


# Unlikely Partners

CHINESE REFORMERS, WESTERN ECONOMISTS,  
AND THE MAKING OF GLOBAL CHINA

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since he had suggested that Włodzimierz Brus and Ota Šik be invited to visit China. In early November 1985, Liu published an article in the *People's Daily* in which he cited Kornai's concept of "investment hunger," described his own "increased understanding" of the relationship between macroeconomic policy and microeconomic policy and the need to reform both systems together, and called for gradualism in doing so.<sup>9</sup> These proposals were bolstered by a report that a group of economists at the System Reform Commission submitted to the State Council in October 1985 before being published in 1986, which drew on data collected from surveys of 429 enterprises to argue for near-term "bold yet prudent microeconomic reforms."<sup>10</sup>

Heading into 1986, many of the participants at the Bashan Conference were making major plays for influence in the contentious debates over the future of China's economic reform. For example, in December 1985, Wu Jinglian and several of his colleagues at the State Council Development Research Center submitted a report to the leadership on the seventh five-year plan, in which they declared, plainly, "It is necessary to carry out coordinated reform."<sup>11</sup> In 1986, a moment of transformation would occur for both economic thought and policy, in no small part because of the surge of new ideas and analytic tools that entered China in the wake of the Bashan Conference.

One dramatic trend in particular swept through China's economic circles—what was called "Kornai fever" (*Kèrnai fēi*).<sup>12</sup> Kornai's ideas, transmitted through diverse channels, flooded into Chinese debates, including the 1986 publication of the Chinese translation of *Economics of Shortage*.<sup>13</sup> Dozens of articles in periodicals introduced an even wider readership to what *Dushu*, then a prominent liberal magazine, called the "enlightening" views of Kornai, whom they dubbed "the economic theorist that the reform cried out for."<sup>14</sup> With its bright aquamarine cover, the two volumes of *Economics of Shortage* [*Duanque jingjizue*] seemed designed to garner attention. "Kornai fever" would go on to fuel sales of over 100,000 copies of the Hungarian economist's book.<sup>15</sup> Kornai was mentioned hundreds of times in academic and research journals in the period 1986–1989, including in regional and provincial journals in areas as varied as

Guangxi, Hubei, Anhui, and Heilongjiang.<sup>16</sup> A group of faculty and graduate students at Peking University even held a seminar devoted to *Economics of Shortage*, at which it was agreed that Kornai had made a major "theoretical innovation." According to a notice in the Peking University newsletter, the participants—who included the dean of the Economics Department—roundly praised the value of Kornai's ideas, although views on how to solve the problems he identified varied widely.<sup>17</sup>

Many responses presented Kornai's ideas with adulation, praising the "soft budget constraint" and Kornai's analysis of the relationship between the economic system and enterprise behavior as "revealing."<sup>18</sup> The *Dushu* article labeled Kornai as an "innovative" figure in the new era of reform in China. Lauding *Economics of Shortage*, the author cited several specific ways in which China could "borrow from" (*jiejien*) Kornai's works. His "method of researching the socialist system," especially the use of advanced mathematics, were sorely missing in China, where mathematical and model-oriented aspects of economic study were still "relatively weak." At a less instrumental level, the article argued that Kornai represented a synthesis of the best aspects of international economic research, focusing on his "use of the tools of Western economic theory and analysis to study the socialist economic system, combining the scientific elements of Marxian economic theory and Western economic theory." In this formulation, Kornai seemed to provide a methodological correlative to the policy synthesis of the "planned commodity economy," showing how the methods and techniques of Marxist and mainstream Western economics could align and cooperate, much as the plan and the market cooperated in China's mixed system. At the same time, in the context of the Bashan Report, the *Dushu* article's understanding of Kornai pointed toward a particular interpretation of the amorphous "planned commodity economy" concept, which would involve enlarging the scope of the market mechanism, enlivening enterprises, and achieving macroeconomic balance.<sup>19</sup>

