UNDERSTANDING CHINA'S REFORM
Looking beyond Neoclassical Explanations

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Jane Duckett. *The Entrepreneurial State in China: Real Estate and Commerce Departments in Reform Era Tianjin*. London: Routledge, 1998, 273 pp.
Lance L. P. Gore. *Market Communism: The Institutional Foundation of China's Post-Mao Hyper-Growth*. Hong Kong: Oxford University Press, 1998, 354 pp.
Jean C. Oi. *Rural China Takes Off: Institutional Foundations of Economic Reform*. Berkeley: University of California Press, 1999, 253 pp.
Edward S. Steinfeld. *Forging Reform in China: The Fate of State-Owned Industry*. Cambridge: Cambridge University Press, 1998, 300 pp.

THEORETICAL CONTEXT: LOCAL STATE CORPORATISM VERSUS NEOCLASSICAL POLITICAL ECONOMY

POST-Mao reform in China has not only transformed the political, economic, and social dynamics of the country but also has provoked rethinking on a wide range of theoretical issues: How could China have achieved rapid economic growth without privatization? Why have Chinese officials not been resistant to market reform? What makes the Chinese state developmental rather than predatory? These questions pose important challenges to neoclassical political economy (NPE), which contends that economic growth is impossible under public ownership, that state bureaucrats always oppose marketization, and that states tend to be predatory.

Jean Oi was among the first to respond to those questions. In an article published in *World Politics* in 1992, Oi identified "local state corporatism" (LSC) as the secret of China's success. Her thesis has attracted wide attention among China scholars and has served as the common starting point of a number of studies on China's reform, including the recent books by Jane Duckett, Lance Gore, and Edward Steinfeld. More recently, Oi updated her arguments in a book-length study. The

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purpose of this article is to show how these works attempt, and all fail, to establish China as a case to refute NPE. But first, a review of the general arguments in the LSC-NPE debate may be helpful.

According to Oi, the decollectivization and the institution of the household responsibility system in rural China transferred the income rights over agricultural production from collectives to individual households. While this significantly enhanced the production incentives of peasants, the change deprived local governments of a major source of income. At the same time, China's fiscal reform granted local governments the right to retain part of the extra tax revenue they raised. That is, the higher the economic growth rate, the higher the tax revenue, and the greater the income of local governments. Given such a stake in economic growth, local governments were motivated to mobilize and coordinate resources under their jurisdiction to engage in entrepreneurial endeavors. They established and ran rural enterprises and took the profits to pay for expenditures and reinvestment. In such a way, local governments functioned like a large corporation with diversified businesses, thereby serving as the engine of China's economic development.[1]

In Oi's view, her LSC thesis explains why China could achieve rapid economic growth without privatization, why Chinese officials have not been resistant to the reform, and why the Chinese state has been developmental rather than predatory. These phenomena indeed represent important challenges to NPE. Recalling Adam Smith, NPE starts with the view that individuals are ultimately self-interest seekers. They will engage in economically productive activities only if they have maximum control over the value they produce. Thus, ownership of private property is a prerequisite for economic prosperity. Applied to the case of China, NPE holds that privatization is a necessary, though not sufficient, condition for the country to make the transition from a central command system to an efficient market economy. The World Bank, the most influential institutional advocate of such a view, thus contended that "the [Chinese] government should *completely withdraw from* inherently competitively structured industries where small and medium sized firms predominate."[2] While China's nonstate enterprises have been able to grow rapidly for almost two decades without the formal privatization of state enterprises, "the limits of this strategy may be ap-

[1] Jean C. Oi, "Fiscal Reform and the Economic Foundations of Local State Corporatism in China," *World Politics* 45 (October 1992).

[2] The World Bank, *China's Management of Enterprise Assets: The State as Shareholder* (Washington, D.C.: World Bank, 1997), xiii, italics in original.

proaching," the World Bank said.[3] Such an NPE view has been echoed by scholars both in the West[4] and China.[5]

Another major proposition of NPE is that state bureaucrats, like individuals in the market, are also self-interest maximizers. Only different institutional environments give rise to different behaviors between market individuals and state bureaucrats. Given hard budget constraints, individuals in a market economy based on private property rights are conditioned to be self-utility maximizing, resulting in a Pareto-efficient distribution of resources. In contrast, state bureaucrats could achieve an "authoritative allocation of values" by exercising political power. Given such privilege, they are constantly tempted to extract resources from the economy using nonmarket measures. To protect vested interests, bureaucrats will resist any reform that aims at withdrawing political influence in the market. States thus tend to be predatory rather than developmental.

