

THE STATE AND THE MAYOR ECONOMY

Today, hundreds of industrial parks are peppered across the full length and breadth of China's vast landscape. In recent years, more than one hundred fifty high-tech development zones have been built in small and medium-size cities around the country, with the aim of developing commercial hubs for electronics, biomedicine, and clean energy. Nearly all of China's twenty-three provinces and four municipalities have experimental commercial development projects under way: there is one in Guangdong for a maritime silk road, one in Fujian for connectivity investments with Taiwan, one in Shanghai to position the city as a center for international financial services, and many others. Within the city of Shanghai, individual districts choose a particular focus like trade logistics, shipping, high tech, finance, or industrial development. In addition to conventional power and steel plants, there is a plethora of cultural centers, museums, exhibition galleries, and tourism projects cropping up as China finds creative new ways to boost economic growth through regional and local initiatives.

This phenomenon is known as the mayor economy. In recent decades, pioneering local government officials have rushed at a frenetic pace to expand their local economies, transforming former fishing villages and farmland to technology hubs and industrial centers. These officials vie with each other for primacy in everything from economic growth to foreign investment, from the number of industrial, trade, and horticultural exhibitions to the size of cultural events like concerts and film festivals. Local governments busily commission landmark bridges, skyscrapers, opera

houses, and gymnasiums with the latest avant-garde architecture. In 2019, more than three thousand exhibitions around the country showcased the latest environmental technology or new beauty product or breakthrough in gift wrapping—the focus of fifty-eight exhibits around the country. In Shanghai alone, a visitor would need to visit more than one new exhibition every day in order to see them all in any given year. Each expo aims to be larger than the next.

When foreign officials and business executives come to visit China, they are invariably impressed by the enthusiasm of provincial governors, municipal and county mayors, and even village chiefs as they rattle off awesome statistics about local industry, agriculture, services, import and export growth, and most especially the measures they are taking to improve their investment climate and ease of doing business. In China, the mayor economy rivals the market economy in importance.

Western countries often complain that there is too much state in China—that its inefficiencies, meddling, and rigidity combine to stifle private business development and create drag on the economy. It's certainly true that the Chinese state can sometimes throw obstacles in a business's way for its own reason, but much less known is the fact that it purposefully seeks to offset the rigidities of a central authority and its institutional deficiencies by giving tremendous economic authority and autonomy to local governments. In the mayor economy, local governments have strong incentives to help promising businesses overcome barriers and to foster innovation in their locality. Adam Smith's concept of invisible hands working behind the scenes is, in the case of China, replaced by the thousand-arm Buddha's extended and very visible hands.

The best term for describing China's developmental paradigm is “political economy”: in China the state and the economy are deeply intertwined. Sometimes one moves to take the wheel, and at other times they switch seats, but rarely does either operate in isolation. When we consider the China model, it is this political economy that is truly distinctive. Complex and nuanced mechanisms embedded in the system—incentive schemes, competition, and a fluid system of checks and balances at work within

various levels of government and business—make it one of the most fascinating subjects of study when it comes to understanding China.

There are three prominent features of the Chinese state. The first is its power: it has the resources and administrative skill to mobilize rapid collective action in service of the nation's goals. The second is its structure of political centralization paired with economic decentralization, which makes room for creative local business activity under central guidance. The third feature is its adaptability. It can adapt to the changing circumstances rapidly and flexibly, dialing back policy measures if they have gone too far and shifting between priorities when the situation warrants it.

In their seminal book *Why Nations Fail*, Daron Acemoglu and James A. Robinson argue that countries with narrow concentrations of political power give rise to institutions that allow the ruling elite to exploit the rest of the nation, instead of emphasizing growth, new technologies, education, and investment. China certainly fits the bill when it comes to power concentration, but it is far from being an extractive state. Instead of limiting growth by siphoning off the nation's wealth to a small elite, the state has encouraged twenty million private firms to spring up almost overnight; rather than inhibit new technologies, the government is fueling a national drive to make China the global leader in pioneering new technology, deploying trillions of dollars to support entrepreneurs, research centers, universities, and high-tech zones. As for the Chinese people, not only do they save and invest long term, they also spend huge sums to educate their children based on rosy expectations of the future. Clearly, something is working. Some would even argue that political concentration prevents political gridlock, while others believe that it was important for delivering China's stellar growth.^[1] In this chapter we take a closer look at the role the state plays in this larger dynamic.

A Central Government and a Political Party Intertwine

The onset of the COVID-19 pandemic in March 2020 gave me firsthand experience of the reach of the state. I had returned to Beijing from London just before the outbreak engulfed the UK. The airport felt like a theater for military operations—hundreds of men and women in uniform were strategically placed at various checkpoints, questioning every passenger, accumulating detailed information before sorting visitors into various hotels. It took me about eight hours to clear all the checkpoints, and at the end of the process I was introduced to a member of the residential committee that would make sure that I honored my mandatory fourteen-day quarantine.

In nearly every Chinese town or city, large or small, residential neighborhoods include a residential committee comprised mostly of older volunteers; it's a Communist Party cell, tightly organized and charged with administering the locale. The chief of the committee, often an older woman, wields enormous power. Even ministerial-level officials in our compound defer to this woman, who enforces residential rules and regulations. For the next fourteen days a residential committee member checked on me twice a day to make sure that I had not sneaked out of my apartment. The door was sealed from the outside with a paper strip. When daily necessities were delivered, the strip was temporarily removed and then affixed again. I had to report on my health via a community online chat that was administered by a committee member. This system would be difficult to create or accept in many parts of the world, but Chinese citizens readily comply. They accept limitations on privacy in exchange for the sense of safety provided by a highly organized, capable, and paternalistic Chinese Communist Party. The party's network and organizational capacity proves helpful in times of crisis, like a global pandemic.