Reviews of the translation of *Economics of Shortage* were also exceptionally positive. One reviewer, describing the excited response from Chinese readers interested in reform, acknowledged that the book studied Eastern European experiences but claimed that the similarities

and relevance to China of the phenomena it described were incontrovertible. A researcher at the State Council praised the utterly "unique" quality of Kornai's writings, adding, "Kornai's economic theory is successful . . . because it explores a new method for researching the problems of socialist economies."<sup>20</sup> These authors placed particular emphasis on two related aspects of the book: why the shortage economy was innate to socialism and how enterprise behavior under socialism created shortage phenomena—focusing, as a result, on Kornai's arguments about the "soft budget constraint" and "paternalism."<sup>21</sup> These ideas, which the reviewers defined as priorities to address in future reforms in China, would remain the most salient aspects of Kornai's thought for Chinese economists.

In addition to the great attention to *Economics of Shortage*, the most obvious consequence of "Kornai fever" was that Kornai—and, in a related manner, the Basha Conference—became a central part of economic debates on a diverse range of topics. The primary challenge now facing the participants at the Basha Conference was to determine how to apply the ideas to China's circumstances, and they processed them in diverse and often divergent ways.

For these individuals, the power of Kornai's ideas to diagnose, name, and clarify China's policy problems did not appear to be fundamentally contested. For example, the mild-mannered Zhao Renwei argued, in an article the same year, that Hungary (Kornai's archetypal IB system) may not have had a formal dual-track system in place but "Hungarian state enterprises had a dual dependence, responding to both higher administrative authorities and to the market." (Despite the similar-sounding names, China's dual-track system and Hungarian-style "dual dependence" were completely different in both structure and economic realities, but Zhao's insight was that in both situations enterprises were forced simultaneously to respond to vertical planning authorities and horizontal market incentives. Zhao, in other words, was looking for echoes between these two systems.) At the Basha Conference, Zhao added, Kornai had defined the Hungarian IB model as permissible only as a "transitional" device.<sup>22</sup> Similarly, the dual-track system in effect in China should only exist to facilitate China's transition. For many of these economists, Kornai

had framed China's policy challenges in such a way that it connected their policy dilemmas to a greater range of international economic debates than ever before.

However, the praise of Kornai's diagnoses did not imply uniformity in their interpretation and application to China. In September 1986, the aging Xue Muqiao delivered a speech in which he called for a "strengthening of macroeconomic control" to help the economy find "balance," an idea Wu Jinglian had advocated in 1984 and 1985.<sup>23</sup> Xue presented the need for China to develop a mode of "macroeconomic regulation" that differed from what "Western capitalist countries" used, asserting, "We are not the same as them."<sup>24</sup> Xue then turned to Kornai, relying on his analysis but suggesting a different conclusion:

It seems from these cases [in *Economics of Shortage*] that "investment hunger" is a disease that socialist countries cannot cure. I am not so pessimistic, as long as the whole country from top to bottom, and especially Party leaders, develop a deep understanding of this widespread disease . . . and strictly and consciously use macroeconomic controls to avoid this problem.<sup>25</sup>

Thus Chinese-style "macroeconomic controls" would differ from their "Western capitalist" equivalent principally with regard to the goals of such macroeconomic controls—goals that Xue found defined in Kornai's work, such as curing "investment hunger."<sup>26</sup> Yet Xue's disagreement with Kornai's "pessimism" ran deeper, because he was fundamentally disagreeing with Kornai's implicit condemnation of socialism itself. Within the framework of foreign ideas presented at the Basha Conference, Xue articulated a Chinese vision of a "cured" socialism—using a medicine, macroeconomic controls, adapted to suit China's needs.

Other participants seemed to agree that investment hunger was an affliction that could be "cured" within the context of the socialist system, while giving greater credence to Kornai's proposals for China's future path and not just his diagnosis of China's problems. For example, referencing the many theories propounded by "foreign scholars and domestic theorists," Liu Guoguang asserted the

most important was Kornai's new classification from the Bashan Conference.<sup>27</sup> He dismissed the *laissez-faire* IIA model as "capitalist" and "incompatible with socialism" because it had no central control, but he praised the IIB system as having attributes that allow it to "play a leading role" as a theoretical foundation for formulating the goal model for the reform.

