

Happy birthday to Janos

Janos, you are my teacher, my mentor, and my father-like friend. You have not only influenced my research, my scholarly work, but also my life.

Before my talk, let me forward greetings from your other Chinese friends

- “Kornai’s thoughts have a strong influence in China. Happy birthday to Janos.” (Wu Jinglian)
- “Marx has thoroughly dissected traditional capitalism, while Kornai has thoroughly dissected traditional socialism” (Zhao Renwei)
- “Kornai’s insights have values to peoples all over the world. Wish him the best of continued physical health and sharp mind!” (Wang Yijiang)

Institutions which Determine the Future of China: for Prof. Kornai's 85th Birthday

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Abstract

Professor Kornai has been one of the most influential economists in China in more than three decades. One of his biggest influences to Chinese reformers is on the necessity of institutional change. Following his steps, this talk discusses the problems in China's institution. The question I will address is, what are the major obstacles that have prevented China from establishing constitutional rules? I argue that grave socio-economic problems in China, e.g. low domestic demand, worsening corruption and inequality, intensifying social conflicts, etc. are all created from China's fundamental institution: Regionally Decentralized Authoritarianism (RDA). The RDA regime which contributed to China's reform and growth in the past now threatens the stability and sustainability of China. However, reforming this regime posts great challenges, since the power of the party-state is unlimited, although administration and economy are decentralized; the party-state has nested interests to resist any constitutional reform. The fate of constitutional reform in China is the biggest factor which determines China's future.

China's future is highly uncertain

- Optimistic views: R.Fogel (2010); OECD (2012)
 - a la classic growth model assuming away institutions
 - In 2040, the Chinese economy will count for 40% of global GDP; the US share of the global GDP will be 14%
- Pessimistic views: China will collapse soon
 - Financial/fiscal problems may trigger crisis
- The biggest uncertain factor which determines China's future is China's governance institution
 - It creates severe socio-economic problems
 - It hampers stability and sustainability of China

China is NOT Japan, South Korea, Taiwan

- In stable market economies, without severe institutional problems, if an economy has a substantial distance from the world's technology frontier, this economy will catch up the frontier quickly
 - Japan, South Korea, Taiwan etc. experienced this after the WWII
 - In terms of the distance from the world technology frontier, today's China is at the level of Japan in the 1950s in nominal per capita GDP [i.e. about 1/10 of the US per capita GDP]
 - If China follow the rout of Japan (South Korea and Taiwan), China will have 30 more years of fairly high growth
- Yet, China's institution is qualitatively different from Japan etc.
- The sustainability of China's growth depends on her stability and governance institution
 - Historically the biggest factor which prevents China's development is almost always China's own institution

The institutional cause of China's recent rapid slowing down

- The direct reason of rapid slowing down of China's economy in 2012 is low domestic demand
- The low domestic demand is the outcome of the growth model chosen by the authoritarian regime
 - Complete state ownership of land
 - Deprive citizens' rights and opportunities for wealth/income
 - High land prices crowd-out service industry
 - State monopoly of banking and financial markets
 - State monopoly of energy, telecommunication, railway...
 - The share of labor income in GDP has been declining for 15 years

China is destabilized by its institution

- More dangerous than slowing down is China's instability
- The unprecedented large scale urbanization since 1998 led by an authoritarian regime creates grave socio-economic conflicts between citizens and government
 - Depriving more citizens' rights; worsening rent-seeking and corruptions; heavier censorships; more suppressions to citizens
- Chinese government's huge expenditure on "maintaining social stability(维稳)" indicating its rapid losing control
 - 2010 social stability budget 549 billion RMB (84 billion USD), increased by 16%; defense 533 billion RMB, increased by 7.8%
 - 2011 social stability budget 624 billion RMB (95 billion USD), increased by 14%; defense 600 billion RMB, increased by 13%
 - 2012 social stability budget doubles that of the defense budget (a confidential internal source)

China's Institution: RDA

- I characterize China's governing institution as Regionally Decentralized Authoritarianism (RDA)
 - Unlimited power of the party-state
 - Highly centralized political and personal control power
 - Highly decentralized admin and economic powers
 - Regional competition/experimentation as the major mechanisms
- The RDA regime is responsible for China's reforms and growth in the past 30 years (Xu, 2011)
- It is also the source of serious socio-economic-political problems, the recent abrupt slow down, and sustainability
 - Structural problems
 - Widening inequality; worsening injustice; deepening corruption
 - Social and political stability problems
 - Serious mismanagement associated with the above problems

The nature of China's RDA regime

- The Chinese RDA regime is an institutional mixture of the Chinese imperial system and the Soviet totalitarian system
- Regional competition/experiment played decisive roles in overcoming political resistances to the reform at early stages
 - The transition from a totalitarian regime to RDA regime and from central planning to market is over
 - The transition from very poor to lower-middle income is over
- Regional competition/experiment do not work anymore beyond these transitions
 - Most socio-economic problems are created by the RDA regime
- No better alternative incentive solution in the RDA regime
 - Other approaches are much worse in providing incentives to party-state bureaucrats