In China, the Communist Party and the government each function according to its respective mandate, but instead of working in parallel, they are intertwined. They function like a double helix, stabilized by cross-links between the two systems. Unlike the classic structure of DNA, however, the two systems merge at the top. China is a socialist republic run by a single political party, the Communist Party of China, or CPC. Its Politburo stands at the zenith of power and is directed by the Standing Committee, which makes

decisions about major policies, legislation, and other important matters. At the next level down, power splits into two branches, with the party on one side, and the legislature and government on the other. The chairman of the National People's Congress heads up the legislature, while the premier directs the government; both are members of the Standing Committee, where the two strands of China's double helix converge. The secretary general of the party serves both as head of the state and as chairman of the Central Military Committee, assuring that the party maintains control over the military.

On the government side, there are a number of ministries under the State Council and provincial governments (see Figure 5.1 for a hierarchy of administrative divisions). The same parallel party/government structure is at work here. The highest-ranked leader in any organization at any level is invariably the party secretary. Likewise, in a municipal government, the municipal party secretary ranks above the mayor. One represents the party and the other represents the government, and both work closely together.

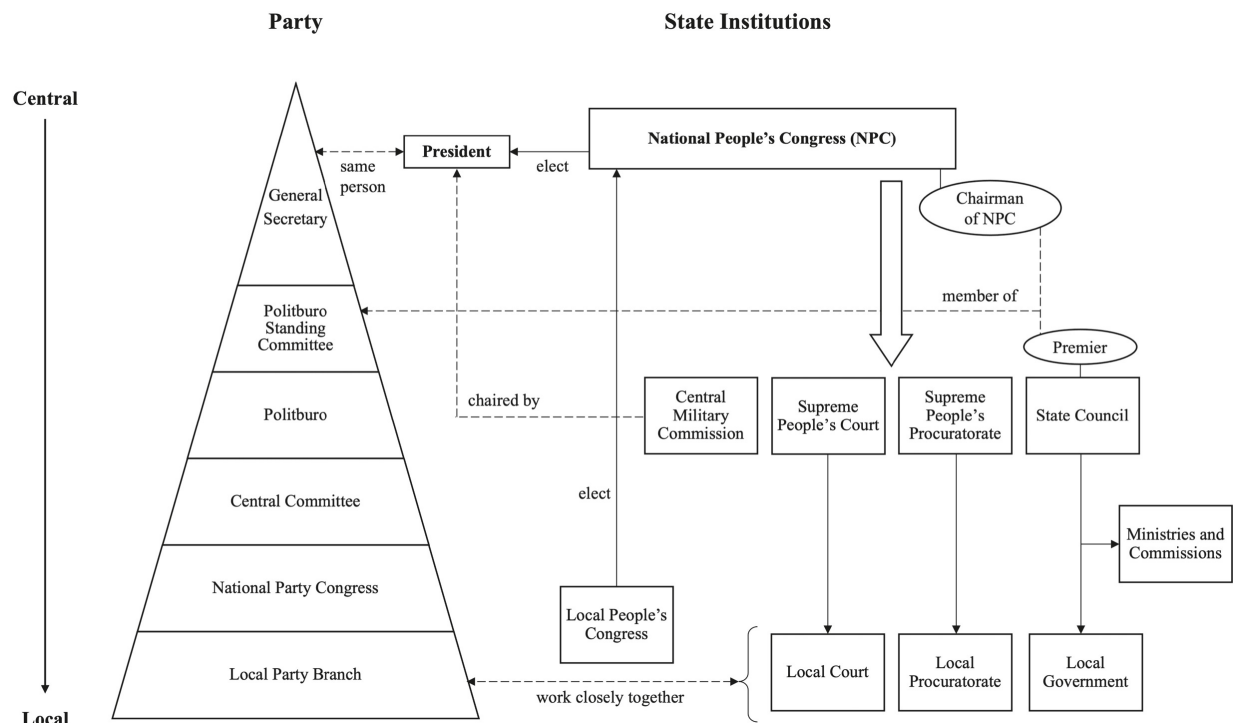


Figure 5.1: Hierarchy of Government Administrative Divisions

China's concentration of political power dates back to imperial times, when the emperor held supreme control. Today, it is exercised by the top leadership of the Communist Party, but this is not the case when it comes to day-to-day management of the economy; here, power emanates outward from the center to the local level. It is local officials in provinces, municipalities, counties, and towns who push for local development, meet growth targets, implement reforms, and attract foreign investment. These are the local cadres who have transformed fishing villages and rural backwaters into modern export hubs, manufacturing centers, and high-tech economic zones. Behind every economic success story stands a local government that has supported it at every step along the way.

	Division	2020
Province	Provincial Level	23
Municipality		4
Autonomous Region		5
Special Administrative Region		2
Prefecture-Level City	Prefectural Level	293
District	County Level	973
County-Level City		388
County		1,312
Town	Township Level	21,157
Township		7,693
Subdistrict		8,773

Figure 5.2

Data source: Statistical table of administrative divisions of the People's Republic of China (December 31, 2020), <http://xzqh.mca.gov.cn/statistics/2020.html>.