Using the above perspective, Yves Chevrier has shown how China's system of factory director responsibility failed due to resistance from vested interests of the party. The difficulty with China's reform is that "the existing power structure would have to find enough internal strength to reform itself while reforming the economy and society."[6] More specifically, Nigel Harris and David Lookwood argue that since communist states emphasized national defense, communist vested interests tend to concentrate in military industries. Hence, as in Russia, Vietnam, and Ukraine, the military industrial complex in China has been particularly resistant to privatization. As a result, the Chinese effort to transform the "war-making state" into a "market-facilitating state" has instead resulted in the creation of a "rent-seeking state."[7]

Duckett: China as an Entrepreneurial State

As mentioned, the LSC thesis proposed in Oi's 1992 article was the first major attempt to show how China has proved an exception to NPE

[3] The World Bank, *Bureaucrats in Business: The Economics and Politics of Government Ownership* (Washington, D.C.: World Bank, 1995), 75.

[4] Wing Thye Woo, "The Art of Reforming Centrally Planned Economies: Comparing China, Poland, and Russia," *Journal of Comparative Economics* 18 (June 1994).

[5] Shaoguang Wang, "Learning by Debating: The Changing Role of the State in China's Economy and Economic Theories," *Policy Studies Journal* 23 (1995), 17.

[6] Yves Chevrier, "Micropolitics and the Factory Director Responsibility System, 1984–1987," in Deborah Davis and Ezra F. Vogel, eds., *Chinese Society on the Eve of Tiananmen: The Impact of Reform* (Cambridge, Mass.: Council of East Asian Studies, Harvard University, 1990), 131.

[7] Nigel Harris and David Lockwood, "The War-Making State and Privatization," *Journal of Development Studies* 33 (June 1997).

analysis. Duckett's *The Entrepreneurial State in China* is a further exploration of this issue. According to Duckett, post-Mao China is an "entrepreneurial state" (ES) characterized by the following major features: (1) the basic actors are individual state bureaus and their subordinate agencies; (2) these bureaus are directly involved in business; (3) they establish new profit-seeking businesses; (4) the new businesses are also risk-taking; (5) the state is adaptive to market reforms; and (6) ES activities are potentially productive and are thus not necessarily rent-seeking (pp. 14–15, 155–60).

While Oi focused on governments at the village, township, and county levels, Duckett narrows the unit of analysis to state bureaus. According to Duckett:

> The ES model focuses not on local government as a unitary actor, but on its constituent departments. It examines and describes the separate and autonomous profit-seeking economic activities of individual departments, explaining them as undertaken for the benefit of those individual departments, rather than for the development of the locality as a whole." (p. 13)

With the engagement of state bureaus in profit-seeking and risk-taking activities, Duckett argues, China has emerged into an ES rather than a predatory state. She believes that this has invalidated NPE's analysis (pp. 5–11). But from the viewpoint of NPE, Duckett's focus on the activities of bureaus does not provide sufficient basis for microanalysis. According to NPE, the basic unit of all social analyses should be individuals who share the same utility-maximizing natural desire. Human behavior must be explained in terms of the payoffs to the individuals involved rather than to any group to which they belong. Duckett "accepts that policy implementation and other 'state' activities are in the hands of individual officials" (p. 10). Throughout her analysis, however, she focuses on state bureaus, not individual bureaucrats.

The focus of Duckett's ES model (bureaus) is thus wider than that of NPE (individual bureaucrats) but narrower than that of LSC (local governments). The question then is, Why do bureaus provide a more meaningful level of analysis than individual bureaucrats and local governments? While deviating from NPE's individualist approach, Duckett identifies, in passing and in just two paragraphs, some personal incentives for officials to become entrepreneurial: higher status, more income, a better working environment, and diversion from the usual routine (p. 166). Haven't these ultimate concerns changed individual bureaucrats from opponents to supporters of market reforms? As long as *personal* incentives matter, the NPE rather than the ES perspective is more relevant. For NPE, the disaggregation of local governments into individual bureaus could be useful if the change in group size is shown to have an impact on the tendencies to free ride and on principal-agent relations. But Duckett makes no efforts along these lines.

Duckett claims that she "criticises NPE not for its individualist method, but for its neglect of the context in which officials operate." Her examination of the responses of state officials to a particular set of structural constraints is, she thinks, "able to show how officials may adapt to marketisation if they can benefit from the opportunities that reform generates. State officials need not only seek to maintain the *status quo* to preserve vested interests; in some contexts they may have an interest in promoting reform" (pp. 10–11). What are those "contexts"? According to Duckett, several institutional changes have caused the emergence of the Chinese ES. In the first place, state bureaus have been subjected to increasing financial burdens as their tasks grow and expenditures rise on the one hand, but revenue falls on the other. State bureaus thus established new businesses not only to generate income but also to provide career outlets for officials laid off as a result of the state's reorganization. At the same time, the emergence of a nascent market in a still state-controlled economy, the continuation of communist party control and the work-unit system, and changing social attitudes toward doing business have facilitated state bureaus' engagement in profit-seeking activities. (pp. 161–65)