In this context, Liu Guoguang voiced a question that dominated Chinese economic debates in the mid-1980s: "What exactly is a 'planned commodity economy'?"<sup>28</sup> Each economist's answer, of course, seemed designed to nudge this officially accepted ideology in the direction of his favored policies. Liu's definition stressed "enlivening" enterprises while also increasing macroeconomic management, with an eye toward curing "investment hunger" and prioritizing "adjustment of supply and demand."<sup>29</sup> "We are demolishing the formerly paramount vertical relationships between government and enterprises," he declared proudly.<sup>30</sup> In another speech delivered the same year, Liu elaborated on these ideas, using the Bashan Report to argue that moving beyond the dual-track system and the use of indirect administrative controls as quickly as possible was necessary to develop a system of macroeconomic controls with market adjustments (Kornai's IIB model).<sup>31</sup> Thus, for Liu, international knowledge was indispensable to determine both the meaning of the "planned commodity economy" and the means of managing such an economy—all while maintaining socialism.<sup>32</sup> As Liu elaborated elsewhere, these reform ideas would not overtake the country's specific conditions and commitment to socialism because China's economists would promote "continuity" and respect for the "legacy" of the old system.<sup>33</sup> Liu was a savvy and politically minded operator, and his conceptualization of China's economic reform deployed elements from the Bashan Conference to address what he saw as China's distinct circumstances and to define the Party's stabilizing role in exercising macroeconomic control.

Outside the circle of participants, the Bashan Report and the ideas shared at the conference became a standard reference for framing many issues facing China. This touchstone function was evident at a Nanjing conference in October 1986 on the "goal model of the re-

form," sponsored by Nanjing University, two economic institutes at the Chinese Academy of Social Sciences (CASS), and the Jiangsu Academy of Social Sciences. Approximately one hundred delegates attended the meeting, including senior economists and many younger scholars.<sup>34</sup> After Liu Guoguang's opening lecture, the second speech at the session focused exclusively on the Bashan Conference.<sup>35</sup> Its report has garnered "universal attention," the industrial economist Zhou Shulian declared, pointing to Kornai's goal model of market coordination with macroeconomic controls as the idea of greatest interest.<sup>36</sup> Without directly endorsing the report, Zhou presented engagement with Kornai's ideas as indispensable for any Chinese economist who hoped to devise an alternative "goal model." Kornai had "captured the core problem of economic system reform," which was the relationship between enterprises and the state and the "core" goal of "transforming socialist enterprises into real enterprises." Zhou wove Tobin's ideas into this tapestry, saying that the Bashan Conference also demonstrated that indirect economic management through monetary and fiscal policy was possible and desirable.<sup>37</sup> What emerged was a synthesis of the ideas of Kornai and Tobin, framed in terms of China's national conditions (although Tobin, perhaps because he was an American of "bourgeois liberal" tendencies, did not receive the same explicit acknowledgment that the Chinese accorded to Kornai, who had come up through a socialist system and maintained his Hungarian Academy of Sciences affiliation).

Many of the subsequent papers presented at the Nanjing conference alluded to the Bashan Conference and to Kornai's proposals. For example, Kornai's categorizations appeared throughout one economist's paper on an important emerging interpretation of the "planned commodity economy," as meaning that "the state manages the market, and the market guides the enterprises" (*guojia tiaojie shichang, shichang yindao qiyè*). The paper asserted this new ideological interpretation closely resembled Kornai's theoretical goal model but was "more in keeping with Chinese characteristics." In addition, "under China's conditions," the author wrote, "It is first necessary to develop toward [indirect administrative control], and then later [we] can move toward the mechanism of the plan guiding the market."<sup>38</sup> This paper thus used Kornai to describe both the theoretical

underpinnings and the implementation challenges of the emerging concept of "the state manages the market, and the market guides the enterprises"—a concept that would become critically important to the future of the Chinese system.<sup>39</sup> At this elite economic research meeting, the message was clear: The Bashan Conference, especially Kornai's ideas, had become threads woven through the Chinese discourse on reform, even though many possibilities remained open for interpretation and application.<sup>40</sup>

