

Corruption and Market Reform in China

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The transitional societies of the former communist world are important cases to consider if we wish to understand the relationship between corruption and liberalization. While these countries share a distinctive institutional heritage, their patterns of transition have diverged, falling into two broad categories. On the one hand, there are the nations of east and central Europe and the former Soviet Union (FSU) where the transition to a market economy has been accompanied by varying degrees of political democratization; on the other hand, nations such as China and Vietnam have embarked upon economic liberalization within a basically unchanged political framework of authoritarian state-socialism. This basic difference is likely to affect relationships between liberalization and corruption. In the transitional societies of Eastern Europe and the FSU, one can attempt to assess the effects of both economic and political change, whereas in the two Asian cases it is only possible as yet to assess the impact of economic reform. In the case of China, which is the focus of this article, the issue of the relationship between democratization and corruption enters not as a current reality but as a future possibility. However, it is a society in which market reforms have been fast and far-reaching and have been accompanied by increasingly pervasive and large-scale corruption. As such, China is a potentially fruitful context to explore the detailed dynamics of the relationship between corruption and economic liberalization.

1 The Nature of 'Corruption'

All shades of opinion both in China and abroad agree that politico-bureaucratic corruption, defined simply in terms of the abuse of public office for private gain, has increased during the era of post-Mao economic reform in terms of the numbers of people and layers of authority involved and the financial scale of abuse. Corruption emerged as a political issue in the mid-1980s and played an important role in fuelling the urban popular movements which led to the Beijing Massacre of June 4, 1989. In spite of strenuous efforts to stem the tide on the part of the post-Tiananmen leadership of the Chinese Communist Party (CCP), moreover, the rate of increase accelerated during the 1990s. While the phenomenon is particularly rife among officials in departments in charge of the domestic

economy and foreign economic relations, it has also spread into the judicial, cultural, educational and military spheres. Given the fact that the CCP is all-pervasive throughout both government and economy, corruption in these varying institutions reflects corruption within the party apparatus and membership themselves. Corruption also extends well beyond the politico-bureaucratic apparatus proper, to include professionals such as doctors and accountants and petty functionaries such as bank-tellers, ticket-sellers and shop-assistants.

This overall trend can be identified both through the official Chinese statistics on cases which have been identified and prosecuted and through the guesstimates of local and foreign observers (for example, political and business risk analysts in Hong Kong). By late 1993, for example, one of the main officials in charge of countering corruption, Deputy Procurator-General Lian Guoqing, admitted that corruption 'is now worse than at any other period since New China was founded in 1949. It has spread into the Party, government administration and every part of society, including politics, economy, ideology and culture'.¹ U.S. and European business people interviewed in Hong Kong in 1995 ranked China's 'business corruption performance' as Number 1 in Asia along with India and Indonesia (with Japan and Singapore ranking the lowest).²

While there is agreement on these broad descriptions of corruption in China, there is a great deal of unclarity about what 'corruption' entails in practice. While the notion of abuse of some form of institutional power for private ends underlies all perceptions, the range of phenomena included varies enormously. This partly reflects the rapid pace of socioeconomic change in China which is continually throwing up new forms of corruption and new labels to describe them. It also reflects the fact that corruption embodies a wide range of activities lying along a continuum which are distinguished by the clarity of the norm-breaking and the personal self-seeking involved. We can conveniently cut this continuum into three categories of 'corrupt' practice

(A, B and C). At one extreme, Class A corruption, are activities which are clearly illegal in formal terms and involve a personal or group infringement of institutional rules for individual greed. These involve 'economic crimes' such as smuggling, embezzlement of public funds, stealing state property, large-scale bribery, fraud and insider dealing in emergent stock markets, which are dealt with by legal means (including execution) for more serious and administrative means for less serious cases. Class B corruption involves the pervasive practice of 'state business' whereby individuals, political/administrative agencies and local governments act, often in highly entrepreneurial ways³, to seize opportunities for their own benefit by exploiting loopholes or contradictions in official regulations and using their institutional power to exploit the market potential of resources under their control. Thus, for example, government departments and state enterprises used the opportunities for arbitrage inherent in the 'two-track price policy' of the late 1980s to purchase scarce materials and goods at (low) official prices and sell them on at (high) market prices. Similarly, in the early 1990s, local governments and departments used their power to enter the real estate market by selling land directly under their control or using their powers to commandeer (often scarce agricultural) land to establish 'development zones' to attract foreign capital in the interests of themselves and their localities. Throughout the reform period it has also been a common practice for government departments to establish satellite companies for their own institutional purposes, partly to find places for personnel declared supernumerary by official governmental reforms, partly to build up the status of their departments (for example, by building impressive offices or houses for the workforce, or purchasing luxury foreign cars for the senior officials), partly to generate extra revenue to combat fiscal constraints and ultimately to guarantee an 'exit option' for senior officials who foresee a greater future in the non-state sectors of the economy. The beneficiaries of these activities include individual officials (and their friends and families), entire institutions and local communities as a whole. Class C corruption

¹ Lian was cited by Lincoln Kaye in the *Far Eastern Economic Review*, 10 September 1993, p 16.

