

Rule by Market: The Chinese State in Factor Markets

Meg Rithmire

F. Warren McFarlan Associate Professor
Business, Government, and the International Economy
Harvard Business School
mrithmire@hbs.edu

March 2023

Abstract: Political economy on China and beyond generally has been premised on a trade-off between state and market power. In the context of China's reforms, markets and market mechanisms were hypothesized to replace state power in allocating important economic resources. Yet, even as market mechanisms have been introduced in important realms, the state appears to retain power over supply and demand, and, by extension, prices. This paper examines the introduction, and eventual adjustment and constraint, of markets in two important arenas: land and equity markets. Through process tracing and by analyzing a large body of policy documents from various levels of government in both arenas, I uncover a cycle by which the Chinese state embraced market mechanisms to address problems of misallocation, met uncomfortable outcomes of instability and "bubble" behavior during partial liberalization, and reconfigured state control over supply and demand of land and capital while retaining market mechanisms to facilitate competition but not set prices. In both arenas, the Chinese state "rules by market," by which market mechanisms facilitate, rather than replace, state control over allocation of resources. Rule by market is characterized by authoritarian responses (including populist crackdowns and the use of the state's coercive apparatus) to respond to market instability as well as institutional reconfigurations involving "red lines" to structure exchange, the setting of indirect price controls, and the rise of novel institutions to enforce these. Rule by market helps make sense of a number of empirical puzzles in China's political economy, such as bubbles that never seem to pop and cycles of liberalization and crackdown, and suggests amendments to several ideas about how the CCP has managed markets with monopolized political power.

Keywords: China, political economy, state-market relations, land, equity markets

Acknowledgements: For research support, I thank the Harvard Business School Division for Faculty Research and Development. For research assistance, I thank Hao Chen, Jamie Chen, and Jingyu Liu. Nancy Hearst at the Fung Library provided helpful materials. For feedback, I thank Kristin Fabbe, Jonas Nahm, Margaret Pearson, Kellee Tsai, and Saul Wilson, as well as seminar participants at the Blavatnik School of Government at Oxford University.

I. Introduction

The juxtaposition of market coordination and state authority has been paradigmatic in theorizing about variation in political economies and, especially, in the transition from socialism.¹ While scholars, and policymakers, have emphasized that efficient markets require good governance and regulatory authority, but nonetheless dominant frameworks focus on how state institutions support and reinforce markets in allocating resources and facilitating competition. Frequently, the suite of rules that enforce property rights, contracts, and even intervene to facilitate strategic competitive efforts in global markets are called “market-supporting institutions.”²

Scholarly thinking on the role of states in markets evolved in reaction to the emergence of rapid industrializing states in East Asia, in which “developmental states” featured a mix of bureaucratic initiative and private ownership to catalyze economic growth.³ Further, the emergence of “state capitalist,” hybrid systems in the late 20th and 21st centuries initiated a new round of interrogation of the relationship between states and markets. Many economies featured both economic dynamism and extensive state intervention, even globally competitive state-owned firms.⁴ The economic rise of China in particular prompted serious reconsideration of the relationship between markets and concentrated state power. Initial debates revolved around which Chinese state institutions most closely proxied “market-supporting institutions” to enable capitalist growth, and many observers expected that political and economic reforms would “lock in” commitments to markets.⁵ More recently, scholarship on China’s political economy has sought to explain the resurgence of the state as an economic force, often noting that neither global forces of liberalization like China’s accession to the World Trade Organization (WTO) nor the rise of a domestic business class enabled markets to supplant the state as the primary force in the economy.⁶

¹ Kornai, János. 1992. *The Socialist System : The Political Economy of Communism*. Princeton, N.J.: Princeton University Press.

² Vogel, Steven Kent. 2018. *Marketcraft : How Governments Make Markets Work*. New York, NY: Oxford University Press. Dani Rodrick. “Institutions for High-Quality Growth: What They Are and How to Acquire Them.” Remarks for the IMF Conference on Second Generation Reforms. Oct. 14 1999. <https://www.imf.org/external/pubs/ft/seminar/1999/reforms/rodrik.htm>.

³ World Bank. 1993. *The East Asian Miracle : Economic Growth and Public Policy*. New York, N.Y.: Oxford University Press. Wade, Robert. 1990. *Governing the Market : Economic Theory and the Role of Government in East Asian Industrialization*. Princeton, N.J.: Princeton University Press. Haggard, Stephan. 2018. *Developmental States*. Cambridge: Cambridge University Press.

⁴ Bremmer, Ian. 2010. *The End of the Free Market : Who Wins the War between States and Corporations?* New York: Portfolio. Kurlantzick, Joshua. 2016. *State Capitalism : How the Return of Statism Is Transforming the World*. New York, NY: Oxford University Press. Musacchio, Aldo. 2014. *Reinventing State Capitalism : Leviathan in Business, Brazil and Beyond*, Edited by S. G. Lazzarini and S. G. Lazzarini. Cambridge, Massachusetts: Harvard University Press.

⁵ Ang, Yuen Yuen 2016. *How China Escaped the Poverty Trap*. Ithaca, NY: Cornell University Press, Montinola, Gabriella, Yingyi Qian and Barry R. Weingast. 1995. "Federalism, Chinese Style: The Political Basis for Economic Success in China." *World Politics* 48(1):50-81, Naughton, Barry. 1995. *Growing out of the Plan : Chinese Economic Reform, 1978-1993*. New York, NY: Cambridge University Press, Oi, Jean Chun. 1999a. *Rural China Takes Off: Institutional Foundations of Economic Reform*. Berkeley: University of California Press, Shirk, Susan L. 1993. *The Political Logic of Economic Reform in China*, Vol. 24. Berkeley: University of California Press.

⁶ Lardy, Nicholas R. 2019. *The State Strikes Back : The End of Economic Reform in China?* Washington, DC: Peterson Institute for International Economics, Minzner, Carl. 2018. *End of an Era : How China's Authoritarian Revival Is Undermining Its Rise*. New York, NY, United States of America: Oxford University Press, Tan, Yeling.

This paper examines the introduction and retrenchment of market reforms in factor allocation in China, specifically land and capital. In both arenas, the Chinese state embraced market mechanisms to address problems of misallocation, met unwelcome outcomes of instability and bubble behavior during partial liberalization, and then reconfigured state control while retaining market mechanisms to facilitate market competition, but not market allocation or market price-setting. Rather than viewing state institutions as market-supporting, I show how market mechanisms supported state control, a phenomenon I call “rule by market.” Scholars of China’s legal regime have argued that it is best characterized as “rule by law” rather than “rule of law” because laws enable the party-state to govern society but do not provide a substantial disciplinary constraint on state actors.⁷ Rule by market is analogous; market mechanisms enable the state to introduce competition and discipline for market actors, but also allow the state to retain discretion and evade market discipline when it sees fit.

Understanding factor allocation as “rule by market” helps resolve a number of empirical puzzles in China’s land and finance markets. Namely, it helps make sense of the perpetual presence of bubbles that never really pop, cycles of liberalization and crackdown, and the presence of arbitrage and fraud. The paper’s theoretical contribution, in addition to the argument that markets can augment rather than supplant authoritarian rule, is in disaggregating what functions markets take on. The next section discusses the role of markets in allocation, competition, price-setting, and firm entry and exit. The bulk of the paper applies a process-tracing approach to the evolution of land and equity markets in China to illustrate the dynamics of rule by market. I argue that market mechanisms have facilitated market competition in those arenas, but not allocation, price-setting, and firm entry and exit. The conclusion considers the political and economic dangers that accompany the Chinese state’s desire to deploy market mechanisms but deny their disciplinary powers.

II. Markets and States

Classic economic thinking since Adam Smith has characterized markets as self-correcting forces for aggregating individual choices productively into aggregate social outcomes. As opposed to the “visible hand” of a state that sets prices and quotas for production and consumption, markets, in an ideal formulation, facilitate exchange (in currency) and allow supply and demand to set prices and, by extension, allocate social resources toward productive ends. Fundamental discipline comes from competition: agents who supply quality products and services can command appropriate prices and stimulate appropriate demand, while agents who cannot compete are forced to exit markets because they cannot. Lindblom characterizes market systems as featuring “consumer sovereignty,” whereby overall “production is largely controlled

2021. *Disaggregating China, Inc. : State Strategies in the Liberal Economic Order*, Edited by M. Project. Ithaca [New York: Cornell University Press.

⁷ In general, see Ginsburg, Tom and Tamir Moustafa. 2008. *Rule by Law : The Politics of Courts in Authoritarian Regimes*. Cambridge [UK] New York: Cambridge University Press. On China, see Lee, Ching Kwan. 2007. *Against the Law: Labor Protests in China's Rustbelt and Sunbelt*. Berkeley: University of California Press, Liebman, Benjamin L. 2014. "Legal Reform: China's Law-Stability Paradox." *Daedalus (Cambridge, Mass.)* 143(2):96-109. doi: 10.1162/DAED_a_00275. Gallagher, Mary Elizabeth. 2017. *Authoritarian Legality in China : Law, Workers, and the State*. Cambridge, United Kingdom ; New York, NY, USA: Cambridge University Press.

by the market demands of millions of consumers.”⁸ Planner sovereignty, by contrast, vests the power to determine production and consumption to the state.

Political economies clearly vary significantly, with infinite points between consumer and planner sovereignty. Scholarship has endeavored to characterize how states differ in their modes and logics of intervention, generating a large literature with adjectives to describe their efforts (developmental, rent-seeking, predatory, nightwatchman, and so forth) and capitalism or markets with adjectives to describe their differences (state capitalism, liberal versus coordinated market economies).⁹ Yet few efforts have been made to detail the functions of markets in a way that would allow unbundling. Rather than theorizing how states intervene in markets, what functions do markets perform?

Understanding how factor markets work is fundamental to comparative political economy, yet they have been conspicuously absent from analysis of transitions from socialism. Generally speaking, both post-socialist political economy and broader discussions of “state capitalism” have focused on ownership, including whether the state owns (typically large, strategic) firms and to what extent those firms are subject to market discipline.¹⁰ By contrast, the political economy of advanced industrial democracies, dominated by the “varieties of capitalism” (VoC) school, focuses intensely on factor markets. The degree of coordination between firms and state institutions in labor and capital markets is a primary source of variation between liberal and coordinated market economies.¹¹

Instead of focusing on ownership, the approach I take investigates what markets do when they exist in a context of state intervention and ownership of firms. Earlier work on the initiation and takeoff of market reforms in China found that product markets came first, facilitating firm entry and price-setting, and incentivizing market competition for firms of various ownership types. The result was “privatization from below” as firms adapted in form and practice to compete in product markets.¹² In product markets, then and now, markets allocate resources through “consumer sovereignty,” they set prices, facilitate firm entry and exit, and market

⁸ Lindblom, Charles Edward. 1977. *Politics and Markets : The World's Political Economic Systems*. New York: New York : Basic Books, c1977. P. 97

⁹ Evans, Peter B. 1979. *Dependent Development : The Alliance of Multinational, State, and Local Capital in Brazil*. Princeton, N.J.: Princeton University Press, Hall, Peter A. and David W. Soskice. 2001. *Varieties of Capitalism : The Institutional Foundations of Comparative Advantage*. Oxford England ; New York: Oxford University Press, Kurlantzick, Joshua. 2016. *State Capitalism : How the Return of Statism Is Transforming the World*. New York, NY: Oxford University Press, Pempel, T. J. 2021. *A Region of Regimes : Prosperity and Plunder in the Asia-Pacific*. Ithaca New York: Cornell University Press.

