

## **Senior Seminar on The Wealth and Well-Being of Nations:**

Each year, seniors in the department of economics participate in a semester-long course that is built around the ideas and influence of that year's Upton Scholar. By the time the Upton Scholar arrives in October, students will have read several of his or her books and research by other scholars that has been influenced by these writings. This advanced preparation provides students the rare opportunity to engage with a leading intellectual figure on a substantive and scholarly level.

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With generous support from the Charles G. Koch Charitable Foundation, the department has initiated a research colloquium that gives students the opportunity to read and discuss seminal articles aimed at deepening their understanding of the market process. Students also develop original analysis that applies economic ideas to novel contexts. Colloquium participants receive close mentoring as they craft an article with the eventual goal of publication in a newspaper, magazine, or academic journal. The themes of the research colloquium and annual forum are supported with a speaker series featuring the next generation of scholars working on questions central to our understanding of the nature and causes of wealth and well-being.

## **Annual Proceedings of The Wealth and Well-Being of Nations:**

The keynote address presented by the Upton Scholar is an important contribution to the public discourse on the nature and causes of wealth and well-being. Further, the annual forum includes presentations by noted scholars who expand upon or challenge the work of the Upton Scholar. These presentations are assembled in the *Annual Proceedings of the Wealth and Well-Being of Nations*, which serves as an important intellectual resource for students, alumni, and leaders within higher education.



THE ANNUAL  
PROCEEDINGS OF THE  
WEALTH AND WELL-  
BEING OF NATIONS

2015-2016

VOLUME VIII

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The Annual Proceedings of the Wealth and Well-Being of Nations, 2015-2016.

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Printed in the United States of America

ISBN: 978-0-578-18317-6

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# Introduction

**Warren Bruce Palmer<sup>1</sup>**

**A**s the Elbert H. Neese, Jr. Professor of Economics, it was my pleasure to organize the eighth *Wealth and Well-Being of Nations: a Forum in Honor of Miller Upton*, and now, in turn, to introduce the eighth *Annual Proceedings of the Wealth and Well-Being of Nations*, a selection of papers presented at the Forum.

Through its Miller Upton Programs, the Department of Economics at Beloit College focuses the attention of its students, faculty, broader College community and alumni on the core issues of human freedom and on what promotes and what impedes the wealth and well-being of nations.

The centerpiece of this suite of programs is the annual *Wealth and Well-being of Nations: A Forum in Honor of Miller Upton*. Held each fall, the Miller Upton Forum features one of the world's most influential thinkers on the ideas and institutions necessary for advancing the freedom, wealth and well-being of the nations and peoples of the world. Each year's Miller Upton Scholar is joined on campus by a group of other thinkers and practitioners who engage us in a week of enlightening classroom discussions, forums, and one-on-one conversations, capped off by the Miller Upton Scholar's keynote address -- The June B. Martin'40 and Edgar W. Martin Memorial Lecture.

The Miller Upton Programs and the Miller Upton Forum are named in honor of Miller Upton, the sixth President of Beloit College, and are inspired by Miller's unflinching dedication to the ideals of a liberal society: political freedom, the rule of law, and peace and prosperity through the voluntary exchange of goods and ideas.

In this eighth forum, we turned our attention to "Entrepreneurship and the Chinese Economy". The economic well-being of one-fifth of the world's population depends on the performance of the Chinese economy; more than 1.3 billion people make their living in this ancient land that holds less than 7 percent of the

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<sup>1</sup> Warren Bruce Palmer is the Elbert H. Neese, Jr. Professor Economics, Beloit College.

world's cultivated acreage. No other event in the last forty years has done more to advance wealth and well-being in the world than the revival of entrepreneurship in China.<sup>2</sup>

### *Historical Context*

China had a long history as the dominant Asian power with a vibrant, commercial economy. In 1800, China's economy was the largest in the world, accounting for over 25 percent of global output. But the industrializing world soon eclipsed traditional China, which suffered through 150 years of domestic crisis and economic stagnation exacerbated by foreign invasion. By 1949 one-fourth of the world's population lived in China, but its economy produced only 5 percent of global output, and most of its citizens lived in terrible poverty.

The triumph in 1949 of the Chinese Communist Party in its civil war with the Nationalist Party produced China's most effective national government in more than 100 years. The new government achieved some remarkable successes, particularly in public health, raising life expectancy from less than forty years in 1949 to near seventy years by 1978. Yet, the economic record was very mixed.

The Chinese Communist Party adopted a Soviet-style command economy, bringing to a halt China's rich history of entrepreneurship and commerce, shutting down private market activity and putting 'politics in command' of the economy and people's daily lives. By the late 1970s, China had established itself as a major industrial power, but its industry was inefficient, producing inferior products using antiquated technology, and its industrial expansion served mainly to expand heavy industry itself, not to expand consumption or rapidly improve living standards. Even in urban China, which received preferential treatment, consumer goods were low in quality, lacking in variety and hard to get, even with ration coupons. In rural China, with 80 percent of the nation's population, the growth of agricultural output had barely kept pace with the growth of population. Hundreds of millions of China's rural citizens still lived in severe poverty, and China was substantially poorer than Sub-Saharan Africa.

After thirty years attacking market activity and repressing individual freedom and entrepreneurship, the Chinese State at the direction of the Chinese Communist Party suddenly pivoted in late 1978, relaxing its stranglehold on entre-

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2 This and following three paragraphs are based on Palmer (2010).

preneurship, first in the countryside and then in the urban economy. The results have been phenomenal – China sustained an 8% average annual growth rate of real GDP per capita for the next thirty years, an unprecedented rate of growth for such a long period in such a populous nation.

In this, the eighth Miller Upton Forum, we wished to explore the meaning and impact of entrepreneurship in China, both past and present. We assembled a distinguished, eclectic group of scholars and practitioners – Beloit College faculty, Beloit College alumni and top China scholars who led us through four days of class visits, private conversations and three panel discussions as they joined this year’s Miller Upton Scholar, Professor Yasheng Huang.

### *Yasheng Huang, Eighth Miller Upton Scholar*

Yasheng Huang is the International Program Professor in Chinese Economy and Business, Professor of Global Economics and Management, and Associate Dean for International Programs and Action Learning at the MIT Sloan School of Management. He is a promoter and scholar of entrepreneurship. He founded and directs MIT’s China Lab and India Lab, which help entrepreneurs improve their management skills.

The *Economist* magazine named his most recent book in English on the Chinese economy “one of the best books of 2008”. His book, *Capitalism with Chinese Characteristics*, shows how rural private entrepreneurship, supported by financial liberalization and microeconomic flexibility, played a central role in China’s economic miracle.

The topic of this path breaking book owes much to Professor Huang’s own educational journey. Professor Huang grew up during the Cultural Revolution which disrupted education across China. Instead of a formal education, Professor Huang pursued his own reading agenda, studying what books he could find, and learning English by clandestinely listening to Voice of America.

Educational liberalization in China coincided with Deng Xiaoping’s economic liberalization. Rejecting China’s isolation during the Mao years, Deng Xiaoping’s opening to the world made it possible once again for Chinese students to study abroad, and Professor Huang was among the earliest group of Chinese undergraduates to study in the US. In 1981 he began his undergraduate studies at Harvard University where he completed his undergraduate degree, and then his Ph.D. at Harvard’s Kennedy School. The arc of Professor Huang’s education and

scholarship follows the economic reforms in China that transformed the most populous nation on earth.

Since 1978 China's economic growth -- first led by an explosion in rural entrepreneurship as Huang (2008) shows -- has raised more people from the direst economic poverty in the shortest time than has ever happened in human history. China's economic reforms have literally lit up the sky: examine the cover of this volume and compare the darkness of North Korea to the bright lights of China today. In 1978 China's per capita electricity consumption was lower than what impoverished North Korea currently consumes.<sup>3</sup> China now is the world's largest producer and consumer of electricity and has, at least, the world's second largest economy. What happens in the Chinese economy affects the entire world. Understanding the past and future of China's economic performance must play a central role in our study of the wealth and well-being of humanity.

As impressive as China's growth has been, China still has a long way to go to raise its GDP per capita to the level of other advanced economies, a standard that Huang sets as the criterion for success in his paper for this publication which expands his keynote address for the Upton Forum. (His keynote talk can be seen at <http://bit.ly/29xyqbY>, starting at 9:30 in video.)

In his paper "State Capitalism in China", Professor Huang asserts that "state capitalism is indeed an empirically accurate characterization of the Chinese economy today", but rather than serve as the source of China's success, "state capitalism is the source of many structural problems in the Chinese economy today" and is "detrimental to China's balanced and broadly-based socioeconomic developments."

According to Huang, achieving such a living standard should be the measure by which China's economic success is judged. As he notes, "Not a single centrally planned economy has ever succeeded in attaining high income status and a living standard comparable to that of the West." A vibrant, entrepreneurial economy is necessary for such success. In Huang's view, earlier Chinese reforms provided more scope for entrepreneurship, particularly in rural areas, than did economic policies from the 90s onward (Huang 2008). The earlier entrepreneurial growth decreased income inequality in China and rapidly raised living standards, particu-

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<sup>3</sup> In 1978 China's per capita consumption of electricity was 246 kilowatt-hours (kWh), and in 2013 North Korea's per capita electricity consumption was 660 kWh. In 2013, China's per capita consumption of electricity was 3,762 kWh -- still far below that of neighboring South Korea at 10,428 kWh. Source: World Bank: <http://data.worldbank.org/indicator/EG.USE.ELEC.KH.PC>.

larly in rural China. Under state capitalism, the share of household consumption in GDP declined, reaching a low of 35% in 2009. Recently, Huang notes that even with the over-emphasis on investment, growth is slowing down, and China may experience “simultaneously both a growth slowdown and a worsening structure of the economy.” Rather than reverse the over-emphasis on investment and depressed consumption, Huang doubts that China’s current leadership will end state capitalism and instead emphasize entrepreneurship. Huang fears that without this policy, China may suffer an economic crisis.

### *The Ideas and Influence of Yasheng Huang*

Three scholars, Loren Brandt, Carrie Currier and Barry Naughton, presented papers at the panel discussion “The Ideas and Influence of Yasheng Huang” on Friday, November 6, 2015. Their papers complement or utilize Huang’s analysis of state capitalism and entrepreneurship in China’s recent era of economic reform and growth. (The entire panel discussion can be seen at <http://bit.ly/29C4mvA>.)

In his paper, “Entrepreneurialism, New Firm Dynamics and the State: Implications for Economic Growth in China”, Loren Brandt, Professor of Economics, Noranda Chair in Economics and International Trade, University of Toronto studies the impact of new firm formation on China’s economic growth. New firms are an important source of growth in GDP and in productivity. Brandt’s paper provides support for the concerns Huang raised about state capitalism retarding economic growth, showing that new firms in sectors dominated by state capitalism tend to be less productive and less profitable than new firms in sectors with less state control.

Carrie Liu Currier, Associate Professor of Political Science and Director of Asian Studies, Texas Christian University, also considers the impact of state policies on entrepreneurship in her paper, “Entrepreneurship with Chinese Characteristics: China, Taiwan and the Tech Industry”, with a focus on policies in Taiwan. Currier builds on her earlier research on entrepreneurship in China (Currier 2007, 2009). Her paper summarizes how state policies in Taiwan have hampered Silicon-valley style tech entrepreneurship in Taiwan, based on her “interview data from 56 entrepreneurs, government officials, angel investors and venture capitalists in Taipei in 2012.” Currier cautions that in both China and Taiwan, a strong state hampers the lean start-up model of entrepreneurship that promotes innovation in the tech industry.

Barry Naughton, Sokwanlok Chair of Chinese International Affairs, University of California, San Diego, examines the insights into China's economic growth provided by Yasheng Huang's research and writing in his paper, "Yasheng Huang and the Turning Points in China's Transition". Naughton, one of the leading experts on the Chinese economy, praises Huang as "one of the few analysts of China who contributes genuinely new perceptions." For example, Naughton notes that Huang (2002) uniquely asserted that China's reversal of Maoist autarky and its opening to foreign direct investment was not only a move toward the market, as scholars thought, but also "reflected the lack of trust China's political leaders felt for China's indigenous capitalists." Naughton summarizes Huang's important contributions to identifying key turning points in China's transition process (Huang 1999, 2002, 2008). China, Naughton says, "is once again facing a profound turning point" that is both economic and political, and he expresses the hope that Huang's continued work will help scholars understand the new turning point, wherever it might lead.

### *Interdisciplinary Perspectives on Entrepreneurship in China*

On Tuesday, November 2, 2015, Don Wyatt'75, Beloit College Trustee and John M. McCardell, Jr. Distinguished Professor at Middlebury College, moderated the panel discussion, "Interdisciplinary Perspectives on Entrepreneurship in China", and three speakers submitted the papers described below. (The entire panel discussion can be seen at <http://bit.ly/29xDOvs>.)

In "The Values of Entrepreneurship in Early Modern China", Sarah Kile'03, Assistant Professor, Department of Asian Language and Cultures, University of Michigan, introduces "the entrepreneurship of the seventeenth-century maverick literatus, Li Yu (1611-1680)" and employs her review of Li Yu's money-making literary enterprises to discuss the potentially radical, transformative roles of literature, art and entrepreneurship in promoting social innovation and transformation. Li Yu's life bridged the end of the Ming and the founding of the Qing dynasties, a tumultuous time that called into question the desirability of success via the traditional examination system. As Kile describes, Li Yu adapted to the turmoil by writing fiction and plays, making "a brand of his name", and marketing his output to a diverse audience. Li Yu's pursuit of wider and wider markets for his literary output led him "to challenge the elitism of the literary world" and to promote widespread literacy for both men and women. Such efforts, Kile writes,

illustrates the “capacity for entrepreneurial activity to break down social barriers and bring previously excluded groups into the dominant cultural sphere.”

Robert André LaFleur, Beloit College Professor of History and Anthropology, takes the reader on a pilgrimage in his article, “Divine Entrepreneurs: Buying and Selling (the Same Thing, Over and Over) on China’s Southern Sacred Mountain”. Drawn to China’s sacred mountains by his interests in Chinese history and anthropology, LaFleur describes his increasing interest in the market activity flourishing on these mountains, supporting visitors recovering the traditional experience of visiting the mountain temples. The long tradition of such visits was banned during the Cultural Revolution (1966-76) when many important cultural and historical sites were damaged or destroyed. In his discussion of divinatory economics, LaFleur shows that temple entrepreneurship plays a key role in helping modern pilgrims know the proper devotional practices required when visiting these mountain temples.

Daniel M. Youd, Professor of Chinese Language and Literature, Beloit College, explores entrepreneurial themes and what it means to live “our lives as economic beings” in his paper, “An Economy of Words: Observations on Fictional Narrative and Entrepreneurship in Early Modern China”. Youd echoes Adam Smith and Deirdre McCloskey on the rhetorical character of economic activity and market exchange. Language is at the heart of economic interactions, and Youd explores the language of economic activity in prominent early modern Chinese literature. Youd contrasts the pessimistic view of market activity in *The Plum in the Golden Vase*, which he calls “a morally (and economically) conservative work”, with the more optimistic view of entrepreneurship contained in “By Excavating New Cesspits, a Skinflint Becomes a Moneybags”, one of the short stories in *The World-Reflecting Cup*. Youd then discusses the layers of economic meaning in one scene from *The Dream of the Red Chamber*. The depiction of economic life in these three literary works are quite different, and for Youd, that is precisely the point. As he writes, “these texts have varied voices and complex intellectual lineages” that each contribute to understanding our economic lives.

### *Beloit College Alumni and Entrepreneurship in China*

On Thursday, November 4, 2016, Phee Boon Kang’73, Beloit College Trustee, President and Founder at Boon Associates LLC, moderated (via SKYPE) the panel discussion, “Beloit College Alumni and Entrepreneurship in China”. The

panel featured three other Beloit College alumni pursuing successful ventures in China: Eddie Deming Tang'84, grandson of the first Chinese student at Beloit College, President and CEO of Shanghai Lexvu Opto Microelectronics Technology Co., Ltd.; Phillip Ying Chen, Founder and CEO at QianQian Tech; and Anthony Skriba'07, Executive Director at Z-Ben Advisors. While we do not have written versions of their talks, the entire panel discussion can be seen at <http://bit.ly/29kkLnM>.

### *Acknowledgments and Thanks*

On behalf of the Department of Economics let me acknowledge and thank Jennifer Kodl, Program Coordinator to the Upton Programs and Managing Editor of this volume. Her work has been crucial to the success of the Miller Upton Forum since its founding. As in all previous years, she adroitly handled all of the logistics of the many moving parts that comprised the 2015 Upton Forum, and its success derives from her expert management of an event filled week.

The Miller Upton Forum also could not achieve its current level of success without the stellar leadership of Robert Elder, chair of the Department of Economics.

Let me also extend my gratitude to members of this year's Economics Senior Seminar who eagerly embraced the opportunity to lift their economics education to a higher level, and demonstrated their success in doing so by intellectually engaging with the 2015 Upton Scholar, Yasheng Huang, and with the other scholars and experts who participated in the Upton Forum. Once again our students made the faculty of the Department of Economics proud to have been their professors.

Finally, continued thanks are due to the many alumni, friends, and charitable foundations who have supported the Miller Upton Programs. Their initial support launched the Upton Programs, and their continued support enables the Department of Economics to invite to campus the world's top scholars and practitioners who are committed to understanding and promoting the sources of the wealth and well-being of nations.



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# State Capitalism in China

Yasheng Huang<sup>1</sup>

One way to characterize Chinese economy today is that it is an economic system rooted in “state capitalism.” However, this characterization is not without controversy, both about whether the characterization is valid factually and/or whether the characterization entails prescriptive value for policy. On the more positive spectrum, Ian Bremmer, in a widely circulated article published in *Foreign Affairs*, entitled “State Capitalism Comes of Age: The End of the Free Market?” argued that the 2008 financial crisis exposed the Achilles heels of the free market system and that state capitalism was the correct antidote to excesses of capitalism. In this article as well as in his book, *The End of the Free Market: Who Wins the War Between States and Corporations?*, Bremmer went further and argued that state capitalism was not just an anti-cyclical tool but also a source of China’s long-run economic boom.

In recent years, Nicholas Lardy has offered one of the most forceful rejections of the view that Chinese growth resulted from the state capitalism model. In his book, *Markets Over Mao*, Lardy shows and argues that Chinese growth has followed a path similar to other successful economies—an overwhelming reliance on the private sector and an expansion of the market economy. He has also rejected the view that state capitalism is an empirically accurate characterization of Chinese economic strategy. He argues that reforms in China have been unidirectionally linear—toward more privatization and market economy.

In this essay, I will put forward the view that state capitalism is indeed an empirically accurate characterization of Chinese economy today but that, contrary to the claims posited by Bremmer, state capitalism is the source of many structural problems in the Chinese economy today, such as its unsustainably high level of investment, massive and most likely increasingly unproductive accumulation of

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<sup>1</sup> Yasheng Huang was the 2015 Miller Upton Scholar and is the International Program Professor in Chinese Economy and Business and a Professor of Global Economics and Management at the MIT Sloan School of Management. He is also an Associate Dean at MIT Sloan School of Management.

debt and the lackluster growth of labor income (relative to GDP growth). This account of the Chinese economy contradicts both the normative account provided by Bremmer as well as the positivistic account provided by Lardy.<sup>2</sup>

At least in terms of policy rhetoric, the Chinese policy makers have signaled at least some willingness to rethink the viability of the prevailing state capitalism model. However, the policy rhetoric has not been matched with actual policy actions. An indication of this ambiguity is the much heralded communique of the Third Plenum of the 18th Party Congress, issued in November 2013. The communique, which is the programmatic platform of the Chinese Communist Party, signaled two somewhat conflictual policy goals: 1) the Chinese Communist Party (CCP) believes that the current configuration of Chinese economic system, i.e., state capitalism, requires some substantial retooling and revamping, and 2) the CCP has ruled out reforming or attenuating the two institutional pillars of state capitalism—namely the ownership arrangements of SOEs and the political monopoly of the CCP. The intellectual debates about the utility of state capitalism among the CCP leaders appear to be largely behind us; the remaining issue is one of tactics and political will—how to reform state capitalism while preserving the fundamental institutional pillars of state capitalism.

This essay argues that state capitalism has been detrimental to China's balanced and broadly-based socioeconomic developments and to China's growth prospects. The essay does so in three steps. First, it shows that China today is still a fundamentally state-capitalistic economy. Second, it shows the trajectory of state capitalism over the past three decades. In particular, the essay shows that China's initial takeoff in the wake of rural reforms of the late 1970s followed a directional shift toward entrepreneurial capitalism. Sometime in the mid-1990s, the country made another directional shift, this time toward the version of state capitalism that characterizes the Chinese economy today.