² *The Economist*, May 20-27, 1995. I am grateful to Robert Wade for supplying this reference.

³ For analyses of the 'entrepreneurial state', see Blecher 1991 and White 1991.

reflects the influence of the pervasive networks of personal ties (*guanxi*) which cut across institutional boundaries and constitute an alternative pattern of social relations in contrast to the politico-administrative and market realms. These personal relations operate in ways similar to a 'gift economy' and give rise to patterns of behaviour which are often regarded as 'corrupt': preferential treatment for friends and relatives, 'bending' formal rules and regulations to benefit individuals or small groups, and conspicuous expenditures on gifts and entertainment which are deemed necessary to create and maintain *guanxi*.

These categories overlap to some extent and people vary as to where they would draw the line in defining corruption across A, B and C. There is only a clear consensus that Class A activity constitutes 'corruption': it is palpably illegal and is usually for purely personal enrichment at institutional or public expense. Class B is an ambiguous entity, however. While it may involve reprehensible or sharp practices, these are not necessarily for purely personal gain - on the contrary, they are commonly on behalf of institutions or localities and therefore may provide broader social benefits. The common element between A and B, however, is that each of these practices involves a more or less clearly illegitimate use of public power for individual or sectional purposes, whether by the 'exchange of power for money' (A) or 'power entering the market' (B). As such, they can both be popularly construed as 'official profiteering' and included as forms of 'corrupt' behaviour.

Class C behaviour is a pervasive societal phenomenon, however, and extends far beyond the realm of official power abuse. For most people, it is a way of making the system work in one's favour, of getting round the myriad institutional and regulatory obstacles to individual initiative. Thus popular perceptions on the issue are highly ambiguous: while people may excoriate high officials for allowing their children to benefit from their parents' position, they **would not** hesitate to engage in such practices **themselves**, albeit on a much smaller scale. Thus the attacks on the corruption involved in the **dubious** activities of the children of high officials can be seen less as a criticism of 'corruption' and more as an expression of resentment at the inequalities generated by the reforms and the fact

that certain groups are far better placed to benefit from the opportunities opened up. This is not a phenomenon peculiar to China; as Gillespie and Okruhlik remark (1991: 87), observers of corruption in many other countries have noted that 'the administration and state-dependent entrepreneurial groups benefit from corrupt activity only by the exclusion of other groups from the spoils'. From this perspective, it is not *guanxi* as such which are regarded as illegitimate, but their use by powerful groups (which may also include private business people and foreign capitalists) to increase their privileges ahead of the rest.

Even if we were to accept the narrow Class A as our working definition of corruption, the problem has become increasingly serious during an unprecedented era of economic reform in which an incumbent Communist leadership has moved the economy decisively away from central planning and vastly expanded the range of market activity in most sectors. As the extent of marketization has increased, corruption has increased **in tandem** and as the pace of marketization accelerated in the early 1990's, the incidence of corruption also mushroomed. How can we understand this relationship?

2 Corruption and Marketization: Some Explanations

Numerous conflicting explanations exist to explain the rise of corruption as an aspect of Chinese economic reforms. Conservative members of the CCP ruling elite see the problem as one of 'spiritual' corruption caused by 'unhealthy' capitalist practices entering the country from abroad. Reformist CCP leaders see corruption as an inevitable accompaniment of the transition from central planning to a market economy, reflecting a 'half-way house' in which market relations are developing, yet state agencies still retain a great deal of power. As a 'socialist market economy' is gradually established over the longer term, the problem of corruption will decrease. More radical commentators, both inside and outside the Party, go further and argue that, while it is true to see corruption as an offshoot of incomplete economic reform, its root cause is the Leninist political system which still pervades the economy and has not changed decisively during the reform era. The only effective answer to corruption, therefore, is not merely a continuation of

the market reforms, but also political reforms in the direction of greater pluralism, openness, freedom and popular participation.⁴