¹⁰ Naughton, Barry and Kellee S. Tsai. 2015. *State Capitalism, Institutional Adaptation, and the Chinese Miracle*. New York, NY: Cambridge University Press. Eaton, Sarah and Genia Kostka. 2017. "Central Protectionism in China: The “Central Soe Problem” in Environmental Governance." *The China quarterly (London)* 231:685-704. doi: 10.1017/S0305741017000881. Oi, Jean Chun. 1999b. *Rural China Takes Off : Institutional Foundations of Economic Reform*. Berkeley: University of California Press.; Hertog, Steffen. 2010. "Defying the Resource Curse: Explaining Successful State-Owned Enterprises in Rentier States." *World Politics* 62(2):261-301. doi: 10.1017/S0043887110000055.; Steinfeld, Edward S. 1999. *Forging Reform in China : The Fate of State-Owned Industry*. Cambridge ;New York: Cambridge University Press. Kornai, János. 1992. *The Socialist System : The Political Economy of Communism*. Princeton, N.J.: Princeton University Press.

¹¹ Hall, Peter A. and David W. Soskice. 2001. *Varieties of Capitalism : The Institutional Foundations of Comparative Advantage*. Oxford England ; New York: Oxford University Press.

¹² Naughton, Barry. 1994. "Chinese Institutional Innovation and Privatization from Below." *The American Economic Review* 84(2):266-70.

competition is fierce.¹³ **Table 1** describes these basic functions and outcomes of market mechanisms in allocating resources, facilitating firm entry and exit, and setting prices. The product market experience is illustrative. Most firms in early reform era China accessed capital from retained earnings, informal financial markets, or foreign investment, which allocated resources via market competition.¹⁴ Prices for products were set by “consumer sovereignty” supply and demand, and competitive firms survived and thrived while non-competitive ones exited the market through bankruptcy or absorption. China developed highly competitive sectors where markets performed these functions, and market competition (and productivity) was lower where they did not.¹⁵

Table 1: Conceptualizing Market Functions

Function	Target	Via Markets	Via Planners
Resource allocation	Investment capital Licenses	Competitive firms and activities receive resources	State agents choose which firms receive resources
Price setting	Supply and demand	Consumer sovereignty sets supply and demand	State agents determine supply and demand
Firm entry and exit	Who competes	Uncompetitive firms enter bankruptcy; low barriers to entry	Limited bankruptcy: state sets high barriers to entry

This paper looks at the relationship between state and market in the context of factor allocation in China, and principally land and capital. Examining factor allocation is a critical means through which we can understand the dynamics of China’s political economy. First, and most obvious, factor allocation affects growth and the distribution of economic power. Literature on economic growth has focused on the relative importance “getting prices right” in the context of developmental statism, and classical theories of the organization of economies focus on whether markets or states set prices for critical inputs.¹⁶ Second, factor allocation processes constitute what we might think of as a “hard test” for state tolerance of markets and capitalism. While much of the literature focuses on ownership and the relative balance of state versus private ownership of the means of production, whether the state allows market mechanisms to set prices of important inputs through supply and demand is a critical feature of capitalism. Prices and allocation of land, labor, and capital constitute the architecture of any political economy, and analyzing the vicissitudes of reforms in these arenas reveal much about how the Chinese party-state governs.

¹³ Brandt, Loren and Eric Thun. 2010. "The Fight for the Middle: Upgrading, Competition, and Industrial Development in China." *World Development* 38(11):1555-74. doi: 10.1016/j.worlddev.2010.05.003, Brandt, Loren, Johannes Van Biesebroeck and Yifan Zhang. 2012. "Creative Accounting or Creative Destruction? Firm-Level Productivity Growth in Chinese Manufacturing." *Journal of Development Economics* 97(2):339-51. doi: 10.1016/j.jdeveco.2011.02.002.

¹⁴ Rithmire, Meg 2023. *Precarious Ties: Business and the State in Authoritarian Asia* New York Oxford University Press. (Forthcoming, especially Chapter 5).

¹⁵ Brandt, Loren, Trevor Tombe and Xiaodong Zhu. 2013. "Factor Market Distortions across Time, Space and Sectors in China." *Review of economic dynamics* 16(1):39-58. doi: 10.1016/j.red.2012.10.002, Hsieh, Chang-Tai and Peter J. Klenow. 2009. "Misallocation and Manufacturing Tfp in China and India." *The Quarterly Journal of Economics* 124(4):1403-48. doi: 10.1162/qjec.2009.124.4.1403.

¹⁶ For a review, see Fields, Gary S. 1982. "Growth and Distribution in the Market Economies of East Asia." *World Politics* 35(1):150-60. doi: 10.2307/2010284.

The study of factor allocation also reveals an alternate logic to the one emphasized by most research on the Chinese state's— or most states'— intervention in markets. Work on specific sectors or China's adjustment to the requirements of WTO accession has focused on state and subnational efforts to facilitate state strategic goals oriented toward competition in globalized sectors.¹⁷ Intervention in factor allocation reveals a separate orientation of the Chinese party-state: risk aversion and preferences for discretion. The emergence of rule by market in factor allocation in China follows a similar logic to the development of legal institutions, which Liebman has argued have been hampered by a “law-stability paradox,” by which the party-state seeks to introduce legal reform to enhance stability and regime legitimacy, but then grows to distrust legal institutions to solve social and political problems.¹⁸ Markets and stability are subject to the same dilemma, and it is the Chinese state's authoritarian preferences, rather than its developmentalism, that shapes its orientation toward markets and limits the trajectory of liberalization. While earlier work on the evolution of markets and the institutional reform of the Chinese state saw market competition and even crisis as generative of liberalization, the factor market experience shows how markets, especially limited ones, and the crises they can create militate against further liberalization by threatening authoritarian stability.¹⁹

III. Rule by Market in China

Rather than seeing Chinese state institutions as reshaped to be “market-supporting,” market mechanisms in factor markets in China have been configured as state-supporting. In both land and equity markets, the state repeatedly introduces market forces when policymakers seek to catalyze economic growth, more effectively allocate resources, and discipline agents of the party-state itself in their distribution of resources. Each bout of liberalization is followed by a period of exuberant economic activity and overinvestment. The excessive activity comes from pent-up demand but also from speculation, a driver that increases in strength with successive bouts of liberalization as market participants learn to read state signals that it seeks to stimulate investment and that it will not tolerate downside risk.

In response to overinvestment and speculation, rather than embracing market corrections, policymakers become apprehensive that market mechanisms of correction would bring political instability and adversely affect the state's strategic goals. Fears of political instability are especially acute with factor markets. Unlike policy toward specific sectors or industries, overinvestment or speculation in land, finance, or equity markets have generalized effects on the economy and on society through households. In land markets, excessive market activity affects how cities look, involves politically contentious “land-grabbing” activities that affect political stability in urban and rural areas, and involves activities of urban households investing savings in real estate. In finance, in addition to the generalized effects of financial systems that appear in any political economy, the increased participation of retail investors in various parts of China's financial system have brought popular attention to how these markets work, including occasional

¹⁷ Hsueh, Roselyn. 2011. *China's Regulatory State : A New Strategy for Globalization*. Ithaca: Cornell University Press, Tan, Yeling. 2021. *Disaggregating China, Inc. : State Strategies in the Liberal Economic Order*, Edited by M. Project. Ithaca [New York: Cornell University Press.

¹⁸ Liebman, Benjamin L. 2014. "Legal Reform: China's Law-Stability Paradox." *Daedalus* (Cambridge, Mass.) 143(2):96-109. doi: 10.1162/DAED_a_00275.

¹⁹ Yang, Dali L. 2004. *Remaking the Chinese Leviathan : Market Transition and the Politics of Governance in China*. Stanford, Calif.: Stanford University Press.

popular protest.²⁰ Moreover, although party-state policymakers both introduce market mechanisms in the financial system in part to bring discipline to state-owned firms, they do not want those firms to suffer the costs of unbridled market discipline, such as higher costs of capital or threat of bankruptcy (market exit).

Rule by market emerges in response to fears of instability of adverse effects for important political constituencies (like urban households and state firms). Rather than allowing markets to set prices for factors and facilitate market exit for underperforming firms, the state reacts to overinvestment and speculation with an authoritarian response and by reconfiguring market institutions to facilitate state oversight. The authoritarian response involves a populist crackdown and the use of the state's coercive apparatus, rather than markets, to discipline badly performing firms.²¹ The authoritarian response occurs in the short-term, involving propaganda about malevolent actors and the party-state as a necessary political solution to the inherent problems of markets. In the medium term and in the wake of a crackdown, the state reconfigures institutional features to preserve some market mechanisms but retain state power for setting overall supply and demand for factors.

²⁰ Examples include the 2018 protests over the collapse of several peer-to-peer (P2P) lending platforms and protests in Henan in 2022 over a bank collapse.

²¹ Again, the analogy to legal development is helpful. See Benjamin Liebman. "A Return to Populist Legality?" In Heilmann, Sebastian and Elizabeth J. Perry, 2011. *Mao's Invisible Hand : The Political Foundations of Adaptive Governance in China*. Cambridge, Mass: Harvard University Asia Center : Distributed by Harvard University Press.

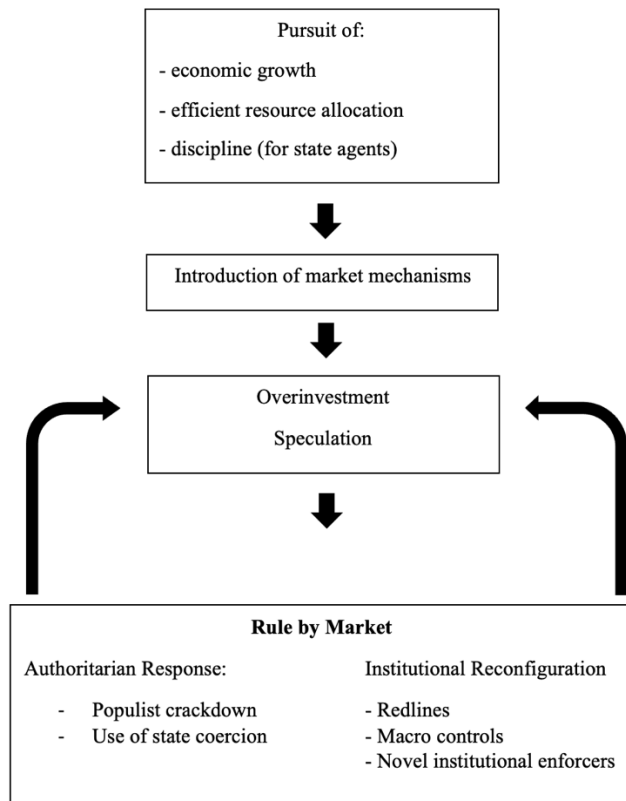


Figure 1: Rule by market in China

This general process of introducing markets and harnessing them as state-supporting institutions is represented in **Figure 1**, and the following sections narrate this process empirically, focusing on episodes in the development of land and equity markets between the 1980s and the present. My argument on rule by market speaks to findings on regulation in other arenas, both in China and elsewhere. Roselyn Hsueh finds that, in both India and China, policymakers undertook market liberalization in various sectors to compete in globalized industries and then re-regulated at subnational or sectoral levels to protect local players, a process she calls the “regulatory two-step.”²² Similarly, Richard Snyder has found that neoliberal reforms in Mexico were followed by re-regulation in a process that involved grassroots interest articulation and demands for social protection. The “regulatory two-step” is motivated by a logic of interest protection and fostering global competitiveness and, especially for Snyder, is shaped

²² Hsueh, Roselyn. 2011. *China's Regulatory State : A New Strategy for Globalization*. Ithaca: Cornell University Press, Hsueh, Roselyn. 2012. "China and India in the Age of Globalization: Sectoral Variation in Postliberalization Reregulation." *Comparative Political Studies* 45(1):32-61. doi: 10.1177/0010414011421305.

by societal forces as well as bureaucratic interests.²³ Protecting vested interests (like state-owned firms and privileged social groups) is part of the logic of rule by market, but it is a secondary objective. In China, the authoritarian party-state prioritizes social and political stability, and this is the first order objective that motivates policymakers to limit the disciplinary power of markets. In addition to establishing market-shaping practices, however, market mechanisms are preserved in land and capital markets to facilitate competition and aid policymakers in collecting information about market participants. The combination of market mechanisms, new institutions of market governance that bolster state control over supply, demand, and participation, and the state's discursive and coercive apparatuses supplement, rather than supplant, the power of the state over society.