The most important takeaway of this part of the discussion is twofold. One is that the ascendancy of state capitalism predated the 2008 financial crisis (by a long shot). A popular view among both China economists and outside analysts is that the 2008 financial crisis pivoted China toward state capitalism. This is

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2 I have proposed this way of looking at Chinese economy more expansively elsewhere. In my book, *Capitalism with Chinese Characteristics*, I showed that policies of state capitalism have tended to correlate strongly with relatively sluggish household income growth, especially income growth of rural households compared to GDP growth. *Journal of Economic Perspectives* published a shorter summary of the main arguments in the book. See Huang (2008) and (2012).

wrong. The year 2008 marked an acceleration of state capitalism, not its origin. The right way to view the 2008 version of state capitalism—“State Capitalism 2.0”, if you will—is that it was based on an existing institutional apparatus that was some 10 to 13 years in the making already. In other words, both the scale and microeconomic tools of the state capitalism 2.0—in Chinese often referred to as “advancing of the state and the retreat of the private sector”—implemented since 2008 required a strong bureaucratic and funding platform (such as State-owned Assets Supervision and Administration Commission or SASAC and State Development Bank). That platform was not constructed post 2008 but long before 2008. SASAC was formally established in 2003, having been amalgamated from many government agencies that were established in the mid-1990s (See Wang, Guthrie, and Xiao, 2012). The State Development Bank was established in 1994.

The second takeaway of this discussion is that there has been considerable heterogeneity with respect to the *directional* characteristics of Chinese economy. I stress the word “directional” to underscore an often neglected point that it is the change, not the level, that explains variables such as growth and/or broad socio-economic developments.

The third section of this essay argues that state capitalism is unsustainable, economically, politically and environmentally. I single out two issues for emphasis. One is the relatively lackluster growth of personal income relative to GDP growth; the other is the increasingly problematic structure of the Chinese macro-economy that is investment heavy and consumption light. These two features of the Chinese economy are closely related to each other.

At least there is now probably an abstract recognition of the huge downside of state capitalism among China’s ruling elites. The evidence so far suggests that the Xi Jinping leadership is willing to announce ambitious but vague and extremely long-term reform objectives but is equally willing to preserve the fundamental pillars of state capitalism. The reforms the Xi leadership has already implemented have been extraordinarily incremental and granular. They amount to baby steps that have the effect of “reversing the reversals,” i.e., reversing some of the reform reversals by the Hu Jintao leadership. While returning China to the status quo ante (i.e., 2002) should not be equated with true market reforms, the effects of the Xi leadership so far have largely been either neutral on or marginally detrimental to reforms. The concluding section discusses this and related issues.

## *The “State” of State Capitalism Today*

Analysts who argue that China today is not state-capitalistic point to the private sector’s large and growing shares of total output and employment. In his book, *Markets over Mao*, Nicholas Lardy (2013 pp. 72) shows that the private sector as of 2011 accounted for 74% of industrial output value. He also shows that net employment has been generated entirely in the private sector. The statistics cited by Lardy are meant to support his optimistic view that China today has a vibrant private sector and that China’s growth prospects are robust due to its private sector.

Whether Lardy is right or wrong critically depends on what benchmarks we apply to China. Lardy, as many other analysts, takes China in 1978—the year when China began its economic reforms—as the benchmark. Compared to that benchmark—China at that time did not have any private sector at all—74% of industrial output value is indeed substantial. But it is important to note that the issue under debate here is not whether China is still a communist, centrally planned economy. It is clearly not a Soviet-type centrally planned economy. The issue here is whether China is a heavily state-controlled economy with many shared characteristics of the commanding-heights economies of the 1970s and the 1980s’ vintage (Yergin and Stanislaw, 2002).

By the benchmark of commanding-heights economies, the size of the private sector in China is unremarkable. In a 1995 study, the World Bank (1995) tracked the production and control roles of the state in much of the developing world (outside of the communist countries). What is revealing from the data in that report is that even some of the most statist economies in the world at that time, such as Tanzania, Brazil, India, and Congo, had private sector output shares in excess of 80% of GDP. All had private sector employment shares in excess of 90% of total employment. These figures easily exceed the most optimistic estimates of the size of the private sector in China today.

None of these statist economies from the 1970s and the 1980s turned out to be successful economic performers in the long run. This is an important lesson from history. A large private sector is most likely to be a necessary but not a sufficient condition for economic success. All successful economies in history have been primarily private-sector and market-driven. Not a single centrally planned economy has ever succeeded in attaining high income status and a living standard comparable to that of the West. The sheer size of the private sector, however, is

not a sufficient condition for long-run economic growth and development. There are other factors at work, such as how competition among firms is structured, the basic orientation of the financial system, the role of innovations in growth, and the extent of the *de jure* and *de facto* constraints on the power of the government. In my ongoing book project, I use “quantity of capitalism” to describe the size of private sector and “quality of capitalism” to describe the textured relationships between market and firms and between political and economic controls in an economy.<sup>3</sup> China today has quantity of capitalism, but so did Brazil and India of the 1980s. History is clear on quantity of capitalism—it is not enough to get a country to high income.

The second issue has to do with the statistical complications of how to classify the Chinese private sector. Lardy accepted the Chinese definition of the private sector at its face value, but as anyone who works on this topic knows, defining the private sector in China today is fiendishly hard. The reason is that the right definition of private or statist nature of an entity does not or should not entirely rest on the revenue rights—the rights to receive dividends from the operations of the owned entity—of this entity but on the control rights of this entity—the rights to hire and fire top management and dispose of owned entity. Two complications ensue. One is that we have more information on the revenue rights of Chinese firms than we do on the control rights. We have information on equity ownership by state, legal-person entities, and private shareholders in a dataset widely-used by economists, the National Bureau of Statistics’ (NBS) Census of Industrial Firms. But the Chinese government does not disclose information on who actually controls these firms.

The second complication is that it is a hazardous exercise to infer control rights from the information on revenue rights. For one, we do not know what the control threshold is for an average Chinese firm. Is 51% equity necessary for the state to establish controls or 10%? Indeed is 0% by the state sufficient to nullify state controls? Many completely private firms have established branches of the Chinese Communist Party (CCP) as is mandated by law, and we do not have enough information to know whether establishing these branches has an effect on the operating decisions of the nominally private-sector firms. For the other, we have very little information about who actually controls many of the holding

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3 This book project extends and updates my 2008 book, *Capitalism with Chinese Characteristics* and traces the rise of and speculates on the future of state capitalism in China.

companies that have equity claims on those firms for which we do have data on equity ownership. We must know whether these holding companies themselves are state-controlled before we can make any meaningful statements about the ownership nature of their subsidiaries. For any analyst to be able to assert confidently that Chinese economy is 65% or 75% private today presumes an amount of knowledge that simply does not exist.

To reconcile the discrepancies resulting from various and competing definitions of private firms, in what follows, we present estimates based on a set of metrics that approximate a firm's control rights, however imperfectly. Control rights refer to the rights to appoint managers, dispose of assets, and set the strategic direction of the firm and in the context of the Chinese SOEs, these two sets of rights often do not overlap. The government can exercise substantial control rights over firms over which its revenue rights are minimal. Control rights are more meaningful measures of firms' ownership than revenue rights. An operational difficulty in applying this definition, however, is that it is not easy to know whether a firm's control rights are private or governmental. An early attempt to get at this question is a paper by Dougherty and Herd (2005), two economists working at OECD. This essay follows their approach but with one substantial variance about an important assumption that Dougherty and Herd (2005) made in their estimation. That assumption has to do with the ambiguity of classifying a type of firms in China known as "legal-person shareholding firms" (subsequently abbreviated as LPS firms). It turns out that the estimates by Dougherty and Herd (2005) are extremely sensitive to the assumption we make about LPS firms.

Dougherty and Herd's paper is based on a unique dataset compiled by the National Bureau of Statistics (NBS) that covers over 160,000 industrial firms in China between 1998 and 2005. The dataset contains fairly detailed breakdowns of the ownership structure of firms. One caveat, however, is that the NBS dataset is biased toward large firms—defined as those with at least five million yuan in sales (or about \$750,000, a cutoff for medium-sized firms in the Chinese context). We should keep in mind that the estimates based on this dataset reflect the private share of the industrial value-added produced by the large and medium firms in China, not the private share of the entire industry.

The classification methodology adopted by Dougherty and Herd (2005) involves two steps. First, they divide firms into state and non-state firms. State firms in turn comprise two types of firms: SOEs and collective firms in which the collective share capital exceeds 50 percent. The second step is to classify all those firms



in the non-state category as those with more than 50 percent of share capital held by legal person entities, individual investors, and foreign firms. This definition is broadly consistent with the definition used in Lardy's estimates. Dougherty and Herd conclude that the private economy accounted for 28.9 percent of industrial value-added in 1998, 52.3 percent in 2003, and 71.2 percent in 2005,<sup>4</sup> -- quite close to Lardy's (2013 pp. 72 and 75) more recent estimates.

The OECD economists assign the entire output by legal-person shareholding firms to the private sector. Is this a reasonable approach? Getting this question right is critical. In 1998, legal-person shareholding firms accounted for 40 percent (11.3 percent/28.9 percent) of the purported private sector. Excluding these firms would reduce the share of the private sector in industrial value-added from 28.9 percent in 1998 to only 17.6 percent (28.9 percent minus 11.3 percent). For 2005, the private sector exclusive of legal-person shareholding firms would be 39.8 percent rather than 71.2 percent (71.2 percent minus 31.4 percent). Getting this detail right really matters. The difference is on the order of 40 percent.

LPS structure refers to cross-shareholding by firms. Probably because of the connotations of this term, the OECD economists might have assumed that legal-person shareholding implies that China has a keiretsu arrangement similar to that in Japan where firms own each others' stocks. The difference with Japan, however, is that in China much of the legal-person share capital originates in the state sector, i.e., SOEs establishing or holding significant equity stakes in other firms. These firms then become affiliates or subsidiaries of the SOEs. The subsidiaries of the SOEs, on account of their final control rights are still SOEs.

One way to learn more about these legal-person shareholding firms that the OECD study classified as private is to check their names. Such an exercise would have immediately revealed that many of the LPS firms are among the best-known and quintessential SOEs in China. They include subsidiaries of Daqing and Dagang oil-fields, owned and operated by two of China's largest SOEs. Daqing is owned by PetroChina, and Dagang is owned by China National Petroleum Corporation (CNPC). The list also includes subsidiaries of NORINCO, a large defense product firm. PetroChina, CNPC, and NORINCO are not only SOEs; they are known as central SOEs directly supervised by the State Council. In fact, some of these firms have the word "state-owned" in their names.

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<sup>4</sup> Dougherty and Herd (2005) only have estimates up to 2003 but I extended their methodology to data for 2005.

Another well-known SOE on the list classified by the OECD study as private is SAIC Motor Corporation Limited (SAIC Motor). In the NBS dataset, the state share of SAIC Motor's share capital structure is 0 percent. It is 70 percent legal-person shareholding and 30 percent individual shareholding. So this firm qualifies as a private firm in the OECD definition. But SAIC Motor is not even remotely a private firm. SAIC Motor was established in 1997; its predecessor was Shanghai Gear Factory. In 1997, 30 percent of the share capital was issued on the Shanghai Stock Exchange and the rest of the share capital was held by Shanghai Automotive Industry Corporation (SAIC), which is 100 percent owned by the Shanghai government. Because the Shanghai government owns SAIC Motor via SAIC—a legal-person shareholder—the state share capital is reduced to zero, but from a control perspective, there is little question who controls this firm.

The high concentration of the ownership structure of the legal-person shareholding firms is another sign that these firms are not private at all. In the NBS dataset, SAIC Motor has the most dispersed shareholding structure among the legal-person shareholding firms with 30 percent of its shares owned by individuals (This is because the firm is listed on the Shanghai Stock Exchange.) In contrast, of 16,871 legal-person shareholding firms in the NBS dataset for 1998, 75 percent have no ownership by individuals. For the entire sample, individuals only account for 3.7 percent of total outstanding shares. This is entirely expected given the heavily accounting nature of the SOE reforms. As evidence, 7,612 of these so-called legal-person shareholding firms are actually factories—i.e., they are simply production subsidiaries of other SOEs. This explains the extraordinary concentration of ownership and control of these firms.

The exercise above to decompose Chinese private-sector firms into more granular ownership categories focuses on the division of output between the state and private sectors. Another complementary approach is to examine the inputs that go into SOEs and private sector. The output measure tells about the size of the private sector in the Chinese economy but it has also been used by many economists as a short-hand indicator of the policy treatment of the private sector. This second application of the measure is fraught with methodological problems.

The biggest problem is that the measure incorporates two effects. One is the policy effect of policy liberalization; the other is the firm-level effect having to do with the relative efficiency differences between private firms and other types of firms. Suppose one observes the rise of private share of output over time (as we have seen happening in China). On that basis, can we draw the conclusion

that government policy toward the private sector has become progressively more liberal over time?

The source of interpretational ambiguity is that we do not know the relative importance of these two effects. One is policy liberalism and the other is the firm-level efficiency. It is entirely plausible that the private share of output can rise without any policy liberalization. Private firms are more efficient than SOEs and therefore they generate more value-added per unit of inputs—labor and/or capital—deployed. A rise in the output shares of private firms over those of SOEs can happen without any improvement in policy environment so long as private firms are more efficient than SOEs.

We can cite two examples to demonstrate this dynamic. In 1989, in the wake of Tiananmen crackdown, the newly ascendant political conservatives strengthened central planning and arrested many private entrepreneurs. (During the demonstration, private entrepreneurs donated food and money to protesting students.) Yet in 1990, the output ratio of the private sector relative to the SOEs still increased. Clearly, this rising ratio had nothing to do with policy liberalization. Another example comes from the former Soviet Union. No one accuses Leonid Brezhnev of being pro-market, but under his leadership, private plots contributed half of agricultural household income in the Soviet Union: private farming was so much more efficient than the state farming that its contributions to income were disproportionate to the inputs allocated to it. Private plots only accounted for 1.4% of cultivable land in the Soviet Union.<sup>5</sup>

This Soviet example shows that input, not output, is a more reliable measure of private-sector policies. The most relevant input measure is capital allocation and specifically capital allocation to fund fixed asset investment activities of firms. Fixed asset investment activities are a policy measure for a simple reason: They are tightly controlled by the state, and throughout the reform era, this control has not abated. While there is an issue about whether this control rests with the central government or with the local governments, that fixed asset investment is state-controlled is not in doubt.

There is a great deal of economic evidence that the governmental control of the investment process has remained substantial during the reform era. A telling piece of evidence, as marshaled by Tom Rawski, is that China's seasonal investment cycles matched almost perfectly those prevailing during the centrally-planned era.

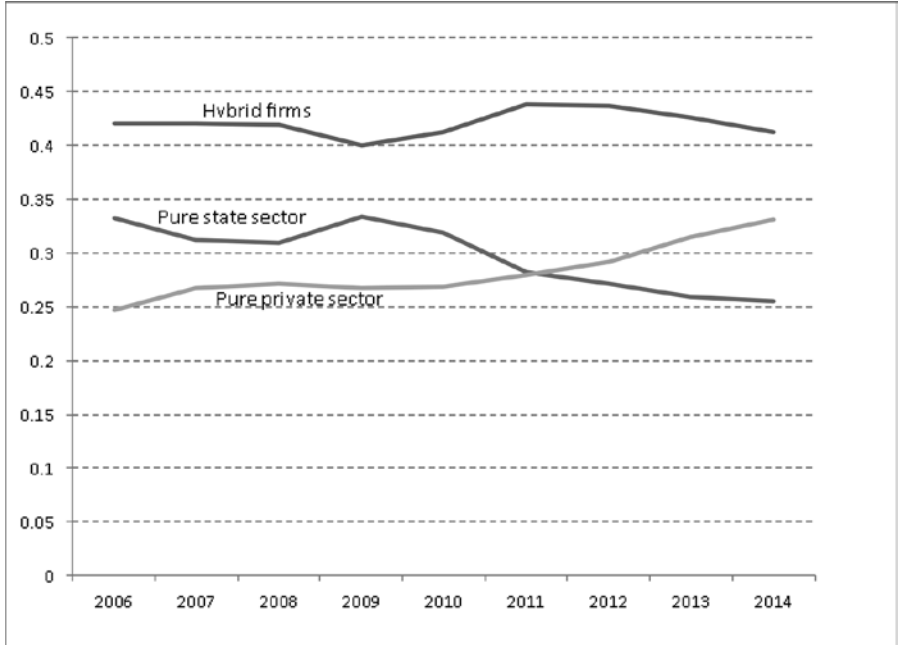
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<sup>5</sup> I detailed this example in Huang (2008).

Since fixed asset investment is a large component of China's GDP, the fluctuations of investment levels have a substantial impact on GDP. Here Rawski (2001a) shows that China's quarterly GDP growth patterns differed substantially from those in South Korea, Taiwan and Hong Kong, an indication that factors such as weather or traditional Chinese holidays are not the principal determinant of China GDP's seasonal rhythm. Rawski (2002 pp.368) quotes a Chinese economist in his overall assessment of Chinese investment process:

*Many basic components of a pure market economy are still in their incipient stage in China, although market-oriented reform started two decades ago. Government-guided investment mechanisms, a state-controlled banking system and dominant state-owned enterprises...still run in a framework molded primarily on the previous planned economy.*

If anything, until 2012 or so, the Chinese state has further centralized investment approval authority. So fixed asset investment allocation is still a reliable indicator of the division of control between the state and private sectors. So how large is the fixed asset investment share of the state sector? Figure 1 shows the fixed asset investment shares of three types of firms, pure state, mixed ownership and pure private, during the period from 2006 to 2014. (Data were downloaded from the website of the National Bureau of Statistics, <http://www.stats.gov.cn/>.) Pure state refers to traditional SOEs that are registered as SOEs or as collective firms. Pure private refers to de jure private firms registered legally as private firms or as individual proprietorships. Mixed ownership refers to three types of firms: joint-ownership firms, various types of shareholding firms, and unclassified firms. (There is also a fourth category, foreign-invested enterprises or FIEs, but for the purpose of this discussion FIEs are excluded as the essay focuses on domestic firms.)

**Figure 1:** *Fixed asset investment shares of three types of firms, 2006-2012*

Source: The data are from the website of National Bureau of Statistics at <http://www.stats.gov.cn/>.

There is no question that the pure private sector has increased its share of fixed asset investments, from 25% in 2006 to 33% in 2014, while the pure state sector experienced a decline. On the basis of this data, we can draw the conclusion that China has been trending away from state capitalism, not toward it. However, there are complications with this interpretation. One is that while the pure private sector has unambiguously increased its share since 2006, it is important to note that the pure private sector in the 1980s already accounted for some 20% of fixed asset investment activities, almost all of which were in rural areas (Huang 2008). While the 20% figure cannot be directly compared with the figures presented in Figure 1 (because the data in Figure 1 exclude rural data), it is important to note that the share of the private sector in fixed asset investments in the 1990s and early 2000s either failed to increase or increased only slightly.

The second complication is how to factor in the effect of investment approvals. We refer to fixed asset investments as private in the sense that the financing and organization are performed by private sector firms, but the expansion of investment approval power must have attenuated some of the control rights of the private sector firms. This attenuation does not show up in the fixed asset invest-

ment data.

The other pattern in Figure 1 is the clear importance of mixed ownership firms. Whether the private sector is judged as small or big substantially rests on how we assign the ownership rights of the mixed ownership firms. The largest category of mixed ownership firms are shareholding firms. They account for about 70% of the fixed asset investment activities in this category. It is entirely possible that some and even most of the mixed-ownership firms are closely controlled by the state and their control rights are fundamentally statist. There are two principal types of shareholding firms under Chinese corporation law. One basically consists of SOEs that have been “corporatized,” i.e., they have been given a shareholding organizational form. This is known as state wholly owned firms. In terms of ownership, there is little difference between these firms and traditional SOEs. The second principal category consists of those firms that have issued shares on China’s two main stock exchanges in Shanghai and Shenzhen.<sup>6</sup> (There are also exchanges for small-cap firms but these were established only in recent years. The firms listed on those exchanges are primarily private.) According to an article on Xinhuanet, an official website, cumulatively between 1990 and 2003, only 6.97 percent of the firms that issued IPOs on these two stock exchanges were private sector firms. The rest are SOEs that have issued minority shares.<sup>7</sup> While there have been more listings of private-sector on the two main exchanges since 2003, the vast majority of the listed firms are unquestionably state-owned and/or state-controlled.

Assigning the entire mixed-ownership firms to either state sector or to private sector would lead to estimation biases in opposite directions. One simple approach is to assign 50% of the fixed asset investments by the mixed-ownership firms to state and private sector each. This methodology would yield an estimate of the private-sector share of fixed asset investments around 45% for 2006 and 51% as of 2014. To provide a benchmark, in 1983, at the height of the “License Raj,” the private sector in India accounted for 58% of fixed asset investments (World Bank, 1989). China today is more state capitalistic than India of the Indira Gandhi era.

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6 There is also a third category of shareholding firms known as shareholding coops but under the Chinese statistical conventions they are grouped together with collective firms.

7 See [http://www.baidu.com/s?cl=3&wd=http://news.xinhuanet.com/stock/2004-09/07/content\\_1952118.htm](http://www.baidu.com/s?cl=3&wd=http://news.xinhuanet.com/stock/2004-09/07/content_1952118.htm).

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*Milestones of State Capitalism*

I have argued elsewhere (Huang 2008) that the most entrepreneurial era of Chinese economy is in the 1980s when the Chinese state implemented large-scale financial reforms in rural China, protected property rights of rural entrepreneurs and began some initial steps to curb the power of the CCP. I dated the end of this era to 1989 in political terms (in the form of the downfall of Zhao Ziyang) and to the mid-1990s in economic terms (in the form of re-imposing tight financial controls). The rise of state capitalism can also be traced to these political and economic policy episodes.