This model of political concentration of power married with economic decentralization is unique to the Chinese state. It stands apart from wholly centralized states like the former Soviet Union, where all decisions were made at the top, and every major economic policy was coordinated and

implemented by specialized central ministries. It also differs from American-style federalism, where the economic clout of state governors and city mayors elected by their constituents comes primarily in the form of fiscal allocations from state legislatures. Chinese local officials directly control vast resources, from land, energy, and raw materials to local banks. They can make and enforce regulations, build infrastructure, and undertake major commercial projects. In China the central government takes care of domestic and international politics and sets overall economic policy, while local governments tend to the economy itself.

CHINA INC.

China's unique governance structure became a turbocharged engine for economic development. But how, exactly, did this work? One way economists approach the Chinese state is by imagining it as a gargantuan corporation, China Inc., whose goal is to maximize both revenue and sustainability by motivating employees, ensuring that innovative ideas are not buried under layers of bureaucracy, and promoting healthy debate for every important decision. A fundamental challenge for China Inc. is how to align the best interests of its employees not just with the goals of management but also with its shareholders—the general public.

The Politburo's Standing Committee, which consists of the most important officials in the country, functions much like the senior management team of a giant corporation, with executives like a chief operating officer, head of human resources, and chief marketing officer, each in charge of a particular domain. Local government officials work much like department managers, finding ways to meet objectives set out by the central leadership. Power permeates the hierarchy layer by layer, from the province's boss to the municipal and city mayor, the county head, and the village chief.

As in any large corporation, designing an effective incentive structure is crucial. In China Inc., this is based on a governance system called *nomenclatura*, which appoints officials to key positions throughout the government and the party's own hierarchy. The Organizational Ministry of the

Central Committee is responsible for screening cadres for promotion to senior positions in the party, the government, and major SOEs. This powerful ministry is effectively the largest human resources department in the world. All ambitious officials dream of rising through the party's ranks: city mayors set their sights on provincial governor or party secretary posts, and those who have already become province-level leaders aspire to the higher rungs of central government, even the supreme Politburo. Personnel management is the central government's mechanism for encouraging excellence and enforcing compliance. It decides which local officials are promoted, demoted, appointed to key positions, or thrown in jail on criminal charges.

In China Inc., economic achievement by local government officials translates into political capital. That is to say, those who can deliver economic growth in their region have a greater chance to be promoted in the party hierarchy. The official criteria for promotion include integrity, diligence, and competence, but performance—how well the local official manages the local economy—is essential. Historically, the primary yardstick in this regard has been GDP growth, although, as we'll see later, this is changing. Although imperfect as a measure of people's overall welfare, GDP does gauge how much the economy has expanded over a particular period, and how much employment has been created.

China Inc.'s ambitious annual growth target fosters competition among local governments to accelerate GDP growth in their respective regions, a phenomenon often referred to as GDP worship. Major media outlets play their part by publishing annual rankings of GDP growth rates across regions for everyone to peruse and gossip about. Why did the province of Jiangsu grow at only 10 percent this year versus 11 percent last year? And what's going on in the neighboring province of Anhui, with its 12 percent rate?

The Mayor Economy

The city of Kunshan offers a good example of how a local government single-handedly transformed an unremarkable agricultural town into a

booming industrial and high-tech city. In 1978, its residents were saving an average of about US\$12 per year. Sandwiched between two powerful neighboring cities, Shanghai and Suzhou, Kunshan had no chance of successfully vying for the attention of US and European multinationals. So its local government decided to reinvent itself as a niche market for wealthy Taiwanese investors. To do so, it initiated a wide range of business-friendly policies, including financial and fiscal support, land leases, one-stop license applications, and lower thresholds for capital. In addition, it adopted a tough no-tolerance policy on corruption. As a result, Taiwanese investors felt both sought after and safe. When several fell sick on one visit and were hospitalized, local leaders came to visit them and personally attended to their well-being and recovery. In the wake of this support and warmth, more than four thousand new companies sprang up in Kunshan.

Success stories like this also highlight the variety of motives that drive local authorities. Some are intrinsic: as we've seen, the importance of achievement is deeply embedded in Confucian culture. Other inspirations are external, including the possibility of greater responsibility at a higher level and popular acclaim. And, as is so often the case, success breeds success. Higher GDP generates more income, which local officials can then allocate as they see fit. These resources come in handy. Local government can spend the funds on building a subway system, the hallmark of a prestigious city. They can improve the environment, which has recently taken on more significance in the metrics of performance evaluation, cleaning up lakes and rivers and tackling air pollution and waste. They can finance social programs, including education, social welfare, and healthcare. A successful local government can also preen its tail feathers to attract new investment by constructing spectacular landmark buildings, as well as organizing world-class exhibitions and festivals. When a town is upgraded to a city, or a county-level city becomes a prefecture-level city, these promotions bring local officials prestige, visibility, and political clout.

This explains why local government officials not only are invested in promoting their own state enterprises but also actively support the private sector. This was not always the case. Until the 1990s, state-owned

enterprises commanded wide swaths of the economy, including consumer products, from household appliances to bicycles to beer. Highly lucrative, SOEs drew local attention and resources because part of their profits went directly into local state coffers. But as many local SOEs became unprofitable or went bankrupt over time, local officials turned to promoting more innovative and resilient private enterprises, tending the seeds of their development.

Early on in this process, in the 1980s, when private-sector companies began to be politically countenanced but still bore the stigma of capitalism, officials sometimes dressed them up as collective enterprises, giving them what became known as “red hats” to wear while carrying out their normal business. As the state became more tolerant of private enterprise—and it proved its effectiveness and value—local governments began to actively woo the best firms, engaging in beauty contests that included lavish tax breaks and flexible regulations.