That rule by market strengthens the power of the state does not mean it is not without adverse consequence. On the contrary, cycles of crisis and authoritarian response illuminate opportunities for arbitrage and collusion between market participants and state agents. The dynamic gives rise to periodic bubbles, which only reinforce the party-state's sense of threat from instability and reduce its willingness to undertake liberalizing reforms that would support market discipline or rule of law. As a result, the party-state remains trapped ever deeper in cycles of speculation and overinvestment, distorting economic growth and threatening long-term stability in the political economy. I return to these consequences in the conclusion.

IV. Land

Forty years after the initiation of market reforms and thirty after the introduction of land markets, land in China remains owned by the state. Rural land is owned "collectively" and urban land by local governments; both types of land can be developed and leased for commercial, residential, and industrial purposes, but local governments are parties to all of these transactions, and overall land supply is determined through government allocation via a system of hierarchically distributed quotas on an annual basis.²⁴ The institutions that structure land allocation are not a vestige of unreformed state socialism, but rather the product of extensive reforms involving the introduction of market mechanisms, discoveries of how market participants behave, and considered refinement of institutions over time. The overall process of land market reforms in China and individual cycles of reform constitute the rule by market dynamics described above. Rather than deepening liberalization over time, expanded market participation and real and potential crises have been met with populist crackdowns rather than market discipline and reconfigured institutional controls over land that leave the state with discretion over resource allocation, pricing (via supply controls), and firm entry and exit.

Rule by market in land allocation bolsters state strength in a variety of ways. Most simply, the state as ultimate property owner confers it with powers to decide the direction of economic development, who benefits from construction and urbanization, and the physical distribution of urban wealth. Overall control over land supply, and prices, also enables central policymakers to use land as a means of macroeconomic control, a function most states perform but more

²³ Snyder, Richard. 2001. *Politics after Neoliberalism : Reregulation in Mexico*. Cambridge, UK ; New York, NY: Cambridge University Press.

²⁴ See Rithmire, Meg. 2015. *Land Bargains and Chinese Capitalism : The Politics of Property Rights under Reform*. New York: Cambridge University Press.

indirectly through fiscal policy and central bank efforts to affect interest rates.²⁵ The control over land imbues the state with extraordinary political and social power over citizens and firms. A large literature explores the power dynamics of land expropriation in urban and rural China and shows that state power over land, and over people through power over land, is not uncontested. Expropriation and social protest over dispossession may attenuate regime legitimacy or political trust in important ways, but it also empowers the state to make broad choices about where and how Chinese citizens live and renders households dependent on the state's choices about how land is allocated. Firms, especially those in real estate but also any firm that requires land for its operations, also find their fortunes tethered to their closeness to the party-state. Market mechanisms in land markets, then, have not abated or replaced state control over resources, but rather facilitated information collection on the part of the party-state as its own control over economy and society has grown through control over land.

Introducing market mechanisms

Market mechanisms by which land could be used as an income-generating asset and be allocated by means other than administrative assignment were introduced gradually beginning in the 1980s, when policymakers sought to expand financing for urban construction. During the period of state planning, land was allocated to state units (firms, administrative offices) through administrative assignment and essentially without financial exchange. CCP leaders first experimented with land use fees—not lease fees, but rather small fees levied on land users based on the long-term impact of land use—and later with leasing long-term land use rights in exchange for capital.²⁶ The 1988 revision of the Land Law of 1986 determined that: “Land use rights may be transferred according to law.”²⁷ The revision was a result of brief and local experimentation: reformers in the CCP had succeeded in executing two land-leasing programs, one in Shenzhen in 1987 and another in Shanghai. The Shanghai lease, which took place on August 8, 1988, a date chosen for its auspiciousness, was the first time that a foreign business took independent control over a plot of Chinese land since the revolution.²⁸

Overinvestment and speculation

After 1992, real estate took off nationwide. The period from 1992 through the middle of 1994 is described by officials local and national, scholars, and the media as a “real estate craze” (房地热) and a “bubble” (泡沫). Real estate investment went from essentially zero in 1985 to 5 trillion RMB in 1992, or 20% of fixed asset investment²⁹; there were 117 development zones

²⁵ Rithmire, Meg. 2017. “Land Institutions and Chinese Political Economy: Institutional Complementarities and Macroeconomic Management.” *Politics & Society* 45(1):123-53.

²⁶ 现代中国的建设 *Xiandai Zhongguo de Jianshe* [*Contemporary China's Construction*] (Beijing: Academy of Social Sciences Press, 1990): p. 132, p. 22.

²⁷ Wang Yan and Yang Xiaojiang, *房地产业经营管理手册 (Real Estate Industry Management and Operation Handbook)* (Shanghai: Shanghai People's Press (上海人民出版社) 1990): p. 22.

²⁸ The number 8 is considered auspicious in China. Geng Yaxin. “The Reform of Urban Planning Work after the Introduction of Land Leasing” (土地批租促进了硅化管理工作的改革). In China Urban Planning Society, eds. *Looking Back on Fifty Years: Urban Planning in New China* (五十年回眸：新中国的城市规划). (Beijing: Commercial Press, 1999): pp. 162-165.

²⁹ National Bureau of Statistics, via CEIC.

nationally at the end of 1991, and 1,993 by the end of 1992.³⁰ Cities enlarged at a rapid pace as urban officials took to converting rural land at a large scale for the first time.

The frenzy of real estate investment was not coming from local governments alone. Universities, hospitals, enterprises, and government departments at all levels and devoted to all tasks established real estate arms, staked claim to “state” land, and tried their luck in developing commercial real estate. Official speeches and documents refer to an “enclosure craze” (圈地热), in which various work units and land occupants parceled out land for development and sale, and “speculative winds” (炒卖风), in which work units invested substantial capital in property speculation.³¹ At the time, the majority of land use was determined by administrative allocation (划拨), by which “the state” (typically the local government but sometimes provincial or central agencies) would assign land use rights to enterprises or institutions free of charge. After land was “assigned” to an institutional user, the user could then allow the land to enter the real estate market and thereby “make money through land” (以土生财).³²

A 1992 investigative report from Xinhua revealed changes in land prices that alarmed central authorities. In addition to uncovering the sale of central urban land at incredibly low prices in cities like Xiamen and Shenzhen, the report also concluded that commercial housing prices had risen on average 5.5 times in the larger cities, a rate far faster than that of wages. Central authorities, concerned about a bubble and fearful of social instability and a housing crisis, concluded that the real estate sector needed discipline. As the central government began to contract the discretionary flow of lending in the second half of 1993—part of a “macroadjustment” in response to fears about property oversupply and overinvestment—empty residential and office buildings peppered the urban landscape in major cities as all kinds of firms and institutions struggled to repay debt they had taken on toward real estate investments.³³ In coming to understand the growth potential of real estate, early CCP experiences in land markets also revealed markets’ potential to threaten economic stability. As a leading academic and finance policymaker said in an introductory speech to a conference reflecting on the bubble, “The lesson is very clear: abnormalities and overdevelopment of the real estate industry can create an economic bubble and false prosperity, with extremely serious consequences.”³⁴

Rule by market: Authoritarian response and institutional reconfiguration

How CCP policymakers understood the causes of “abnormalities and overdevelopment” affected the institutional reconfiguration to come. Official speeches and reports reveal that primary blame was attributed to the role of decentralized finance and low barriers to entry in the

³⁰ Yu Yongshun, ed. *中国房地产业于金融发展问题研究 (Research on Issues in of China's Real Estate Industry and Finance Development)*. (Beijing: Jingji Guanli Chubanshe, 1995).

³¹ Liu Weixin in Yu, *中国房地产业于金融发展问题研究 (Research on Issues in of China's Real Estate Industry and Finance Development)*, pp. 8-9. Speech of Vice Premier Zou Jiahua at the Ministry of Construction on August 10, 1991. Full text in Zhang Yuanduan (张元端), *中国房地产业趋势 (Trends in Chinese Real Estate)* (Harbin: Harbin Shipping Academic Society Press (哈尔滨船舶学会出版社), 1992).

³² Huang Xiaohu, *中国土地管理研究新的期 (A New Era in China Land Management Research)*. (Beijing: Dangdai Zhongguo chubanshe, 2006): p. 18.

³³ Liu Weixin in Yu, *Research on Issues in China's Real Estate Industry and Finance Development*. pp. 10-12.

³⁴ Zhou Daojiong, in a speech to the Real Estate and Finance Working Group of the China Construction Bank and the Urban Management Scholarly Committee, September 1994. In Yu *Research on Issues in China's Real Estate Industry and Finance Development*, p. 1-4.

sector in creating conditions for overinvestment.³⁵ The conclusion was that the state had to limit who could get involved in the business of real estate and at which stages of property development. Policymakers also drew conclusions about regulating the supply of land for development. Because real estate is a particular sector for which overheating has inevitable effects on the entire economy and on the structure of the urban built environment, then leaving land development entirely to markets, they reasoned, endangers the functionality of urban plans for infrastructure, land use, transportation, and so forth.

The authoritarian response after the events of 1992-1994 entailed campaigns against “real estate speculation” (囤积) and tying party discipline and anti-corruption efforts to local government land development efforts. Jiang Zemin linked land control to efforts to protect farmland and prevent food crisis, invoking the CCP’s historical nationalist efforts. Zhu Rongji, premier at the time, warned at an agriculture work conference: “If you take all the land to erect development zones, let the farmland go to waste, don’t cultivate the rice paddies, the volume of food production falls suddenly, you could originally support yourself, but now are buying grain from the outside, then what? If you don’t have local food needs and supply in balance, then you have no job responsibility as a provincial governor.”³⁶ When local state-owned firms and other work units, even hospitals and universities, in places like Dalian, Guangzhou, Shenzhen, and Xiamen could not pay employees because real estate efforts did not yield income, their managers were arrested in the wake of social protest.³⁷ Rather than allowing markets to discipline firms, the party-state at local and central levels responded with populist efforts and its own coercive apparatus.

The policy solution would be to unite the power to lease land with the power to create urban plans, and therefore to designate urban governments as the only legal owners of land. The Minister of Construction, in a speech reflecting on lessons from the bubble, said: “State-owned land use can be transferred for compensation, the goal being to attract domestic and international capital for construction...Beginning now, the government will strengthen regulation-building in the real estate market, establishing rule of law.” And, crucially, “From now on, the Chinese government will monopolize (垄断) land supply to strengthen economic and land planning. When urban land is transferred, the government will control the macro supply of land.”³⁸ In essence, the structure of land politics in contemporary China—in which local governments claim exclusive rights of ownership over land and generate revenue directly from land leasing—emerged in these policy clarifications in response to the real estate bubble of the early 1990s.

The decision to designate municipal governments to “represent the state” (代表国家) as landowners was born of the perceived need to designate a coordinating actor but also of the realization of how much local governments stood to gain. Of course, the power of real estate to generate government revenue through taxes (one-time taxes on real estate exchanges or value-added taxes on real estate) was evident even before the bubble, when cities in the southeast, such as Shenzhen and Guangzhou, saw real estate contributing about 10 percent of annual government revenue through taxes. But if municipal governments were the designated owners of state land,

³⁵ Vice Premier Zou Jiahua, cited in Zhang *Trends in Chinese Real Estate*: p. 3.

³⁶ Ministry of Land Resources 1996 Yearbooks, pp. 4-5.

³⁷ Liu Weixin in Yu, *中国房地产业于金融发展问题研究 (Research on Issues in of China's Real Estate Industry and Finance Development)*, pp. 9-11.