If we have to pick a date for the rise of state capitalism, then it would have to be 1997 at the 15th Party Congress. On the surface, this dating is paradoxical because the 15th Party Congress is famously associated with Zhu Rongji's audacious privatization program. Estimates are that 30 to 40 million SOEs workers were laid off. (By contrast, India, which actually established a Ministry of Disinvestment, only privatized 48 SOEs.)

Zhu Rongji's program deeply impressed many outside economists. Yingyi Qian (1999 pp.26) proclaimed, 'It is quite remarkable for China to have overcome ideological and political opposition to embrace the market system and private ownership without a political revolution.' Another leading China economist proclaimed that the process of transition was already complete. The remaining challenge was one of economic development (Naughton, 2007).

China did privatize. This is not in dispute. However, the best way to characterize Chinese privatization is that it was a tactical privatization: the state never fully embraced privatization as a policy goal in and of itself. Privatization was intended as an instrument in the service of a larger goal. One goal of the CCP is to maintain political control. Maintaining political control in turn requires maintaining economic control of vital sectors of the economy. Viewed this way, the privatization program of the late 1990s was really a means to fund those SOEs the state intended to control and to reduce operational and managerial complexities so that the state could focus on operating and managing fewer but larger firms. Tactical privatization did not reduce the power of the state; it funded and made smarter the power of the Chinese state. It is in this sense that the 15th Party Congress of 1997 was the genesis of state capitalism.

The official formulation of the privatization program at the 15th Party Congress was "Grasping the big and letting go of the small." In important ways, the

Chinese state is far more consistent both in its pronouncements and in its policy practices than outside economists often credit. Many economists assumed that the Communist Party in 1997 endorsed a full privatization programme, when in fact the Chinese state has done exactly what it said it would do in 1997. ‘Letting go of the small’ meant that the government supported privatization of individually small but numerically numerous SOEs. These are labour-intensive firms, and singling them out for privatization, with no established social protection in place, led to massive unemployment, social instability, and wrenching human costs. (Coincidentally and concurrently, the Chinese state tightened its political and security controls in order to suppress dissent.)

The idea of state capitalism is illustrated by the first part of the Chinese privatization formula—‘Grasping the big’. ‘Grasping the big’ meant restructuring, consolidating, and strengthening China’s largest SOEs. ‘Letting go of the small’ is the tactic employed to ‘grasp the big’ by reducing or ending government subsidies and social liabilities which, in turn, reduced operating and managerial complexities. Instead of managing tens of thousands of small firms scattered around the country, the Chinese state could now focus on only a few thousand firms. Taken together ‘Grasping the big and letting go of the small’ really means a massive reallocation of financial, human, and managerial resources away from the small SOEs to a handful of the largest SOEs.

For the Chinese reformers, the dilemma has been how to leverage the state’s limited and shrinking financial resources to achieve *greater* corporate control. The shareholding reform program was justified as a means to fortify the allocative functions and corporate control role of the state, not to weaken state control in the economy. It is difficult, if not impossible, to reconcile the official justification with the standard privatization rationale that seeks to reduce state interference in the economy and to introduce efficient management and supervision by private investors. Another inconsistency with the prevailing privatization rationale has to do with the use of the privatization proceeds. Some of the privatization proceeds were used to finance investment and technology acquisition programs of the large, pillar SOEs.<sup>8</sup> Such use of funds does not reduce the aggregate ownership role of the state in the economy; it has only changed the composition of the state’s role. It is far from clear how this manner of privatization has provided an exit

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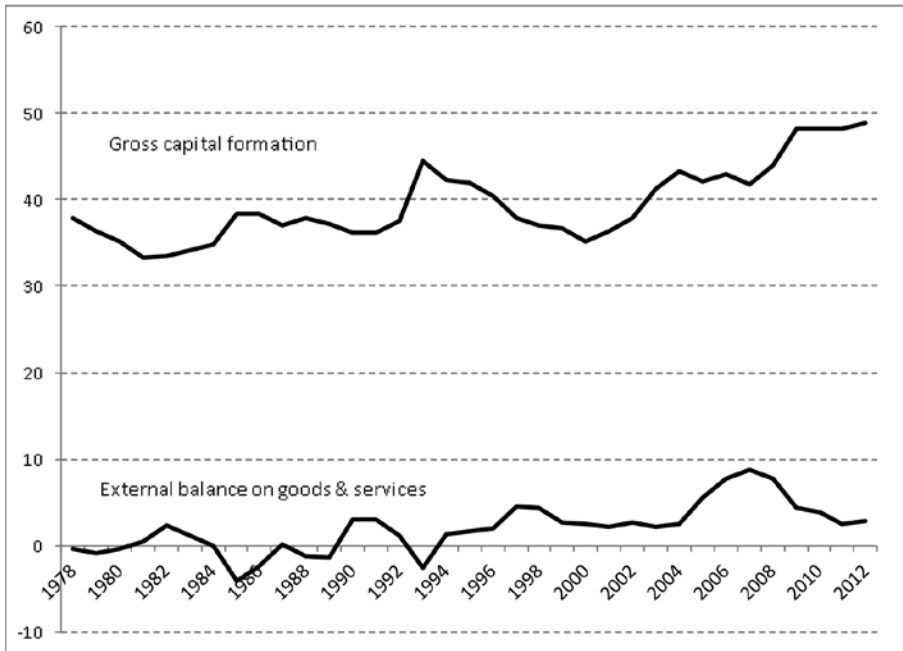
8 A number of researchers have documented instances in which local governments invested in SOEs, while at the same time divesting from smaller SOEs Cao, Qian, and Weingast (1999).



option to the state.

One problem with studying state capitalism is that the growth model is not easily observable. In this section, I will try to present data showing some evidence on “discontinuity” in a number of economic indicators. Discontinuity here implies that there is a break in the data series that suggests the effect of concrete policy changes. The underlying assumption here is that normal economic forces and dynamics produce smooth data series whereas policy changes lead to breaks in the data series.

**Figure 2:** *Gross capital formation and external balances (% of GDP), 1978-2012*



Source: *World Development Indicators by the World Bank*

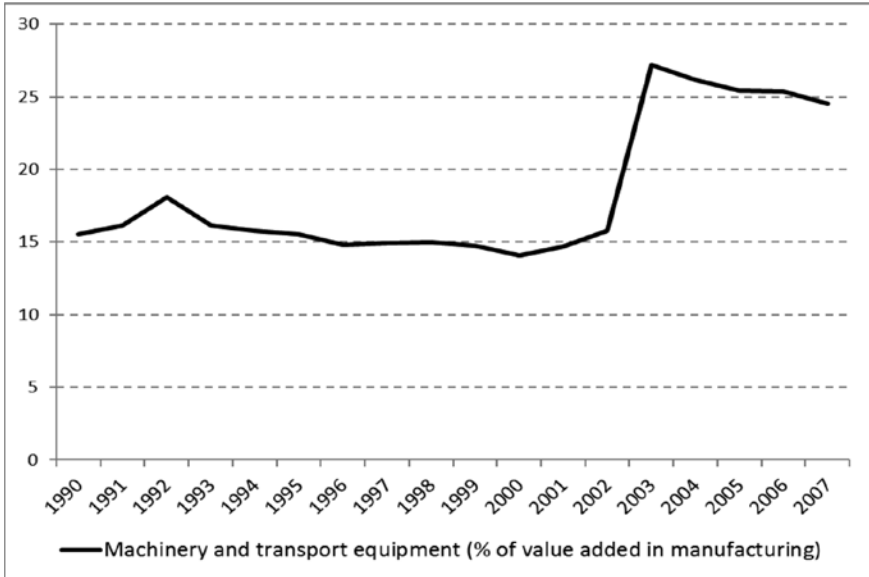
Figure 2 presents two ratios. One is gross capital formation as a percentage share of GDP; the other is external balance as a percentage share of GDP. Two patterns stand out from the graph. One is that until 1992 China invested at a high rate but it was always below 40% of GDP. This is on a par with other East Asian economies during their takeoff era, i.e. between 35% and 40% of GDP. The year 1993 marks a turning point. In that year China invested 45% of GDP, followed by three years above 40% and six years below 40%. Starting in 2003, the ratio in-

creased dramatically, to nearly 50% in the 2010s. No other country, during peace time, ever invested 50% of its GDP.

One explanation for China's growth is that it is skillful in using undervaluation of its currency as a roundabout way to subsidize industrialization (Rodrik 2013). Figure 2 does not support this explanation. Until 1990, China's external balance of trade and services—measured as percentage share of GDP—either had a deficit or a small surplus (the biggest being 2.4% in 1982). As is well known, China in the 1980s had an overvalued exchange rate and yet it was able to industrialize at a rapid rate. Contrast this pattern with the one since 1990. China ran trade surpluses every year except in 1993, and in 2007 its external balances were almost 8.8% of GDP, a massive number for a country the size of China. (It should be noted that since 2007 the surpluses have declined substantially.) The mercantilist strategy that Rodrik proposed really only applied to China since 1990 and in its extreme form, only since 2004. One has to explain why during the 1980s China was able to industrialize with an overvalued exchange rate but since 1990 it had to rely on an undervalued exchange rate to industrialize. The turn toward state capitalism, which is investment intensive and is consumption suppressing, provides a plausible explanation for this shift of these two ratios over time. Investment shares of GDP correlate positively with shares of external balances of GDP.

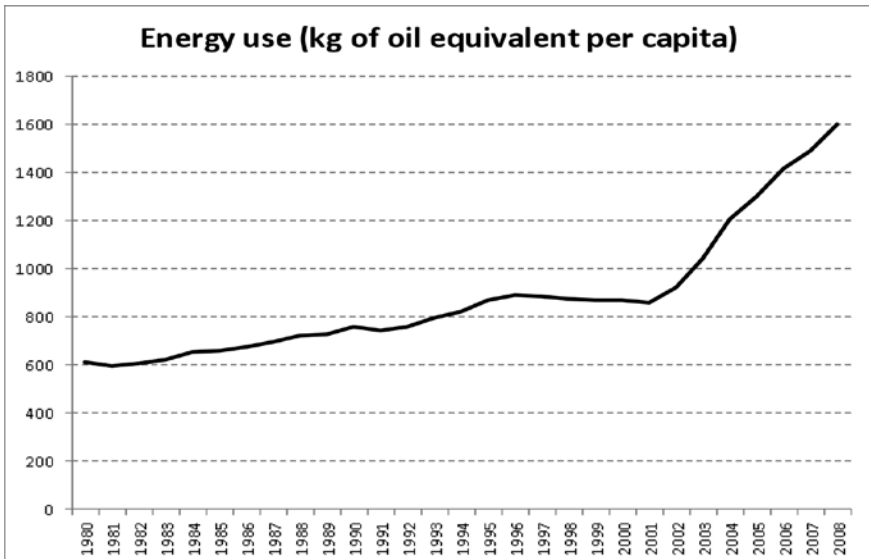
The acceleration of investment intensity also implies a shift of growth drivers of GDP. During the less statist growth phase, the growth was driven by more broad-based, rural entrepreneurship and by light industries, such as textile and garment. During the more statist phase, the growth drivers shifted, toward heavy industries and commanding-heights sectors of the economy. It is important to distinguish a gradual economic maturation from skill-extensive growth drivers to skill-intensive growth drivers over time from one that is an outward shift of the growth drivers. The telltale evidence is whether there is a discrete discontinuity in the data series or whether there is a smooth movement of the data series.

**Figure 3:** Heavy industry tilt: Shares of machinery and transport equipment in manufacturing value added



Source: World Development Indicators by the World Bank

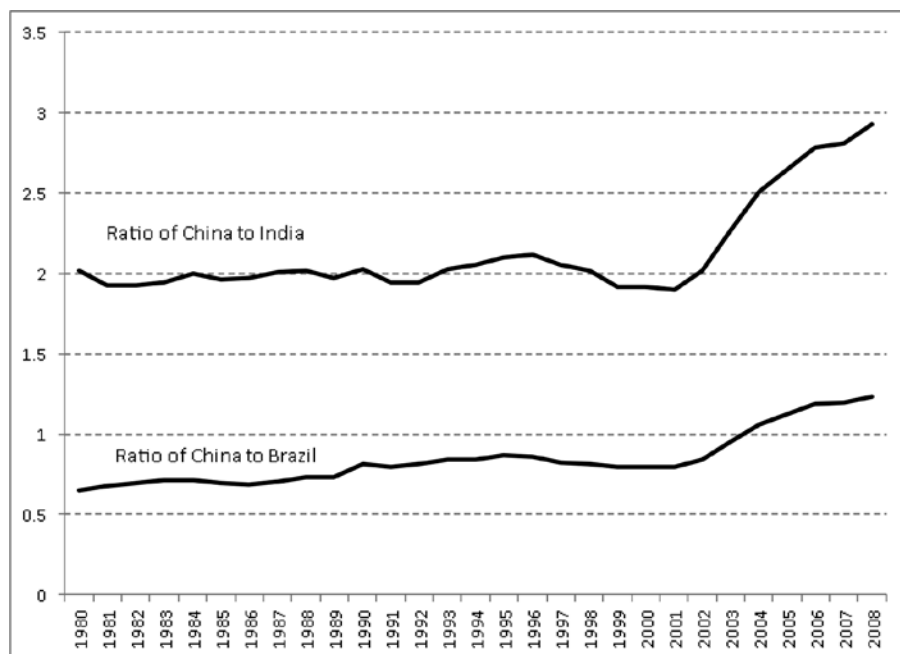
**Figure 4:** China's energy intensity shift



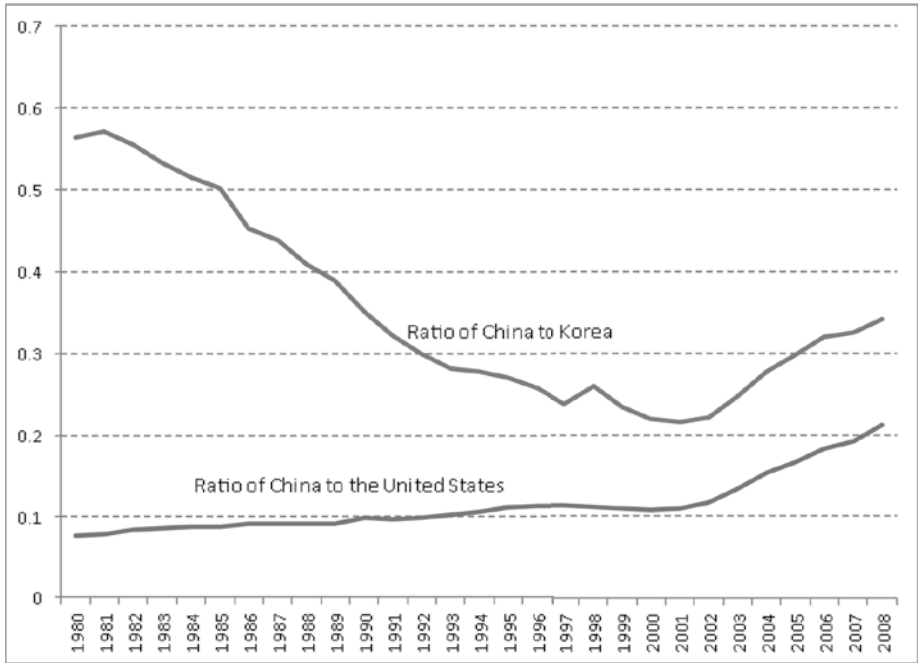
Source: World Development Indicators by the World Bank

Figures 3 and 4, based on the World Bank data, provide some suggestive evidence. Figure 3 presents the shares of machinery and transport equipment of the total manufacturing value-added over time. I use this ratio to show the importance of heavy industry in Chinese manufacturing. The most interesting and an extremely noticeable pattern is the hockey-stick shape of the curve. Between 1990 and 2000, the ratio first rose but mostly remained flat throughout the 1990s. Starting in 2000, the ratio began to climb and then in 2002 the ratio climbed sharply, from about 0.15 to 0.27 in 2003. This almost doubling of the ratio had to be driven by policy decisions, not by factors such as the gradual accumulation of skills and technology. Figure 4 provides another measure of the same dynamic and this is per capita energy consumption measured in kilograms of oil equivalent. Before 2001, the curve rose gradually and smoothly but in 2001 there was a sudden doubling of the energy consumption in seven years (2001-2008). By contrast, before 2001 it took China roughly 30 years to double the per capita energy consumption, from 1971 to 2001. This kind of discontinuity is most plausibly a result of a shift of growth models.

**Figure 5a:** *Per capita energy usage: Ratios of China to Brazil and to India*



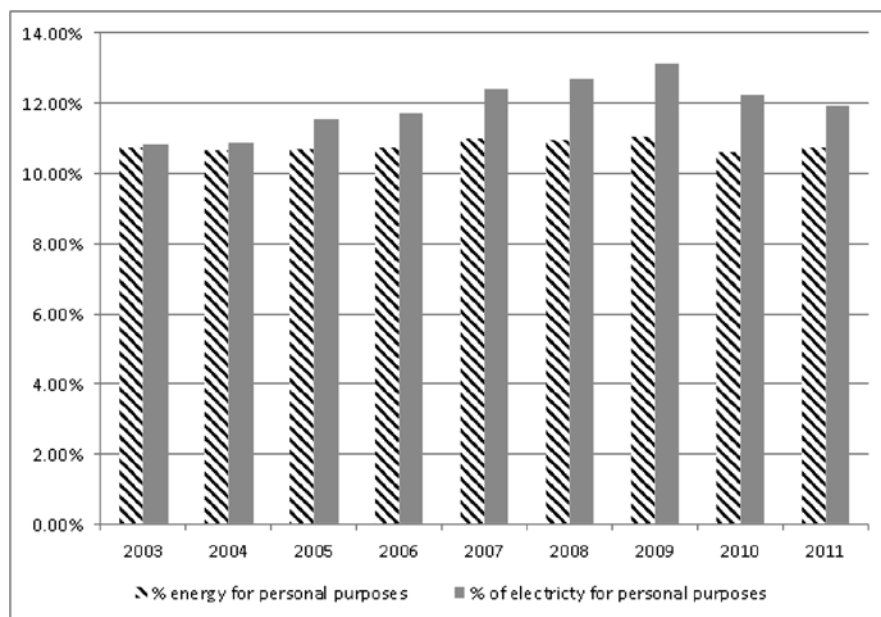
Source: *World Development Indicators by the World Bank*

**Figure 5b:** *Per capita energy usage: Ratios of China to Korea and to the United States*

Source: *World Development Indicators by the World Bank*

Figure 5a and Figure 5b show that this sharp rise of per capita energy usage is unique to China-specific factors, not due to any common shocks that uniformly affected other countries. Figure 5a presents ratios of Chinese energy consumption relative to those of India and Brazil. The pattern is very clear. Before 2001, Chinese energy consumption grew roughly at similar rates as these other countries as indicated by the flatness of the lines. After 2001, the Chinese energy consumption rose substantially relative to Brazil and India and the lines moved up steeply beginning in 2001. Figure 5b contrasts China with two developed countries, Korea and the United States. Relative to Korea, Chinese per capita energy usage declined prior to 2001, despite its rapid GDP growth. The break in the data occurred in 2001 and 2002 when the Chinese ratio to Korea rose. Prior to 2001 or 2002, the Chinese ratio to the United States climbed steadily but it accelerated after 2001.

**Figure 6:** *Percentage shares by personal usages of energy and of electricity in China (%), 2003-2011*



*Source: Calculations are based on data downloaded from the website of National Bureau of Statistics.*

Energy consumption can go up both because income growth increases the energy intensity of usage and because production becomes more energy intensive. It is important to distinguish between these two drivers of energy intensity. A pivot toward state capitalism implies an increase of energy intensity on the production side, not an increase of energy intensity on the consumption side. This is what Figure 6 shows. Figure 6 provides information on the trends of the personal shares of Chinese energy and electricity usage of the total energy and electricity usage. It is important to note that 1.3 billion Chinese are not the heavy users of energy. In terms of total energy usage, personal usage accounted for a little bit over 10%; for electricity usage it is 12%. The trends for both, especially for energy, are relatively flat and they are at a sharp variance with the rising energy-intensity shown in other figures in this essay

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## *Performance of State Capitalism*

Advocates of state capitalism often cite China's high GDP growth as evidence of the efficacy of state capitalism. One problem with this view is that there has not been one growth model in China. There are at least two: one—prevailing in the 1980s and up to the mid-1990s—that is less statist in terms of the policy orientations and one since the mid-1990s that is increasingly rooted in state capitalism. GDP growth under both of these policy models has been robust. To say that state capitalism is responsible for China's fast GDP growth is to have committed an attribution error.

The differentiators between the two policy models go beyond GDP growth rates and are centered on the growth of personal income. During the more entrepreneurial phase of Chinese growth, personal income grew on a par with GDP growth and there was an initial improvement in income distribution. While China continued to grow rapidly during the phase of state capitalism, personal income growth slowed down substantially and income distribution deteriorated.

In Huang (2008), I documented in great detail that household income growth in the 1980s exceeded GDP growth but it lagged substantially behind GDP growth in the 1990s. In fact, in the second half of the 1990s, there was no growth of rural household nominal income at all. All the growth came from a severe deflation experienced by China in the late 1990s. In the 2000s, household income growth improved substantially from the level prevailing in the 1990s but so did GDP growth. So the gap between economic growth and personal income growth has persisted.