The currently most popular analytical framework used by the few Chinese academics who dare to tackle the topic is that of 'rent-seeking', an approach which fits most closely with the Chinese notion of 'exchanging power for money' (*quanqian jiaoyi*) (Hu and Kang 1994). While this may be useful in understanding much of Class A and B behaviour, the theory of 'rent-seeking' has certain analytical limitations in explaining the particular dynamics of corruption in China for several reasons: (i) If corruption reflects the desire of public officials to exploit their position for private benefit, why was it not more widespread before the reforms when the state's control over the society and economy was much greater? (ii) Since all government officials are potentially able to exploit their rents at any time, how does one account for the facts that, even now and within the same sector, some do and some don't, that people in similar positions may create and use rents in very different ways and that the incidence and scale of corruption are increasing when the ability of officials to assert direct control over economic resources is waning? (iii) Since rent-seeking theory tends to assume that the activity is a negative force in social terms by reducing the overall efficiency of the economy, it may be difficult to account for the fact that certain 'unorthodox' (Class B) behaviour by public officials, institutions and governments may bring clear corporate and public benefits and may make a positive contribution to economic development. Thus Smart (1993: 16) argues that 'in certain circumstances the rents might be socially desirable ... (In) a socialist society with subordinate capitalist relations of production, rent-seeking may serve to increase the efficiency of an economy by serving to overcome obstacles imposed by existing institutions'.

To capture the complexity of the dynamics of corruption in a post-socialist transitional society of the Chinese type, one needs to spread the conceptual net to include at least the following factors. First, it is important to analyse changes in the **institutional**

dynamics of the politico-bureaucratic system itself under the impact of market reform. It is commonly acknowledged that there was less 'corruption' in the sense of abuse of public office for private gain under the pre-reform Maoist system. However, if the very notion of corruption depends on a distinction between 'public' and 'private', then it is largely irrelevant to a system in which the 'public' encompassed and virtually obliterated the private. It is true that the Maoist system was pervaded by patron-client relations and there was a system of unequal privileges based on political and administrative power, but these were *de facto* institutionalized features of the system and, except in extreme cases, would not qualify for the term 'corruption', particularly in the Class A sense of the word. The latter was kept in check by a pervasive system of institutional controls at the macro- and micro- levels, organized and implemented by the CCP apparatus.

This does not mean that pre-reform China was largely free of corruption. Indeed, there had been large-scale recurrent campaigns against corruption up until the eve of the Cultural Revolution and the Cultural Revolution itself in its early stages involved an often violent mass movement against allegedly corrupt officials. However, the Cultural Revolution imposed such a high level of conformity on both officials and populace and their insecurity increased to such an extent that blatantly corrupt behaviour was too dangerous to contemplate. By contrast, the reform era has brought about a pervasive (and partly unintentional) dispersion of power and control: from central to regional/local governments, from governments at all levels to their departmental components and from governmental agencies of all kinds to increasingly assertive socioeconomic groups (such as state enterprise managers and private business people). This means that not only has the range of institutional and local discretion substantially increased within the political system, but also the capacity of governments at all levels to implement policies and enforce regulations - including those designed to combat corruption - has substantially diminished.

⁴ For an example of this approach, see the proposal by 12 prominent dissidents submitted to the Standing Committee of the National People's Congress in

February 1995, reported in Lien Ho Pao, Hong Kong and translated in BBC, **Summary of World Broadcasts: Far East** (hereafter SWB:FE), 2241, 2 March 1995.

Second, Chinese observers stress the importance of **public values and personal morality**. Indeed the CCP organ *People's Daily* published an article reminding readers of the Confucian principle that 'government officials should embody uprightness',⁵ echoing the Leninist-Maoist emphasis on the need for officials to have a 'correct workstyle and ideological standpoint'. In short, clean people make for clean government and, even faced with temptations arising from a defective regulatory environment, 'a high quality person with honesty and self-discipline may "repeatedly walk along the riverside without wetting his shoes"'.⁶ But the concern about public morality is not confined to the CCP leadership; it is also widespread among the general population who complain that the reforms have swamped the previous traditions of social solidarity and mutual responsibility in a wave of 'money-making fever'. Radical critics of the regime are also sensitive to the issue, complaining of a 'value vacuum' and a 'collapse of faith' which means that 'some people have forgotten the most rudimentary sense of righteousness essential to a society and of professional ethics'.⁷