³⁸ Hou Jie, Minister of Construction. “The Promising Chinese Real Estate Sector” (大有可为的中国房地产业). In Cheng and Zhang, *Special writings collection on China's real estate craze (中国房地产热点大特写)* (Beijing: Zhongguo shenji chubanshe, 1993): pp. 4-5.

they would access the revenue generated from the sale of land-use rights as well as the taxes, providing local governments with a significant new source of income. In the words of one high-level official in the Ministry of Construction, “Land development and the real estate industry will serve as a secondary source of finance for the cities.”³⁹

In the aftermath of the real estate bubble of 1992–1994, China’s fiscal and financial institutions were reorganized so as to increase central control over resource allocation, supply, and firm entry and exit. In addition, a dramatic 1994 fiscal recentralization, by which local governments lost access to tax revenue but remained responsible for most expenditures, intentionally made local governments reliant on both land and debt, and land-related debt, to meet their expenditure burdens.⁴⁰ This fiscal “grand bargain” established what scholars in and outside China call “land fiscalization” (土地财政), by which local governments depend on land revenues for fiscal resources. The institutional arrangements that produce fiscalization—decentralized land ownership with hierarchical land management—constitute rule by market. Given what they had learned about the dangers of land market liberalization, CCP authorities adopted decentralized land ownership with hierarchical land supply management in an attempt to benefit from land markets but mitigate economic volatility.⁴¹

Subsequent cycles

Following the introduction of land resources as fiscal assets of local governments in the mid-1990s, policymakers reinforced decentralized land ownership and hierarchical land supply management through the late 1990s and 2000s. The Ministry of Land Resources (MLR) issued periodic clarifications that local governments must monopolize the land markets and therefore have exclusive claim to lease revenues. For example, in reflecting on the 2004 moratorium on development zones, a high-level MLR official referred to the 1993 decision to have the local state “monopolize the first level of the urban construction market,” warning, “If the government doesn’t strictly control the amount of land entering the market for construction, it not only affects the money available for urban construction but also does damage to peasant interests.”⁴² As local governments eagerly used that ownership to generate revenues, the institutions of hierarchical management were concomitantly strengthened, sharpening Beijing’s ability to use land as an economic and development policy tool.

The primary means of controlling supply would be annual quotas. Beginning in 2004, the MLR in Beijing began setting quotas of land for urban construction, allocating each province an

³⁹ Speech by Zhang Yuanrui, director of the Real-Estate Office of the Ministry of Construction, at the Meeting of the Coastal Cities Housing Association on Several Current Real Estate Issues), in Zhang *Trends in Chinese Real Estate*: p. 74.

⁴⁰ Liu, Adam Y., Jean C. Oi and Yi Zhang. 2022. “China’s Local Government Debt: The Grand Bargain.” *The China Journal* (Canberra, A.C.T.) 87(1):40-71. doi: 10.1086/717256. Rithmire, Meg. 2017. “Land Institutions and Chinese Political Economy: Institutional Complementarities and Macroeconomic Management.” *Politics & Society* 45(1):123-53. Huang 1996: preface; Shih 2008; Sebastian Heilmann, “Regulatory Innovation by Leninist Means: Communist Party Supervision in China’s Financial Industry,” *The China Quarterly*, no. 181 (2005).

⁴¹ On experimentation, see Heilmann and Perry, *Mao’s Invisible Hand*, 17; Sebastian Heilmann, “Maximum Tinkering under Uncertainty: Unorthodox Lessons from China,” *Modern China* 35, no. 4 (2009).

⁴² Li Yuan, then Vice Party Secretary of the MLR, in a speech entitled “中国城市化进程中的征地制度改革.” Li referenced the “loss of control” in the Hainan real estate market in the early 1990s, and remarked that peasants were selling their own land for incredibly low prices, which requires that the state intervene to coordinate markets. MLR 2006 Yearbook, pp. 4-6.

amount of land for urban built-up areas and restricting how much agricultural land they may convert. These quotas are decided jointly with the National Development and Reform Commission (NDRC), China's economic planning and management agency. Provincial governments, then, negotiate with municipal governments, who in turn negotiate with county and township governments, over the allocation of land for development.⁴³ In 2006, the center further strengthened what it called the "strictest" system for managing land, including a "red line" of 120 million hectares of arable land (180 billion mu, 十八亿) which is, they argue, the base line necessary for food security. Local governments throughout China are constrained by the quotas, and acknowledge the red line to be a "buzzword" or "sacred number."⁴⁴

State control over allocation, supply, and market entry, however, sought to leave space for market competition. National-level documents heavily encouraged the paid transfer of land, strictly limiting the administrative allocation of land without compensation to very few uses.⁴⁵ Compensated land use was billed as a way of introducing market mechanisms into land management (to meet the spirit of WTO accession requirements and achieve "socialism with market characteristics") while not relinquishing government power to protect sensitive land resources. Official speeches exhorted local governments to pursue paid transfer of land resources by citing the vast amounts of capital they could generate.⁴⁶ Markets were meant to constrain the behavior of local governments and developers, but the party-state itself would discipline them using its own institutional and coercive measures.

Rule by market in land strengthened the party-state vis-à-vis other social and economic actors. Control over supply and allocation facilitates management of the macroeconomy; quotas direct land development toward ends the state desires, such as regional development programs, and policymakers use overall supply as means of fiscal stimulus and austerity to attempt to smooth growth.⁴⁷ Rural residents are unable to transfer their own land holdings without the intervention of representatives of the "collective" and urban governments, who can transform rural land into urban land for construction. Policy experiments vary widely, but, in the broadest sense, Chinese rural residents remain dependent on the state through both land management and the *hukou* system of residential registration in their fundamental life choices.⁴⁸

⁴³ Yuan Xiao. "Making Land Fly: The Institutionalization of China's Land Quota Markets and its Implications for Urbanization, Property Rights, and Intergovernmental Negotiation." PhD Thesis in the Department of Urban Studies and Planning. MIT 2014.

⁴⁴ Xiao, "Making Land Fly;" p. 52. The language of the "world's strictest" system for land management was present as early as 1999. See speeches by Zhou Yongkang, inaugural Minister of Land and Resources, February 3, 1999 and December 3, 1999. Ministry of Land Resources Yearbook 2000 (中国国土资源年鉴) p. 33 and p. 58.

⁴⁵ Specifically, 2001 Documents 11 (关于加强国有土地资产管理的通知, Memorandum on strengthening management of state-owned land) and 15 (关于整顿和规范市场经济秩序的决定, Decision on rectifying and strengthening the market economic order).

⁴⁶ Tian Fengzhan, December 5, 2001. The Minister of Land Resource's speech at the 2001 work conference included: "In order to implement the urbanization strategy of the 10th FYP...we should reform and perfect land use institutions, adjust the organization of land use, mobilize land reserves into circulation, and mobilize land for urban construction while protecting arable land and peasant rights. We should also enthusiastically promote compensated land use, giving full play to the market's role in allocating land resources, making clear the value of land, generating capital for urban development and making use of the role of land resources in encouraging urbanization." Printed in MLR 2002 Yearbook, p. 69.

⁴⁷ Rithmire, Meg. 2017. "Land Institutions and Chinese Political Economy: Institutional Complementarities and Macroeconomic Management." *Politics & Society* 45(1):123-53.

⁴⁸ That rural residents' choices are framed by these institutions does not mean that they are without power. A wide literature examines dynamics of protest and response. See Cai, Meina. 2016. "Land for Welfare in China." *Land Use*

Because of the state's determination of entry barriers and the participation of local governments in all land market transactions, real estate firms and local governments are "reciprocally dependent" in ways that constrain both parties.⁴⁹ On the one hand, the state has effectively governed access to the real estate market and ensured that the state benefits.⁵⁰ On the other, real estate firms are so fundamental to the state's own fiscal health and the wealth of urban households that the state also governs market exit, reluctant to allow markets to perform that function for fear of political and financial instability.

The rule by market cycle, especially overinvestment followed by populist response and institutional reassertion of state control, has repeated several times since the early 1990s. Following the global financial crisis in 2008 and the party-state's stimulus efforts, massive infrastructure construction renewed fears of overdevelopment, accumulating public and private debt, and overreliance on land revenues. By the early 2020s, several of China's largest national and regional real estate firms, notably Evergrande, were teetering on bankruptcy, with unrest and unease in many urban centers as households feared they had sunk generations of savings into apartments that would never materialize or rapidly decline in value. Rather than bankruptcy, however, firms like Evergrande entered what Theodore Lowi called a "state of permanent receivership," whereby local and central state actors assumed responsibility for firms "too big to fail" and once again used the state's populist response and coercive apparatus to discipline firm managers and restore public confidence.⁵¹ As the conclusion revisits, these efforts allow the state to rule by market and embolden its own strength vis-à-vis other actors, but also engender and even incentivize a disruptive form of business's structural power that constrains the state's autonomy in making and executing economic policy.

V. Equity Markets

The contested pursuit of financial market modernization under the CCP has been as politically and ideologically thorny as the development of land markets. Because the size of China's equity markets was relatively small through much of the reform era and because these markets were not the main source of financing for firms, they have not received much scholarly attention; political economy work instead has focused primarily on the banking system and the informal means by which the non-state (private) sector has grown.⁵² In recent years, especially

Policy 55:1-12. doi: 10.1016/j.landusepol.2016.03.014, Cai, Meina and Xin Sun. 2018. "Institutional Bindingness, Power Structure, and Land Expropriation in China." *World Development* 109:172-86. doi: 10.1016/j.worlddev.2018.04.019, Heurlin, Christopher. 2016. *Responsive Authoritarianism in China : Land, Protests, and Policy Making*. New York, NY: Cambridge University Press, Looney, Kristen E. 2020. *Mobilizing for Development : The Modernization of Rural East Asia*. Ithaca New York: Cornell University Press, Mattingly, Daniel C. 2020. "The Art of Political Control in China." Cambridge, United Kingdom ; New York, NY: Cambridge University Press,. Retrieved, Ong, Lynette H. 2022. *Outsourcing Repression : Everyday State Power in Contemporary China*. New York, NY: Oxford University Press, Sargeson, Sally. 2013. "Violence as Development: Land Expropriation and China's Urbanization." *The Journal of Peasant Studies* 40(6):1063-85. doi: 10.1080/03066150.2013.865603, Smith, Nick R. 2021. *The End of the Village : Planning the Urbanization of Rural China*. Minneapolis: University of Minnesota Press.

⁴⁹ Culpepper, Pepper D. 2015. "Structural Power and Political Science in the Post-Crisis Era." Pp. 391-409, Vol. 17: Cambridge University Press.

⁵⁰ Saul Wilson. "The Landlord State." PhD Dissertation. Harvard University, May 2022.

⁵¹ Lowi, Theodore J. 1979. *The End of Liberalism : The Second Republic of the United States*. New York: Norton.

⁵² Huang, Yasheng. 1996. *Inflation and Investment Controls in China : The Political Economy of Central-Local Relations During the Reform Era*. Cambridge [England] ;New York, NY, USA: Cambridge University Press, Shih,

under Xi Jinping, equity markets have grown in size and political importance, and the relationship between the CCP and stock markets illustrates the logic and consequences of rule by market. Equity markets were introduced in the 1990s and strengthened in the 2000s to provide a means of raising capital and also, like with land, disciplining state agents—state-owned firms in the case of stock markets. But development of stock markets entailed expanding participation on the part of both firms and investors, and the CCP became wary of market instability. Like in land, the state turned to populist crackdowns, coercive discipline, and institutional reconfiguration to benefit from the information gathering and resource generation functions of market mechanisms but emboldening the state to control resource allocation, prices of equities, and firm entry and exit.