Given the substantial discrepancy between the per capita GDP and the personal-income measure of performance, the question is to which measure should we assign more weight? There is a technical and there is a substantive response to this question. In technical terms, Chinese GDP data are often criticized for their inconsistencies, lack of definitional clarity, and the inadequate explanations of and disclosures about reporting norms and procedures (Rawski 2001b). Indeed, recently local governments reported a GDP figure 10 to 15 percent larger than what the national government reported and Chinese GDP purportedly grew at a rapid rate despite a sharp slowdown in the growth of electricity usage. In contrast, the personal income data were obtained through painstaking household surveys. Such household surveys are widely held by outside analysts as well-designed and informative.

The substantive reason is that personal income represents a better measure of the welfare of the Chinese populace compared to national accounting data such as GDP. Economics, John Stuart Mill famously stated, is the study of “the sources and conditions of wealth and material prosperity for aggregate bodies of human beings.” Mill (1865) reminds us that economic growth matters primarily because growth improves the health and welfare of the majority of the population, not simply a few elite members of a society. The normative justifications of the China model are also offered on welfare grounds. One famous formulation in the economics literature is that the Chinese reform has been “Pareto-optimal” in that it has created winners without creating losers (Lau, Qian, and Roland 2000).

We do not have an exact measure of “welfare” but we have something closer to the concept than GDP—personal income and consumption data. We will also pay particular attention to China’s rural population. Although the rural population now is 45% of China’s population, it is important to note that this is defined in terms of the residence status, i.e., they are rural as long-term residents—defined as more than six months—in rural China. Added to that is another some 200 million rural migrant workers who reside in cities but lack the legal benefits of urban citizenship (such as free basic education and healthcare). This bifurcation between residency and legal status is a feature of what is known as the “hukou” system in China. China’s rural population is the Chinese equivalent of “the aggregate bodies of human beings” Mill emphasized in his justification for economic growth.

Figure 7 divides the developments into three periods: the first policy period, from 1979 to 1988 (referred to as the “1980s” in this essay), is the era of Hu Yaobang and Zhao Ziyang in terms of economic policy. Hu and Zhao are widely regarded as the most liberal Chinese leaders during the reform era. The subsequent years, 1989 to 2002 (referred to as the “1990s” in this paper), Jiang Zemin and Zhu Rongji governed the country and managed the economy. Both of these leaders came from Shanghai, a city that laid down the intellectual and operational foundation of state capitalism (Huang and Qian 2010).

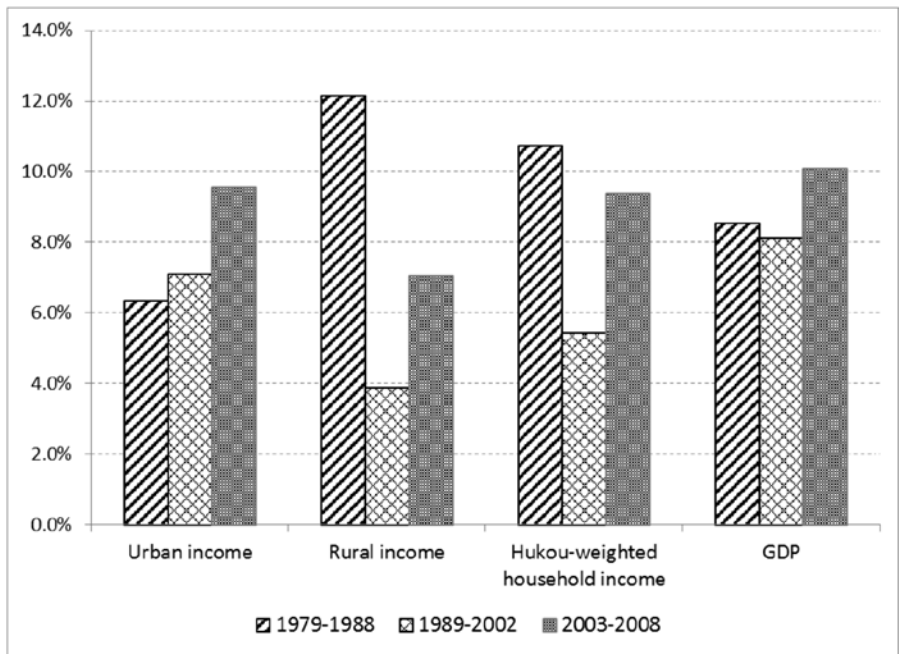
The third policy period between 2003 and 2013 is the era of Hu Jintao and Wen Jiabao. This period is mixed in terms of the orientations of the state capitalism. In rural policy, this group of leaders reversed some of the anti-rural policies from the 1990s but in other areas, such as state monopolies and investments in SOEs, there has been a substantial exacerbation of the statist biases from the 1990s. While the developments during the third policy period hold important, although conflicting, clues about China’s economic future, the decades of the



1980s and 1990s provide the cleanest way to test some of the claims about the state capitalism model. Much of our analysis will thus focus on these two policy periods. I will touch on the most recent policy period, under President Xi Jinping, in the concluding section of the paper.

Figure 7 presents Chinese economic performance broken down along two dimensions. One is the familiar GDP dimension and in this case it is the period average of the real per capita GDP growth rates. The other is the less familiar dimension of Chinese performance—the growth of the household or personal income. Both types of growth statistics are in per capita terms calculated on the basis of their values expressed in 1978 prices.

**Figure 7:** *Per capita household income and GDP growth during three policy periods (1978 prices, %)*



*Notes:* The rural and urban income deflators are used to deflate the values to their 1978 values. For GDP, the implicit GDP deflators were used. The weights used for calculating weighted rural-urban income are population shares based on the hukou status (the urban and rural legal status of a resident). *Sources:* The GDP data are available from the website of National Bureau of Statistics. The household income data are from the rural and urban household surveys, various years, published by National Bureau of Statistics.

Let's first examine the GDP series. During the first period, 1979 to 1988, GDP per capita grew at an annual average rate of 8.5 percent in China, versus 8.1 percent during the second period, 1989-2002. On the basis of GDP data alone, one could conclude that the Chinese economic performance has been consistently robust. Yet one comes to a very different conclusion when looking at household income. Household income measures personal income or take-home pay. It refers to money that goes to the household sector in the form of wage, benefits, transfer payments, property income (rental income, interest payments on bank deposits, or stock dividends), and profits from operating small businesses. In other words, unlike GDP, which is an abstract accounting construct, household or personal income denotes the actual monetary and material gains accruing to the Chinese people, and it is closer to the concept of welfare than GDP.

In sharp contrast to the consistency of the high GDP growth, household income performance exhibits a highly varied pattern. We show household income developments in three ways—urban, rural and weighted rural-urban income growth. The source of household income data is the annual survey conducted by the National Bureau of Statistics. (For details, see Huang, 2008). Because NBS conducted rural and urban household surveys separately, we need to pool the rural and urban household income together to calculate the household income growth for the entire country. In my calculation I weighted the rural and urban income by the shares of rural and urban population based on their legal status under the hukou system.

In the 1980s, the weighted rural-urban per capita household income growth exceeded GDP per capita growth by 2.6 percentage points (11.1 percent minus 8.5 percent). In the 1990s, the pattern reversed itself. Per capita GDP growth averaged 8.1 percent annually between 1989 and 2002, but weighted rural-urban per capita household income growth slowed down sharply, from 11.1 percent in the previous decade to only 5.4 percent. The difference between household income growth and GDP growth is now negative at nearly -3 percentage points.

The biggest change has to do with the growth of rural household income. Rural household income in the 1980s grew at an extraordinarily robust rate, averaging 12 percent for the 1978-88 period (after inflation is excluded). In the 1990s, the growth slowed down to 3.9 percent. Urban per capita income averaged 7.1 percent annually in the 1990s as compared with 6.3 percent in the 1980s. However, the increase in the growth rate of the urban income was not enough to offset the decrease in the growth rate of rural income both because the acceleration of

the urban income growth was relatively modest and because of the large number of rural residents.

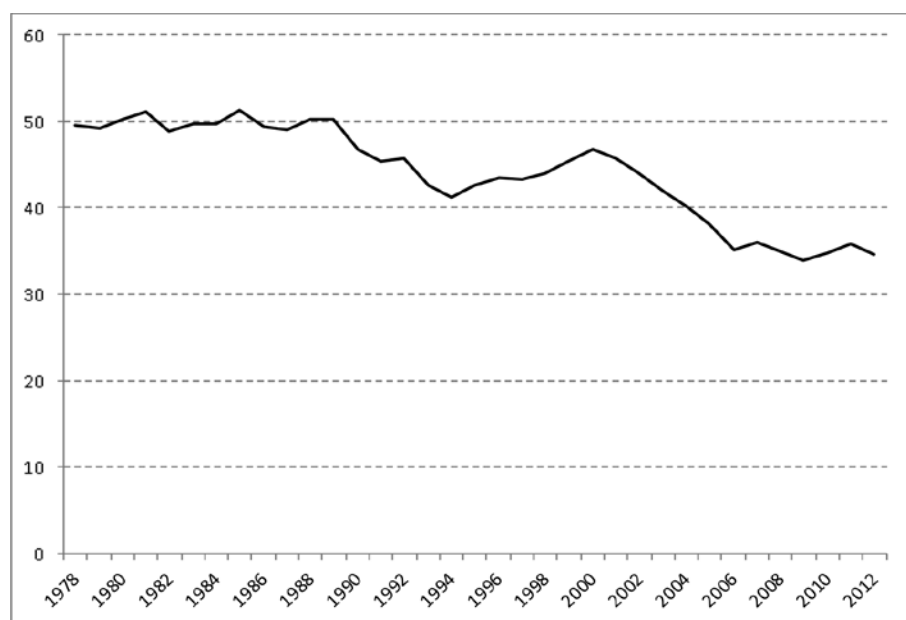
There are, however, some data issues that need to be resolved. Naughton (2007) points out that the rural consumer price index for the early 1980s understates rural inflation (and thus over-states growth). One exercise to get around this objection is to assume that the performance in the second half of the 1980s—for which we have better data on inflation—prevailed throughout the entire 1980s. Between 1984 and 1989, the annual growth rate of rural household income per capita averaged 7.2 percent. This is surely an extremely conservative estimate for the 1980s. Rural economy put out its strongest relative performance in the first half of the 1980s. But even this estimate is still a far stronger performance than the growth in the 1990s (3.9 percent).

It should be noted that the annual difference between the 7.2 percent assumed for the 1980s and the growth rate of 3.9 percent of the 1990s is not an abstract matter. It entails real and substantial income and welfare implications for hundreds of millions of Chinese rural residents. This is not only because of the difference in the two growth rates, but also because of the extraordinary length of the second policy period, thirteen years. Assuming that Chinese rural households had grown in the 1990s at 7.2 percent instead of the actual 3.9 percent, by 2002 an average Chinese rural resident would have been 52 percent richer than he actually was. This is the counterfactual scenario for China. Had China continued with its policy model of the 1980s and had rural Chinese thus been 50% richer, many of the hot-button issues prevailing today such as domestic consumption, exchange rate valuation, and global imbalances would have been much less severe and of much less importance.

The personal income development provides the best clue into one of the most important macroeconomic challenges facing China today: the low household consumption shares of GDP. Because the Chinese financial system is organized to fund supply, not demand, household consumption can only be funded by personal income, not by personal borrowing. A slowdown in personal income growth inevitably leads to a slowdown in personal consumption growth. This dynamic is illustrated in Figure 8 that shows final household consumption as a share of China's GDP for 1980 to 2012. Notice the break in the data around 1990. Before 1989, the share of household consumption stayed around 50% throughout the decade of the 1980s. In 1989, the ratio began to decline and since 1989 the ratio stayed well below the level prevailing in the 1980s. The lowest point was reached

in 2009 when the ratio was only 35% but then it began slowly climbing, giving rise to the hope that China was going to rebalance toward more consumption. That hope was dashed in 2012 when the ratio declined again. Very significantly in 2012 both the consumption ratio of GDP and the GDP growth rate began to decline simultaneously. This is a worrisome sign. It shows that investments have reached a clear point of diminishing returns and that the Chinese economy may have entered into an entirely new period in which the economy moves away from this tradeoff of growth vis-à-vis balancing, i.e., fast growth at the expense of the right balance of the economy or vice versa. It is now possible to have simultaneously both a growth slowdown and a worsening structure of the economy.

**Figure 8:** *Household final consumption expenditure in China (% of GDP)*



Source: *World Development Indicators by World Bank.*

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## *Conclusion*

In 2012, a new leadership took the reins of the country. President Xi Jinping assumed his position at a time when the GDP growth rate began to slow down and the household consumption ratio of GDP declined. This is the situation that Xi Jinping and his colleagues inherited from their predecessors.

Four years into his leadership, we are able to formulate some initial judgement on what the Xi leadership intends to do about China's state capitalism growth model. The communique of the Third Plenum of 18th Party Congress has been much debated and commented upon. A close reading of that document gives rise to three plausible interpretations. One is that the Xi Jinping leadership has endorsed a reform blueprint that is far more comprehensive and complete than the previous reform documents. The document covered no less than 26 policy areas, touching on economics, education, and military. The second interpretation is that the Xi leadership has explicitly rejected reforming or attenuating the institutional pillars of the state capitalistic model—i.e., the SOEs and the absolute power of the CCP. Thus we know that the Xi leadership has an intellectual vision for reforms but we also know that it has not endorsed the two pathways toward realizing that vision—i.e., reforming SOEs and reforming Chinese politics.

A third interpretation is that the communique presents a set of long-term visions, not short-term action plans. Many of the reforms are set against a deadline of completion by 2020. One way to interpret this deadline is that the Xi Jinping leadership does not believe that the challenges China faces present imminent risks, a view that would be at odds with the fact that Chinese economy today is heavily indebted and is dangerously addicted to the real estate bubble as a way to reduce its over-capacity.

While many analysts have equated the communique of the Third Plenum of 18th Party Congress with the Third Plenum of the 11th Party Congress of 1978, the truly revolutionary document that launched China's transformational rural reforms in the 1980s, in fact there are more differences than similarities. Two differences stand out. First, the 1978 communique is a short-term action program that unleashed what economists call "endogenous reforms," i.e., reform in one area—specifically in agriculture—that would lead to reforms in many other areas. The 2013 communique contains a laundry list of textbook building blocks of a market economy but it is remarkably silent on a strategy to move the Chinese economy from its current state capitalistic model to one more closely resembling

a market economy. The document is not a call for action.

The second difference is the rationale provided for reforms by the two communiques. The 1978 communique was direct and explicit. The document went into great detail discussing the problems facing the Chinese economy such as agricultural stagnation and inefficiencies. Not so with the 2013 communique. What is remarkable about the 2013 communique is that the seemingly radical visions for the Chinese economy presented in the document are completely detached from the realities of the real economy on the ground. The document does not provide any rationale for why China needs the radical reforms outlined in it and it does not provide any detailed discussions of the enormous economic and social challenges. It is a bit like a physician, after prescribing an organ transplant, a surgery, and chemotherapy, declaring, “Other than that, you are in good health.”

Aside from uncertainties about the future directions of Chinese economic policy, what is most worrisome is the state of Chinese politics. The fundamental pillar of state capitalism is the political monopoly of the CCP. Four years into his first term (ending in 2017), it is abundantly clear that Xi has assigned the highest weight to protecting, perpetuating and even strengthening the monopoly controls of the CCP. The disconnect between the seeming rhetorical rejection of the state capitalism model in the Third Plenum Communique and the numerous actions and measures taken since 2012 to consolidate the power of the CCP is truly jarring.

At the time of writing this essay, the news coming out of China is all about a bifurcation of repricing of housing assets—in the first-tier cities such as Shanghai and Shenzhen property prices are increasing rapidly (fueled by loose credit and monetary policies) and in second or third-tier cities property prices are either soft or declining. The Chinese leadership is addicted to policies that do relatively little to the real economy except to inflate property prices (including stock market prices in 2014 and first half of 2015). This is clear evidence that the leadership prefers to rely on policy gimmicks rather than on genuine reforms to deal with the emergent challenges.

The bifurcation of the property prices, however, is a sign that this policy is only able to achieve its intended purpose in a small number of locations (such as a handful of first-tier cities). The lack of response from the rest of the country signals risks of an undisciplined unwinding of the state capitalistic model. State capitalism depends on two economic forces to succeed: 1) strong external demand and 2) strong housing demand. The 2008 financial crisis ended the first

and China's out of whack economic fundamentals will end the second. Despite high expectations, so far the Xi Jinping leadership has only shown high rhetorical commitments to reforms. It is all but certain that state capitalism will end under the watch of Xi Jinping, possibly under his second term (from 2017 to 2022), either in a crisis or in a gradual transition engineered by reforms. At the time of this writing, the crisis scenario is inching upward in probability relative to the reform scenario.

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# Barriers to Entry and Regional Economic Growth in China

**Loren Brandt<sup>1</sup>**

## *Background*

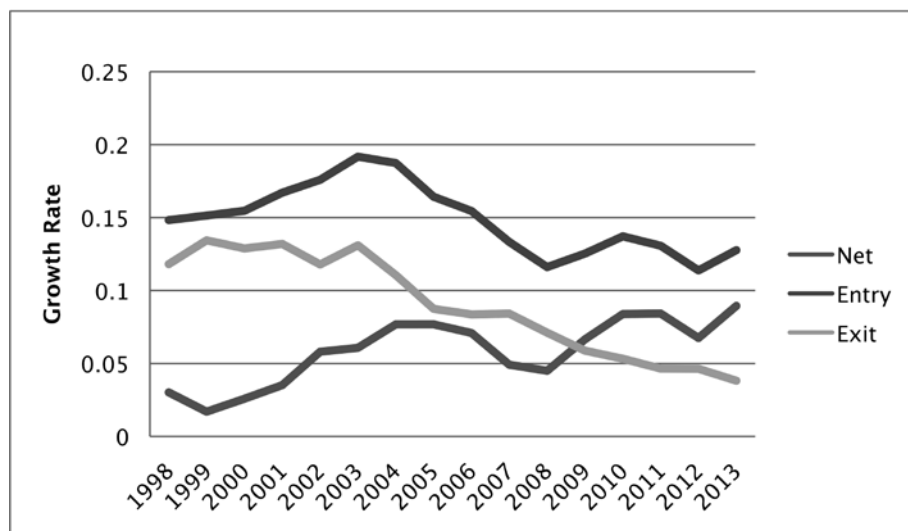
Since the onset of economic reforms in China in the late 1970s, new firms have been an important source of growth. However, huge differences persist in their contribution across sectors and regions, likely signaling differences in the entry process, and more generally in the political and economic environment in which they operate. This paper summarizes ongoing work looking into the role of new firms, and briefly considers some of the policy implications. In its focus on new firms and entrepreneurship, the paper connects directly with Yasheng Huang's seminal contributions on China's emerging private sector (Huang, 2003 and 2008).

## *How Do New Firms Matter?*

New firms are an important source of growth in an economy, and contribute on the both the extensive and intensive margin. On the extensive margin, they draw in new resources, e.g. labor and capital, to the economy; on the intensive margin, they can help to raise total factor productivity in the economy. The magnitude of these productivity gains will depend not only on how much more productive new firms are than incumbents, i.e. established firms, but also their size and market share.

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**Figure 1:** *New Firm Dynamics Industry*

Source: *Business Registry of Administration of Business and Commerce*.

China has enjoyed very high rates of new firm entry the last decade and a half. In Figure 1, we draw on a unique resource, the Business Registry of the State Administration of Industry and Commerce (SAIC), to track new firm entry, as well as firm exit, in industry, which includes manufacturing, construction and public utilities.<sup>2</sup> We normalize new firm entry in each year by the number of firms in business at the end of the previous year, thus giving us a “rate of entry”. We do the same thing with respect to exit. Net entry is the difference between the entry and exit.

Between 1998 and 2013, new firm entry averaged nearly 15% per annum. Most of these firms were Chinese-owned and private, reflecting falling barriers to entry. Entry rates rose with China’s WTO accession, fell through the onset of the Great Recession and then leveled off. In 2013, more than 300,000 new firms in industry were established. Exit rates were generally declining over this period, giving rise to slightly cyclical but rising rates of net entry over the period.<sup>3</sup> To help

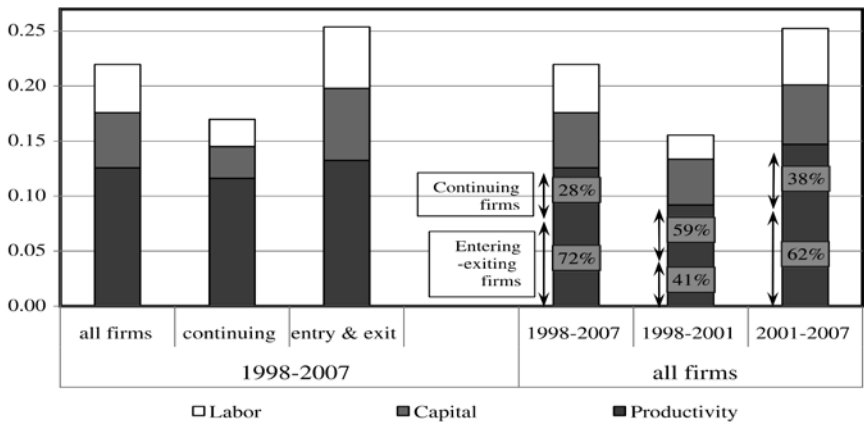
2 The Business Registry includes all firms that were ever registered in China, and provides information on each firm’s date of establishment, investors, primary business activity, as well as the date the firm deregistered and went out of business or had its license revoked. Non-payment of taxes is the most frequent reason for the latter.