In the decadent environment of the mid 1990s, it is commonplace to hear people indulging in nostalgia about the purer and cleaner days before the reforms. In pre-reform society, even though the convolutions of the Cultural Revolution had created a great deal of cynicism about official standards of public morality, an apparently large number of the Party/government apparatus continued to adhere to at least some of the principles of the official ideology. As the reforms proceeded during the 1980s and the official 'strategic task' of the CCP shifted from political class struggle to economic modernization, Maoist political morality became an increasingly irrelevant attribute of public office. New-style officials were to show their mettle by showing initiative and entrepreneurship in organizing economic progress. Moreover, although attempts were still made to socialize the bureaucratic elite in the values of the old ideology, 'ideological and political education' was not given high priority and had diminishing effects.⁸ The depoliticization of the

elite has been accompanied by an even more intense depoliticization of society. Whether one is speaking of Class A, B or C corruption, they spell various ways of 'getting a piece of the action' in an environment of increasing normative anomie in which social motivations and relationships are becoming rapidly commercialized but a new framework of social morality has not yet arisen to replace that of the *ancien regime*.

The third element which has changed in the reform era is that the **opportunities** for corruption have vastly increased. The gradual dismantling of the previous system of directive planning, the increasing commercialization of the public sector, and the rise of vibrant new economic sectors such as small collectives, household or self-employed businesses, larger scale private firms and foreign-invested enterprises (notably joint ventures) have created a myriad of opportunities for officials to use their still substantial powers to benefit themselves and their clientele. It is not merely economic reform but also economic growth which has fuelled corruption because it has rapidly expanded the incentives for malfeasance and created a 'demonstration effect' by opening up a widening gap between the *nouveaux riches* in business and government employees on fixed and relatively low salaries. Increasingly attractive opportunities are made even more tempting by the regulatory vacuum or ambiguity which officials face in exercising their powers. This latter reflects in part the transitional 'half-way house' wherein the previous set of rules for organizing governmental and economic life have broken down but a new set is not yet in place. In part it reflects the deeper processes of political and administrative decentralization. Not only do officials have more leeway to exploit loopholes in the regulatory framework, but they are more likely to avoid detection and retribution in doing so.

These increasing opportunities have been coupled with an increasing **demand** for official malfeasance on the part of newly rising economic forces who find it necessary or advantageous to seek official

⁵ Dong Yan, 'Government officials must be upright', *Renmin Ribao* (People's Daily), Beijing, 2 August 1993, in *SWB:FE*, 1769, 17 August 1993.

⁶ The words are those of those of CCP General Secretary, Jiang Zemin, in a speech on 23 January 1995, reported by NCNA, Beijing, 1 March 1995.

⁷ See footnote 4.

⁸ For a more detailed account of this 'ideological decay', see White 1993, Chapter 5.

assistance to facilitate their business or gain competitive advantage against their business rivals. This is leading to an increasingly widespread and quasi-institutionalized system of personal and organizational relationships between officials and business people to their mutual benefit. In Chinese, this is described as 'an exchange between people with money but no power, and people with power but no money'. This is not necessarily perceived as an 'unhealthy' yet inevitable result of the transition to a market economy, but rather as a potentially long-term arrangement which can create a business environment conducive to economic growth.

Analysts of this relationship have argued that it should be perceived as a positive-sum relationship of mutually beneficial inter-dependence which can further economic development while at the same time strengthening **both** the state and (more powerful sections of) the emergent private sector. This merger of elites has been remarked upon by researchers working on the East Asian capitalist NICs, notably South Korea (Suh 1989), and on the Chinese urban economy, particularly in the more dynamic coastal areas. For example, Solinger (1992: 121) concludes that 'the essential economic monolith of the old party-state now shapes official and merchant alike; both have become dependent, mutually interpenetrated semiclasses, even as both share a new kind of dependence on the state'. David Wank, on the basis of his fascinating study of state-business relations in the east-coast commercial city of Xiamen, concludes that 'the local state-society symbiosis is difficult to conceive as a transitional or corrupt phenomenon; rather it is based on patterns of a mutually beneficial alliance that are the sum of individual calculations of advantage' (1992: 21; see also Wank 1995). The relationships are cemented by the morality and social conventions of the *guanxi* relationship, based on personal trust and reciprocity, the terrain of our Class C corruption. But then one person's 'trust' is another person's 'corruption'.