Introducing equity markets

The rationale for introducing stock markets in the late 1980s and early 1990s was definitively to facilitate more efficient capital allocation and to provide a disciplinary constraint on managers of state-owned firms in particular.⁵³ The Shanghai Stock Exchange (SHSE) opened in 1990 with 8 listed companies and 25 members, and the Shenzhen Exchange (SZSE) was established primarily for small and medium enterprises (SMEs) in 1991. Speculation, stock “fever” (股市热) and “bubble economies” (泡沫经济) were immediately apparent, including one that coincided with the period of excessive investment in land markets and general enthusiasm for market development following Deng Xiaoping’s 1992 Southern Tour. Generally, initial bouts of speculation were blamed on unsophisticated investors, a lack of standardization and transparency in corporate accounting procedures, and malevolent corporate actors who sought speculation and profiteering rather than long-term growth.⁵⁴

Despite many scholars and policymakers arguing that more market discipline would be the answer to early turbulence in equity markets, developments over the next two decades included cycles of expanded market activity, overinvestment and speculation, and state intervention that would advance the architecture of equity markets, limit the role of market discipline, and establish party-state control over prices, entry, and exit. Bubble periods in 1999-2001 and 2006-2007 accompanied increased amounts of IPOs and enthusiasm for listing of large state firms.

Victor C. 2008. *Factions and Finance in China: Elite Conflict and Inflation*. Cambridge: Cambridge University Press. Tsai, Kellee S. 2002. *Back-Alley Banking: Private Entrepreneurs in China*. Ithaca: Cornell University Press. An exception is John Yasuda. “Regulatory Anxieties Under Authoritarianism: Building a Regulatory State in China.” *Comparative Political Studies* (forthcoming).

⁵³ This widespread consensus among scholars and policymakers emerges in early and reflective writing on the 1980s and 1990s. See Rong, Yue. 1994. *血战中国股市：中国股民悲喜录*. Ha'erbin Shi: Dong bei lin ye da xue chu ban she, Wang, Dong. 1993. *股票风潮动*. Beijing: Shou du shi fan da xue chu ban she, Zhong, Su. 1992. *世纪之交股票潮冲击中国：深沪股市新新闻 = at the across of Century China Shocked by Share Tide : News from Shen Zhen & Shanghai Stock Exchange*. Beijing: Jie fang jun wen yi chu ban she.. Cheng Minxuan 程民选, “What kind of share economy should be established in socialist China” 社会主义中国应当建立什么样的股份经济, 《经济问题探索》, 1988.5. Cheng, Siwei and Ziran Li. 2015. *The Chinese Stock Market*. Houndmills, Basingstoke, Hampshire New York, NY: Palgrave Macmillan.

⁵⁴ Guo Qilin 郭其林, “Excessive speculative nature - the crux of abnormal volatility in China's stock market” 过度投机性——中国股市异常波动之症结, 《浙江师大学报》(社会科学版) 1994. Liu Xianqing 刘显清, “The generation and governance of our bubble-like economy” 我国泡沫式经济的产生与治理, 《函授学习》, 1994.4. Ding Wei 丁巍, “China's stock market 'bubble' phenomenon” 我国股票市场“泡沫”现象透视, 《中国投资与建设》股市纵横, 1994.7

Here, I focus on the most recent cycle under Xi Jinping, between 2014 and 2017 because efforts to develop equity markets during that period were the most well-developed and, critically, most open to non-state firms. One might expect that stock markets dominated by state firms, whose bottom lines are often political and whose corporate structures are designed to insulate them from market discipline, do not operate with substantial rule of market. But the party-state's turn to authoritarian responses and institutional reconfiguration to preserve its own ability to set prices and govern access for non-state firms is more surprising and illustrates the market-stability paradox in stark colors.

Toward the end of 2014, China's economic growth was slowing for the first time since the AFC. With a 7.3 percent growth rate in the third quarter of 2014, its slowest pace in almost five years, economists predicted that China might not meet its annual growth target for the first time since 1998.⁵⁵ Faced with a slumping economy, the Chinese government initiated several unusually broad reforms to increase bank lending.⁵⁶ The government also encouraged public investment in the stock market through other means. In an editorial published on 21 April 2015 that quickly went viral, state-run news outlet *People's Daily* urged the public to place its trust in the stock market and continue to invest.⁵⁷ The article claimed that the recent stock market rise marked only the beginning of a bull market, dismissing fears of a bubble—"What's a bubble? Tulips and Bitcoins are bubbles," the author taunted—while claiming that continued investment would enjoy "support from China's grand development strategy and economic reforms."⁵⁸

Overinvestment and Speculation

The government's efforts, both direct and indirect, saw results. In December 2014, investors in Shanghai and Shenzhen opened almost 900,000 new stock trading accounts in the span of one week, the most in seven years.⁵⁹ Stocks climbed to unprecedented highs in the first half of 2015: the Shanghai and Shenzhen stock markets doubled and even tripled over the course of a year, with some companies trading at 300 times trailing earnings by the stock market's peak on 12 June 2015.⁶⁰ The rapid growth raised concerns for multiple reasons, however. First, stocks rose, but the economy was still slowing. The International Monetary Fund (IMF) predicted that the Chinese economy would grow at only 6.8 percent in 2015, well below the 7.4 percent growth seen in 2014. Second, it appeared that much of the growth coincided with an explosion of margin lending or using borrowed money to buy securities. On 27 May 2015, total margin debt

⁵⁵ Lingling Wei, "China Central Bank Cuts Interest Rates," *The Wall Street Journal*, 25 August 2015.

⁵⁶ In September and October 2014, the People's Bank of China (PBoC), China's central bank, injected more than \$126 billion into Chinese banks. In another effort to increase the volume of loans, the PBoC cut interest rates for the first time in two years on 23 November 2014, lowering the benchmark one-year loan rate by 0.4 percentage point to 5.6 percent. On 4 February 2015, the PBoC relaxed the reserve ratio by half a percentage point, in effect freeing up about 500 billion yuan, or \$81 billion, in funds for banks to lend. On 16 April 2015, the PBoC offered commercial lenders 10 billion yuan of reverse repurchase agreements, or reverse repos, also to facilitate lending. See Lingling Wei, "China Central Bank Cuts Interest Rates," *The Wall Street Journal*, 25 August 2015; Shen Hong, "PBOC Cash Injection May Dim Hopes for Stronger Easing," *The Wall Street Journal*, 25 June 2015.

⁵⁷ Evan Osnos, "The Real Risk Behind China's Stock Market Drama," *The New Yorker*, 15 July 2015.

⁵⁸ 王若宇 (Wang Ruoyu), "4000 点才是 A 股牛市的开端" (4000 is the Beginning of an A-Share Bull Market), *People's Daily*, 21 April 2015.

⁵⁹ Neil Gough and Cao Li, "Seeking to Ride on China's Stock Market Highs," *The New York Times*, 29 December 2014.

⁶⁰ David Barboza, "Chinese Investors Who Borrowed Are Hit Hard by Market Turn," *The New York Times*, 6 July 2015.

outstanding grew five times in just one year, reaching 2 trillion yuan, or \$322 billion.⁶¹ Margin debt accounted for 8.7 percent of the free float on Chinese stocks, compared to only 2.8 percent in the U.S. Margin lending created extra volatility in markets because if the markets headed south, brokers could call in margin loans and force investors to repay borrowings, often by selling stocks. Moreover, individual investors often traded stocks bought quickly with borrowed money, amplifying volatility. In May 2015, stocks with margin debt changed hands an average of twenty-three times, while stocks without traded five times.⁶²

The government recognized the threat that widespread margin lending posed and took measures to curb its growth. The China Securities Regulatory Commission (CSRC) conducted an inspection of forty-five securities companies in December 2014, and found three of the largest companies—CITIC Securities, Haitong Securities, and Guotai Junan Securities—were violating regulations, including illegally extending margin contracts past the six-month limit set by the CSRC.⁶³ The imposed limit was intended to force investors to recognize losses and close out accounts instead of using credit to extend trades indefinitely. As punishment, the CSRC banned the three brokerages from opening new accounts for three months. Nine other brokerages were also found to have been serving unqualified clients, and following further investigations, the CSRC punished six for related violations, also banning new accounts.⁶⁴ Great Wall Securities Co., Ltd., Huatai Securities, and Guosen Securities, three of the top brokerages, were included in the sanctions.⁶⁵

Markets unraveled quickly in response to fears that the government was cracking down on margin trading. Even as China's four securities newspapers published editorials claiming that the bull market remained alive, the Shanghai Composite Index lost more than one-third its value during the second half of June 2015. After first embracing a "normal self-correction," the CSRC said in late June that an "excessively fast correction" would be unhealthy. By early July, the CSRC had reversed the exact limits on margin lending it had imposed less than a month earlier to boost markets and it also announced a probe into potential illegal stock manipulation and sources of the stock market rout.⁶⁶

Rule by market: Authoritarian response and institutional reconfiguration

Early July brought two heavy-handed moves on the part of the CSRC and the PBoC to stabilize markets: IPOs were suspended on 4 July, affecting an estimated four trillion RMB in planned issuances, and the government announced it would establish a market-stabilization fund comprising a "national team" (国家队) of brokerages to purchase shares of blue-chip exchange

⁶¹ Editorial Board, "China's Unsettling Stock Market Boom," *The New York Times*, 15 June 2015.

⁶² Jack Wong and Chao Deng, "Chinese Firms Discover Margin Lending's Downside," *The Wall Street Journal*, 30 June 2015.

⁶³ Gabriel Wildau, "Explainer: Margin Finance in China," *Financial Times*, 19 January 2015.

⁶⁴ Adam Jourdan, "China Punishes Six Brokerages for Margin Trading Violations-Regulator," Reuters, 4 April 2015.

⁶⁵ The three other sanctioned brokerages were Minmetal Securities Co., Ltd., Huaxi Securities, and China International Capital Corp.

⁶⁶ The decisions were to relax margin lending rules and allow brokerages to roll over contracts and wait to close out accounts. The CSRC also announced it would lower the threshold for individual investors to trade on margin and expand funding channels for brokerages. Lu Jianxin and Pete Sweeney, "Timeline of China's Attempts to Prevent Stock Market Meltdown," Reuters, 28 August 2015.

traded funds (ETFs).⁶⁷ The Central Huijin Investment Company, which traditionally held banking assets, assured the public it would continue to purchase ETFs, and the China Securities Finance Corporation (CSFC) quickly followed. Various measures to ease investment accompanied the massive deployment of state capital by the “national team,” and government-owned news media projected confidence. Tsinghua University graduates were instructed to shout, “Revive the A-shares, benefit the people!” at their 2015 commencement ceremony.⁶⁸

The capital injections seemed to arrest the market decline in July, but August brought troubles anew. First, the PBoC loosened convertibility of the RMB and immediately devalued the currency by 2 percent against the dollar, the largest devaluation since the modern exchange-rate system was introduced in 1994. The devaluation was part of the PBoC’s efforts to comply with IMF expectations for the RMB’s inclusion in the SDR basket, but the rapidity of the decline was not expected. Some interpreted the devaluation as an effort to boost exports amid slowing growth, but others saw the movement as unintended and a reflection of a lack of confidence in the RMB. Indeed, 2015 and 2016 saw significant capital outflows from both foreign investors and domestic capital holders who were pursuing safety outside of China.⁶⁹ Later that year, the IMF would add the RMB to its “Special Drawing Rights” (SDR) basket of reserve currencies, the first addition to the basket since adoption of the Euro. The decision was heralded as a statement of China’s standing as a global economic power, but the push toward a “freely usable currency” also enabled capital flight, prompting eventual controls in 2016 and 2017 on “irrational” outbound investments and efforts to “protect 3 trillion” of reserves and defend the RMB against further drops.⁷⁰

The so-called “national team,” principally comprising Central Huijin and the CSF, made over 1.3 trillion RMB from purchasing on China’s two stock exchanges between June and September 2015, eventually holding shares in half of all listed firms.⁷¹ While intervention by the “national team” may have staved off further collapse, the use of state capital was not unproblematic. By the end of 2015, six out of twenty-one securities companies on the “national team” were under investigation for short-selling or insider trading. According to one person, “People at CITIC and

⁶⁷ These companies comprised about 30 percent of the Shanghai market.