In short, just over a year after the participants disembarked the S.S. *Bashan* at Wuhan, Kornai's reputation in China had grown to an astonishing level. Attending a conference in New York, Zhao Renwei and Wu Jinglian spoke with Yale professor John C. H. Fei, who closely followed the latest trends in Chinese economic thought. He allegedly exclaimed to Zhao and Wu, "Some mainland economists have raised up Kornai too high, as if putting him on par with Marx! But how can you compare Kornai to Marx?"<sup>41</sup>

How can we understand the extraordinary interest in Kornai's work by such a wide range of Chinese economists? The most prominent reason, of course, was intellectual: the broad appeal of his ideas lay in the precision of his identifying, naming, and interpreting the problems of China's socialist economy. But "Kornai fever" was not only an intellectual craze. Even more than Brus and Šik, Kornai represented a kind of counterfactual life that China's economists had not been able to live. He was born and educated in the socialist world but he produced work that earned him acclaim and respect on both sides of the Iron Curtain. His writings were grounded in Hungary's experience, but he had attained, for his Chinese audiences, a thrilling universality. In a recent essay, a prominent Fudan University professor wrote, "When Yu Guangyuan died, I was reading Kornai's autobiography, and suddenly I thought: What would have happened if Yu and Kornai could have switched the environments in which they lived?"<sup>42</sup> Reflecting on the older generation of Chinese economists, the Fudan professor realized that, despite that generation's immense capacities and the historic transformation they had lived through, there was no "Kornai-type character" among them—and they knew it. In this sense, Kornai was at once a foreign expert who descended from a distant land and almost—only *almost*—became one of them.

This possibility is mirrored by Kornai's own understanding of his influence in China. Writing with his wife, Zsuzsa Dániel, in 1986, Kornai attributed the success of his ideas to his personal history. "We think that French or American authors, lacking personal experience, can hardly understand and interpret the Chinese events of the last decade. . . . With Hungarians, empathy comes much more naturally."<sup>43</sup> Writing from Cambridge, Massachusetts, as a Hungarian, about what he learned on the Yangtze River, Kornai suggested that he believed his influence in China had both personal and intellectual bases.<sup>44</sup>

The prominence of the Bashan attendees and the dense networks of China's leading economists during this period allowed the contestation of these ideas to extend far beyond the publications by the conference's immediate participants. Their disagreement on how to apply the ideas to China did not limit their influence. To the contrary, this spread may, in part, have been the result of how contestable the ideas were. Because the ideas had great diagnostic precision but ambiguous application to China's policy dilemmas, they acted as newly cleared ground on which a wide selection of China's reformers could hash out their disagreements.

Across the intellectual spectrum, this moment in 1986 was one of extraordinary openness—to the point that the thirtieth anniversary of the Hundred Flowers campaign, an abortive attempt under Mao to encourage dissenting opinions from Chinese intellectuals, was celebrated as the beginning of what the *New York Times* called "a new 'Hundred Flowers' drive." Deng Xiaoping had helped lead the crack-down on the original Hundred Flowers campaign after Party leaders decided that the openness they had encouraged had gone too far, but Deng promised that the 1956–1957 fiasco would not be repeated in 1986.<sup>45</sup> In the heady atmosphere of 1986, Chinese intellectuals felt free to make bold claims, clearly demonstrating their sense of empowerment due to the encouragement of Zhao Ziyang, Hu Yaobang, and even Deng.