Effectiveness is certainly a key factor in this process. As political scientist Francis Fukuyama notes in his book *Political Order and Political Decay*, a meritocratic bureaucracy is essential to the success of a modern state. Luckily for China, this essential ingredient has been baked into its civics since the third century BC, as we’ve seen. But just as with any other system, patronage also matters. In Western countries, the winning political party lavishes government jobs on its supporters. In China, patrons are particularly important because they are associated with loyalty; senior leaders who promote their own protégés can count on their unfailing political support, particularly in times of crisis.^[2] Political connections to senior party leaders are particularly important for senior-level promotions. Although officials with strong political connections would not be promoted if they were woefully incompetent or lacked valuable experience, a local leader who performs well but has no political connections is likely to hit a glass ceiling. Top-performing *and* well-connected provincial leaders have gone on to become the nation’s highest-ranked cadres. In fact, all three general secretaries of the Chinese Communist Party since Deng Xiaoping were once provincial leaders: Jiang Zemin was the head of Shanghai, Hu Jintao was

provincial head of Guizhou and Tibet, and Xi Jinping was the leader of Zhejiang and Fujian provinces.

As we've seen, a complex system of mechanisms and incentives is instrumental to China's economic growth. But the astute student of economics might ask why this extraordinary effort to engage local government participation was needed in the first place. Wouldn't the markets just do the work by themselves? The state is forced to take unusual measures because free market forces are still not in full swing in China. Some markets are still tightly controlled, the financial system is still adolescent, and inadequacies in the legal system make China's economy incapable of functioning as mature market economies do. It took hundreds of years for Western economies to develop markets that function relatively smoothly on their own, and they still contain many wrinkles that warrant government intervention. As we have seen, China's strong government coupled with weak formal institutions distinguishes it from other economies, and explains why China's hybrid market and mayor economy came into being and works so well under the circumstances.

In most countries, an ineffectual state underlies many major problems. China is not in this situation. When needed, the Chinese state has the capacity to intervene, providing money, logistics, and even the military, as I saw firsthand when China was faced with COVID-19. When it comes to the economy, China also provides a stabilizing political presence—the ability to stay the course when pursuing long-term goals and to resist pressure from short-term exigencies and special interest groups. For better and—sometimes, as we will see—for worse, China's is a political economy.

CHANGE, INNOVATION, AND RISK

One big factor in the success of China's economy is its ability to embrace change, innovation, and risk—qualities we do not typically associate with politically centralized regimes. As is so often the case, this tone was first established at the top. It was none other than Deng Xiaoping who threw his weight behind the local cadres when reform initiatives were being resisted

by conservative party leaders clinging to ideology. Change is difficult, and in the late 1970s China's new economic landscape was terra incognita. At a time when nobody really understood how market economies worked, it required a giant leap of faith to grant so much economic power to the local officials. The stakes were high, but from the beginning, local chiefs were encouraged to try out bold ideas.

Importantly, there were few penalties meted out for trying and failing. Because these efforts were local, the fallout from failure was contained, but successful plans were lauded and emulated around the nation, their sponsors showered with recognition and praise. This high-risk, high-reward environment led to the development of an entrepreneurial state within a highly centralized one. Officials were encouraged to bend or even break rules and traditions, to come up with even the most outlandish original ideas, and to make creative or intuitive decisions even when the outcome was uncertain. They were both emboldened and empowered.

As it turned out, sharing power at the local level made sense in many ways. It was local officials, after all, who knew local conditions best, had the most extensive local networks, and knew how to collect local information and to make informed decisions on allocating resources. This put them in a far better position than a distant central government to develop their local economy. Indeed, a perennial dilemma for political centralization is that while it is good at establishing long-term goals for the greater good, it is often associated with distant bureaucracies insensitive to local needs. China's local officials enjoyed substantial autonomy to deviate from the norm, and they ran with it.

FLIES IN THE KITCHEN: CORRUPTION

For all its many benefits, a system that confers power and resources on local officials also comes with its downsides. One is that it creates ample opportunity for corruption. When development projects are up for grabs, there are many rent-seeking opportunities along the way: issuing licenses, channeling finances through local state banks, and auctioning land leases all

offer local government officials many opportunities for profiteering. For some, the temptation to abuse the power and divert funds into private pockets can prove irresistible. Many of them think, *If I've been so instrumental in growing the economic pie, why shouldn't I have a slice?* Some economists even argue that in developing countries, a certain amount of graft is conducive to growth: it's the oil that greases the wheels when public institutions function poorly.

Throughout history Chinese rulers have struggled with the dilemma of how to provide incentives without letting the corrosive effect of corruption debilitate the system. In the feudal times, the emperor wore a crown that could block out whatever he chose not to see or hear. Literally. It included a small curtain of black gauze along with twelve tassels ornamented with jade beads, with a nugget of jade on each side that could serve as an earplug. Lowering the tassels or inserting the plugs allowed the emperor to see and hear only what he chose. The Chinese crown is symbolic of the ruling style of all Chinese emperors: because paramount importance is placed on keeping the overall situation under control, tasks that might prove impossible get ignored—like purging the kingdom of evil, corruption, political intrigues, or feuds. As the ancient Chinese saying goes, “No fish can survive in water that is too pure.”