⁶⁸ James Kynge, “Prestige of the Communist Party Tumbles in the Great Fall of China,” *Financial Times*, 9 July 2015. “At the critical time during the competition between bearish and bullish factors, such measures will motivate the whole market, which shows the authorities’ resolve in stabilizing the market and will have immediate effects,” an article in Xinhua News declared on 6 July. “Early Bird Report 6-July-2015,” Xinhua Finance Agency, 6 July 2015. http://en.xfafinance.com/html/Early_Bird/2015/114008.shtml. *People’s Daily* also claimed that China was “capable and confident” that it would maintain a stable market, arguing that market risks were firmly under control. “China ‘Capable, Confident’ of Stabilizing Capital Market: People’s Daily,” Xinhua News, July 6, 2015. <http://en.people.cn/business/n/2015/0706/c90778-8916145.html>

⁶⁹ Carlos Tejada, “5 Things to Know About China’s Currency Devaluation,” *The Wall Street Journal*, 10 August 2015; Neil Gough and Keith Bradsher, “China Devalues its Currency as Worries Rise about Economic Slowdown,” *The New York Times*, 10 August 2015.

¹⁹ “IMF Launches New SDR Basket Including Chinese Renminbi, Determines New Currency Amounts,” International Monetary Fund Press Release 16/40, 30 September 2016. <http://www.imf.org/en/News/Articles/2016/09/30/AM16-PR16440-IMF-Launches-New-SDR-Basket-Including-Chinese-Renminbi>.

⁷¹ Chen Li, Chen, Huanhuan Zheng and Yunbo Liu. 2022. “The Hybrid Regulatory Regime in Turbulent Times: The Role of the State in China’s Stock Market Crisis in 2015–2016.” *Regulation & governance* 16(2):392-408. doi: 10.1111/rego.12340. For details on the scope of investments, see Chen, Hao and Meg Rithmire. 2020. “The Rise of the Investor State: State Capital in the Chinese Economy.” *Studies in Comparative International Development* 55(3):257-77. doi: 10.1007/s12116-020-09308-3.

other firms were calling up their friends saying ‘Tomorrow, I am buying [whatever firms].’”⁷² Moreover, initial investments by the “national team” seemed to have moved the market, but subsequent investments were perceived as failures. Because state capital was essentially rescuing collapsing companies, “people were happy for the ‘national team’ to buy because they wanted to sell.”⁷³ Essentially, after revealing that they would intervene on such a scale, the intervention then failed to move the market because it simply generated counterparties. Within a few months, Zhang Yujun, an assistant chairman of the CSRC who had played a critical role in the efforts of the “national team,” was removed from office and under investigation by the Central Commission on Discipline Inspection (CCDI).⁷⁴

During the crisis and in the months immediately following, the CCP turned on financial market participants—business and political elites—in actions that would presage a wider resurgence of state discipline in the financial sector. During the crisis, several high-profile finance professionals were detained. Li Yifei, chairwoman of the Man Group, a large global hedge fund, disappeared in late August 2015, with her husband reporting she had been detained. Ms. Li resurfaced and claimed she had been on a mountain meditation retreat. A few months later, Guo Guangchang of Fosun, nicknamed “China’s Warren Buffet,” was detained, not for the first time. Yim Fung, CEO of Guotai Junan International Securities in Hong Kong, was also reported missing by his company in 2015, and, as in the cases of Li and Guo, returned to work within a month.⁷⁵ In none of these cases were charges announced, and all of these high-profile individuals were either rumored or reported to be assisting regulators to understand how financial markets had become so volatile. Whether “assistance” meant technical explanations, for example on how margin-lending technology platforms worked or providing information about the actions of peers and competitors, was not confirmed.⁷⁶

Not all financial elites were lucky enough to experience catch-and-release. Xu Xiang, dubbed the “hedge fund king,” came under police custody in 2016. His hedge fund, Zexi Investment, had grown by nearly 800 percent between 2011 and 2016 and it had been left unscathed in the stock market crash that past summer, in fact growing spectacularly during the crisis. By the end of the summer, the annual return on his funds was more than 200 percent, but a viral social media post accused Xu and his firm of abusing connections to manipulate stocks in their favor and to gain insider information on government actions. After initially being tipped off that the authorities were headed for him, Xu was captured in a police blockade on a bridge while attempting to flee.⁷⁷ In January 2017 Xu was sentenced to five and a half years in prison for market manipulation as well as fined a record 1.1 billion yuan.⁷⁸

⁷² Interview, private institutional investor, Shanghai, May 2017. See also Hou Qiang, “Securities Firms Fined for Profiteering amid Stock Market Chaos,” *Xinhua News*, 2 September 2015.

⁷³ Interview, private institutional investor, Shanghai, May 2017.

⁷⁴ Yifan Xie and Wei Gu, “China Securities Official is Under Investigation,” *The Wall Street Journal*, 15 November 2015. Zhang Yujun died of cancer in 2021. He was never officially charged, and the CCDI never presented evidence against him.

⁷⁵ Sophia Yan, “Giant Chinese Brokerage Can’t Find Its CEO,” *CNN Money*, 24 November 2015.

⁷⁶ Opinion, “The Case of China’s Missing Brokers,” *The Wall Street Journal*, 8 December 2015; Scott Cendrowski, “The ‘Warren Buffet’ of China Disappears,” *Fortune*, 11 December 2015; Xie Yu, “‘Missing’ Fosun Chairman Guo Guangchang Back at Work after ‘Helping Chinese Authorities with Investigation,’” *South China Morning Post*, 14 December 2015; Scott Cendrowski, “China’s Anti-Corruption Drive Nets Another Top Banker,” *Fortune*, 9 December 2015.

⁷⁷ Alex W. Palmer, “The Fall of China’s Hedge-Fund King,” *The New York Times Magazine*, 29 March 2016.

⁷⁸ Xie Yu, “Once China’s Hedge Fund Guru, Xu Xiang Sentenced to 5.5 Years in Prison for Market Manipulation,” *South China Morning Post*, 23 January 2017.

The CSRC moved to fine and punish the makers and operators of technology platforms (“brokerage access platforms”) that enabled retail investors to open accounts without real-name registration, a violation of the Securities Act.⁷⁹ In early November, the CCDI announced that it was investigating Yao Gang, vice chairman of the CSRC for discipline violations. Yao, who headed the department that chooses which companies go public on the Chinese exchanges, had served in his position since 2009 and he ranked as one of the top CCP officials at the CSRC. After announcement of the investigation, the CSRC removed Yao’s profile from its website, and CSRC chairman Xiao Gang that declared both Yao and Zhang Yujun, the former assistant chairman relieved of his position following probes in September, were “negative examples.”⁸⁰

Although the anti-corruption campaign targeted political officials over illicit ties to business since its inception in 2013, regulatory officials became an explicit focus after the stock market crisis. Zhang Yujun, mentioned above, and Yao Gang were the first financial regulatory officials to come under CCDI investigation in 2015, but between 2015 and 2021, at least thirty-four other officials, in banking, insurance, and securities regulation, met similar fates. At least six of these officials, all in Inner Mongolia’s banking regulatory offices, were publicly linked to Xiao Jianhua and his Baoshang Bank; and three were linked to Xu Xiang, the “hedge fund king” captured on a bridge in 2016.⁸¹ Almost all of these officials were accused of abusing their positions of power for personal enrichment. Lai Xiaomin, who served on the CBRC between 1994 and 2008 and at the time of arrest was president of China Huarong Asset Management, one of the four state-owned asset management companies, was accused of receiving more than 1.7 billion RMB in bribes (more than \$250 million USD), for which he received a death sentence in the largest bribery case in PRC history.⁸²

The CCP also trained its sights on local-level business actors, especially in the 2018 launch of a campaign to “Sweep Away the Black and Eliminate Evil” (扫黑除恶). The campaign was launched by the Office of the Leading Group for the Special Struggle against Gangs and Evil (扫黑除恶专项斗争领导小组办公室) to “normalize the fight against gangs and evil.”⁸³ The

⁷⁹ These were Hundsun Technology, Mecrt Corporation (Shanghai), and Hithink Flush Information company. The technology platforms also enabled hierarchical margin lending; once a borrower’s account had declined in value by a certain amount, lenders could control the accounts to sell or buy, leading to faster changes in equities prices than regulators thought was technically possible—the digital equivalent of breaking the ticker-tape machine. The largest platform was HOMS, owned by Hundsun Technologies in Hangzhou, in which Alipay held a 20.6 percent stake. See Dinny McMahon, “Peer-to-peer Lending Takes Off in China,” *The Wall Street Journal*, 3 June 2015; Chuin-Wei Yap, “China Crackdown on Margin Lending Hits Peer-to-Peer Lenders,” *The Wall Street Journal*, 13 July 2015; Jess McHugh, “China ‘Black Monday’ Timeline: The Chinese Stock Market Crash and How it Happened,” *International Business Times*, 24 August 2015; Ben Mohinsky, “China’s ‘National Team’ is Doing Everything in its Power to Stop Stocks Crashing: Here’s the Playbook,” *Business Insider*, 5 January 2016; Yue Wang, “Hundsun Tech Under Probe After China’s Stock Bust,” *Forbes*, 13 July 2015. Interview, private institutional investor, Shanghai, May 2017.

⁸⁰ Xie and Gu, “China Securities Official Is Under Investigation.”

⁸¹ Data were collected from the CCDI website and media reports.

⁸² “华融公司原董事长赖小民被执行死刑”(Lai Xiaomin, Former Chairman of Huarong Company, Is Executed), 29 January 2021. https://www.ccdi.gov.cn/yaowen/202101/t20210129_235027.html; “权威解读 | 赖小民案案财物近 17 亿元已追缴”(Nearly 1.7 Billion Yuan of Property Involved in the Lai Xiaomin Case Has Been Recovered). https://www.ccdi.gov.cn/toutiao/202008/t20200814_223735.html

⁸³ “检察机关推进扫黑除恶专项斗争：坚持‘稳、准、狠’”(The Procuratorial Organs Promote a Special Campaign against Gangsters and Evil: Adhere to “Stability, Accuracy and Ruthlessness”) 7 January 2020. https://www.spp.gov.cn/spp/cffhjcznzxsfsfwdjzdgz/202001/t20200107_452093.shtml; “扫黑除恶从专项斗争转向

campaign is accompanied by volumes of propaganda, typical of campaigns, that focus on violent organized crime and extortion, highlighting stories of hidden bodies and family triad. But the campaign has also targeted economic crimes, such as illegal finance and business and political actors forming “protective umbrellas” to shield themselves from scrutiny and prosecution.⁸⁴ In some cases, local campaign enforcers go back decades to round up local entrepreneurs for actions that some call “original sin,” things businesspeople simply had to do to work within a prohibitive institutional environment.

In addition to these populist and coercive responses, the CCP has made a concerted effort to rearticulate the party-state’s institutional control over the financial sector. The Financial Stability and Development Committee (金融稳定发展委员会) was established in July 2017, as Xi Jinping himself expressed that the party’s leadership over financial matters should be emboldened to address systemic risk and that “financial security is an essential part of national security.”⁸⁵ The connection between the financial sector and “national security” was not new in 2017; Articles 19 and 20 of the 2015 National Security Law establish “economic security” and “financial stability” as pillars of national security, and Xi’s government increasingly saw many aspects of economic organization as part of an expanded view of “comprehensive national security.”⁸⁶ The securitization of financial governance marks a new turn in the CCP’s management of capital. The CBRC and China Insurance Regulatory Commission (CIRC) were reorganized into a combined commission, and the Office of Financial Stability has begun to organize coordinating bodies at the local levels to reassert central control over a sector with inherent social risks.⁸⁷

Rule by market in equity markets has also entailed the widespread presence of the state as shareholder and corporate governance participant in the wake of the 2015 crisis. The expansion of state capital has a strategic and upgrading logic as well as a risk management logic. The “financialization” of the state’s role in the economy has accompanied industrial-policy efforts, especially the Made in China 2025 plans to upgrade the Chinese economy and facilitate self-reliance and competition in frontier sectors.⁸⁸ China’s industrial-policy efforts have received a

常态化开展未来怎么做?” (What Should We Do in the Future When the Anti-crime Campaign Shifts from a Special Campaign to a Normal One?), Xinhua News Agency, 30 March 2021. http://www.gov.cn/xinwen/2021-03/30/content_5596864.htm

⁸⁴ See Ben Hillman, “Law, Order and Social Control in Xi’s China,” *Issues and Studies* 57, no. 2: 1–21.