Aren't the above institutional changes almost the same as those described by Oi in her LSC? Failing to show that the institutional constraints that apply to bureau officials are more important than those that apply to local government officials, Duckett makes no real improvement to the LSC analysis. Duckett contends that as ideal types the LSC and ES "refer to quite different distinct kinds of activity." The essence of LSC is "non-profit-seeking co-ordination by local government to promote balanced local development," whereas ES "involves the individual, profit-seeking business activities of state bureau" (pp. 12–13). While emphasizing such distinctions between LSC and ES, Duckett also notes that the two models might be compatible with each other: "Since state entrepreneurialism refers to only one dimension of state activity, it may exist within developmental local governments. Governments may co-ordinate the promotion of developmental and infrastructural projects while still allowing individual departments to run businesses" (p. 173). If so, then when should each model be applied? Duckett answers, "If state entrepreneurialism were a dominant feature of activity within local governments, that would justify use of the term ES as a description. If entrepreneurialism were less developed than co-ordinating activities, then the [LSC] might be the better characterisation" (p. 174). Hence, whether bureaus or local governments serve as the basic unit of analysis becomes unimportant, as both bureaus and local governments can be entrepreneurial or developmental. Then why differentiate between ES and LSC?

In fact, the above distinction that Duckett makes between LSC and ES does not seem meaningful. Under LSC, local governments not only coordinate economic activities; they also own and run rural enterprises.[8] Duckett criticizes Oi for making "occasional reference to individual bureaux' [*sic*] activities within the local corporatist state, [making it] unclear just what 'local government' refers to" (p. 173). But for Oi, bureaus and other kinds of local government organizations are alike in the sense that they may all engage in business activities. It is thus unnecessary to make any specific distinction between them.

Gore: Cadres as Bureaucratic Entrepreneurs

Gore's *Market Communism* also quotes Oi's LSC thesis. He even argues that LSC exists not only in Chinese villages but also in cities. According to Gore, "In so far as the institutional mechanisms of local state corporatism is concerned, I am in full agreement with these authors [including Oi]. And as such, local state corporatism exists not only in rural communities but in cities as well" (p. 160). This notwithstanding, Gore differs from Oi in his basic unit of analysis. While Oi was concerned with the response of local governments to institutional changes, Gore focuses on the behavior of individual bureaucrats.

Gore asks the central question, "What has *motivated* the dominant economic actors in the Chinese economy to *generate* such a long, sustained boom" (p. 13)? The dominant economic actors in reform China, according to Gore, are "bureaucratic entrepreneurs" (BEs). They are primarily "leading cadres" of the localities who are directly engaged in business activities aimed at promoting economic expansion (pp. 5, 96–97). By disaggregating local governments and bureaus into individual officials, Gore brings his analysis closer to the starting point of NPE than Oi or Duckett.

However, adopting a rather postmodernist stance, Gore argues that individual rationality is not inherited but is "socially constructed" (p. 28). That is, individual preference is defined by the institutional setting

[8] Oi, (fn. 1), 115–22.

rather than by birth. Under private property rights, capitalist entrepreneurs react to "market profit alone" (p. 276). Reassignment of property rights, however, has little effect on the incentives of BEs. Noting that the earnings of private entrepreneurs were substantially higher than that of BEs, Gore writes: "If [BEs] are motivated by private financial gains alone, they would be better off to become private entrepreneurs" (p. 103).

In Gore's view, "private property rights play little or no role as an incentive" for BEs' activities, because BEs are "embedded in the basic institutions of Communism—the party-state hierarchy and its economic apparati." As such, their interests are intertwined with those of the communities their offices represent. Being simultaneous agents of the state and representatives of the community, they "pursue not only an economic rationale but also political and social objectives that come with their official status" (p. 101). Politically, BEs seek to advance within the hierarchy. Given bureaucratic competition and "the developmental pressure from above," they are induced to speed up local economic growth, as this would become an asset for political promotion. Socially, BEs try to satisfy as much as possible the social welfare demands within their organizations because of their commitment to their own work unit and the need for securing cooperation from their constituents. Only with continuous rapid economic growth can the rising demand for social welfare be met (pp. 106–13).

While playing down the importance of economic incentive, Gore notes that BEs do have economic concerns. However, like the above political and social factors, the economic interests of BEs are intertwined with those of their communities. "When they bargain for policy concessions, state subsidies and other resources on behalf of the community, they bargain for all the members including themselves; when they engage in 'group consumption', they are simultaneously engaged in private consumption" (p. 114). BEs often use their power and other communal resources under their control to start businesses. Yet, the purpose is not solely for private gain but "to generate additional income for their members" (p. 117).