Today, China's central authority is well aware that corruption gnaws away at a system like termites, doing no apparent damage to the structure until it suddenly collapses. On taking power in 2013, President Xi lost no time in launching the most sweeping anti-graft campaign in the nation's modern history. Some 2.3 million officials at various levels have been punished for violating party rules or state laws. These officials run the gamut from elite “tigers” to common household “flies.” In 2017, of the 527,000 officials who were punished, 58 were officials at the provincial or ministerial level or higher, 3,300 were at the bureau level, 21,000 were at the county level, 78,000 were at the town level, 97,000 were ordinary cadres, and the rest were from villages or local enterprises.^[3] This highlights the inherent challenges of monitoring and controlling millions of local officials spread around the country. There may be political motivations

behind the drive, but the scope, depth, and endurance of the program proves the seriousness of the intention to sever the corrosive links fostered in an era of rapid but disorderly growth.

When Zhao Zhengyong, the former party secretary of Shaanxi Province, left his post as provincial party secretary for a seat on the National People's Congress, a number of his business dealings that had led to huge personal gains were made public. The most notorious was a scheme with private developers to build expensive villas on the northern slope of Qinling Mountain, part of a protected area of enormous natural beauty and spiritual significance, known as the Alps of central China. After repeated warnings from top leaders, Zhao falsely reported that the villas had been demolished and the problem solved. When Zhao's various dealings finally came to light, he and a number of his accomplices were arrested and imprisoned.

As this example illustrates, corruption in China is no longer countenanced with a wink and a nod. The national cleanup has received wide public support and is an important contributor to satisfaction with the government, as evidenced in public surveys. But it also comes with its own set of risks for the economy. Without graft as an incentive, local officials may become less motivated to foster growth. They may become reluctant to commit themselves to major undertakings—including positive reforms—for fear they may draw unwanted attention. When the rules are changing, or being enforced differently, it's natural to err on the side of caution by choosing to do little or nothing. Anti-corruption programs can therefore create unintended inertia on the part of the cadres, leading to a slowdown in economic growth. For a party determined to shore up its image of good governance, the anti-corruption drive won't be aborted for fear of losing economic steam. To address this unintended consequence, the party is now increasingly monitoring the behavior of its cadres and punishing passive resistance to anti-corruption by apathy, inertia, sloth, or total inactivity.

Maintaining Control

In addition to corruption, a long-standing issue throughout Chinese history has been rebellious local chiefs in a vast country populated by diverse cultures and ethnicities. Granting autonomy is a good way to boost morale and get things done, but it also has the natural effect of shifting power away from the center. Consolidating and maintaining that power has always been a challenge for China's top leaders, and it is one of the reasons why Mao kicked off the Cultural Revolution in 1966. One way to keep regions from banding together to oppose mandates from the central government is by creating competition, which serves this valuable second purpose, in addition to providing an incentive to succeed.

To foster a competitive environment, the state has come up with all kinds of ways to quantify and reward achievement. A yardstick competition measures both absolute performance (such as GDP growth) and relative performance among officials. In a tournament-style competition, only relative performance matters. In a qualifying competition, local government officials have to meet basic criteria before even being allowed to join the challenge. In an elimination competition, government officials who don't meet a certain standard are no longer eligible for promotion regardless of their scorecards in other domains. What makes this competitive model work is the central government's tight grip on personnel decisions through its personnel ministry, and the fact that only a few cadres will gain appointment to highly coveted senior positions.

Competition, however, can be a double-edged sword. Intense competition between local government officials has contributed to local protectionism, as we have seen in the example of local automobile companies in chapter 4—despite the central government's sporadically successful efforts to encourage collaboration. Local governments can become so engrossed in creating unique economic identities that they work in silos, with little interest in cooperating with their neighbors even when economic synergies warrant it. Their primary goal becomes protecting their own industries and firms against outside competitors, and can extend to helping local enterprises dodge their responsibilities for quality control and meeting environmental standards. This local protectionism has a big impact on the aggregate economy. A 2019

study by economists Trevor Tombe and Xiaodong Zhu shows that removing *internal* trade barriers can result in much higher gains to productivity than boosting external trade via globalization.^[4] These internal barriers not only reduce the nation's ability to take advantage of scale, synergy, and complementary strengths but also produce excessive administrative and jurisdictional constraints.

To prevent local intractability, the central government has another major tool at its disposal. No government official holding an important position is allowed to stay in any one place for too long. Cadre rotation is important because it limits the possibility of local officials building their own independent fiefdoms, where loyalty goes to the local boss rather than to the party's Central Committee. After most party secretaries and governors serve a five-year term, they move on to a new posting. Provincial bosses are brought in from other regions to prevent long-term consolidation of power.

Rotation plays other important roles. When capable, reform-minded local officials from more prosperous coastal provinces are transferred to the hinterlands, this fresh blood serves to strengthen local leadership and beef up local economies. Fresh transfusions of talent help lower-income regions broaden their horizons while promoting regional cooperation. And exposing officials to a variety of challenging situations that sharpen their leadership skills is also useful for grooming future leaders.

THE MIXED BLESSINGS OF GDP

As the jocular saying goes, "GDP figures produce the officials, and officials produce the GDP figures." Given China's all-important system of incentives and competitions, it is not surprising that local officials could be tempted to fudge their GDP numbers. Researchers have found that since 2004, the sum of China's provincial GDP—which should equal the national GDP—is consistently 5 percent higher, indicating that the provincial numbers are being inflated.^[5] But massaging GDP figures is a minor problem compared with the creation of *empty* GDP—that is, GDP with no intrinsic value. When a colleague of mine joined an official trip visiting a county in northeast China,

the local mayor led the visitors to an imposing bridge and pointed out that it had been built under his direction, going on and on about the grand scale and cost of this project. Finally, one of the guests could not help observing aloud that the bridge spanned a stretch of dry, flat land. “What is the bridge for, exactly?” the guest asked. The mayor chuckled and said, “Do not worry. The central government has agreed to dig a river underneath it.”

