficulties, widespread cynicism or corruption, but that the institutional mechanisms that served to promote order in the past—despite these long-standing problems—lost their capacity to do so." It is precisely because labor markets have opened up that workers are no longer absolutely dependent upon the government for job placements; they now have much more leverage to assert the importance of their own rights in the workplace. And while the private

Briefing China and the West



A time for muscle-flexing

As Western economies flounder, China sees a chance to assert itself—carefully

THE room is stuffy on a sunny spring afternoon, and many of those packed into it (see above) must have regretted bringing their coats. The lucky ones have taken the few seats available. The rest are crammed shoulder-to-shoulder in this hotel-room office, listening intently to an hour-and-a-half rant on the threat of American imperialism and how the global economic crisis will result in growing confrontation between China and the West.

Sitting in front of a large portrait of a young Mao Zedong, Zhang Hongliang knows how to play to his nationalist, liberal-despising audience. His rambling discourse ranges from adulation of Mao to scorn of America (it has neither history nor culture), to warning of a “white terror” if rightists (liberals) prevail. The economic crisis is entirely the West’s fault, and as it deepens the West will turn on China. Now is the time to build an aircraft-carrier. A war with America would be “lose-lose”, but China should not be afraid of it.

China’s “leftists” are becoming more active as the global economy sputters. Mr Zhang belongs to an extreme fringe that pines for Maoist egalitarianism, state ownership and the certainty that America is an enemy. His seminar was organised by Maoflag, one of a clutch of like-minded websites in China whose nationalist, pro-

communist rhetoric is suffused with a sense of their country as victim, yearning for revenge. Frequenters of these forums took heart from a flurry of spontaneous celebrations around the country in December to mark Mao’s 115th birthday. The government preferred to play it down.

Few would suggest that radical Maoists are poised to make a comeback. But their nationalism has a broad appeal. As China surveys the world, with the West in financial turmoil and its leaders seemingly desperate for cash-rich China to come to its aid, it sees strategic opportunities. Even before the financial crisis began to hit the country late last year, nationalism had been boiling up. It was evident in public responses to the turmoil in Tibet in March, the West’s support for the Dalai Lama, and China’s sporting triumph at the Olympic games in Beijing in August. Now a battered West presents a gratifying target for pent-up contempt. Even the normally cautious government is beginning to flex a little muscle on the world stage.

For most of the past two decades (flare-ups with Taiwan in 1995-96 and with America in 2001 excepted) China has played a cautious game internationally. Its approach was summed up in the pithy four-character phrases into which Chinese policymakers love to distil their thinking.

The late Deng Xiaoping came up with a string of them: China should keep a low profile, not take the lead, watch developments patiently and keep its capabilities hidden. Now the global economic crisis and the West’s obvious weakness are causing officials to think again.

In public Chinese leaders still try to reassure. During a visit to Europe in late January and early February, China’s prime minister, Wen Jiabao, stressed that China’s development was no threat to anyone. It would be, he said at Cambridge University (an event better remembered for the shoe lobbed in his direction by a protesting German student) a peaceful and co-operative great power. Some sensitive Western diplomats pricked up their ears at the phrase “great power”, but it is one Mr Wen has used to describe China since well before the current crisis. In deference to foreign feelings, an English text released by the government news agency, Xinhua, used the word “country” instead.

On the issue of Tibet, however, China has been digging in its heels. Having conceded a little to Western opinion last year by holding three rounds of talks with representatives of the Dalai Lama in the wake of the unrest in March, China has lost interest. A massive security clampdown has been imposed on the Tibetan plateau to prevent any protests during this month’s 50th anniversary of the uprising that caused the Dalai Lama to flee into exile in India. Foreign journalists (despite pleas for access) have been shut out altogether.

In late February China gave a warm welcome to America’s secretary of state, Hillary Clinton. It had reason to feel proud. Here was an important American official ▶