Gore thus paints a picture in which there is no conflict between private and public interests. BEs strive for local development because it serves not only their personal but also their communal interests. Their personal welfare merges with the community. Gore argues that China has seen such results through its institutional setting, which is characterized by "a state-centred political economy" with continued public ownership and state administration of the economy on the one hand, but weakening central control and emerging market forces on the other. "The mix feature[s] a unique combination of continued state-centricity and increased diversity and flexibility, and permits a market dynamism to emerge from amongst state hierarchies" (pp. 94–95).

In such a way, Gore claims that he provides an explanation of a phenomenon that NPE rejects as an accident—that a state can be developmental rather than predatory. He writes, "Proper institutional engineering can help to produce an incentive structure that may successfully contain the predatory tendencies of state elites. It may also be able to sustain a pattern of interaction among individual actors that can maintain the overall developmental orientation of the state." In Gore's view, his BE model "seems to be the only logical explanation for the puzzle of the developmental state" (p. 282).

Is this so? The answer depends on how we distinguish between developmental states and predatory states. If defined by outcome, there may be little question that China is a developmental state, as evidenced by the fact that the state-led reform has produced a two-decade growth. Yet, to define by outcome inevitably results in a tautology. An alternative is to define by a state's policies. Thus, a predatory state is one "whose policies can be shown to have benefited a monolithic self-seeking ruler and/or a bureaucratic elite," whereas a developmental state is one "that takes strong and direct measures to bring about economic development."[9] Conceptually such an approach seems more useful. But the question remains that if the strong and direct measures that bring about national development also benefit self-interest-maximizing bureaucrats at the same time, is the state developmental or predatory? This is exactly the difficulty that Gore created. When such an incentive system is in place, as Gore describes in his discussion of "bureaucratic entrepreneurialism," it can link bureaucrats' private interests with the national goal. Can we then still distinguish a developmental state from a predatory state? This is in fact a common methodological problem in the developmental state versus predatory state debate.

Perhaps more importantly, is the harmonization of private and public interests really a solution to this problem? Consider the case of a municipal economic bureaucrat in charge of a city's development plan in a liberal-capitalist state. The bureaucrat's private interests include personal income, career, and power. If the city prospers, he/she will reap rewards in all three categories—higher pay, greater chances of promo-

[9] Christer Gunnarsson and Mats Lundahl, "The Good, the Bad and the Wobbly: State Forms and Third World Economic Performance," in Lundahl and Benno J. Ndulu, eds., *New Directions in Development Economics* (London: Routledge, 1996), 257–58, 270.

tion, and increased authority on the job. That is, consistency between private interests and public interests, as depicted in Gore's BE model, could also exist in a liberal-capitalist system. Yet, this might not prevent the liberal-capitalist bureaucrat from placing private interests above public concern. We thus have no reason to expect the predatory tendencies of state bureaucrats under bureaucratic entrepreneurialism to be weaker than under liberal-capitalism. In Gore's view, predatory BEs may at the same time perform developmental functions. But so could their liberal-capitalist counterparts. The unique institutional structure in Gore's BE model simply produces no unique outcome.

Like Duckett, Gore also attempts to account for the apparently weak bureaucratic resistance to market reform in China. While Duckett explains this in terms of bureaus' interests in reform, Gore argues that "the rapid changes and the still-weak legal and procedural basis for coalition-building and other forms of effective political mobilizaton and political participation" in China have so far prevented the retrenchment of vested interests. As a result, bureaucratic resistance to reform "has been mostly passive and reactive, and has not been sustainable in the long run. Indicative of this is the fact that *the centre has eventually been able to push through all major reforms that it deems as essential, despite lengthy and repeated delays caused by local resistance*" (pp. 292–93, italics added). Here Gore makes no reference to his BE analysis. To the contrary, he contradicts his BE model by suggesting that central officials are developmental while local bureaucrats are predatory.

Steinfeld: Constraints as Impetus to Growth

While Oi asked the question, How could China achieve economic growth without privatization? Steinfeld in *Forging Reform in China* asks just the opposite, Why has privatization in China not produced the economic efficiency that property-rights analysis would predict (p. 36)? Oi's question assumes that privatization has not taken place in China. But according to Steinfeld, "although Chinese reformers may not speak the language of privatization, they have certainly internalized the logic" (p. 34).

The reason for the apparent difference between Oi's and Steinfeld's theories is that Oi based her 1992 article on surveys of township and village enterprises (TVEs) conducted during the period 1986–91,[10] and

[10] Oi (fn. 1), 102.