⁸⁵ “全国金融工作会议在北京召开 习近平发表重要讲话,” (Xi Jinping Delivers an Important Speech at the National Financial Work Conference Held in Beijing), 15 July 2017. <https://news.qq.com/a/20170715/035661.htm>.

⁸⁶ See Pearson, Rithmire, Tsai, “China’s Political Economy and International Backlash”; Sheena Chestnut Greitens, “Internal Security and Grand Strategy: China’s Approach to National Security under Xi Jinping,” statement before the U.S.-China Economic & Security Review Commission, 28 January 2021. https://www.uscc.gov/sites/default/files/2021-01/Sheena_Chestnut_Greitens_Testimony.pdf; Helena Legarda, “China’s New International Paradigm: Security First,” *Merics*, 15 June 2021. <https://merics.org/en/chinas-new-international-paradigm-security-first>

⁸⁷ “国务院金融稳定发展委员会成为并召开第一次会议” (The Financial Stability and Development Committee of the State Council Holds its First Meeting), 8 November 2017. http://www.gov.cn/xinwen/2020-01/14/content_5469125.htm

⁸⁸ This section draws on material from Hao Chen, Hao and Meg Rithmire. 2020. “The Rise of the Investor State: State Capital in the Chinese Economy.” *Studies in Comparative International Development* 55(3):257-77. doi: 10.1007/s12116-020-09308-3. See also Margaret Pearson, Meg Rithmire, and Kellee Tsai, “China’s Political Economy and International Backlash: From Interdependence to Security Dilemma Dynamics,” *International Security* 47, no. 2 (Fall 2022): 135–76.

good deal of attention, but the role of the state in corporate governance has focused on the monitoring of firms and has been extended to firms well beyond those involved in frontier technology sectors.

In November 2013, at the Third Plenum of the Eighteenth Party Congress, a Central Committee decision on “comprehensively deepening reform” formally encouraged the establishment of “state-owned capital operation companies” (国有资本运营公司) to shift from “managing enterprises” to “managing capital.”⁸⁹ In July 2014, the first two official “state capital investment companies” were established under the State-owned Assets Supervision and Administration Commission (SASAC)—managed state-owned enterprises (SOEs), COFCO (a food processing company), and SDIC (an investment holding company).⁹⁰ A year later, a State Council directive on SOE reform explicitly encouraged state capital in private firms: “state-owned capital invests in non-state-owned enterprises in various ways” to “focus on public services, high-tech, eco-environmental protection, and strategic industries ... and non-state-owned enterprises with large development prospects and strong growth potential.”⁹¹

In February 2016, two new “state-owned capital operation enterprise” pilots were established within China Chengtong Holdings Group and China Reform Holdings, both asset management holding companies governed by SASAC. Both established multiple funds, with additional shareholders primarily drawn from other SOEs that provided capital for SOEs to buy listed private firms. By the end of 2018, these two pilots managed total assets of RMB 900 billion.⁹² By 2022, twenty-three additional SOEs were designated as “state-owned capital investment companies” (国有资本投资公司) in order to, among other rationales, develop the “risk prevention role of the state economy.”⁹³ Although the official language remains vague about the distinction between capital investment and operation, interviews suggest that capital operation firms may take a more active investment stance, perhaps managing distressed assets, whereas investment firms handle more passive investments.⁹⁴

As the central state has emphasized the need for state capital investment and operation, local governments have joined central shareholding funds and SOEs in pursuit of investments in the private sector. Beginning in the second half of 2017—after the establishment of central-level experimental state capital investment and operation enterprises but before the 2018 document providing official guidance on these firms—local SASACs began to establish state-owned

⁸⁹ State Council, “中共中央关于全面深化改革若干重大问题的决定” (Decision on Major Problems in the Deepening of Reform), 15 November 2013. http://www.gov.cn/jrzq/2013-11/15/content_2528179.htm

⁹⁰ State capital investment companies are called 国有资本投资公司在 Chinese. “国务院国资委举办 ‘四项改革’ 试点新闻发布会” (SASAC Holds Press Conference on the “Four Reforms”), 15 July 2014. <http://www.sasac.gov.cn/n2588020/n2588072/n2591426/n2591428/c3731034/content.html>

⁹¹ State Council, “关于深化国有企业改革的指导意见” (Guiding Opinions on Deepening the Reform of State-Owned Enterprises), 13 September 2015. http://www.gov.cn/zhengce/2015-09/13/content_2930440.htm

⁹² The website of China Chengtong Holdings Group lists these partners in the establishment of “China Structural Reform Fund Corporation Limited.” http://www.cctgroup.com.cn/cctgroupen/about_us/group_profile/index.html; Li Yifang, “A 股股权转让大增的特征，原因及政策建议” (Increase in A Share Equity Transfer: Reason, Future, and Policy Recommendations) 上证研报 (Shanghai Securities Research Report). Number 8 (2019), 16.

⁹³ “5 家中央企业正式转为国有资本欧子公司” (Five SOEs Formally Transformed into State Capital Investment Companies), 21 June 2022. http://www.gov.cn/xinwen/2022-06/21/content_5696886.htm Other rationales include “deepening reform, developing world-class enterprises, and improving economic competitiveness, strength, and control.”

⁹⁴ Interview, former CSRC official, August 2019.

capital investment and operation companies. Local investment companies have, in many cases, gone beyond minority investments, frequently engaging in “ownership transfers” of private, listed firms—essentially nationalization through open market equity purchases.

Most examples of private firms falling under state control involve distressed firms or large conglomerate firms under tremendous political and financial pressure. In many cases, firms experiencing a suspension in trading for a significant amount of time are eventually purchased by local SASACs, as was the case with a technology company in Anhui (Changxin Technology) and several others in Fujian in 2018. Those that welcomed state capital have argued that state investment or ownership helps distressed firms access capital and resources, whereas others (especially academic economists) have worried that such “mixed ownership reform” is inviting state capital into the private sector rather than the other way around. In the cases of large, distressed conglomerate firms, heavy pressure from regulators has forced companies such as HNA, Dalian Wanda, and Fosun to unwind some of their global purchases; HNA reportedly sold its 7.6 percent stake in Deutsche Bank to a group comprising a number of state shareholding firms. Some of Anbang’s insurance assets were taken over by local SOEs in Xiamen and Shenzhen after the company was nationalized and its chairman jailed in early 2018.⁹⁵

State shareholding activities show the role of the state in setting prices and in governing entry and exit. Rather than allowing many firms to exit the market through bankruptcy, they enter state receivership on the open market (or through asset seizure, as in the case of Anbang) and their principals are dealt with by the state’s coercive powers. In the aggregate, the large-scale interventions by the “national team” at the height of the crisis show the state’s desire to arrest price fluctuations even when policymakers themselves initially welcome a market adjustment.

VI. Conclusion: The Inherent Instability of Rule by Market

In their ideal typical form, markets and market mechanisms exert discipline over economic actors; they facilitate firm entry, price-setting, and the exit of un- or under-competitive providers of goods and services.⁹⁶ In many arenas of resource allocation in China, however, despite the appearance and presence of markets, they do not perform these functions. Instead, market mechanisms have been introduced to induce competition and provide a source of information, but the state retains the disciplinary prerogative. Market-supplied discipline would relieve state agents of having to decide which firms should win or lose and how prices should be set, but market discipline also requires a tolerance for some instability (e.g. bankruptcies and price movements) and limits political discretion.

I have argued that market mechanisms in Chinese factor markets have served as “state-supporting institutions” rather than the reverse. State discretion over prices, allocation, and entry/exit in land and equity markets has empowered the party-state vis-à-vis firms and households. But, as is clear from these narratives of land and equity markets, rule by market entails considerable disadvantages. That partial liberalization and markets without discipline distort resource allocation is not a novel observation. Further, measuring distortion or estimating “efficient” resource allocation are tasks best left to economists rather than political scientists.

⁹⁵ Chen Yanqing (陈燕青), “地方国资入主民企再掀高潮: 今年超 10 家民营 A 股公司将变身国企” (Entry of Local State Capital into Private Enterprises Continues: More than Ten Private A-share Companies Will Become State-owned This Year,” *Tencent News: Finance*, 9 October 2018.

⁹⁶ Joseph A. Schumpeter, *Capitalism, Socialism and Democracy* (Florence: Routledge, 2010).

Instead, I conclude by noting the Janus-faced effects of rule by market on the power of the Chinese state. Rule by market has made an economy in which markets have not supplanted state power in allocating resources and a society in which social and economic actors wield considerably less power than the state itself. Yet, in the aggregate, the CCP's intolerance of instability and its willingness and capacity to intervene in markets and issue populist promises to tame their destabilizing effects constrain the state's autonomy in two ways.

First, as I showed in the case of the stock market crisis under Xi Jinping, cycles of market actions and state reactions offer ample opportunities for arbitrage. This outcome, again, is unsurprising, as generations of writing on state-market interactions have identified how greater state intervention furnishes greater opportunities for rent-seeking and corruption. The more interesting constraint on the state's autonomy is that, second, rule by market traps policymakers in cycles of intervention, the result of which is patterns of economic behavior that inhibit the state's periodic efforts to allocate resources more efficiently. What is most politically consequential is not that resources are misallocated according to the estimation of economists, but rather that the CCP itself seems to prefer more market discipline but cannot find itself willing to tolerate it. Efforts to reform land and financial capital allocation through market mechanisms in the context of the CCP's focus on political stability generate self-undermining feedback effects.

Such a pattern suggests amendments to two influential arguments about why the CCP has thus far achieved economic transformation without classic "market-supporting institutions" and while maintaining its monopoly on political power. First, scholars have pointed to the CCP's adaptive capacity—its reliance on experimentation, campaigns, and low levels of power vested in institutions—as sources of policymaking strength that have allowed the regime to learn, pivot, and respond effectively to social and economic problems.⁹⁷ I do not dispute that this "unorthodox policy style" has been effective in facilitating economic development and addressing its many attendant social and economic problems, but rule by market dynamics suggest there are limits to a preference for discretion and an intolerance for instability. To be sure, scholars who emphasize the advantages of "guerilla policymaking" do not contend that it is effective in all arenas, and indeed recognize that advanced financial markets, for example, may require rule of law along with other prevalent "market-supporting institutions."⁹⁸ Nonetheless, it is notable that the reliance on campaigns and party-state intervention ironically constrains the state in advancing its own economic policymaking goals. Unorthodox policymaking may have aided the CCP in lifting millions out of poverty and industrializing with Leninist political institutions, but those precise technologies of governance have also trapped the regime in cycles of liberalization and reversal.

Second, rule by market dynamics, and especially the role of crisis in generating authoritarian response and institutional changes that limit market discipline, may mean that contemporary China has reached the limit of an "evolutionary governance" process whereby "good enough institutions" and market development constituted a virtual cycle.⁹⁹ Rule by market is fundamentally a negative policy feedback loop, by which liberalization produces intolerable

⁹⁷ For seminal statements, see Heilmann, Sebastian and Elizabeth J. Perry. 2011. *Mao's Invisible Hand : The Political Foundations of Adaptive Governance in China*. Cambridge, Mass: Harvard University Asia Center : Distributed by Harvard University Press. Heilmann, Sebastian. 2018. *Red Swan : How Unorthodox Policy-Making Facilitated China's Rise*. Hong Kong: Chinese University Press.