3 Exit rates are equally important to an economy’s dynamism and the focus of ongoing work on China. Failure of poorly performing firms to exit slow up the reallocation of resources to more productive firms, and can be a huge drag on an economy. Declining exit rates the last few years may also reflect cohort

put the gross entry rates in comparative perspective, they are similar to those observed in the US in the 1970s and 1980s (Hathaway and Litan, 2014).

How important is entry and exit to the growth of output and productivity for industry? Firm-level data from China’s National Bureau of Statistics annual firm survey allow us to examine the contribution of new firms for the period between 1998-2007.<sup>4</sup> By 2007, firms in the NBS sample totaled nearly half a million, and were the source of nearly two-thirds of industrial output and value added. Over this period, industrial output grew more than twenty percent per annum. Chinese industry also achieved rates of productivity growth that were on par or better than those enjoyed by other Asian economies, e.g. Korea, Japan and Taiwan, at similar periods of their economic development.

**Figure 2: Output and Productivity Decompositions**



Source: Brandt et. al. (2012).

Figure 2 provides a decomposition of the sources of growth in industry. Several things are noteworthy. First, over this period, productivity growth is the source of more than half (57%) of the total output growth observed (see the panel on the left hand side of Figure 2).<sup>5</sup> The rest (43%) is coming from the extensive margin:

effects related to the high rates of entry and general declining average age of firms.

4 A change in firm IDs in 1998 makes it difficult to link firms in earlier surveys. After 2008, the NBS stopped reporting value added, which poses problems in extending this analysis. In 2010, NBS also increased the minimum size requirements (from 5 million RMB to 20 million RMB) for firms to be included in the survey.

5 On productivity growth, also see Yu (2015).

the increase in the labor and capital used in the sector. Second, nearly three-quarters of the estimated productivity growth is coming from entry-exit behavior (see the panel on the right hand side of Figure 2), almost all of which is a product of entry. Exit plays a very minor role, largely because of the failure of larger, poorly performing firms to exit. This finding is in sharp contrast to the US where the net entry margin is the source of only a quarter of industry output growth (Foster et. al. 2001). And third, the contribution of new firms is actually larger after China's entry into WTO in 2001. One interpretation consistent with this finding is that China's WTO entry helped lower barriers in the domestic economy facing new firms.<sup>6</sup> It is generally recognized that China's entry into the WTO was as much about domestic market reform as it was about acquiring better access to export markets (Branstetter and Lardy, 2008).

### *Sector Heterogeneity*

Analysis at the aggregate level conceals enormous heterogeneity between sectors. And it is here that we can see some of the consequences of the discrimination facing non-state owned firms in key sectors that Yasheng Huang's earlier work called to our attention. Since the mid-to-late 1990s, the state has retreated from the more labor-intensive sectors in industry, e.g. textiles and apparel, and focused on sectors identified to be "pillar" or strategic industries, e.g. iron and steel, electrical machinery (Pearson, 2015). The latter are sectors that China's leadership believes imperative to cultivate domestic capabilities for economic as well as military and strategic reasons; moreover, China's leaders desire to grow these sectors almost exclusively through state-owned firms.<sup>7</sup>

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6 Note also the smaller contribution for the two sub-periods than for the long period between 1998-2007. In general, the contribution of net entry is smaller over shorter time horizons because it takes a few years for new entrants to converge in productivity level to incumbents and to build up their output share.

7 Over time, the door has widened for private firms in some of these sectors, but a case can be made that a bias in favor of state owned firms persists.

**Table 1:** *SOE Shares and Sector TFP Growth, 1998-2007*

	Total Change in ln TFP	Sources of Change in TFP			
		Existing Firms	Reallocation Between Firms	New Firms	Exiting Firms
SOE Share > 0.5	-0.117	-0.048	0.007	-0.080	0.004
SOE Share < 0.5	0.208	0.050	-0.024	0.175	0.007
All Sectors	0.107	0.019	-0.014	0.096	0.007

Table 1 reports estimates of TFP (Total Factor Productivity) growth and a decomposition of the sources of TFP growth, after first dividing sectors on the basis of state ownership. We use as our cutoff a fifty percent share for state firms of GVIO (Gross Value of Industrial Output) in 1998; however our findings are not sensitive to the exact cutoff we use. There are four potential sources of productivity growth: 1. productivity growth of incumbent firms, or the “within” margin; 2. reallocation of resources to more productive firms, or the “between” margin; 3. new firm entry; and 4. firm exit. The “between” margin captures the productivity gains associated with the reallocation of resources to the most productive firms. In principle, these terms can be either positive or negative, the latter indicating that the changes are associated with declining productivity growth.

The contrast between sectors suggested by Table 1 is stark. Over this period, total productivity growth in state-dominated sectors is on average negative, while sectors in which non-state actors dominated experienced robust productivity growth. Even more telling are the contributions coming from incumbents and new firms that enter these two groups of sectors. In the state-dominated sectors, productivity growth of existing firms in the sector is actually negative between 1998 and 2007, as is the contribution of new entrants. The latter occurs when entrants enter at productivity levels that are lower than the marginal firm in the sector, thereby pulling down average sector productivity. We observe the exact opposite in those sectors from which state owned firms have retreated, and in which private firms, domestic as well as foreign, now dominate. Moreover, in state-dominated sectors, both state and non-state firms contribute negatively to productivity growth; in non-state dominated sectors, new state entrants contribute positively, albeit not to the levels of non-state firms.

The negative contribution of new entrants is especially telling. In an environment in which firms face high barriers to entry, we expect only the most productive firms to enter, i.e. firms expecting both to cover entry costs, and make

profits. The fact that the contribution of these firms is negative suggests a highly politicized entry process in which entry is restricted, and entering firms enjoy economic rents from their political connections. These rents can come in a variety of forms including preferential access to credit and key intermediate goods such as electricity, as well as through protected output markets and huge mark-ups. This interpretation is supported by recent work showing that productivity in these state-dominated sectors declined at the same time that their relative profitability was actually rising (Berkowitz et. al., 2015).

**Table 2:** *Heterogeneity in the State Sector*

Sector	Absolute Change in TFP	Source of Productivity Change			
		Existing Firms	Reallocation Between Firms	New Firms	Exiting Firms
Special Purpose Machinery	0.209	0.069	-0.012	0.148	0.004
Transport Equipment	0.163	0.068	-0.021	0.111	0.005
Ferrous Metals	-0.062	-0.014	0.004	-0.045	-0.008
Chemical Products	-0.116	-0.055	-0.001	-0.061	0.001
Non-ferrous Metals	-0.548	-0.213	0.064	-0.386	-0.013
Petroleum	-0.803	-0.312	0.080	-0.570	-0.001

The state versus non-state dominated distinction among sectors is useful but also potentially misleading. To help make this point, Table 2 provides decompositions similar to those in Table 1, but for three separate two-digit sectors dominated by SOEs in the late 1990s. Both the “Transportation Equipment” and “Special Purpose Machinery Sectors” do as well as on average as those sectors in which SOEs were less prominent. Entry remains the most important source of productivity growth, but improvement by incumbent firms represents 35-40 percent of total productivity growth within both of these sectors. Contrast this behavior with that in iron and steel, chemicals, or petroleum, all three of which experienced declining TFP growth over this period as a result of poorly performing incumbents, and very weak entrants. These sectors have also been in the news once again as a result of problems of excess capacity and corruption.

This highly mixed behavior helps highlight that state ownership is probably only part of the problem. Within sectors dominated by non-state firms, one can



also find state-owned firms that perform well.<sup>8</sup> Equally important is the competitive and regulatory environment in which these firms operate, an environment that has been heavily influenced by tariff and non-tariff barriers on imports, restrictions on FDI (foreign direct investment) and forms of technology transfer, government procurement policy, and high costs of entry for private firms. Brandt and Thun (2010, 2016) illustrate this point in the context of “mature” industries such as autos, heavy construction equipment, and telecom equipment. Those sectors that have experienced the most rapid growth, and in which domestic (Chinese) firms are now able to compete in more demanding market segments are, in fact, those that since the onset of reform in the late 1970s and early 1980s have generally been the “most open”.<sup>9</sup>

### *Regional Dynamics*

Our focus to this point has been on differences among sectors within industry. There are reasons to believe that there are equally important differences between localities and regions in terms of the environment facing new firms, which have important implications for regional growth differences. In principle, these regional differences could be manifested in terms of differences in the rates of entry of new firms, their size, as well their level of productivity and wages.

A key stylized fact about China’s growth over the last three decades is that those localities that had the largest state sectors when the reforms began have experienced the lowest growth (Brandt, Hsieh and Zhu, 2008).<sup>10</sup> This relationship is true controlling for important local factors, e.g. mean level of education attainment, percent of the labor force in agriculture, composition of industry output, and is robust to the use of provincial or regional fixed effects. The latter implies that the size of the state sector is as important in explaining differences within regions or provinces as they are in explaining differences between them.

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8 It is also the case that non-state actors in state dominated sectors generally perform poorly, reflecting both the “negative” selection process into the sectors, and a weak competitive environment.

9 Mature industries are those in which a well-defined technology platform already exists. In these sectors, innovation on the part of Chinese firms tends to be incremental, and entail both cost and product innovation. Over time, innovation of this sort enables these firms to narrow the technology gap with firms from advanced countries, and compete in more demanding market segments where margins are usually higher.

10 The size of the state sector in a region often reflected historical factors, most notably, the relocation of industry inland under the Kuomintang before 1949, and similar decisions after 1965 with the Third Front (Naughton, 1988).

Ongoing work (Brandt, Kambourov and Storesletten, 2016) shows a strong negative correlation between the size of the state sector at the prefecture level and new firm activity. The critical question is: through which channel does the size of the state sector affect new firm activity? In principle, any one of a number of factors may be important including the ability of potential entrants to access financing and thus the cost of capital, the level of wages, the price of key intermediate goods such as raw materials and electricity, as well as local taxation. One thing these factors have in common is that they would induce “positive” selection into industry in these locations, i.e. only the most productive of potential entrepreneurs would be able to incur these higher costs and find it profitable to enter.

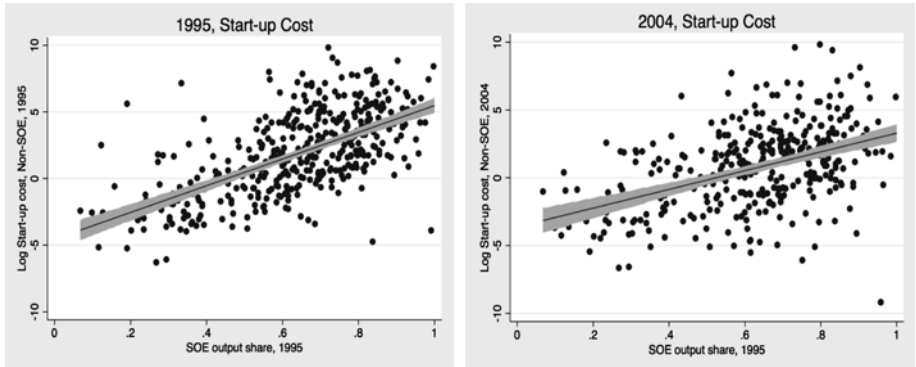
The census data for industry for 1995 allows the size of these barriers and impediments to be quantified at the local level.<sup>11</sup> Significantly, they are not able to explain key differences that we observe in new firm dynamics, namely, the much lower productivity and wages of new firms in localities where state firms dominate. To reconcile these patterns, some other kind of cost is required, most likely, an entry cost. This can be thought of as some combination of formal and informal costs that firms must pay to start up a business. Moreover, not all firms that are willing to pay these costs will necessarily be able to operate.<sup>12</sup>

In the context of a Lucas-Hopenhyn model of new firm entry, Brandt et. al. (2016) are able to estimate these costs (or wedges) for 1995, 2004 and 2008, yielding several noteworthy results. First, entry costs are sizable and highly correlated with how important the state sector is in a locality. Second, the estimated costs are also highly correlated with the formal costs of starting a new business estimated by the World Bank as part of their “Doing Business in China” report in 2008. Figure 3 shows the correlation between the estimated wedges and the size of the state sector in 1995 and 2004. The correlation is weakening slightly over time, but highly persistent.

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11 The methodology used here is similar to that in Hsieh and Klenow (2008).

12 Some kind of rationing of licenses to operate is required to break the link between the tightness of the restrictions on entry, and the productivity of the entrants.

**Figure 3:** *Start Up Costs, 1995 vs. 2004*

More work is required to better pin down the exact link between the size of the state sector and local official behavior that bears on these costs, but the preliminary findings are highly suggestive. They also have potentially important implications looking forward. With the onset of the Great Recession in 2008, and a sharp drop-off in external demand, China once again relied heavily on investment and expansion in the state sector to maintain growth. This kind of behavior was also most prominent in exactly those localities where the SOEs had been historically more dominant. While this may have contributed to faster growth in the short-run, in the long run it also likely helped to reformatify a set of institutions in China that have been consistently inimical to new firm development and economic growth.

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# Entrepreneurship with Chinese Characteristics: China, Taiwan and the Tech Industry

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## *Introduction*

The economies of East Asia have been a focal point of development studies for decades, starting with their unprecedented growth rates and rapid industrialization in the 1960s and 1970s. In the 1980s scholars added China to the list of Asian miracle states that included Japan, South Korea, Taiwan, and Hong Kong. China's inclusion was based on its impressive economic performance following Deng Xiaoping's reform and opening (改革开放) efforts. The attention of scholars was directed at identifying the key factors that made these Asian states so unique and impressive in their economic transformation. Some scholars (Chan 1996, Chang 1998, Chai & Rhee 2010, Clark & Chan 1992, Li 1997) asserted that "Confucian capitalism", a common Confucian-inspired culture that emphasized a strong work ethic, hierarchy and harmony, explains the success of Asian economies. Confucian elements shared across Asian states, created the right environment for growth and development in contrast to non-Asian developing states, such as those in Latin America, that also tried combinations of export led and import substitution industrialization but failed to see similar results. However, the Confucian explanation was a rather loose association and did not hold up well when some of the cases were examined more closely (Cha 2003, Yao 2002). For instance, Yao (2002) claims that China worked hard to stamp out the so-called Confucian elements in the Mao years, and the Confucian explanation largely

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centered around forcing an oversimplified notion of culture on very distinct Asian states. Therefore, arguing that these states should be considered similar systems on the basis of culture was difficult to determine both within and across cases.

As the debate on the causes for Asian growth developed further, scholars argued state directed development was a key factor in economic growth, where heavy government intervention was readily present in each of the miracle cases (Haggard 1990, Johnson 1982, Unger & Chan 1996, Woo-Cummings 1999). The strong role of the state in the economic transformation of each Asian miracle state was evident. These were not democracies but bureaucratic authoritarian states, where governments readily shape political, economic and social life. Thus cultural norms rooted in Confucianism may influence the region's rapid economic development, but these norms were institutionalized by the state through various policies and practices. The idea that a strong state effectively facilitates growth defied capitalist logic, but the cases offered all of the evidence necessary for some scholars to proclaim that state directed development was the key ingredient in the East Asian model (Haggard 1990, Johnson 1982, Unger & Chan 1996, Woo-Cummings 1999). While there is no denying that Asian states necessitate further analysis for their developmental success, I argue there is reason to reconsider the continued role of the state in economic development.

Presently there is a shifting interest by scholars away from identifying the reasons for Asian growth, to a study of the region's economic transformation at a time of greater globalization and economic interdependence. The hope is that scholars can better understand the changes that have transpired, and anticipate problems yet to come. Since recovering from the 1997 Asian Financial Crisis, many Asian states have experienced sustained political and economic stability. Although the Asian economies are not without their own sets of macro challenges, there are many noticeable changes occurring at the micro-level, where the study of individuals and firms adds valuable insight into how political and economic forces are impacting society. An important part of this story involves examining the role of entrepreneurship, not only for its economic impacts but also for the possibility that entrepreneurs may serve as agents of political change (Chen & Dickson 2010, Dickson 2008, Tsai 2007). This intersection between the political and economic realms requires that we not only study the relationship from the top-down but also from the bottom-up. Entrepreneurship is a driving force of capitalism and economic growth, and entrepreneurs enhance the general welfare of the population through their entrepreneurial activities. However,



to understand the relationship between entrepreneurs and economic growth we must move beyond traditional business and economic analysis to include political factors that shape the entrepreneurial environment and the consequences of that interaction between politics and the economy, especially in the more state-driven economies within Asia.

This relationship between state and economy is a complex one, and Yasheng Huang's study of entrepreneurship outlines China's economic and institutional processes that have been instrumental to its growth and development (Huang 2008). As his work demonstrates, China is an ideal case for examining the role of a strong state in economic development, but its size and diversity warrant a closer examination at the micro-level. The framework he provides on the role of the state and its relationship to entrepreneurship can be used to examine other countries with state directed development. It is in the context of these issues that the Chinese case can be used as a comparative model to study Taiwan, with the intent of answering two questions: how much state involvement is still necessary? When does state intervention become a liability?

The challenges that emerge can be seen quite clearly when examining the technology industry in Taiwan. Taiwan's tech industry started under the guidance of the state, and it was one of the hallmarks of Taiwan's overall growth and success. However the technology sector's current structure and state efforts to manage that structure may actually impede Taiwan's continued economic growth. To illustrate these problems, I engage in a comparative analysis of the political and economic factors that contribute to entrepreneurship in China and Taiwan. The first section of this chapter or article reviews the general entrepreneurial environment in each case, to show how the state has attempted to manage the development of entrepreneurship. Next, I analyze the technology industry in Taiwan, based on fieldwork with government officials, venture capitalists, and entrepreneurs. Here I determine the opportunities and constraints specifically related to technology start-ups. Finally, I illustrate the future opportunities and challenges faced by entrepreneurs in states where governments play a strong role in shaping the entrepreneurial environment by implementing regulations that intentionally and unintentionally impede business formation.

## *The Entrepreneurial Environment in China and Taiwan*

Yasheng Huang's groundbreaking work on entrepreneurship in China identified the key role of Township and Village Enterprises (TVEs) in China's post-78 economic takeoff, while reducing the role of Foreign Direct Investment and the South China miracle. Huang argues that beginning in the 1990s, a strengthened state hindered entrepreneurship and decreased prosperity in China, particularly in rural areas. His book documents that entrepreneurship thrived outside of state directives, not necessarily because of them, which reiterates a common theme that sometimes luck rather than intent helped the Chinese economy flourish. When the state tries to adapt to economic changes, it can sometimes redirect attention in the wrong areas.

These questions involving entrepreneurship cannot adequately be examined at the macro-level, especially in a country as large and diverse as China. Yet the literature (Naughton 1996 & 2006, Lardy 2014) remains focused on policies directed from the top down, with only a few areas gaining more detailed exploration. Unique cases like the study of Wenzhou's entrepreneurs (Parris 1993), Shanghai's entrepreneurs (Huang 2009), Shanxi's entrepreneurs (Goodman 2004) or the most successful contemporary entrepreneurs like Alibaba's Jack Ma show us there is much to be learned from micro-level qualitative research. China's disruptors, the new generation of entrepreneurs from the high-tech BAT industries (Baidu, Alibaba and Tencent), demonstrate that studying the exceptional can provide a model that others can emulate even if these models do not represent the norm (Tse 2015).

My own research on female entrepreneurship in China (Currier 2007, Currier 2009) further demonstrated the value of micro-level case studies as opposed to general theories based on labor market forces at the macro level. While other scholars concluded that Chinese women had been negatively impacted by Zhu Rongji's layoffs in state-owned enterprises (Hershatter 2007, Kerr & Delahanty 1996, Wang & Hu 1999), my closer examination of individuals and firms found a more complex story. The state had disproportionately discharged women as redundant workers, but there was variation among the different cohorts of women with respect to their employment opportunities. The state directed women out of the state sector through lay-offs and restructuring, but created new opportunities by permitting the development of a private sector that was able unexpectedly to absorb some cohorts of that newly restructured labor force (Currier 2009). This

research, which was based on interviews with 292 female entrepreneurs in Beijing, found that women with no intention of creating their own businesses were instead thrust into new economic endeavors becoming “accidental entrepreneurs,” when the government downsized the state sector and permitted the development of the private sector and individually owned enterprises rather than only allowing for state owned enterprises. One of the most important findings of this research was that female entrepreneurship among a middle cohort of women (aged 33-45) developed and increased, not *because* the state promoted female entrepreneurship but *in spite of* the fact that the state implemented what might be interpreted as gendered policies designed to disproportionately negatively affect women in the labor market (Currier 2007, Hooper 1984, Jacka 1990, Kerr & Delahanty 1996, Summerfield 1994, Zheng 2003).

As each of these aforementioned studies on entrepreneurship show, there is much to be learned from examining the impacts of policy rather than just the intent behind policies. Although this may not imply there is the rise of local state corporatism (Oi 1995), there is a clear shift to examining localism in entrepreneurship that can be illuminating (Goodman 2004). Huang’s work unites these issues as he uses local cases to illustrate that entrepreneurship thrived *outside* of directives by the state, *not due to them*. These arguments differ from the more established claims that state-directed development was the key ingredient for the Asian economic miracle.