In this context, Kornai may have resonated with reformers worried about perceived problems in the transitional economy, but widespread disagreements about whether his ideas could solve problems

or simply identify them soon cooled the "Kornai fever" into a more critical approach. The ideas introduced to China at the Bashan Conference became protean, invoked to support the contending policies of China's reformist economists, who fought fiercely as power, ego, and the future of China all hung in the balance.

Wu Jinglian's "coordinated reform" group had largely defined their positions before the Bashan Conference, but they used the arguments of Kornai, Tobin, and others to bolster their ideas about the need for immediate reform of the macroeconomic system, aiming to increase the economy's responsiveness to market incentives while simultaneously developing stronger mechanisms for macroeconomic management during periods of economic instability. They began to stress the urgency of price reform in new terms that reflected growing sophistication. Their emphasis on the fact that price reform had lagged behind other reforms under the dual-track system now shifted to assertions that price reform was the "key link" between macroeconomic and microeconomic reform. Wu Jinglian made these arguments in a report on "coordinated reform" to the State Council in January 1986.<sup>46</sup> That summer, in an important article, Wu and several allies drew on the Bashan Report to bolster their related assertions that in China aggregate demand exceeded aggregate supply, despite some economists' claims to the contrary.<sup>47</sup>

Wu's opponents within the reformist camp, however, argued that reform of the enterprise ownership system should come first. Five economists from CASS and State Council research units wrote an article criticizing the Bashan Report and attributing "shortages under the traditional socialist system" to the problems of enterprise ownership, rather than Wu's theory that rigid pricing was the problem.<sup>48</sup> They criticized Kornai's "overgeneralization of the problem," which prevented him from "coming up with a solution" to the problems he had identified. Kornai's inadequacies, and those of his Chinese followers, became an opening for their own proposals for "restructuring of the microeconomic base starting with the reform of ownership."<sup>49</sup> They proposed an "asset management responsibility system" as the goal of restructuring, in which "returns on assets" would be the only metric of enterprise success, solving the problem of "investment hunger" by creating market incentives driven by the pursuit of profit.<sup>50</sup>

Not all was smooth sailing, however. In early March, Xinhua News Agency circulated an editorial titled "Marxian Economics Has Great Vitality." It attacked the ideas of an author named Ma Ding (a pseudonym used by the writer Song Longxiang) for "fawning on foreign theories." In late 1985, Ma Ding had written an essay on Chinese economics that stated, in no uncertain terms, that Marx was holding China's economists back: Chinese economists "must free themselves of Marxist books . . . and establish a new branch of economics in building socialism" explicitly incorporating beneficial insights from Western economics, including Keynesian proposals for monetary and fiscal policy. Although many reformist economists agreed with Ma Ding's assessment, conservatives led by the ideologues Deng Liqun and Hu Qiaomu soon attacked the article's eager embrace of Western economics and its criticisms of Marxian economics.<sup>51</sup> Yet Zhao Ziyang wrote a letter to Hu on March 3 that included a clear warning about those sorts of statements: "You should be cautious when criticizing the liberalization of economic theory." Deng Liqun later said he would never forget those words.<sup>52</sup> A series of periodicals subsequently republished Ma Ding's article in full or released comments praising his ideas.<sup>53</sup>

Amid these disagreements, Zhao Ziyang made comments at a mid-March 1986 meeting of the Politburo Standing Committee that suggested he was leaning toward Wu Jinglian's proposals. Praising the previous year's research efforts and demonstrating his detailed knowledge of the competing reform proposals, Zhao emphasized the goal of reforming three key interrelated systems: the taxation system, the financial system, and the price system. Of these three, he said price reform was "primary," but the three sets of reforms "must be coordinated" (emphasis added).<sup>54</sup>

For opponents of "coordinated reform," there was no time to waste. Li Yining, the Peking University economist who had helped lead the Foreign Economics Lecture Series and coauthored *The English Disease*—in which he discussed the history of British industrialization and the perils of nationalized enterprise as a way of writing about "the stagnation of Chinese industry" when it was otherwise "too sensitive" to do so in 1982—had clearly decided the moment had come to make a dramatic play for influence.