⁹⁸ See Heilmann, *Red Swan*, conclusion.

⁹⁹ Ang, Yuen Yuen 2016. *How China Escaped the Poverty Trap*. Ithaca, NY: Cornell University Press, Yang, Dali L. 2004. *Remaking the Chinese Leviathan : Market Transition and the Politics of Governance in China*. Stanford, Calif.: Stanford University Press.

instability and state response in cycles that entrench systemic problems, such as land finance and equity market arbitrage, rather than solve them. Breaking that cycle would indeed mean imbuing markets, even law, with disciplinary powers at the expense of the discretion of the party-state itself.

References

- Ang, Yuen Yuen 2016. *How China Escaped the Poverty Trap*. Ithaca, NY: Cornell University Press.
- Brandt, Loren and Eric Thun. 2010. "The Fight for the Middle: Upgrading, Competition, and Industrial Development in China." *World Development* 38(11):1555-74. doi: 10.1016/j.worlddev.2010.05.003.
- Brandt, Loren, Johannes Van Biesebeek and Yifan Zhang. 2012. "Creative Accounting or Creative Destruction? Firm-Level Productivity Growth in Chinese Manufacturing." *Journal of Development Economics* 97(2):339-51. doi: 10.1016/j.jdeveco.2011.02.002.
- Brandt, Loren, Trevor Tombe and Xiaodong Zhu. 2013. "Factor Market Distortions across Time, Space and Sectors in China." *Review of economic dynamics* 16(1):39-58. doi: 10.1016/j.red.2012.10.002.
- Bremmer, Ian. 2010. *The End of the Free Market : Who Wins the War between States and Corporations?* New York: Portfolio.
- Cai, Meina. 2016. "Land for Welfare in China." *Land Use Policy* 55:1-12. doi: 10.1016/j.landusepol.2016.03.014.
- Cai, Meina and Xin Sun. 2018. "Institutional Bindingness, Power Structure, and Land Expropriation in China." *World Development* 109:172-86. doi: 10.1016/j.worlddev.2018.04.019.
- Chen, Hao and Meg Rithmire. 2020. "The Rise of the Investor State: State Capital in the Chinese Economy." *Studies in Comparative International Development* 55(3):257-77. doi: 10.1007/s12116-020-09308-3.
- Cheng, Siwei and Ziran Li. 2015. *The Chinese Stock Market*. Houndmills, Basingstoke, Hampshire New York, NY: Palgrave Macmillan.
- Culpepper, Pepper D. 2015. "Structural Power and Political Science in the Post-Crisis Era." Pp. 391-409, Vol. 17: Cambridge University Press.
- Eaton, Sarah and Genia Kostka. 2017. "Central Protectionism in China: The "Central Soe Problem" in Environmental Governance." *The China quarterly (London)* 231:685-704. doi: 10.1017/S0305741017000881.
- Evans, Peter B. 1979. *Dependent Development : The Alliance of Multinational, State, and Local Capital in Brazil*. Princeton, N.J.: Princeton University Press.
- Fields, Gary S. 1982. "Growth and Distribution in the Market Economies of East Asia." *World Politics* 35(1):150-60. doi: 10.2307/2010284.
- Gallagher, Mary Elizabeth. 2017. *Authoritarian Legality in China : Law, Workers, and the State*. Cambridge, United Kingdom ; New York, NY, USA: Cambridge University Press.
- Ginsburg, Tom and Tamir Moustafa. 2008. *Rule by Law : The Politics of Courts in Authoritarian Regimes*. Cambridge [UK] New York: Cambridge University Press.
- Haggard, Stephan. 2018. *Developmental States*. Cambridge: Cambridge University Press.
- Hall, Peter A. and David W. Soskice. 2001. *Varieties of Capitalism : The Institutional Foundations of Comparative Advantage*. Oxford England ; New York: Oxford University Press.
- Heilmann, Sebastian and Elizabeth J. Perry. 2011. *Mao's Invisible Hand : The Political Foundations of Adaptive Governance in China*. Cambridge, Mass: Harvard University Asia Center : Distributed by Harvard University Press.
- Heilmann, Sebastian. 2018. *Red Swan : How Unorthodox Policy-Making Facilitated China's Rise*. Hong Kong: Chinese University Press.
- Hertog, Steffen. 2010. "Defying the Resource Curse: Explaining Successful State-Owned Enterprises in Rentier States." *World Politics* 62(2):261-301. doi: 10.1017/S0043887110000055.
- Heurlin, Christopher. 2016. *Responsive Authoritarianism in China : Land, Protests, and Policy Making*. New York, NY: Cambridge University Press.
- Hsieh, Chang-Tai and Peter J. Klenow. 2009. "Misallocation and Manufacturing Tfp in China and India." *The Quarterly Journal of Economics* 124(4):1403-48. doi: 10.1162/qjec.2009.124.4.1403.
- Hsueh, Roselyn. 2011. *China's Regulatory State : A New Strategy for Globalization*. Ithaca: Cornell University Press.
- Hsueh, Roselyn. 2012. "China and India in the Age of Globalization: Sectoral Variation in Postliberalization Reregulation." *Comparative Political Studies* 45(1):32-61. doi: 10.1177/0010414011421305.
- Huang, Yasheng. 1996. *Inflation and Investment Controls in China : The Political Economy of Central-Local Relations During the Reform Era*. Cambridge [England] ; New York, NY, USA: Cambridge University Press.
- Kornai, János. 1992. *The Socialist System : The Political Economy of Communism*. Princeton, N.J.: Princeton University Press.

- Kurlantzick, Joshua. 2016. *State Capitalism : How the Return of Statism Is Transforming the World*. New York, NY: Oxford University Press.
- Lardy, Nicholas R. 2019. *The State Strikes Back : The End of Economic Reform in China?* Washington, DC: Peterson Institute for International Economics.
- Lee, Ching Kwan. 2007. *Against the Law: Labor Protests in China's Rustbelt and Sunbelt*. Berkeley: University of California Press.
- Li, Chen, Huanhuan Zheng and Yunbo Liu. 2022. "The Hybrid Regulatory Regime in Turbulent Times: The Role of the State in China's Stock Market Crisis in 2015–2016." *Regulation & governance* 16(2):392-408. doi: 10.1111/rego.12340.
- Liebman, Benjamin L. 2014. "Legal Reform: China's Law-Stability Paradox." *Daedalus (Cambridge, Mass.)* 143(2):96-109. doi: 10.1162/DAED_a_00275.
- Lindblom, Charles Edward. 1977. *Politics and Markets : The World's Political Economic Systems*. New York: New York : Basic Books, c1977.
- Liu, Adam Y., Jean C. Oi and Yi Zhang. 2022. "China's Local Government Debt: The Grand Bargain." *The China journal (Canberra, A.C.T.)* 87(1):40-71. doi: 10.1086/717256.
- Looney, Kristen E. 2020. *Mobilizing for Development : The Modernization of Rural East Asia*. Ithaca New York: Cornell University Press.
- Lowi, Theodore J. 1979. *The End of Liberalism : The Second Republic of the United States*. New York: Norton.
- Mattingly, Daniel C. 2020. "The Art of Political Control in China." Cambridge, United Kingdom ; New York, NY: Cambridge University Press,. Retrieved.
- Minzner, Carl. 2018. *End of an Era : How China's Authoritarian Revival Is Undermining Its Rise*. New York, NY, United States of America: Oxford University Press.
- Montinola, Gabriella, Yingyi Qian and Barry R. Weingast. 1995. "Federalism, Chinese Style: The Political Basis for Economic Success in China." *World Politics* 48(1):50-81.
- Musacchio, Aldo. 2014. *Reinventing State Capitalism : Leviathan in Business, Brazil and Beyond*, Edited by S. G. Lazzarini and S. G. Lazzarini. Cambridge, Massachusetts: Harvard University Press.
- Naughton, Barry. 1994. "Chinese Institutional Innovation and Privatization from Below." *The American Economic Review* 84(2):266-70.
- Naughton, Barry. 1995. *Growing out of the Plan : Chinese Economic Reform, 1978-1993*. New York, NY: Cambridge University Press.
- Naughton, Barry and Kellee S. Tsai. 2015. *State Capitalism, Institutional Adaptation, and the Chinese Miracle*. New York, NY: Cambridge University Press.
- Oi, Jean Chun. 1999a. *Rural China Takes Off: Institutional Foundations of Economic Reform*. Berkeley: University of California Press.
- Oi, Jean Chun. 1999b. *Rural China Takes Off : Institutional Foundations of Economic Reform*. Berkeley: University of California Press.
- Ong, Lynette H. 2022. *Outsourcing Repression : Everyday State Power in Contemporary China*. New York, NY: Oxford University Press.
- Pempel, T. J. 2021. *A Region of Regimes : Prosperity and Plunder in the Asia-Pacific*. Ithaca New York: Cornell University Press.
- Rithmire, Meg. 2015. *Land Bargains and Chinese Capitalism : The Politics of Property Rights under Reform*. New York: Cambridge University Press.
- Rithmire, Meg. 2017. "Land Institutions and Chinese Political Economy: Institutional Complementarities and Macroeconomic Management." *Politics & Society* 45(1):123-53.
- Rithmire, Meg 2023. *Precarious Ties: Business and the State in Authoritarian Asia* New York Oxford University Press.
- Rong, Yue. 1994. *血战中国股市: 中国股民悲喜录*. Ha'erbin Shi: Dong bei lin ye da xue chu ban she.
- Sargeson, Sally. 2013. "Violence as Development: Land Expropriation and China's Urbanization." *The Journal of Peasant Studies* 40(6):1063-85. doi: 10.1080/03066150.2013.865603.
- Shih, Victor C. 2008. *Factions and Finance in China: Elite Conflict and Inflation*. Cambridge: Cambridge University Press.
- Shirk, Susan L. 1993. *The Political Logic of Economic Reform in China*, Vol. 24. Berkeley: University of California Press.

- Smith, Nick R. 2021. *The End of the Village : Planning the Urbanization of Rural China*. Minneapolis: University of Minnesota Press.
- Snyder, Richard. 2001. *Politics after Neoliberalism : Reregulation in Mexico*. Cambridge, UK ; New York, NY: Cambridge University Press.
- Steinfeld, Edward S. 1999. *Forging Reform in China : The Fate of State-Owned Industry*. Cambridge ;New York: Cambridge University Press.
- Tan, Yeling. 2021. *Disaggregating China, Inc. : State Strategies in the Liberal Economic Order*, Edited by M. Project. Ithaca [New York: Cornell University Press.
- Tsai, Kellee S. 2002. *Back-Alley Banking: Private Entrepreneurs in China*. Ithaca: Cornell University Press.
- Vogel, Steven Kent. 2018. *Marketcraft : How Governments Make Markets Work*. New York, NY: Oxford University Press.
- Wade, Robert. 1990. *Governing the Market : Economic Theory and the Role of Government in East Asian Industrialization*. Princeton, N.J.: Princeton University Press.
- Wang, Dong. 1993. *股票风潮动*. Beijing: Shou du shi fan da xue chu ban she.
- World Bank. 1993. *The East Asian Miracle : Economic Growth and Public Policy*. New York, N.Y.: Oxford University Press.
- Yang, Dali L. 2004. *Remaking the Chinese Leviathan : Market Transition and the Politics of Governance in China*. Stanford, Calif.: Stanford University Press.
- Zhong, Su. 1992. *世纪之交股票潮冲击中国：深沪股市新新闻 = at the across of Century China Shocked by Share Tide : News from Shen Zhen & Shanghai Stock Exchange*. Beijing: Jie fang jun wen yi chu ban she.