The policies China adopted during the various stages of reform give us a general sense of the state’s plan with regard to introducing capitalist principles into the socialist economy, but it is just as important to see how the private sector evolved outside of any explicit state-directed plan. Today it is clear that market forces are taking on a life larger than their own and raising questions about the state’s ability to manage the economy in the future (Lardy 2014). Rather than continuing to explore the macroeconomic forces that have shaped China’s growth in the past, we must continue to look forward at the effects of privatization and what this can tell us about the path that lies ahead. These lessons are important not just for understanding the Chinese economy, but they can be used to explore states with similar challenges or dilemmas impacting state control in the economic sphere. It is in this context that China can serve as an effective model for examining other cases such as Taiwan.

Like China, Taiwan’s economic development in the modern era has involved heavy state involvement. In the 1950s, Taiwan focused on an export-led growth

strategy combined with high tariffs to protect the domestic economy, creating Export Processing Zones to attract foreign direct investment and developing a comparative advantage in light industry. Although Taiwan's development path started two decades before China's, both economies followed similar patterns: heavy state involvement, export-led industrialization and rapid economic growth. Differences emerge in the 2000s, when China's economy continued to adapt and diversify while Taiwan's lagged behind with its heavy emphasis on the hardware side of the technology industry and its inability to implement structural change.

In the 1970s Taiwan began to shift its light manufacturing focus from textiles to the hardware industry, and it quickly developed into an innovation-driven economy. Once China engaged in reform and opening, light manufacturing began to move there from Taiwan and other Asian nations with increasing labor costs. China's large labor force allowed it to capitalize on these trends, and Taiwan was able to shift its production to technology, with companies like Acer, Asus, and Foxconn building the semiconductor and electronics industry and shifting production to China. Through the 1980s, Taiwan maintained its comparative advantage in information technology, and focused on producing hardware for consumer electronics, information technology, communication peripheral devices and electronic equipment. In the 1990s the government expanded tax incentives to the hardware industry and added some protections to small and medium enterprises in the constitution, designed to cultivate and create a real hardware based economy.<sup>2</sup> By the 2000s companies like Acer and Asus became global brands and solidified Taiwan's position as a hub for information technologies. But it is at this point that Taiwan goes from becoming a leader in the industry to a follower, failing to adequately adapt and adjust to changing global needs. Naturally the size differential between China and Taiwan means that there will be unique challenges for each state, but using the comparative method one can engage in a systematic evaluation of the two entities to determine important points of comparison and differentiation (Lijphart 1971, Collier 1993).

One of Taiwan's biggest challenges in the contemporary era is that it remains focused on hardware and has not allowed the entrepreneurial environment in the software industry to flourish. Meanwhile increasing competition from Vietnam and China has weakened Taiwan's hardware advantage. Taiwan lacks the lean start-up environment necessary to move from hardware manufacturing to

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2 Interview with officials in the Small and Medium Enterprise Association, March 10, 2012.

software development. The state has tried to carve out a space for start-ups, with a variety of programs designed to guide and structure a start-up market, but by definition the start-up industry requires flexibility and less state intervention to foster creativity, adaptability and innovation. Therefore strong directives by the state may actually be hindering growth rather than facilitating it, particularly when we examine the cases of less “exceptional” entrepreneurs rather than focusing on only the most successful cases of entrepreneurs who have turned their ideas into highly profitable global companies. As this analysis of Taiwan’s technology start-up environment will show, state-guided development must decline if economies are to adapt to changing global dynamics.

### *Taiwan’s Tech Industry*

The technology industry is an interesting sector to examine with respect to entrepreneurship, as it exemplifies the importance of innovation and adaptability. Entrepreneurship is about discovering undeveloped profit opportunities or finding a better way to deliver products or services to a market (Kirzner 1973). However, this becomes difficult when the state adds too many restrictions to the business environment. In this overview of Taiwan’s tech industry, I draw on interview data from 56 entrepreneurs, government officials, angel investors and venture capitalists in Taipei in 2012. The interviews included questions about the motivations of entrepreneurs, the businesses they established, the role of the government, the marshaling of resources, and assessments of reforms that have hindered or helped business development. The main findings demonstrate that the programs and institutions created by the state have constrained innovation.

#### *3.1 The Lean Start-up Model*

The focus of this project was on the technology “start-up” industry, which requires some explanation. The start-up industry is generally used to refer to new companies in technology, originally in reference to the explosion of dot-com businesses in Silicon Valley, which are designed to create business solutions and a scalable product in a short period of time. Another way to explain this is to use the start-up methodology (Ries 2011) where the goal of the entrepreneur is to build a minimal viable product (MVP), measure the results, learn from these findings and

either persevere or pivot in order to keep the business alive.<sup>3</sup> This build-measure-learn feedback cycle is designed to be short, in order to minimize waste and avoid the problem of “paralysis by analysis” that new potential entrepreneurs may face.

The way the start-up environment generally works is that entrepreneurs visit a start-up event with an idea and a pitch, looking for individuals to form a development team (programmers, marketing specialists, etc.) who can help them refine their idea into a functioning product in a very short amount of time. At the end of the start-up event, they pitch to find investors or search for an incubator or accelerator that can help them further develop their idea. Their idea then becomes a business and the entrepreneurs become founders. This is the Y-combinator model that emerged in Silicon Valley in 2005, which is now a community of over 2,500 founders and has funded more than 1,000 start-ups for a combined valuation of \$65 billion USD.<sup>4</sup>

Once the entrepreneurial idea is ready to become a business, angel investors or venture capitalists may offer the founders seed money in return for equity in the company. If there is an incubator or accelerator available (through an investor or another private or government entity), the founders may be offered dedicated space to work on their business, as well as a network of mentors or other founders to maintain their creativity and increase the likelihood of bringing their product to market. After a few months in the incubator or accelerator, the founders are ready for Demo Day where they pitch their idea to a group of potential private investors hoping to find further financial assistance and mentorship that culminates in taking the firm public. This lean start-up process has become the new global model for the technology industry and fosters a creative environment for entrepreneurial activity. In most contexts these incubators have developed organically, by private investors or interests outside of the state.

### *3.2 Hardware to Software*

The technology environment in Taiwan is slow to adjust to the lean start-up model and is antiquated in its approach since it is still hardware focused rather than software focused (Yu 2009). For Taiwan, the tech industry is still about

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3 In the lean start up method “to persevere” is to continue to engage in scalable growth and “to pivot” is to rework the idea to make it into a viable business endeavor capable of making money.

4 The Y-combinator model is described in more detail at [www.ycombinator.com](http://www.ycombinator.com)

mass produced tangible products, with the model being large companies based in industrial parks focused on assembly and manufacturing rather than on idea creation. The revolution in information technology experienced by the rest of the world over the past fifteen years has only begun to make its way to Taiwan in the last six years, and it is experiencing a variety of setbacks due to efforts by the state to manage the start-up environment.

Taiwan's state investment in a technology economy dates from the 1970s. The government created Hsinchu Science Park in 1978, and it quickly became a regional hub for information technology production as well as research and design (Fell 2012). Pipelines established from National Chiao Tung University and National Tsing Hua University to industries in the Science Park provided a ready supply of talented young graduates to fill positions. Engineering is one of the most popular majors in Taiwan, representing one-fourth to one-third of all university degrees offered.

However, the state has continued to emphasize that hardware is where the national comparative advantage lies, even when profit margins for technology manufacturing have fallen in half in recent years (Sui 2013). The state has been slow to realize that Taiwan's real challenges lie in a lack of incentives for start-ups and a work culture that discourages risk-taking and innovation.<sup>5</sup> Although the state has made an effort to create an entrepreneurial environment conducive to start-ups, the programs offered still place too many constraints on new business ideas and favor brick and mortar entities rather than information technology businesses.

### *3.3 The State's Role in Managing Start-ups*

As it stands, the entrepreneurial environment in Taiwan is not conducive to information technology start-ups. The state has acknowledged the importance of continued innovation and has worked to create incentives for individuals to create their own businesses, with programs being offered by the SMEA (Small and Medium Enterprises Association) and the MOEA (Ministry of Economic Affairs). But it has also co-opted the entrepreneurial environment by trying to become the main entity in charge of incubators, seed money and start-up events. To under-

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<sup>5</sup> There is both a business culture and a social norm that places value on working for one of Taiwan's hardware industries. These jobs are seen as desirable, valuable and stable, therefore parents aspire for their children to work for one of these companies in a "salaried" job.

stand how the state has become involved in these activities, we must examine the programs and institutions the state has created.

The SMEA was established in the 1980s, and was designed to address the unequal distribution of wealth across enterprises. It offers new capital, guaranteed loans and capital investment and its main function is to assist with the financing of enterprises.<sup>6</sup> In 2009 the SMEA also focused on developing incubators, centers to assist start-ups, offering management and financing advice, work space, and networking opportunities to help the businesses grow. By 2012 there were 131 incubation centers around Taiwan, most of which are in or affiliated with universities. Essentially the SMEA has become a self-proclaimed one-stop service center for start-ups by helping them secure access to funding, space, mentoring, and other tools to develop their ideas.

The MOEA actually runs many of the incubators but the management of these entities is generally done by the host universities and the Institute for Information Industry (III). III is a hybrid organization encompassing government and private interests to promote innovation particularly in the IT industry, where it oversees cloud technologies, green-technologies, securities software, mobile and other technology related areas.<sup>7</sup> While these aforementioned government affiliated bodies have constructed a space for tech start-ups to thrive in theory, in practice they exerted too much structure and control, thereby stifling innovation.<sup>8</sup> The state has also taken over many of the features in start-up communities that are more commonly directed by private interests such as the creation of incubators, running its own Start-up Taiwan events, and working on seed funding.

Moreover, the mindset in the SMEA and MOEA is still based on a traditional model of product development and turning small enterprises into large companies, rather than building an environment to let smaller enterprises carve out their own niche. The end goal for the SMEA with respect to start-ups is to get them quickly to an Initial Public Offering (IPO), which has a small likelihood of success and keeps entrepreneurs focused on becoming larger and more conventional

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6 To qualify as an SME you must have less than \$80 million NT in capital in manufacturing and less than 200 employees, or have sales revenue less than \$100 million NT in the non-manufacturing sector and less than 100 employees.

7 Interview with Innovation and Information Industry technology start-up project manager, May 11, 2012.

8 One government official remarked that the SMEA tries to offer so much help that the entrepreneur gets caught up in the bureaucracy that he/she cannot focus on the business and has no time to engage in creativity and innovation (Interview April 3, 2012).



as opposed to more flexible and innovative as the start-up industry is commonly known for.<sup>9</sup> Therefore the focus is on concentrating the control of resources and creating the next big companies to be the face of Taiwan, rather than fostering innovation and a true start-up environment.

### *3.4 Financing the Venture*

A second constraint facing the tech start-up industry involves financing. Securing resources is a problem many start-ups face, with many entrepreneurs first approaching family and friends to bootstrap their businesses. Once those more traditional avenues have been exhausted, the remaining options are private capital from an investor or government funding. Private capital is difficult to find for entrepreneurs everywhere, but Taiwan lacks domestic angel investors. As a result, the government fills this void by offering microloans for businesses with fewer than five employees and a variety of other loan programs designed to help entrepreneurs in any industry. These financial incentives to assist start-ups include priority lending and deferred interest payments, but the problem is that the application criteria and structures are still geared towards more traditional businesses and are not conducive to the tech industry.<sup>10</sup>

In the interviews, most entrepreneurs reported that they were unable to secure funding from government sources and unanimously agreed that government funding criteria were unclear, and the application process required too much time and requested too much information. For instance, in order to receive funding a start-up firm's capital value must be verified, which is difficult for a technology start-up without an operational product already in the market. Once valued, the government then taxes the start-up based on that paper valuation, which would include finances obtained from investors, even if the company is not yet profitable (Sui 2013). Since many tech start-ups need investment at the research and development stage, and may take a few years before they see a profit, these conditions

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9 Keith Bradsher reviews the declining hardware industries in Taiwan and the crisis in innovation that is plaguing the country today. The challenge is that Taiwan does not have the cheap labor advantage of some of its Asian neighbors and it does not have the right business environment or mindset in the tech industry to allow for innovation and creativity anymore (Bradsher, 2013).

10 There are different loan programs available through the SMEA. For example they offer special loan programs for youth (aged 24-45), through the National Youth Commission, and for women owned businesses through the Council of Labor Affairs. Some of the loan incentives they offer are quite favorable, where interest is paid by the government for the first two years.

make it less likely start-ups will be either eligible for government sources of funding or could sustain a revenue base to remain operational even in the short-run.

Among the 43 start-up companies interviewed, most began an application for government funding in some form but found the process to be overwhelming and the success rates were too low to make it a valuable use of their time.<sup>11</sup> Therefore many of the entrepreneurs never submitted a completed application to be considered for government funding. Only one of the entrepreneurs was able to secure government funding for his start-up, and noted that it took a year from the time of application submission to the time the first funds were received. This is an eternity in the information technology world, where the market changes so rapidly. In order to receive funds individuals must fill out a detailed 100-page application, attend sessions on how to run a business and then wait while a board of seven to eight bankers, scholars and government officials study the application. Once accepted, the state offers the entrepreneur further assistance on writing a business plan and more business management courses. The loan itself is also dependent on the amount of collateral one is able to offer, where loan amounts can vary from up to \$4 million NT (New Taiwan Dollars) with a ten year repayment timeframe versus only \$1 million NT with a shorter six year repayment plan (Interview 12 April 2012). However, the resources that are available are not the problem, it is the time required and low likelihood of success that deter applicants.

Other entrepreneurs among the start-up companies interviewed reported similar problems, spending months to fill out documents, being required to take business development courses, and then discovering even if loans were granted they would have numerous restrictions. An entrepreneur with an iOS mobile shopping application complained that the paperwork required a detailed projection and timeline of financial goals, and only when those targets were met would the funds be released at each stage (Interview April 30, 2012). In addition, if approved the entrepreneur would only be allowed 60% of the registered capital in loans, so if he/she did not start with enough capital it would be difficult to secure enough funding. The challenge is that the programs are naturally focused on reducing potential risks, which is even trickier with a start-up. With bureaucrats worried about maintaining their own jobs and securing promotion, which depends on demonstrating “success,” they simply avoid funding more risky en-

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11 27 of the respondents reported beginning the application process, with only five completing the application for funding, and only one of those five receiving funding.

terprises.

Some entrepreneurs were not easily deterred and had multiple application attempts. The discouraging part was when the proposal finally reached the review board and the committee ultimately did not understand the design or simply concluded the business was too risky without further explanation (Interview 29 May 2012). In another case, the board reported to the entrepreneur the business was unable to produce reasonable profit projections at this early stage in the application, making it too risky, and the applicant was invited to reapply when the actual product was complete (Interview 7 May 2012). The entrepreneur in this case argued that since he was applying for seed money to actually build the mobile application, it was hard to offer projections on a product not yet in existence. Therefore it becomes a catch-22: if he had the final product on which he could base the projections, he would not need the funding for the build.

Entrepreneurs who did compete for government funding commonly reported that their funding requests were denied because their business concepts were “too risky”; the entrepreneurs thought the board did not understand their product. Government officials who sat on the review boards agreed that many of the technology start-up ideas were too risky and the concepts or need for products were not always clear (Interview, 3 April 2012). Since the financing options were not unique to the tech industry, the boards are reviewing a variety of business proposals that may range from selling shoes to creating mobile applications and the composition of the board does not necessarily have to include computer programmers or those knowledgeable in your particular industry. It truly becomes a case where one is comparing apples and oranges, or at least apples to the concept of an orange. When given these trade-offs, and considering less than 30% of applications will be funded, it is easier for the board to view shoes as a better investment than a mobile application.

Outside of the limited state sources of funding, the private sector is also challenged with investing in tech start-ups in Taiwan. Domestic angel investors have the strongest incentives to invest in local start-ups, and Jamie Lin of *Appworks* is among the most well-known of the tech industry investors and runs his own incubator.<sup>12</sup> However, many Taiwanese angels are not comfortable with the soft-

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12 At the time of the interview in 2012, *Appworks* was only on its third class of start-ups in its accelerator program. In two years they graduated 80 start-ups, but not all of these turned into viable companies. There are other well known incubators in Taiwan run by angel investors such as Volker Heistermann's *Yushan Ventures*, but there is a different commitment between foreign and domestic angel investors that

ware industry because their experience is in Taiwan's traditional hardware and labor-intensive industries. Thus, they hesitate to support a tech start-up, and as one angel put it "I am more comfortable filling a building with product rather than funding a start-up that creates technologies I don't understand or use" (Interview May 28, 2012). In addition, many of the angels are older, more traditional, and want quicker returns on their investments, making them unlikely to invest in a company where it may take a few years to generate any profits. Foreign angels can more readily see some of these challenges, and as one foreign investor remarked: "Taiwan angels are just too conservative, so most true technology start-ups have to rely on their family members to be their angels" (Interview March 19, 2012). Ultimately it comes down to the fact that sources of funding in Taiwan are extremely limited given the lack of domestic angels and the efforts by the state to take a more active role in managing the start-up environment.

### *3.5 Additional State-Directed Constraints*

Finally, with respect to the tech industry there is one additional obstacle involving the state, the issue of consumer protection and iOS versus android applications. Due to government regulations, consumers must be allowed to purchase items from the internet and have at least seven days to review the purchase and receive a full refund if they do not like the product. Apple negotiated with the government and allows users to purchase iOS applications and receive a refund after 2 weeks if they do not like the product. Google refused these terms; therefore, paid Android apps are not permitted on Taiwan mobile devices. From a technology standpoint this means Taiwan start-ups, should they want to operate in the local environment, can only offer iOS apps, limiting the platform and market share they are able to obtain outside of Taiwan (Interview March 9, 2012).

As this overview of Taiwan's tech industry demonstrates there are many obstacles the start-up industry must overcome. The state has not facilitated a culture of entrepreneurship and innovation that allows individuals to take risks and seek opportunities outside the control or directive of the state. The main challenge for Taiwan involves having adequate access to private financing (both early and late

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might be attributed to a stronger sense of nationalism and investment in local talent that is more prevalent in the latter. The success rate for start-ups is relatively low in other markets as well. The Y-combinator model, one of the most successful programs, has a business failure rate of 93 percent (Blodget 2013).

stage capital) and breaking the hardware versus software mentality that keeps Taiwan more risk averse and prevents an investment in technology innovation that will allow the economy adapt to the changing needs of the global market.

#### *4. Future Opportunities and Challenges*

Although China and Taiwan may not appear to share many similarities, several lessons from Huang's research on entrepreneurship in China can be applied to the start-up industry in Taiwan. The most important factor to remember when examining entrepreneurship in any context is that innovation and creativity are essential and require flexibility in the market. A culture of entrepreneurship is difficult to create when the state is heavily involved in managing the economy.

As Huang's work has pointed out, entrepreneurship flourished in China in spite of state controls and efforts to "manage" capitalism. We must constantly ask how much state involvement is needed in transitional economies and recognize when state intervention becomes a liability. To answer these questions requires analyzing the impacts of government policies, not just their intent. Therefore we must shift our level of analysis from the national to the sub-national or individual level to better understand how the market responds and where there is still room for improvement. Moreover, we must direct our attention away from the rarest, largest, most successful cases of entrepreneurship to study the more typical or average cases. As entrepreneurs know, there are just as many lessons to be learned in failure as there is in success.

Where does this leave entrepreneurs in China and Taiwan today? In this study of the entrepreneurial environment in both countries, we know that the climate for start-ups is rapidly changing. Huang notes that the freedoms entrepreneurs had in the early stages of reform in places like Wenzhou, where the waters were relatively untested, do not exist in the same ways today. Yet it was in this environment that entrepreneurship thrived and developed outside of state control. In Taiwan there have been similar challenges, where the mindset of the state is still rooted in the notion that heavy state involvement is the path to future success. However, as this discussion of the tech start-up industry has shown, the state cannot actively guide entrepreneurship in the modern era and expect to develop the environment that fosters creativity and innovation, which the Taiwanese economy desperately needs to transition away from being a hardware state. Although the developmental state model tells us a strong state role was evident in China and

Taiwan in the early stages of their industrialization, the state may now actually be more of a hindrance to development than a catalyst for it. What both of these countries need is not more state-led development but more entrepreneurial-led development, and the future of each depends on a decreasing role for the state.

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# Yasheng Huang and the Turning Points in China's Transition

**Barry Naughton<sup>1</sup>**

**T**he transformation and rise of China after 1978 was one of the most fundamental events of the twentieth century. Perhaps, in the period between World War II and the turn of the twenty-first century, there are only four or five stories with genuinely global significance: the extraordinary stabilization and growth of the capitalist world system after 1945; decolonization; the (unfinished) liberation of women; the collapse of the Soviet Union; and the transformation and rise of China. From the perspective of today (2016), we already take these stories for granted. They are simply the pillars of today's world, and although the achievements may seem slightly more precarious since the global financial crisis of 2008-9, they are still the fundamental events that structure the only world we can imagine.