Building bridges boosts GDP. So does digging rivers, for that matter. And bizarre behavior driven by GDP worship has been all too common in China. While visiting a resort city nestled in the scenic mountains of southern China, I noticed that we were driving on a wide road that was noticeably out of place. I asked the taxi driver, “Why do you need a street as wide as Beijing’s Changan Avenue here at the foot of this mountain?” To which he replied, “We have a new mayor.”

GDP worship has often led to excessive urban reconfiguration, sometimes at great cost to cultural and historical sites. Everything is seen through the lens of magnifying GDP—every square inch of redesignated land, every tree cut down or moved, every demolished historical site. The former mayor of the city of Nanjing, the capital of Jiangsu Province, lived up to the literal meaning of his name, Jianye (which in Chinese means “building or undertaking great enterprise”). He earned his sobriquet “Mayor Bulldozer” by launching into a massive wrecking and rebuilding spree that literally left no stone unturned. Enough of that money spent on generating empty GDP went directly into Jianye’s pockets that he is currently serving prison time.

Feverish pursuit of GDP growth gave rise to too much of everything in China, an overkill of industrial parks and science parks, exhibition centers, steel factories, and coal mines. State-led, rather than market-led, allocation of resources led to excess capacity and also to a race to the bottom in prices: cheap steel, iron, and solar panels flooded the global markets and upset trading partners. Speed was the priority as the nation sought to sprint through a marathon. Everyone thought fast, acted fast, tried to make money fast, and moved on fast when they ran into obstacles. There was little time to take stock and learn lessons in order to adapt to a rapidly changing environment.

The economy was running faster than the ecosystem's ability to renew itself, and faster than society could keep up.

China's New Playbook: Beyond GDP

Achieving high growth can be impressive, but the key question is, at what cost? China's excessive push for growth left hazardous environmental consequences in its wake: polluted rivers and lakes, cities blanketed in smog, topsoil turned toxic, and mountains denuded of vegetation, triggering landslides as the ecosystem lost its balance. Being the world's factory is an enviable position, but it has come with a high price tag. As advanced economies transferred polluting industries to low-income countries in order to reduce their own emissions, they have effectively passed on the environmental cost to others. China gladly took over a lot of such activities early on in order to industrialize, but it resulted in a much-ruined landscape across the country, beset with solid wastes and polluted water and overhung with a canopy of perpetual smog. For a long time local governments had little incentive to control and reverse environmental degradation at the expense of GDP growth, although today this is changing. Huge costs are being incurred to clean up lakes and rivers and to free cities from their Dickensian shrouds.

China has woken up to the urgent need to shift to a new developmental paradigm—from maximizing output to improving quality, from meeting hard growth targets to pursuing soft infrastructure, most notably education, healthcare, and other public services. This pivot reflects the new requirements of a nation with a rising middle class. A society attaining “modest prosperity,” in China's terminology, requires more than a decent life, represented by a range of variables beyond material satisfaction. Hence, the state needs a new playbook. The Twentieth Party Congress, held in late 2022, made it clear that economic growth, which used to be a central fixture of the party's agenda, is no longer the only priority. It's a matter of quality over quantity, as well as security and common prosperity.

The wish list of citizens in a post-basic-needs society is a long one, and not always easy to satisfy. They enjoy driving to work, but cry out against smog; they appreciate the convenience of electric appliances, but prod the authorities to do more to stave off climate change; they buy higher-quality products that require more mining and resource extraction, but environmental protection is a priority. And the new generation is wondering, What is the point of having all this money if I can't make sure that what my children are eating and drinking is safe, plentiful, and of high quality?[6] The environmental Kuznets curve shows that pollution follows an inverted U shape: as income rises, pollution first increases and then falls.[7] Although there are various explanations for this, people's shifting preferences are prominent among them. In the beginning people are willing to trade environmental quality for a rapid rise in income, but after their income reaches a certain level, they prefer cleaner ways to grow, even though they are costlier. As a society becomes more prosperous, it also becomes more demanding about health and the environment.

Rising housing prices, horrendous traffic, and environmental degradation are all consequences of the rush to raise GDP, fueled by local governments that also pushed up land prices and encouraged consumerism. The emphasis was on speed and quantity. Today that emphasis is shifting away from creating as much GDP as possible and toward improving the quality of everyday life. A decade ago, foreigners visiting China were struck by "the spitting habit." People loudly hawked and spat, or blew their noses right onto the street, wherever they might be. Littering seemed to be the national sport. Streets, rivers, lakes, and other public places were used as wastebaskets. Empty bottles, cans, and other trash were jettisoned by cars flashing by. Today, the streets of Beijing and Shanghai are spick-and-span, and residents have significantly changed their behavior. The government recently issued an elaborate trash-sorting ordinance, and the fact that there was more compliance than complaint speaks to the convergence of people's growing expectations and social norms.

Although the growing middle class in China has not formally been granted greater political participation, it is becoming an important political force.

According to political theory, the rise of a middle class creates pressure on the political system, as increasing prosperity encourages people to feel they have a greater stake in that process. If political institutions fail to evolve along with socioeconomic progress, it can lead to social discontent. Some pundits believe that the Arab Spring may be a harbinger of things to come in China. But what makes China different is that the ruling party is acutely aware of the hazards of social discontent, and its political institutions evolve to keep up with the changing needs of the Chinese people. In the party's own words, "moving forward with the times" (*yu shi ju jin*) is critical. To that effect, it has strengthened people's power and held governments at all levels accountable. The National People's Congress, whose deputies are elected by local constituencies, is no longer expected to automatically ratify bills endorsed by the Standing Committee of the party's Politburo. The newly revised Administrative Procedure Law of 2015 expands the people's rights to sue the government, and cases have been won. Power is not taken for granted: if the legitimacy is not based on the ballot box, it critically depends on the party's ability to ensure an ever-improving living standard of the Chinese people, whose aspirations are still a political guarantee for their economic stability.