How the RDA regime creates problems

- Appointed bureaucrats are not responsible to the constituencies: citizens have no basic rights in this authoritarian regime
 - The local governments are accountable to the bosses
 - There is no way for the bosses to design an incentive scheme
- No checks and balances, no separation of powers
 - Unstoppable diseases from abuse power, rent seeking, corruption
 - Destabilize the economy and the whole system
- Invasion of citizens' rights threatens socio-economic stability
 - Citizens' rights, e.g. land rights, rights to raise funds, are deprived
 - This is in contradiction to the market economy
 - The limitation of the market economy is set by the RDA regime
- The key problem is the unlimited power of the party-state
- A constitutional reforms is necessary for China's stability – a consensus among reformers

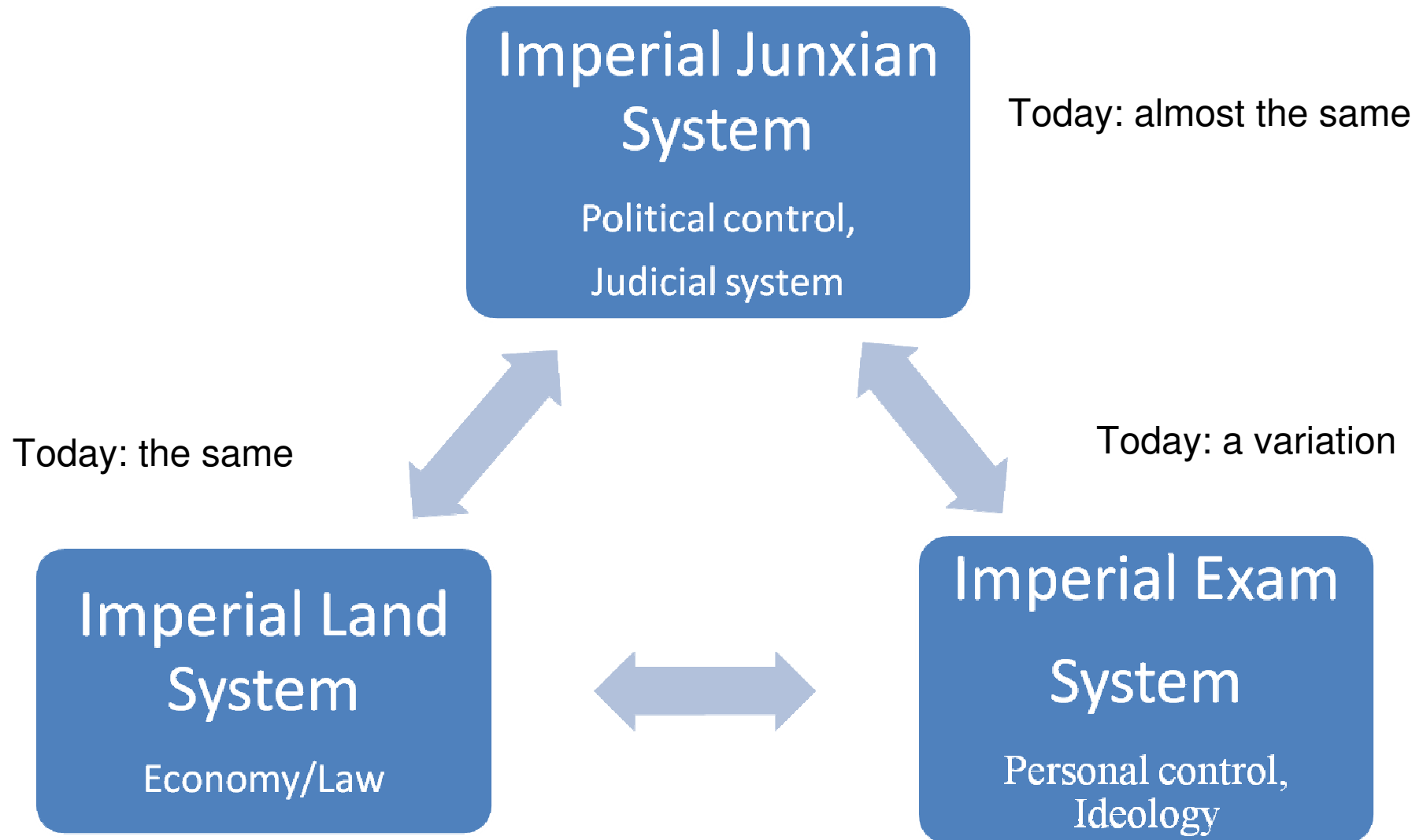
What obstacles have prevented China from establishing constitutional rules?