Steinfeld, in his 1998 book, wrote about the more recent reform of large industrial state-owned enterprises (SOEs). When Oi carried out her study, privatization of TVEs was inhibited by political constraints. But when Steinfeld conducted his research, privatization of SOEs was taking place under the name of corporatization, a program that includes the evaluation of firm-level assets, issue of shares to private investors, and requirement of real returns on investment (p. 122). The two authors thus address different processes taking place in different sectors during different periods.

Yet, this does not mean that Oi and Steinfeld share no common ground. According to Steinfeld, privatization in China, as in Russia and Eastern Europe, has not brought about any significant improvement in economic efficiency. Rather, "in China today, the state firms that exhibit behavior most associated with private enterprise in the West—value maximization, strict budgeting, rational investment strategies, efficiency maximization—happen to be among the *least* privatized in the country. . . . Proximity to some forms of state control *is* affecting performance, but in the opposite way from what traditional property-rights theory would predict." In other words, like Oi, Steinfeld found evidence of growth *without* privatization in China. Steinfeld calls it "the great paradox of Chinese SOE reform" (p. 38).

The problem with applying property-rights analysis to transition economies, Steinfeld argues, is that two fundamental theoretical assumptions do not hold. First, for privatization to work, the principle of "rule of law" must be upheld so that "rights" can be made into really "enforceable claims." The socialist economies from which transition systems evolved, however, were ruled by commands, not law. What is required, therefore, is not privatization or the transfer of property rights but the creation of such rights from scratch. Since only the state has the legitimate authority to create rights, it is the solution to, as well as a cause of, economic inefficiency (pp. 38–40).

Steinfeld is of course right in emphasizing the importance of rule of law in the maintenance of private property rights. But the fact remains that some forms of private-property rights legislations have already been introduced in Russia, Eastern Europe, and more recently, China. While it is true that the rule-of-law condition was absent in former socialist countries, it may not be completely correct in today's transition economies. More importantly, it is not clear why the creation of private property rights and privatization should be treated as two separate strategies, as Steinfeld has done. Shouldn't the creation of private property rights be an indispensable component of privatization?

The second assumption of property-rights analysis Steinfield found problematic is that individuals are regarded as the basic economic actors. Given private ownership, rational economic beings are expected to maximize their personal utility, leading to Pareto-efficiency. "The problem is that transitional systems are industrialized economies. Because they are industrialized economies, the relevant economic actors are firms, and often extremely large firms at that." Steinfeld's unit of analysis (firms) is thus different from that of Oi (local governments), Duckett (bureaus), and Gore (individual officials). "Once firms are taken to be the major actors, however, the terms of debate shift dramatically. Property rights per se, particularly the degree to which those rights can be brought together and merged into the hands of clearly specified owners, recede in importance. Instead, a host of new issues take precedence" (p. 40). Steinfeld then goes on to show how the principal-agent problem characterizes modern industrial enterprises (pp. 40–44).

Transitional systems, as Steinfeld noted, are industrialized economies. But so are developed capitalist systems. Should we therefore also replace individuals with firms as the basic unit of analysis in capitalist economies? The principal-agent problem does illustrate the complexity arising from the separation of ownership from control; it shows that private property rights may not be a sufficient condition for efficient corporate governance. But to use it as an argument against the importance of privatization in transition economies is rather far-fetched. Finally, the principal-agent problem arises exactly because agents are found to be self-interest-seeking individuals rather than loyal servants of the firms they serve. Firms' behavior, therefore, is ultimately determined by individual rationality.

Dissatisfied with property-rights analysis, Steinfeld proposes what he calls a "constraints-based approach." In his view, the determining factor of enterprise behavior is the degree of hardness of budget constraint rather than ownership.

> For the specific case of Chinese SOES, an important variable to focus upon is access to soft subsidization—more specifically, access to the state banking system. Once firms have access to unlimited bailout loans, pressure to shift over to market-oriented behavior decreases for government regulators and enterprise managers alike. Opportunities for rent seeking are created, and ultimate constraints—namely, the bankruptcy and liquidation of the firm—never quite materialize. Predatory state taxation and managerial distortions of performance data can go on unabated. . . . In short, even as ownership is held constant, varying the firm's access to the banking system shapes the degree to which relevant economic actors engage in market-oriented behavior. (p. 47)

Hence, "*the imposition of hard budget constraints should be the prime goal of transitional reform*" (p. 247, italics in original).

According to Steinfeld, his constraints-based approach differs from property-rights analysis in that his approach views reform as a "clamping down," whereas the latter approach sees it as a "loosening up" (p. 9). Instead of assuming that economic dynamics will emerge once actors are granted certain property rights, Steinfeld holds that efficiency can be obtained only by imposing hard budget constraints on them. "Behavioral change is viewed not as a spontaneous response to new freedom but rather as a forced response to new pressures and strictures" (p. 229). Here Steinfeld mistakenly treats his constraints-based approach and property-rights analysis as two competing theories. Property-rights analysis does emphasize the importance of freeing economic actors to pursue personal interests but the general equilibrium is the condition that all individuals make optimal choices subject to hard budget constraints. It is the interactions between rights and constraints that result in Pareto-optimality.