Yet although we have begun to take these transformations for granted, our understanding of them continuously changes and, hopefully, deepens. This is especially true of the rise of China, because throughout much of China's transition away from Maoism, information was extremely limited; interpretive frameworks were rather simplistic; and robust many-sided discussions were rare. Many of us—I include myself in this group—watched China from the outside but analyzed a changing China in basically teleological terms. That is, we thought, or hoped, we understood where China was going: from a poor, backward society hobbled by a highly politicized and inefficient command economy, toward a prosperous, market-driven economy and a more diverse and less constrained civil society. To a greater or lesser extent, we analyzed contemporaneous developments in terms of how far they moved China in this direction. When China moved forward dramatically, we applauded.

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From his earliest work, Yasheng Huang stood slightly to one side of this general tendency. Repeatedly, Huang advanced interpretations that were subtly subversive to the predominant narratives. He took some aspect of the news from China and executed a judo-like flip that turned the perspective upside-down. Most strikingly, he did this in his work on foreign direct investment in China: while most of us were applauding the sudden flood of investment into China, Huang pointed out that the welcome mat laid down to foreign capitalists also reflected the lack of trust China's political leaders felt for China's indigenous capitalists. Foreigners were easier to control. Thus, information taken as a sign of steps in the "right direction" was also revealing other aspects of Chinese society and the Chinese political system.<sup>2</sup>

This unique, slightly offbeat, sensibility has continued to mark Yasheng Huang's work. He is one of the few analysts of China who contributes genuinely new perceptions. The freshness and creativity in Huang's work, though, should not distract us from the fact that the work is also marked by a consistent underlying theme. As I see it, Yasheng Huang's great theme is the following: Throughout the era of economic reform, China has had an authoritarian political hierarchy that matters immensely in all political and economic outcomes. This matters not just for political reasons, but also because it shapes the economic outcomes that we are often monitoring, and using as a guide to the system's trajectory. In addition, that political hierarchy is evolving in ways that really aren't parallel to the main economic trajectory (marketization), and so the interdependent evolution processes create some genuinely surprising hybrid outcomes. These insights should therefore shape our interpretations. This overall perspective is present in all of Yasheng Huang's books, and arguably is the motivating factor in each of them. However, each book has its own theme, and none of them are reducible to the overarching and motivating theme. Precisely because he unites a consistent and coherent viewpoint with a creative and surprising range of interpretations, Yasheng Huang is one of the few individuals to have influenced our overall understanding of the Chinese transition process.

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2 Yasheng Huang, *Selling China: Foreign Direct Investment During the Reform Era*. New York: Cambridge University Press, 2002.

### *Turning Points in the Transition Process*

Yasheng Huang's perspective on China's transition has made him one of the first, and most important, scholars to call attention to "turning points" in the transition process. There is a widespread resistance to calling turning points in China's recent development. Sympathetic portrayals of China's economic transition have frequently emphasized that China's approach to transition is experimental, incremental, and adaptive. As attributes of policy-making, these are all good things. They suggest a deep pragmatism, and willingness to work for a broad set of social benefits. They incorporate "discovery" (of what works and what doesn't) into the process of policy-making. These accounts clearly capture something about Chinese policy-making and the Chinese policy process. Moreover, the best accounts, such as those of Sebastian Heilmann, embed their appreciation for experimentalism with a careful understanding of the Chinese institutional and political context.<sup>3</sup> As a result, these studies of particular policy processes are satisfyingly realistic, while also highlighting these strengths of the Chinese policy process overall.

However, the emphasis on adaptiveness and experimentalism has two built-in intellectual pitfalls. The first is actually the less important, which is that analysts may suffer from selection bias. Case studies are intrinsically more interesting when they describe important and successful policy outcomes, and policy deadlock and failed policies are much less interesting. Students of the policy process are therefore naturally drawn to examine successful policies, even though actually understanding China's transition and policy process clearly requires attention to both. The second, even more important, pitfall is that the experimental and pragmatic paradigm encourages analysts to see almost any policy change as part of an overall effective process. What if an experiment is abandoned after a few years? What if goals are reformulated? What if there is a period of policy quiescence in which no new reforms or policies are enacted? In fact, it is easy to interpret these episodes as part of the overall adaptive policy process. The experiment, we sup-

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3 Heilmann, Sebastian (2008). "Policy Experimentation in China's Economic Rise," *Studies in Comparative International Development*. Vol. 43, No. 1 (March). Pp. 1-26. Indeed, the attention to context is even more explicit in Heilmann and Perry's anthology, *Mao's Invisible Hand: The Political Foundations of Adaptive Governance in China*. The contributors to this work (Cambridge, Mass: Harvard Contemporary China Series, 2011) identify a "guerilla style" dating back to even before the establishment of the People's Republic.

pose, was abandoned because there might be better ways to achieve the objectives; and since there have been less fertile policy-making periods in the past, perhaps we're merely observing a necessary "fallow" period. A process in which we identify "trial and error" as a key part of success may inhibit us from actually identifying the "error" in outcomes when we see it.

Indeed, consider the difficulties. Once we have discarded the teleological view of China's transition, what standard should we use to evaluate policy-making? It is easy to see the fallacies involved in extreme forms of teleological thinking—"they are reforming so that their political and economic system will become more like that in the advanced capitalist democracies, which is to say, more like ourselves." Statements like that are easy to debunk. However, if we don't have a yardstick with which to evaluate Chinese policy, we are in danger of making the opposite error. When we accept any policy changes as being part of the experimental policy process, no matter where it leads, we lose our ability to evaluate the policy process and, indeed, the political system. No doubt, we hope and expect that China will emerge from this period of super-charged growth with a prosperous economy and with more efficient institutions that will support this prosperity, but nobody knows for sure which of the institutions of developed societies are the most essential. If we don't specify the kind of outcomes we hope to see, we end up in danger of accepting any new policy initiative, or any reformulation of objectives, as being part of the experimental and adaptive policy process.

The above are serious intellectual challenges, and they are made more difficult by the continuous looming presence of the Chinese Communist Party propaganda apparatus. The basic objective of this organization—staffed by hundreds of thousands of intelligent people—is to make the ordinary person believe that the Communist Party is infallible. Of course, no one is foolish enough to actually believe that the Communist Party doesn't make mistakes, but few of us are willing or able to invest the time and intellectual effort to systematically account for the bias created by the "official version." In the CCP's official version, the objective of policy and social transformation is always something vague, and even contradictory: the "socialist market economy" or the "China dream." These objectives cannot really provide benchmarks for assessing policy. Moreover, the reader's attention is always focused on something promising, emerging, about to happen. In fact, virtually everything that government does is presented as a "reform." When things don't work out, issues and initiatives disappear from view with astonishing speed. Redefinition of objectives complements this forgetfulness. We are encouraged to

believe that various half-forgotten initiatives in fact made contributions to the realization of certain vaguely defined objectives. All is well. Nobody has much incentive to dig up the discarded slogans, failed targets, and misguided programs of the past, or to ask whatever happened to the noble objectives and aspirations that were once widely shared and even taken for granted.<sup>4</sup>

The result of these factors, as stated above, is a serious reluctance to impose clear turning points on the Chinese transition process. If the end-point of transition is not known, and if experimentation and reformulation are continuous concomitants of an adaptive policy process, it won't be easy to identify or agree on turning points. To be sure, one can debunk many of the pretensions of the CCP, but doing so doesn't contribute much to understanding the key dynamics of Chinese society. After all, China really has been undergoing unprecedented growth and development for 35 years; living standards really have risen a blistering pace; society has become more diverse and life more free. The "growth miracle" China underwent between 1978 and 2010 has transformed things for the better for the vast majority of Chinese citizens. If we do not seek to debunk this overwhelmingly positive process, but also do not wish to fall into the trap of thinking that all government actions are for the best, we don't have many intellectual choices. Perhaps our best choice is try to identify important turning points in the transition process. This requires that we take a deep breath and select particular features important enough to define individual sub-periods, such that the characteristics of the sub-periods and the associated turning points stand out clearly. It is in this, I think, that Yasheng Huang has made his most important contribution.

### *The Turning Point in 1991-92*

Yasheng Huang's third book is to a large extent a description of the policy turning point around 1991-92.<sup>5</sup> Huang gives narrative drive to this book by drawing a clear and interesting contrast between the 1980s and the 1990s. Huang

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4 In this sense, the flood of information available to the average Chinese is biased in exactly the opposite way that the flood of information available to the average American is. Americans are treated to a constant flow of information about incompetence, policy failures, and faded glory, while Chinese are treated to a constant flow of information about successful policy, problems that are being bravely faced, and glorious times ahead. Of course, we are all too smart to fall for such over-simplifications. These differences contribute mightily to communications failures between the two sides.

5 Yasheng Huang, *Capitalism with Chinese Characteristics: Entrepreneurship and the State*. New York: Cambridge University Press, 2008.

describes the 1980s as a golden age of grass roots, bottom-up, reform. Focusing on rural areas, Huang discusses the strong strain of private entrepreneurship mixed in with the explosive growth of township and village enterprises (TVEs). During the 1980s, according to Huang, economic dynamism and power shifted to the rural areas. By contrast, in Huang's view, the 1990s were the period when power shifted back to urban areas. Larger companies—often state run or with close ties to government actors—were the ultimate beneficiaries of economic policy. Huang underlines this contrast with a striking portrait of business in Shanghai. Shanghai is known to many as the standard-bearer for externally-oriented reform and a welcoming host for foreign investment. Of course, Shanghai is also one of the few Chinese cities with a “brand image” abroad, relating to its highly colorful, international, exotic and corrupt past, particularly in the 1930s. What Huang shows is that these images of Shanghai are at least misleading, and that Shanghai is a city whose economy is dominated by state-owned enterprises (SOEs). Indeed, what is distinctive about Shanghai's SOEs is that most of them are controlled at the local government level. While the SOE systems of many localities simply collapsed during the SOE down-sizing of the 1990s, the better-managed Shanghai SOEs managed to restructure and thrive.<sup>6</sup> There is thus a form of local-government corporate control that is distinctive in Shanghai. This portrayal adds strength to Huang's portrayal, because the institutional changes that took place in the early 1990s—after Huang's turning point—were designed to make large corporations like those in Shanghai more efficient and robust.

Yasheng Huang achieves his fundamental objective, which is to define the crucial parameters upon which he will base his judgment, and then use them to define a turning point between different sub-periods. In Huang's case, the crucial parameters are those having to do with grass-roots entrepreneurship, and the distribution of power between urban and rural, and between large-scale and small-scale. Thus, Huang's definition is clear and his execution is consistent on its own terms. It is only fair to point out, however, that there are alternative parameters that lead to different judgments about the significance and character of the 1991-

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6 A visitor to the Pudong Development Bank in 2014 would see many features that corroborated Huang's account. The bank is owned by Shanghai Municipality, and occupies the lavish premises on the Shanghai Bund that were built by the Hong Kong and Shanghai Bank which had its first headquarters here. The entrance rotunda and mahogany-paneled meeting rooms have all been refurbished. Bank managers made clear their allegiance to the Shanghai city government and their objective to make the Bank the financial centerpiece of a municipal corporate conglomerate.



1992 turning point.

There is no doubt that 1991-92 was an important milestone in China's transition. Even in the official CCP view, Deng's Xiaoping's "Southern Tour" of January 1992 is celebrated as a reform breakthrough. It is less often emphasized that the reason it was such a breakthrough was because die-hard opponents of reform within the CCP had been trying to strangle the newly born reforms before they could grow up, carrying out a politically repressive and economically regressive policy regime in the years after June 4, 1989. Deng's "Southern Tour" shattered this reactionary polity just at the point when it was collapsing of its own weight. What Huang reminds us is not so much that 1991-92 was an important milestone as that it demarcated sub-periods with sharply different features. However, we do not necessarily have to agree with Huang about exactly what those features were or which were most important. Indeed, you might say that there is a touch of nostalgia in Huang's work about the 1980s. In fact, there is a great deal about the 1980s that is attractive, in political terms even more than economic terms. During the 1980s, top leaders of the CCP actually did try to carry out political reforms that would limit the power of the CCP and make the government more independent of the Party and more responsive to citizens. During the 1980s, top leaders of the CCP actually did admit the disastrous mistakes the Party made in earlier years and actively tried to compensate the victims and correct the errors. There is plenty, then, to be nostalgic for in the 1980s in China.

However, from an economist's viewpoint, it is difficult to see the 1980s as superior to the 1990s. The differences are palpable: the 1980s reforms introduced market forces into an economy from which they had been largely banished. With dual-track reforms and partial liberalization, 1980s reforms cracked open the monopoly of the command economy. Incentives were strengthened for SOE managers and government officials alike to contribute to economic growth. Policies were realistic, so that the economy began to grow out of the plan.<sup>7</sup> But the very growth of the economy and the burgeoning of market forces created a whole new set of challenges that needed to be addressed. The 1980s economy functioned without a decent financial system and without macroeconomic policy instruments that functioned efficiently in a market economy.<sup>8</sup> There was no legal code to govern

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7 Barry Naughton, *The Chinese Economy: Transitions and Growth*. Cambridge, Massachusetts: MIT Press, 2007. Chapter 4.

8 Of course, those macroeconomic instruments did function, but through brute force, delivering enforceable credit and investment quotas to local governments. Indeed, this is the convincing argument

corporate organization or intellectual property rights. A secondary “grey market” was the only way that non-state exporters could access foreign exchange. Finally, there was no clear strategy for economic reforms going forward, that would work as the economy became more complex and sophisticated.

One of the remarkable things about the 1991-92 turning point is that it was accompanied by a much more coherent approach to creating the institutions required by a modern market economy. It was an ideological breakthrough when a Communist Party congress accepted the “socialist market economy” in 1992, and there was an even more surprising breakthrough a year later at the “Third Plenum” of that Communist Party congress. The “Fifty Articles” document that came out of the 1993 Plenum was in fact a “blueprint” for further economic reform. It outlined a set of important corporate, fiscal, financial and foreign trade reforms. It is true that there was no sequencing built into the document. Rather it was a set of sector-by-sector initiatives, outlining the most fundamental steps of institutional creation that needed to take place in each sector. Although the institutions in each sector were conceived of as an inter-dependent whole supporting a market economy, the implementation process allowed each to be put in place separately. In other words, the reforms had a *de facto* modular structure. One of the remarkable things about the 1990s sub-period was that the vast majority of the sectoral reforms laid out in the 1993 document were in fact implemented. It is probably fair to say that when the document was issued at the end of 1993, almost no external observers had any confidence that it would be implemented. Assessments of China were at that time still at an all-time low in the wake of the Tiananmen chaos: not only did people have little confidence that the CCP would seriously commit to fundamental economic reforms, they had little confidence in the ability of China’s leaders to carry out the kind of difficult implementation that would be required. In fact, though, one after the other, each of these “modules” was carried out.

We owe the implementation of this series of important reforms primarily to Zhu Rongji, as Vice-Premier (until 1998) and then as Premier (1998-2003). In fact, not only did Zhu carry through most of the reforms outlined in the 1993 “Fifty Articles,” he added two important reforms that were either not envisioned or not articulated in 1993. The first of these was the substantial down-sizing of

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of Yasheng Huang’s first book, *Inflation and Investment Controls in China: The Political Economy of Central-Local Relations during the Reform*. (New York: Cambridge University Press, 1999).

the state sector that took place between 1996 and 2002, in which employment in public sector enterprises was reduced by more than 50%. To be sure, this dramatic step was partly forced on Zhu by the near-bankruptcy of the state sector. But it was carried through boldly and it was made possible in part by the new commercial banking sector that grew out of the reforms described in the 1993 document. The second additional reform was membership in the World Trade Organization (WTO). The crucial concessions for WTO membership were made and agreement reached in 1999, and China actually entered the WTO in December 2001. As the final WTO commitments phased-in during the new century, China emerged with a complete set of market institutions that were sufficiently robust to power another decade of high-speed growth.

Surely, then, it is not appropriate to see the 1990s as a disappointment just because they did not retain the bottom-up and grass roots feel of the 1980s. There is simply too much on the other side of the ledger: the 1990s witnessed an astonishing breakthrough in the process of economic reform and the creation of a set of institutions whose existence we today take for granted. However, it is more important to agree on the timing of the turning points and the main features of sub-periods, than it is to agree on the evaluation of each sub-period. A period in the evolution of an economy, a society, is inevitably a complex combination of positive and negative phenomena. Even as China was growing a vibrant market economy in the 1990s, it was also fostering corruption and increasing inequality. Yasheng Huang directs our attention to other aspects of the complex changes that occurred at that time: a shift in the focus of policy-makers from the country to the city; a shift in the drivers of change from the grass-roots to the technocrats; and a shift of power to large-scale economic organizations. These were not the only changes that defined an important turning points, but they were important aspects of the society that was emerging from those changes. We can acknowledge that different analysts touch different parts of the same elephant, without accusing any of those analysts of being blind.

### *Many Turning Points?*

It is relatively easy to agree that the 1991-1992 period was an important turning point, but more difficult to agree on other important turning points. Indeed, the same intellectual habits that lead analysts to resist the idea of major turning points encourage the view that there are merely cycles of liberalization

and re-control. Political leaders open up, make progress, but then retrench; it's always two steps forward, one step back. Of course, this is a genuine pattern, and one with a long history in the People's Republic of China. There are even standard Chinese names for the phases of relaxation (*fang*) and reconrol (*shou*), implying recurrence that readily takes the form of a cycle. However, most often when outside analysts use this framework, it is a way of organizing the narrative material, not the main story.<sup>9</sup> Cycles of compliance, cycles of decentralization and recentralization constitute an interpretive framework that is the opposite of one of real turning points. Real turning points occur only when the fundamental dynamic of the policy process has been altered, when the structure of power takes on a new form in a new sub-period.

I argue that another turning point occurred around 2002-2004. Of course, this corresponds with the end of the terms of Jiang Zemin and Zhu Rongji's term as Party Secretary and Premier, and their replacement with Hu Jintao and Wen Jiabao respectively. In addition to the expectable changes of style and emphasis as the new administration took over, much more fundamental changes took place around this time, which are evident in both economic policy and political system. In economic policy, market-oriented reforms gradually ground to a standstill. This was not immediately apparent, because an ambitious agenda of reforms had been inherited from the Zhu Rongji administration, and some of these continued to be implemented. For example, the banking system was restructured—writing off bad loans, recapitalizing the banks, and floating them on the stock market—in a perfect example of policy that combined dealing with an important problem (a dangerous overhang of bad debt) in a way that improved the resilience and market orientation of fundamental institutions. This program was designed under Zhu Rongji and executed under Wen Jiabao. But after the bank restructuring, no major market-oriented reforms were implemented in the Wen Jiabao administration.<sup>10</sup> Perhaps it was nothing more than a question of urgency: with the economy booming there was little pressure to carry out radical reforms.

In the political system, the CCP around the turn of the century put into place

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9 Baum, Richard. *Burying Mao: Chinese Politics in the Age of Deng Xiaoping*. Princeton: Princeton University Press, 1994.

10 This is not to say that there were not important policy achievements. Wen Jiabao carried out important expansions of the welfare capacity of the state, improving health insurance, education and urban-rural equity. It was only in the area of market-oriented reforms that the policy achievements dropped off drastically.

a much clearer and broader set of norms and rules than had ever been in place before. As it re-conceptualized itself as a “governing party,” the CCP formalized a set of procedures that had been developing since the 1980s. The crucial step was the institution, at the very top, of term limits and age limits. After a regular process of succession had been created at the top, term and age limits were extended down through the administrative hierarchy. Education credentials were put in place, and continuing education was required of all bureaucrats. Finally, steep incentives were put in place to reward officials who promoted economic growth: both short-term income and career success were tied to economic growth and fiscal performance. These changes created a “more perfect” bureaucracy. They did not create a system with external accountability, still less a democracy. But they subjected officials to an explicit set of requirements and norms that were binding within the Communist Party organization.

These changes have hardly been studied at all. David Shambaugh has written about the recreation of the Communist Party administrative system, but he looks at it as a gradual process with its roots in the twin traumas of Tiananmen and the shock of the collapse of the Soviet Union.<sup>11</sup> I have written a short piece on the ways that the career changes produced a more stable and predictable system overall.<sup>12</sup> There is an uneven and unsatisfying literature on Chinese “meritocracy” that alludes to some of these characteristics.<sup>13</sup> However, these very disparate pieces of analysis don’t even add up to a coherent view on whether there was a significant turning point in the Chinese system in the early 2000s. There is no consensus, not even about how the question should be phrased.

In my view, we start to see very different policy outcomes from the Chinese system after about 2003. From 1978 until the turn of the century, Chinese policy-makers seemed driven by a sense of predicament, a sense that their system was faced with deep flaws that could lead to crisis at any time. The search for solutions, for “escape from predicament,” was palpable. Then, fairly suddenly, in the wake of the economic take-off after Zhu Rongji’s reforms, this sense of predicament faded. The system evinced a new stability, but also much greater inertia. As

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11 Shambaugh, David (2008). *China’s Communist Party: Atrophy and Adaptation*. Washington, D.C.: Woodrow Wilson Center.