In Western societies, accountability is based on the rule of law, enforced by an independent judiciary and a free press. Although these systems are still underdeveloped in China, a combination of formal institutions and informal channels have come to fill in the gap. Because China does not practice Western-style, one-person-one-vote democracy, its best strategy going forward is to maintain popular support through accountability and responsiveness. Local officials are sacked summarily should they fail to respond to natural disasters or to outbreaks of epidemics, or if there are local coal mine blasts or serious accidents due to dereliction of duty.

Government responsiveness is not unique to democracies. Nor is a democracy always responsive. The US can be sluggish in meeting its people's needs, as it was in the aftermath of Hurricane Katrina and the outbreak of COVID-19. By contrast, Singapore, which is an authoritarian regime, is free of corruption and highly accountable to its citizens. In China,

within three weeks of the first appearance of COVID-19 in Wuhan, the Chinese government built sixteen massive mobile hospitals in the city and dispatched forty thousand medical staff there. In addition, the Ministry of Finance allocated funds so that all medical expenses associated with COVID became free for everyone in the country. That said, sometimes *over-*mobilizing can be a problem; in many parts of China the direct costs of the COVID response were enormous.

An Attentive Power

The legitimacy of the Communist Party in China has always been an interesting question. As we have seen, numerous international surveys have shown a high level of satisfaction toward the government. It is, of course, due to the material prosperity and security delivered to a large swath of its citizens. But on a regular basis, satisfaction comes from the fact that the government remains an attentive and responsive power. The system's accountability mechanisms can sometimes hold their own with those of democratic countries, particularly when it comes to confronting societal problems. For instance, the number of Chinese departments with investigatory powers has been rising in recent years, as they look into fire prevention, safety measures in the workplace, food safety, pharmaceutical standards, IP protection, pollution control, and anti-corruption measures. A quarter million cadres are regularly dispatched to investigate private and public institutions at all levels. Between 2016 and 2017, environmental protection inspections resulted in more than seventeen thousand officials being disciplined, prosecuted, and convicted.^[8] National and provincial tournament events for environmental protection have been held to award prizes to winners for their vigilance and tenacity. As a result, the air in Beijing has been cleaned up enough so that its citizens are now enjoying far more “blue-sky days.” Largely in response to public sentiment, the government has taken tough actions like breaking up big oil companies such

as PetroChina and Sinopec and shutting down factories in Hebei, the neighboring province to Beijing.

In addition to dispatching inspection teams, the government has instituted widespread use of complaint mailboxes, physical or virtual, encouraging whistleblowers to report all kinds of wrongdoing. Results indicate that this system is working, and that contrary to popular belief, a one-party state like China can successfully create and enforce a potent set of curbs and checks on public officials. Online public platforms where local citizens can post complaints and demands are closely monitored by the central government. Because local officials often prefer to be bearers of glad tidings rather than messengers of bad news, all too often covering up scandals or misrepresenting data, the central government has made citizen engagement a crucial source of information. Today more than three quarters of the three thousand counties all over the country have these public online platforms.

Social media can play a similar role. Despite tight government control of the internet, social media still offers a medley of diverse views on contemporary life in China and fosters a thriving civic debate on a wide range of issues. People of all generations spend hours online each day. With more than 1.2 billion monthly active users on the social media platform WeChat and half a billion microbloggers on Weibo (owned by Sina), the Chinese people are connected in real time. A study published in *The Journal of Economic Perspectives* looked at 13.2 billion blog posts on Weibo between 2009 and 2013. To their great surprise, American researchers found that many sensitive issues were openly discussed. Even the most contentious subjects—including ethnic conflict, scandals involving local government officials, anecdotes about top leadership, political protests, and most recently, US–China relations—were widely broached.^[9] For example, there were millions of posts on collective action events, such as protests and riots, which are highly sensitive subjects. Posts can even predict actual organized protests in the following days.

Although the Chinese state keeps close tabs on the internet, the common assumption that social media is completely censored is incorrect. For one thing, it's not easy to block posts and trolls, which are widely forwarded

instantaneously. Despite government surveillance, millions of bloggers post in the middle of the night, and before the government can filter out the innumerable threads of the topic a national commotion may already be under way. Even if some are completely deleted, the footprint left on the memories of netizens cannot be erased (however, this may change as artificial intelligence and machine learning are increasingly deployed). More important, top leaders are aware of the value of letting people express their opinions. Tuning in to this information also allows the government to respond swiftly to negative public opinion before it gives rise to social unrest. So long as postings do not touch the third rail—subversive views of the party itself or attacks on very senior party officials—a wide range of politically and socially sensitive issues are tolerated.

It is also useful to have social media whistleblowers helping the government monitor the party's cadres. According to the same *Journal of Economic Perspectives* study, 11 million of the 13.2 billion blog posts were government related, and of that 11 million, more than half involved corruption cases. Amateur civilian paparazzi of the Chinese variant are interested not only in chasing celebrities; they use their telephoto lenses to catch corrupt officials. When a senior official from Beijing paid a visit to a local official, a hawkeyed photographer noticed a band of lighter skin around the local official's wrist. A little digging into local archives uncovered images of that same official's wrist gleaming with a variety of luxury watches; posting the images online led to an official investigation and charges of corruption. Amateur and freelance investigators snap and post photos of officials sneaking out of a luxury mansion at night, or in other inappropriate situations.