To summarize, Chinese market reforms have created an environment in which an official has greater freedom to abuse his or her position, has more motivation to do so and less motivation not to, has an expanding variety of channels and opportunities, and has many well-resourced people willing to join the transaction on terms which offer

security as well as material advantage. If we look at the problem of corruption at the level of the individual official or agency therefore, it is not surprising that levels have increased steadily during the reform era and have accelerated along with the increasing pace of reform in the mid 1990s. During this latter period, moreover, there are signs that Chinese society has begun a new phase of structural change, of which 'corruption' is but one manifestation. One can detect a profound process of **class transformation** which, at its roots, embodies the emergence of a new, post-communist bourgeoisie through a dual process: on the one hand, a stratum of economic influentials is rising in the 'private' sector aided by connections with state officials and foreign (mainly overseas Chinese) business and, on the other hand, state officials are attempting to convert their power into control over economic assets, transforming political into economic capital.

This process can be seen as a response to the changing political context of the 1990s. There appears to have been a rapidly growing recognition among public functionaries that 'the writing is on the wall', prompted by a number of events and trends: the collapse of state socialism in Eastern Europe and the FSU, the acceleration of the Chinese economic reforms from early 1992 onwards and the increasing pressure for governmental reforms (notably involving the reduction of state personnel). These changes created a growing perception that 'power is something to be abused before it becomes useless'. Class A corruption is a risky way of doing this, whereas Class B activities offer a multitude of methods. These range from using bureaucratic privileges to secure private houses on highly favourable terms, thereby ending officials' dependence on their work-unit for housing; setting up satellite companies to generate capital or open up lucrative jobs; engaging in real estate speculation through joint ventures with domestic or foreign business or speculative trading in the new stock markets; or gaining priority access to the initial share issues of state enterprises being put on a joint-stock basis. Some of these ventures result in the establishment of new and productive enterprises, but to a greater or lesser extent they are financed by a drain of state assets either for free or on a knockdown basis. One report, based on a briefing from the head of the National Administration of State Property, concluded: 'If state assets are likened to a chest of

valuables, some people are opening big and small holes in the bottom of the chest and the state assets are running out quietly and unnoticed'.⁹ This usurpation and exploitation of state assets was particularly visible in the 'real estate fever' of the early 1990s when local departments and agencies sold land leases to developers or invested in real estate themselves, profiting from the concurrent rise in land values. This was 'rent-seeking' in a literal sense. Some Chinese observers describe this process as one of 'primitive accumulation' and point out that the officials involved in it - particularly the older generation who have been working in and for the state for a long time - have developed a sense of proprietorship over state assets. They feel that, since the assets are going to be alienated in any case, they are the righteous inheritors because they worked so long and suffered so much to create them. This usurpation is thus not perceived as 'corrupt', but as a legitimate reward for a lifetime's service.

From this broader perspective, the tide of corruption sweeping China in the mid 1990s is indeed a phenomenon of transition, but not merely in the sense of a transition in the economic system from directive planning to a market economy, but also of the creation of a new class of influentials created through a merger of officialdom and business. Optimists interviewed in China view this latter transition as taking place over a relatively short period (say 10-15 years), expecting the wave of usurpation to reach a peak and then recede as a truly 'private' business class forms and the state

apparatus can be reconstituted along professional civil service lines with limited responsibilities. Self-styled realists point in conversation to the distinctive nature of emergent Chinese state-business relations - notably the omnipresence and unquenchability of *guanxi* relations - and argue that the 'public-private' distinction will not assume the clarity assumed by Western dichotomous models of state/market, state/civil society or state/business. Rather the boundary will be spanned and blurred by a dense latticework of mutually advantageous, personalistic power-money exchanges which can be expected to persist over the long term, regardless of changes in the overall political and institutional contexts. In other words, even if Class A corruption can be controlled and Class B corruption loses its historical purpose and withers away, Class C behaviour will remain pervasive whether one chooses to call it 'corruption' or not. To the extent that the realists are right - and the research by Wank, Solinger and others suggests that they are - the key developmental question is whether this form of symbiosis is likely to prove economically productive over the longer term - in Chinese terminology, whether it pours oil or sand into the machinery of economic development. This opens up the broader comparative question of whether rent-seeking alliances between political and business classes are developmentally negative or positive, an issue which has long been raised in the context of other developing societies. The sustainability of the current Chinese growth momentum depends heavily on the answer to this question.

⁹ 'State-owned assets are running off', **Guangming Ribao** (Glorious Daily), Beijing, 5 October 1993, in **SWB:FE**, 1824, 20 October 1993.

¹⁰ For example, by Boone (1990) in the case of Senegal and Hutchcroft (1991) in the case of the Philippines.

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