For Steinfeld, Oi's notion of LSC is a property-rights analysis and is thus defective in its neglect of constraints. He challenges LSC by asking, Why are TVEs successful only in southern China but not in the inland or northern areas? While all local governments in the country are granted income rights over TVEs, why are there such regional differences in outcome? Applying his constraints-based approach, Steinfeld explains that due to the traditional secondary position of the south in China's command economy, state subsidies are less available in the south than in the inland and the north. It is thus the difference in the degree of hardness of budget constraints rather than ownership that accounts for the different economic performance of TVEs (pp. 237–41).

In her more recent work, Oi addresses this question of regional disparity without referring to Steinfied (see below). But to the extent that Steinfeld's criticism is valid, it is the problem of LSC, not of property-rights analysis. Moreover, if Oi committed the error of neglecting constraints, then Steinfeld incorrectly forgot the importance of rights. Property-rights analysis emphasizes both rights and constraints; rights must work with constraints and vice versa. It is Steinfeld who mistakenly separated the two.

Finally, while Duckett and Gore both attempt to show that states can be developmental, Steinfeld's constraints-based approach lends support to NPE's predatory state thesis. According to Steinfeld, "When the large firm is state-owned, predatory agencies extract profit in their role as owners. If the firm is declared 'private,' those same agencies will extract tax money in their role as agents of governmental authority" (p. 62). That is the state will be predatory whenever possible, irrespective of ownership form.

Oi: Local State Corporatism Revisited

In *Rural China Takes Off,* Oi presents her latest version of LSC. While noting that the new tax system instituted in 1994 has reduced localities' claim to the residual, Oi believes that her LSC analysis is still valid. The reform has increased the center's share of tax revenue, but in absolute terms local governments have been guaranteed a minimum income not less than the 1993 level. More importantly, localities have retained their exclusive rights over a wide range of income, including sales tax, local-enterprise income tax, and individual income tax. Hence, in Oi's view, the incentives for practicing LSC have remained (pp. 54–56).

However, Oi is rather unresponsive to the works reviewed above, which all center on her LSC thesis. Duckett's ES analysis is used by Oi to supplement her point that local governments, given sufficient incentive and resources, can assume an entrepreneurial role. Oi notes that her study "recognizes that there are also distinct interests within local governments" (p. 193). But whether this necessitates narrowing the unit of analysis from local governments to bureaus, as Duckett does, is not discussed. Gore's study, which further disaggregates local governments and bureaus into individual bureaucrats, is not even included in Oi's bibliography.

While Oi focuses on local governments, her attitude to their basic components—individual officials—is ambiguous. She says that "there is no need to make assumptions about the nature of communist officials—either . . . they are corrupt or . . . they are motivated by lofty ideals that lead them to want to enrich their communities" (p. 6). Shortly thereafter, however, we find the following statement: "[This book] begins with the simple premise that local officials in a communist system, like officials in any political system, are rational actors who respond to incentives and existing constraints within the limits of their cognitive ability to evaluate alternatives and process information" (p. 7).

Indeed, only with such an NPE assumption do we find Oi's discussion of personal incentives relevant. According to Oi, fiscal contracting granted local governments autonomy in the use of residual they generated. "On a personal level, increased revenues in local government coffers directly translated into lucrative (and legal) economic rewards for local officials. Local governments used the residual for bonuses. Linking cadre bonuses to the size of the residual gave local officials a direct stake in economic growth" (p. 49). Besides earning bonuses, individual officials who achieved outstanding economic growth in their localities were promoted to higher ranks within the bureaucratic hierarchy (p. 102). These personal incentives explain why Chinese officials were motivated to promote economic growth and not to obstruct market reform. They are the secret of the Chinese experience. As Oi notes, "China's economic reforms took off in many parts of the countryside precisely because the key entrepreneurs leading the charge were those who had the economic and political resources—the cadres themselves" (p. 192).

The above analysis should bring Oi in line with the NPE school, which emphasizes individuals as the basic unit of investigation. In fact, Oi claims that her study "is an institutional analysis of economic development at the local level that *views local officials as political economic actors* distinct from the central state" (p. 9, italics added). However, she does not adhere to such an approach. In most of her book Oi treats local governments rather than individual bureaucrats as the basic actors. For example, she writes, "[Even though the rights to residual] were granted to governments, *not individuals*, the re-allocation of property rights gave localities positive inducements to promote rapid economic growth" (p. 28, italics added). Here Oi tends to trivialize the importance of personal incentives.