Social media campaigns can also lead to change. In one high-profile case, a blogger shared a video about a woman who was abducted and forced into marriage, causing a national outrage that blamed government negligence for the episode and others like it. This quickly prompted the central government to launch a nationwide special campaign in 2022 to crack down on the trafficking of women and children. Another widely discussed campaign started when a student died from a heart attack after being defrauded of her

tuition. It led the government not only to crack down on fraud but also paved the way for the enactment of one of the strictest data-privacy laws in the world. Although dissent on many sensitive issues is silenced on social media, the platform embodies a complex interaction between government and people, one that constrains the ability of the government to act without oversight and plays a broad role in the dissemination of information and propaganda, surveillance, and the aggregation of public opinion.

This emphasis on quality and safety is part of a new set of governing principles from the state's playbook. It marks a significant shift from an era when GDP creation was the holy grail and much was countenanced in its pursuit, including outright corruption. For a long time the state's attitude toward officials at both high levels and low was one eye open, one eye closed, so long as targets were met. But today the approach is both eyes wide open with a third eye in the back of one's head, as a broader set of social indicators—one that is inherently much harder to measure than GDP growth—has come to dominate the all-important process of performance evaluation.

In addition to addressing pollution and corruption, the state's new agenda includes one of the most glaring problems of the day: income disparity, which invariably comes along with rapid growth. Markets do not resolve this on their own; instead, they can exacerbate it. Rising inequality has become a critically important issue around the world, leading to polarized societies, rising populism, and widespread discontent with government.

Once again, the onus falls on local governments to tackle it; they have been given targets for the number of people who need to be lifted out of poverty each year in their jurisdictions, and their success or failure will be based on these metrics. President Xi put on the table a list of specific measures to bring prosperity to the most vulnerable. These include relocating people from rural areas prone to natural disasters or hardship to cities and towns; providing incentives and resources for people to start small businesses; improving rural infrastructure, and providing public goods in these areas, such as healthcare and public services; and education and vocational training for the young. Qualifying households are even provided contact information for those officials responsible for poverty elimination in

their region. As a result of this program, the number of very poor rural residents declined from nearly 100 million in late 2012 to 16.6 million by the end of 2018. By the end of 2020, the target of eliminating extreme poverty altogether was achieved when the last cohort of 40 million people in rural areas were lifted out of abject destitution. The next milestone for the government, as we will discuss further in chapter 10, is to attain to the ambitious goal of common prosperity promised by Deng Xiaoping at the very outset of reform and opening up.

To opt for slower but higher-quality and more sustainable growth is the right approach. In fact, it is the only feasible strategy for an economy that has exhausted itself of low-hanging fruit and quick wins. But incentive mechanisms for local governments are put to the test. In the past, their performance was easily measurable under a single set of quantifiable targets related to GDP growth. But a multifaceted, broader objective that spans employment, environment, pandemic controls, to growth itself can sometimes lead to confusion and mismanagement of the local economy. Local officials can veer too much in one direction to avoid punishment at all costs rather than balance a wide range of objectives that ensure an improvement in the overall well-being of for their citizens.

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China's unique system of government intertwined with the economy and power sharing at the local level creates both outside opportunities and notable obstacles. And despite the limits China imposes on free market forces, and the absence of a free press, independent judicial system, and the individual right to vote, we see that there are other mechanisms in place to respond to the needs of its citizens and to address the threats posed by income inequality.

Different systems lead to different trade-offs. As economist Pranab Bardhan points out, centralized regimes can be good when it comes to making a long-term commitment but less effective when it comes to accountability or flexibility. Political pluralism has its benefits in terms of

representing diverse populations, but it is often achieved at the cost of weak collective action. Democratic deliberations contribute to social legitimacy, but competition between political parties in a democracy can also lead to a race to the bottom. Rather than serving broad-based interests as originally intended, democracies can be distorted through the power of money and the process of lobbying. People of different persuasions prize certain values over others. Some may emphasize freedom, where others are more interested in prosperity, stability, or security.

Borrowing from a distinction made by Markus K. Brunnermeier in his analysis of post-COVID societies,^[10] China's political economy system is robust, but is it resilient? Resilient societies are supple: they can absorb shocks and get back on their feet quickly. Robust societies are sturdy: with their many layers of buffers they are resistant to shock waves. But a robust system can be knocked off course by an extreme event, taking a long time to recover or potentially never fully recovering at all. As we have seen throughout this chapter, China's structure, with its centralized powers, financial muscle, and administrative capacity for policy implementation, has made it robust. It also possesses qualities of resilience; it is an agile state quick to trigger the decision-making process with a readiness to change tack in real time. But overall, robustness still outbalances resilience in China: its growth model is reliable but not flexible. To keep it going, credit needs to be pumped constantly into the economy, and property prices and stock prices need to be propped up. To maintain stability, huge costs must be incurred—whether it is to save the economy from plunging into deep financial crisis or to maintain a strict zero-COVID policy.

Resisting downward pressure on the economy at all costs or maintaining stability at all times does not help build resilience. Like a body living in a sterile environment, it eventually loses all immunity. To be able to withstand turbulence one has to experience it and draw lessons from it. Brunnermeier's metaphor of a reed that "bends often but does not break" is apropos: an economy, or a system, is most sustainable when it can be more like a reed than an oak. That would be a worthy goal for China's new playbook.