- What can be done in a constitutional reform is confined by the existing institutions evolved in the history
- A successful reform must be in participants' interests
- China has eliminated independent political and economic powers since the imperial time
 - Social elites are appointed bureaucrats; no independent intellectuals
- All previous failed constitutional reforms in China relied on self-constraint of the ruler
 - No support from independent political-economic forces
 - Reforms were aimed at strengthening the state, not citizens' rights

China's RDA regime is a modern variation of the Chinese imperial system

- Chinese empire is the far longest lasting empire on earth
 - However, it is not well studied in economics/political economy
- The same factors, which support a super stable Chinese empire, make constitutional reform extremely difficult
 - Absence of independent political/economic social forces
 - Eradicate foundations that citizen can assemble independent forces
 - Ideology that baffle citizens to yield their rights even when they are deprived
- The above factors are outcomes of the Chinese imperial system governed by the following institutional trinity
 - The Imperial Junxian political system
 - The Imperial Exam system
 - The Imperial Land system

Governance structure of imperial China: an Institutional Trinity



The Imperial Junxian System (郡县制)

- Junxian system is the fundamental governance structure of the Chinese empire
 - It was established when the empire was created around 220 BC
- The distinctive governance structure of today's RDA regime is inherited from the Junxian system
- Junxian system as a governance structure
 - Centralized personal control: all local governors are appointed
 - Decentralized administrative operation
 - Distinctively different from a federal system, or a feudal system
- The essence of the Junxian system
 - All independent social elites and aristocracies are eliminated
 - Facilitates the ultimate control over the empire by the emperor through personal control, through bureaucracy

The Imperial Exam System (科举制)

- The exam system is the core of imperial personal control
 - It selects those who are loyal and capable from the society to become bureaucrats
 - It eradicates independent social elites and aristocracies
 - It denies intellectual independence
 - With high powered incentives it buried independent intellectuals
- The exam system is the instrument of ideological control
 - The contents of the exams are designed by the emperor to promote ideologies which support the imperial system
 - Loyalty and obedience to the emperor and to the imperial system
- The creation, design, finance and operation of the imperial exam system were controlled by the emperor/imperial court
 - It was created since Han (136 BC) by the emperor
 - It is a necessary condition for the stability of the Junxian system¹⁵

The Imperial Land System (土地皇权制)

- Unlimited power of the emperor is embedded with the ultimate property rights of all the land in the entire empire
 - “private ownership” of land is restricted to using rights, including transferring of using rights
- The imperial land system is the property rights’ foundation for the unchallenged power of the emperor
- The imperial land system eradicates the economic foundation of independent social elites and aristocracy
 - e.g. explicit policy of taking away land from aristocracies in the name of protecting peasants in Han Dynasty (董仲舒-限民名田)
- The land system makes China distinctively different from the pre-constitutional reform institutions in UK, US, Japan
 - Long existing private ownership of land is a key factor in their reforms, in particular as a foundation of independent social forces¹⁶

From the imperial system to Totalitarianism

- Repeated failed constitutional reforms leads to revolution
 - Hundred Days' Reform (1898); the post-boxer reform (1901-08)
- Failed constitutional revolution paved the roads to totalitarianism
 - Republic Revolution (1911); civil wars; ill-fated 1946 constitution
- Consolidation of totalitarianism
 - Transplanting Soviet political/legal system and ideology at a full scale and centralization: the Party has all the control rights
 - Anti-Rightist campaign: ideologically eliminate constitutionalism
 - Nationalization/collectivization: deprive private property rights – the economic foundation of constitutionalism
- Regionally Decentralized Totalitarianism (RDT)
 - The Great Leap Forward (1959); the Cultural Revolution (1966)
 - Restoring the Junxian system in a totalitarian system

From totalitarianism to authoritarianism

- A transformation from the RDT to the RDA since the 1990s
 - The objective of the Party was changed to “economic development”
 - The central planning was largely replaced by markets
 - The dominance of state sector (a totalitarian feature) was partly replaced by private (an authoritarian feature)
 - These changes are codified in the 2004 Constitution
- The unchanged institutions (2004 vs. 1975 constitutions)
 - Unlimited and unchallenged power of the party-state
 - Highly centralized political/personal control through the Party
 - Highly decentralized to sub-nationals in administration, resources and economic control
 - Complete state ownership of all the land
- Sharing major features from its predecessors, the RDA regime is unable to resolve most socio-economic problems

China faces an uncertain long way

- Some Chinese reformers have reached a consensus
 - An economic reform without a political reform has reached its limit
 - The authoritarian regime itself is the biggest threat to the stability of the economy and the society
 - Launching constitutional reforms is necessary
- The resistance to a constitutional reform is very strong
 - Historically such reforms all failed in China – a key to understand China
 - The party-state's tolerance to constitutional reforms is less than their predecessors in the late imperial time (1908) and in the nationalist time (1946)
- The future of China critically depends on how far constitutional reforms can go in China

Happy Birthday to Janos!