The shift away from individual bureaucrats to local governments led Oi to the non-NPE view that privatization is not necessary. According to Oi, the success of the public-owned TVEs in China proved that growth can be achieved without privatization (p. 56). She claims that her study shows that "*individuals* need not have property rights over enterprise profits for economic growth to occur. Growth occurs as long as there are property rights for some organized entity. Local governments, if they have sufficient incentive and resources to pursue growth, can assume an entrepreneurial role" (p. 193, italics in original). Hence, in Oi's view, there is "no inherent reason why only individuals or privately held companies, as distinct from governments, can be entrepreneurs" (p. 10).

Oi overlooks her point that Chinese local governments can be distinguished from their counterparts in capitalist countries by their "corporatist" characteristics. According to Oi, the term LSC "was used primarily to highlight the workings of local government and the economy that it oversees as a corporation. . . . Local governments ran their firms as diversified corporations, redistributing profits and risks, and thereby allowing the rapid growth of rural industry with limited resources" (p. 12). It is important to note that the corporations which Oi compares with Chinese local governments are privately owned entities, that is, the essence of LSC is that Chinese local governments are run like *private* corporations. Individual officials took bonuses from local governments' tax revenue, just as shareholders received dividends from joint stock companies. In the sense that public money (tax revenue) has been translated into bureaucrats' private property through such "corporatization," privatization has actually taken place in China, however informal it has been. Thus, Oi's assertion that China has achieved economic success *without* privatization is not entirely correct.

Regarding Steinfeld's critique, Oi's response is rather enigmatic. She cited Steinfeld as an example of those who "have suggested that China's rural industry would be just where it is today, even without state intervention, simply as a result of market forces" (p. 4). Nowhere can we find in Steinfeld's work any such statement. What he did say is that the rural economic takeoff in China has not been a "national" phenomenon; rather, it has been restricted to "areas neglected during the command period," such as the southern provinces (p. 235). Steinfeld's point is not that market forces have prevailed in these neglected areas. Instead, he uses the regional differences to ask Oi the very valid question, If fiscal contracting is the cause of China's rural prosperity, then why has this national reform worked only in the south but not other areas? As mentioned above, utilizing his constraints-based approach, Steinfeld explains this in terms of the difference in the availability of soft credits among Chinese regions.

Without referring to Steinfeld's point, Oi acknowledges the problem of variation of growth as follows:

> All parts of China's countryside were subject to the incentives embedded in decollectivization and the fiscal reform, but only a portion of the countryside has successfully developed rural industry. Some areas have been left out of the overall trend of industrial growth and the prosperity that has come with it. *In those areas that have succeeded in industrializing,* various forms of ownership have been adopted. Some counties, townships, and villages have relied primarily on collectively owned enterprises, whereas others have favored private ownership. (p. 58, italics added)

Two questions arise from these statements. First, why have the nationwide economic incentives produced growth only in some but not all rural areas? Second, within those areas that have achieved industrialization, why have some adopted mainly collective ownership while others have more privately owned enterprises? Oi argues that the economic incentives provided by fiscal contracting were intervened by the political attitude toward private ownership. She devotes most of Chapter 3 to show how the political factor has affected the form of ownership *in areas that have succeeded in industrializing*. That is, Oi addresses the second question, although not necessarily satisfactorily, and does not even tackle the first (and perhaps more important) question. Steinfeld identifies this as the central methodological problem of LSC: "By examining only situations in which TVEs have thrived, LSC approaches commit the error of selecting on the dependent variable, to use social science terminology. By trying to explain what they themselves define as a constant (TVE growth) and then by selecting only successful TVEs, LSC proponents have no way of proving that state intervention is the key" (p. 237).

Toward the end of her book, Oi writes: "In most villages, the determining factor is the degree of local industrialization. Local governments that control a primarily agricultural, particularly grain-based, economy have few options other than to levy ad hoc surcharges and various other fees and penalties. [LSC] is unlikely to exist in such villages. The greater the level of industrialization, the more likely that the local government will act in a corporate manner to intervene, extract, and redistribute income" (p. 191). On this point Oi seems to be confused about the direction of her explanation. Is it LSC that has facilitated rural industrialization or vice versa?

Conclusion

The four works reviewed above enhance our knowledge of China's reform but they do not adequately establish China as a case to refute the NPE perspective. Deviating from the NPE's axiomatic approach of treating single individuals as the basic political and economic actors, Oi, Duckett, and Steinfeld respectively focus on the behavior of local governments, bureaus, and firms. But they all fail to explain why their units of analysis, when compared with individual bureaucrats, are more relevant respondents to institutional changes. Gore alone focuses on individual bureaucrats. Yet his argument that China's institutional setting can produce altruistic bureaucrats is unconvincing.

However, the failure of these searches for non-NPE explanations does not imply that the NPE approach is adequate. In fact, so far NPE has not provided a satisfactory answer to the China puzzles either. To generate some kind of consensus on the issue, I would like to suggest the following methodological, empirical, theoretical, and comparative directions for future research. Methodologically, to solve China's economic "miracle," we must start with NPE's egoistic assumption because we have sufficient grounds to believe that Chinese bureaucrats have adopted such entrepreneurial behavior purely out of self-interest. There is ample evidence showing that Chinese bureaucrats make use of their public positions to reap private gains, and it is often hard to distinguish their "entrepreneurial" activities from corruption. It is exactly the existence of such bureaucrats that makes the Chinese case puzzling. The NPE perspective has the strength of identifying the China puzzles, and the challenge is to explain these puzzles without departing from NPE's individualistic starting point.

Empirically, we need further research to show how real the puzzles are. For example, a common measure must be established to determine the extent of privatization that has, or has not, taken place in China. This must be done before tackling Oi's question about how China could achieve economic success without privatization and Steinfeld's opposing question about why privatization in China has failed to produce economic efficiency. Likewise, before attempting to explain why Chinese bureaucrats have not been resistant to market reform, more detailed empirical work should be carried out to examine whether any geographical, sectoral, and generational variations in bureaucratic resistance exist. This will improve the focuses of our analyses. Finally, clear and operationalizable criteria must be identified to distinguish between developmental and predatory behaviors. As mentioned, this is particularly necessary, and also particularly difficult, in situations where the incentive system seems to be able to harmonize conflicts between personal and public interest.

Theoretically, insights can be sought from the ongoing collaboration between NPE and institutionalism. While NPE explains behavior in terms of utility maximization of egoistic individuals, institutionalism emphasizes the importance of institutional constraints. The complementarity of the two approaches has produced a fast-growing literature.[11] In fact, some applications of such joint perspectives have been made to the Chinese case,[12] but they do not tackle directly the puzzles that concern us. Efforts along these lines will involve the identification

[11] B. Guy Peters, *Institutional Theory in Political Science: The New "Institutionalism"* (London: Pinter, 1999), 43–62.

[12] Steven N. S. Cheung, *Will China Go 'Capitalist'?* (London: Institute of Economic Affairs, 1986); Steven L. Solnick, "The Breakdown of Hierarchies in the Soviet Union and China: A Neoinstitutional Perspective," *World Politics* 48 (January 1996); and David L. Wank, "The Institutional Process of Market Clientelism: Guanxi and Private Business in a South China City," *China Quarterly* 147 (September 1997).

of the institutional constraints that previous research may have neglected and an explanation of how Chinese bureaucrats have responded to these constraints in a way that makes the Chinese case so special. However, the limitations of such an approach must be specified to avoid making nonfalsifiable conclusions.

Comparatively, it would be useful to situate the Chinese case within the larger perspective of transitions in other postcommunist countries. In particular, Russia would be a good case for comparison, as it shares with China a similar background of indigenous communism but diverges sharply in terms of reform performance. Some have argued that such a comparison is inappropriate since China has some unique favorable initial conditions, such as a deeper sense of crisis, a less centralized agricultural sector, greater availability of surplus labor, a shorter history of communism, higher saving habits, and stronger ties with its emigrant community.[13] However, others have contended that no comparison is perfect. Instead of passively enjoying the favorable setting, China has actively promoted some "right" policies, including adopting an incremental approach, prioritizing agricultural and light industrial reforms, and opening foreign trade and investment.[14] The larger questions are, What leads China to such "right" policy choices? Are they outcomes of specific institutions? If so, are these institutions transferable? After all, it is the transferability of the Chinese experience that has the most practical implications.

In conclusion, the Chinese reform has provoked intellectual rethinking of the NPE perspective. The four works reviewed here represent different attempts in this regard. None of them, however, offer a better alternative. The search for the secret of China's economic "miracle" must be continued.

[13] Anders Aslund, *How Russia Became a Market Economy* (Washington, D.C.: Brookings Institution, 1995); Yuan Zheng Cao, Gang Fan, and Wing Thye Woo, "Chinese Economic Reforms: Past Successes and Future Challenges," in Woo, Stephen Parker, and Jeffrey D. Sachs, eds., *Economies in Transition: Comparing Asia and Eastern Europe* (Cambridge, Mass.: MIT Press, 1997).

[14] Marshall I. Goldman, *Lost Opportunity: Why Economic Reforms in Russia Have Not Worked* (New York: W. W. Norton, 1996); and Barry Naughton, "China's Economic Success: Effective Reform Policies or Unique Conditions?" in Kazimierz Z. Poznanski, ed., *The Evolutionary Transition to Capitalism* (Boulder, Colo.: Westview Press, 1995).