12 Naughton, Barry. “Inside and Outside: The modernized hierarchy that runs China,” *Journal of Comparative Economics* (2015), access at <http://dx.doi.org/10.1016/j.jce.2015.12.009>

13 Bell, Daniel (2015). *The China Model: Political Meritocracy and the Limits of Democracy*. Princeton: Princeton University Press.

bold policy outcomes became less frequent, there was more talk about the power of entrenched interest groups. In policy arenas such as financial reform, state enterprise restructuring, or development of the legal system, it became common for insiders to report that change was difficult or impossible because of the influence of unnamed interest groups. The decisive actions of a ruler like Zhu Rongji were sorely missed, and began to seem impossible.<sup>14</sup>

Was this a turning point? If so, how do we explain it? For many years, I was fortunate to have an office that was next door to that of Peter Gourevitch, the eminent political scientist. One of Peter's dictums—I later realized it is actually the opening line of his classic work *Politics in Hard Times*—was “behind policy there is always politics.” He would frequently ask questions based on this principle. Now, I can hear him in an imaginary dialogue asking, “what do you think the politics is behind this shift in policy outcomes?” Personally, I cannot hope to answer this question with the information and analytic tools I have at my disposal today, but I think that defining and addressing this question should be at the top of our research agenda on China.

The discussion in the last few paragraphs has in fact led me to a series of questions that I hope will be part of Yasheng Huang's research agenda in the next few years. Following the turning point in reforms in 1991-92, can we document a further shift in the agenda after the turn of the century? In the book *Capitalism with Chinese Characteristics*, it frequently seems that the shift in economic agenda is driven by the formation of large corporate interest groups, combining political elites with new corporate businesses: was the 1990s period described there in fact just the first stage of a new system in formation? Has a new stage of development been reached in which enormous economic interests alter nearly everything about China's developmental transition? Where are the next twists and turns likely to take us? We can only hope that Yasheng Huang's future work will shed light on these questions.

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14 The great exception, of course, was the Chinese stimulus response to the Global Financial Crisis. The Chinese regime once again perceived an external threat of enormous magnitude, and the resulting sense of crisis galvanized the leadership into action. But in retrospect, this action also led us to greatly over-estimate the ability of the system for disciplined or decisive action. The system was able to massively expand credit in the face of crisis, but in the seven years since it has not been able to re-impose discipline on the process of credit creation.

## *Conclusion*

China today, in 2016, is once again facing a profound turning point. Once again, this turning point is both political and economic. On the political side, Xi Jinping seems determined to move away from the predictable, somewhat depoliticized, collective leadership of the Hu Jintao era. It is not clear what Xi's ultimate vision is, but it certainly involves more personal power for himself, more political control over individual thought and expression, and more "meaning" infused into the ideological tenets of the Communist Party. In a sense, Xi's approach to governance can be seen as a confirmation that there was a turning point in China after 2003, because Xi seems to repudiate virtually all of the political trends and tendencies of that era. Xi behaves as though the Chinese system had become increasingly stuck, incapable of bold and decisive action, in the previous decade. He makes war on corruption, but also seeks an ideological rejuvenation, as if these initiatives would bring an increasingly sclerotic and disillusioned system back to life.

Xi seeks to combine this political revivalism with a renewed commitment to economic reform. It is almost impossible for us outsiders to see how this makes sense, and perhaps it simply doesn't, but there is still a body of opinion that believes that Xi will turn out to be an economic reformer once he has cleaned out the stables and established a more capable and authoritative leadership. Whatever one thinks of this view—and evidence for it is fading—it is unlikely that the current turning point will be decided by politics alone. One of the most distinctive features of the current turning point is how unmistakably it combines political and economic shifts.

Around 2010, China rather suddenly reached the end of its miracle growth era. A set of demographic and labor force changes occurred at unusual speed. The surplus of labor in the countryside that fueled massive rural-to-urban migration in the first decade of the century was drawn with surprising speed, leading both to rapidly rising wages for unskilled workers and (despite that) a sharp slow-down in the overall pace of rural-urban migration after 2010. Just as this was happening the overall (urban plus rural) labor force suddenly stopped growing, because of the delayed impact of the "one child policy" on the young population. Both these changes are familiar from earlier experiences in Japan and Korea, but in those cases these two labor force changes had occurred at different types separated by decades. China as a whole has stepped into middle class status with incredible speed.

Usually, we expect to find that countries becoming middle class adopt a more relaxed political atmosphere (and sometimes even democratize). Governments become less intrusive and their interventions in the economy “lighter touch.” China seems to be precisely at such a point today, but Xi Jinping is certainly not taking China in a more relaxed and lighter touch direction. Instead, he seems to think that ideological revitalization will fill a gap, providing a sense of purpose he finds missing in today’s China.

Where will this turn take China? It is impossible to say. Clearly Xi’s new era challenges all the established wisdom on China, and all the established wisdom on what happens in the modernization process. This doesn’t look like a pragmatic, adaptive government shaping itself to a more comfortable, diverse and open-minded society. We will need all the tools at our disposal to understand this new, new China. Yasheng Huang has both given us new tools and shown himself a skilled practitioner, and now we must wait and see: How will our perceptions of this new turning point be turned around by Yasheng Huang’s next contribution?



# The Values of Entrepreneurship in Early Modern China

**S.E. Kile<sup>1</sup>**

## *Introduction*

In his 2008 monograph, *Capitalism with Chinese Characteristics*, Yasheng Huang takes a fresh approach to the question of what factors have contributed to the rapid growth of the Chinese economy since 1978, following Deng Xiaoping's economic reforms. Huang demonstrates that although GDP growth in the 1990s was numerically quite similar to that of the 1980s, that growth resulted from very different impetuses: rural entrepreneurship in the 1980s and a shift to state-led development in the 1990s. The discrepancy between these paths to a rapidly growing economy, he argues, has "substantial and real welfare consequences" (Huang 2008, xvii) including more effective poverty reduction, less income disparity, less illiteracy, and more widespread government services during the earlier period when growth was driven by rural entrepreneurship. Huang's account proves that rural entrepreneurship is a more desirable, and more ethical, method of driving economic growth than a state-directed model because it does much more to improve the quality of life – the welfare – of the people. This essay situates some of the concerns motivating Huang's analysis in historical context to demonstrate how our understanding of entrepreneurial values in China today might be deepened through an analysis of entrepreneurship in China before the nineteenth century.

I have approached the problem of the value and values of entrepreneurship from the field of literary studies. I work on the early Qing period (1640s-1670s), which predates the two decades of Huang's study by just over three hundred years.

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Despite differences in discipline and period, I nevertheless share Huang's interest in exploring the functions and ethics of entrepreneurship in a Chinese context. In this essay, I draw some connections between the key terms and concepts used to analyze entrepreneurship at disparate moments in the development of the modern Chinese world. I introduce the entrepreneurship of the seventeenth-century maverick literatus, Li Yu (1611-1680) and bring it into conversation with work on entrepreneurship in the later Qing and the modern period. I use this comparative analysis to broaden our understanding of categories frequently asserted in both contexts – such foundational terms as “Chinese,” “entrepreneurship,” and “welfare.” I conclude by commenting on what can be gained by historicizing these terms and the values associated with them.

### *Entrepreneurship with Chinese Characteristics?*

What is “Chinese” about entrepreneurship in China, and how has it changed over time? In the 1980s, economists began to address the first of these questions under the auspices of comparative social science, marking a significant break from simply considering business practices in China and other places to be belated or underdeveloped relative to the West (Greenfield and Strickon 1981, 469; Redding 1991, 152). Entrepreneurship itself had been understood since the influential work of Joseph A. Schumpeter to be the driving force of development. Schumpeter described the role of entrepreneurship in spurning development in this way: “the creation of new combinations of materials and forces that disturb previous equilibrium states and result in new ones that on a priori grounds are assumed to be better” (Greenfield and Strickon 1981, 469).

What is notable about Schumpeter's theory of development is his focus on the critical role of the individual in driving a society ahead, from equilibrium to equilibrium (Greenfield and Strickon 1981, 468). Comparative studies beginning in the 1980s broke with this model, allowing for the possibility of multiple paths to development and modernity, refusing to begin from the assumption, following Max Weber, that a particular cultural model was superior to others. One such study posited, for example, the possibility of “a non-individualistic version of capitalist modernity” and questioned the inevitability of the “linkage between modernity, capitalism, and individualism” that had previously been assumed (Berger 1988, 6; Redding 1991, 138). Another concluded that Japanese, Korean, and overseas Chinese can be considered together to elucidate an “East Asian develop-

ment model” that constitutes a “movement toward modernity [that] has not been accompanied ... by a noticeable rise in individualism” (Redding 1991, 152).

Comparative studies like these consider entrepreneurship in China largely on its own terms, but the comparative method ultimately remains committed to drawing connections and contrasts between different cultures or systems, comparisons that are accompanied by familiar value judgements. In the study just referenced, for example, the author concludes that Weber’s assumption that “a moral base in religious values is a necessary precondition for the legitimizing and encouraging of entrepreneurship” (Redding 1991, 152) – a moral base he locates in a general adherence to a “secular Confucianism” that promotes widespread paternalism across Asia. While no English-language study of entrepreneurship in China can entirely avoid comparisons with the West, a study that compares the values of entrepreneurship across time in China rather than across modern nation states will look for different kinds of similarities.

A comparative study of entrepreneurship in China that includes the early modern period, when the word itself did not yet exist, must first define the term and its scope. Only in this way will it be able to address the second question with which I opened this section – that of how Chinese entrepreneurship has changed over time. The term “entrepreneurship” can refer to a range of different practices and qualities, which become even more complex when we consider how we might broaden the scope of the term to include historical examples. Let us begin with a modern definition posited by Yasheng Huang. He has noted that “a universally accepted definition of entrepreneurship is self-employment business. Self-employment businesses are single proprietorships, and in China they are formally known as individual businesses (*geti hu*) or individual economy entities (*geti jingji*) in the Chinese statistical reporting system” (Huang 2008, 58). This contemporary understanding of entrepreneurship insists that, most fundamentally, it is about undertaking business activities in such a way that an individual proprietor can exert significant control over the direction of the business. *Geti hu* signifies a very particular modern category of business entity that is by definition contrasted to other types of business entities in the same period, such as state-owned or collective enterprises. While *geti hu* has occasionally been used as an analytical category to analyze business in the Qing dynasty, it does not offer a sufficiently robust definition of entrepreneurship to justify using it as a category for comparative historical analysis.

In recent years, historians have begun to theorize entrepreneurship in Chi-

na in ways that explicitly contest its purported relationship to capitalism and Western influence. As such, they are faced with the challenge of articulating a definition of entrepreneurship in the absence of an obvious contemporary category from the period under consideration. Two recent studies offer particularly promising methodological strategies for dealing with this thorny issue: Madeleine Zelin's *Merchants of Zigong: Industrial Entrepreneurship in Early Modern China* (Zelin 2005) and the collected essays in *The Business of Culture: Cultural Entrepreneurs in China and Southeast Asia 1900-1965* (Rea and Volland 2014). Each seeks, through different methodologies and objects, to revise historical narratives that propose that the lack of development of modern institutions like modern legal or banking systems precluded economic development and creative enterprise in imperial China. Zelin's study of the salt industry in Zigong, Sichuan during the late Qing and early Republican period demonstrates that merchant-entrepreneurs succeeded in developing and regulating a large-scale industry in advance of the adoption of foreign institutions and practices in China. Rea and Volland's edited volume proposes entrepreneurship as a conceptual category that encapsulates in a more robust fashion the range of cultural work undertaken by individuals and institutions for profit from the late nineteenth through the first half of the twentieth century.

In both of these English-language studies, the term "entrepreneurship" is used to theorize a relationship between individuals, institutions, and the market in a way that is distinctive to the particular historical circumstances of this period of Chinese history. Zelin characterizes entrepreneurship as a "willingness to take risks, make long-term investments, and exercise entrepreneurship in seeking new markets, new sources of capital, new technologies, and new forms of business organization" (Zelin 2005, 185). Her study suggests that Zigong's remote location in Sichuan allowed entrepreneurs to develop their industry largely without interference from the state until the final decades of the Qing dynasty (1870s-1900s), when enhanced imperial control finally made it impossible for the private businesses to continue flourishing as they had from the founding of the dynasty until then (Zelin 2005, 2-3). This conclusion resonates with Yasheng Huang's claim that private entrepreneurship is better for welfare.

Rea and Volland propose that a convergence of historical circumstances during the very late Qing dynasty and the first half of the twentieth century encouraged cultural entrepreneurship to an unprecedented and unsurpassed extent (Rea and Volland 2014). In Rea's contribution to the volume, he proposes "cultural entre-

preneurship' as an analytical concept for explaining a particular form of cultural agency that arose in early twentieth-century Asia: a pluralistic approach to the art and business of culture characterized by active participation in multiple modes of cultural production. . . . It is entrepreneurial because it involves the investment of both talent and capital in new enterprises. . . . [new forms of technologies] also encouraged experimentation with a variety of media and genres" (Rea 2014, 10). He proffers technological advances, changes in the political sphere, and the abolition of the examination system as key reasons that this historical moment produced such prolific and creative entrepreneurship.

Both of these studies characterize entrepreneurial behavior in similar ways: a willingness to embrace the uncertainties of risk, to invest in – or create – new markets for their products, to exploit new technologies for profit, and to experiment with new business models or new combinations of established occupations. The combination of these behaviors that we have come to understand as entrepreneurship can be found in the early modern period as well, as my research demonstrates. Identifying this set of qualities and practices makes possible a comparative analysis of how entrepreneurship was perceived in the early modern period, what sorts of change it effected, and what impact it had on social welfare. In short, I look at the values and effects of entrepreneurship in China as it was practiced before self-conscious modernization or significant Western influence.

I contend that a consideration of China's capitalist or socialist particularities, often epitomized in a phrase like "socialism with Chinese characteristics," is better understood through a method that embraces Chinese history. "Chinese characteristics" signifies not only a deviation from Western expectations, but also the persistence, preservation, and expansion of Chinese practices from earlier periods, practices that have a fraught and historically specific relationship to Confucianism. A case study from the Ming-Qing transition will allow for a preliminary exploration of the values and effects of the particular amalgam of characteristics and practices we have come to associate with entrepreneurship. At a time when it seems particularly urgent to nurture entrepreneurship in rural China, we might remember that longstanding Chinese traditions of entrepreneurship far exceed the attention they are usually given in contemporary discourse.

### *Early Modern Entrepreneurship?*

The Confucian division of men into the hierarchical social categories of literati

(*shi*), peasants (*nong*), artisans (*gong*), and merchants (*shang*), which relegated those involved in trade to the lowest ranks of social life, persisted as an ideal throughout the dynastic period, despite significant social and economic changes. From the middle of the Ming dynasty, a commercial boom made merchants wealthier, even as it became increasingly difficult for scholars to obtain an official position in the bureaucracy (Ho 1962; Elman 2000). With the old roles shifting beneath them, many men found themselves occupying positions that were neither literatus nor merchant. It became possible for merchants to purchase official positions, even as great numbers of scholars gave up pursuing success in the examinations to take up trade (Brook 1999). Many of the most famous cultural figures from this period – such as author/publisher Feng Menglong and painter/writer Chen Jiru – supported themselves by selling their works (Greenbaum 2007). Such a blurring of distinctions between merchants and literati poses a significant challenge to the historian because it was elided in most contemporary accounts of social practice: intellectual exchange was not only consistently valorized as superior to mercantile exchange, but monetary or in kind compensation for intellectual labor often went unmentioned as well (Clunas 1991; Cahill 1994; Hay 2001; Chow 2007).

The fraught intersection between the subject position of the literatus and that of the merchant offers the historian a rich trove of material through which to explore the values of entrepreneurship in the early modern period. Faced with supporting themselves financially, many educated men became entrepreneurs, undertaking risky profit-producing business ventures. They explored new markets—Feng Menglong, for example, created a brand-new market for the vernacular short story—and they diversified the range of profitable activities they engaged in, from writing fiction, plays, joke books, and essays, to producing painting manuals, albums of paintings, and exclusive illustrated editions. Despite the fact that they were making a living selling books, investing capital into developing new kinds of books, and building up brand names that would increase sales of those books, these men did not consider themselves merchants. At the same time, merchants engaged in more traditional sorts of trade, and especially those trading in salt, found that wealth could buy them social distinction more readily than it had before. As a result, merchants began to participate enthusiastically in, and even contribute to, literati culture, even as literati began, furtively and in denial, to undertake the activities of the merchant and trader class (Wu 2012).

The analytic category that has been most often used to characterize these hybrid figures is “scholar-merchant” (*shishang*). As Cynthia Brokaw has described

in her study of Sibao book merchants, these *shishang* are individuals who “insisted that they were a special kind of merchant... devoted not just to the petty search for profit, but to the spread of learning” (Brokaw 1996, 64). The figure of the *shishang*, produced in the urban milieu of the mid- to late Ming, effectively collapses the two poles of the Confucian social hierarchy into a single social role. Kai-wing Chow has reconstructed the processes, costs, and profits associated with this group – especially their involvement with the publishing industry – in the late Ming period from a very slim archive (Chow 2007). In doing so, he has been able to uncover the economic realities underlying relationships that *shishang* took great pains to bury.

Exposing the literati’s disavowed profit-seeking in their literary and publishing endeavors is a worthy project, but it does not necessarily differentiate innovative, creative, or risky – in a word, entrepreneurial – endeavors from more commonplace ways for literati to turn a profit (by, say, writing epitaphs or prefaces, or selling paintings). It may very well be the case that the more entrepreneurial literati (or *shishang*) were more willing to talk about their aim to profit through the sale of cultural products, but it is not a given. The distinction I am interested in here is not between those literati who would admit to selling their writing and those who wouldn’t, but between those who found creative ways to develop and expand their products, who took risks, and who sought out new markets, and those who did not, regardless of whether they were explicit about seeking remuneration. Not all salesmen, after all, can be described as entrepreneurial.

In order to fully extricate entrepreneurship from a larger context of early modern market-focused behaviors, I focus on the practice of entrepreneurship, rather than on the figure of the entrepreneur or the *shishang*. In focusing on entrepreneurship as a behavior rather than as a type of person, I follow Keming Yang, who, in his study of entrepreneurship in China, has suggested that entrepreneurship should be conceived of as a behavior, or an activity, which is a temporary, passing quality rather than a particular type of social actor (Yang 2012, 8). In this theorization we can see that, as my research demonstrates, literati were frequently entrepreneurial, more or less discreetly seeking out market-based profit as it became more difficult to earn an official position in the late Ming, and even more so during the turbulent dynastic transition that followed. This was true leading up to and during the seventeenth century, and it became pronounced again as the twentieth century approached.

In asserting this model of historical continuity – of a long and rich history

and culture of Chinese entrepreneurship – I am also arguing that “capitalism with Chinese characteristics” has its own complex line of evolution. Rather than consider the transition from the dynastic Qing to the Republican nation-state as marking a break between the traditional past and the modern present, and relegating the literatus of the past to be generalized, even with caveats, as one who “disdained commerce and concerned himself exclusively with aesthetic and moral matters” (Rea 2014, 11), we should allow that any number of particular historical circumstances have paved the way for entrepreneurship to become a widespread practice in China today. By acknowledging the variety of histories of entrepreneurship within cultural constraints, this approach shows how China at different historical moments made space for individual creativity, and when and how it became possible for that creativity to be profitable.

*Li Yu's Cultural Production:  
A Case Study of an Early Modern Entrepreneur*

I focus in what follows on a case study of a highly educated, risk-embracing, and very profitable seventeenth-century figure known as Li Yu. Born into a family of doctors and pharmaceutical vendors who had settled in Rugao, Jiangsu, Li Yu distinguished himself from a young age through his aptitude for study. His education was to eventually lead to an official position. Despite early recognition by regional officials, Li Yu was not initially successful in the examinations, and when the Ming dynasty fell in 1644, he was approaching his mid-thirties without an official position.

The dynastic transition of that decade caused massive upheavals across China: many of the political and cultural authorities of the Ming were killed, took their own lives, or went into reclusion as loyalists (*yimin*) to the Ming, refusing to serve under the Qing. Those who did serve under the Qing often sought to sponsor loyalist projects in an effort to share in the remembrance of the Ming. Urban hubs throughout the Yangzi River delta experienced major upheaval, and the near total elimination of existing cultural authorities and increased literati mobility generated an unprecedented quantity of profitable experiments of people improvising to survive (Meyer-Fong 2003, 102). In their business engagements, these men practiced strategies of distinction in which reliance on the market was usually paired with disdain for the uncultured.

In the midst of this crisis, Li Yu gave up the traditional pursuit of success



through the examination system and embarked on a career as a writer of fiction and plays in the bustling city of Hangzhou. His fiction abounds in clever plot construction and bawdy humor; his plays are raucous, farcical, and, above all, entertaining. Innovation (*xin*) is the defining feature of Li Yu's literary production, and it was through these stories and plays that he first gained fame (and financial security) across the new empire (Hanan 1988).

Over the thirty years of his career, Li Yu made a brand of his name, and he used that brand to market a diverse array of cultural products. He engaged in experimental cultural production at the intersection of the market, aesthetics, and technology in a practice I propose is best characterized as entrepreneurial. He combined a pursuit of innovation with the production of easily reproducible designs, and the resulting cultural production presents a compelling model for thinking about entrepreneurship in the pre-industrial world.

Just how was his work entrepreneurial? First, he constantly sought to diversify and innovate. During the 1650s, he published on average one new play or short story collection per year. From 1660, he shifted his focus to collections of letters, court cases, and regulated verse that included writing solicited from dozens of cultural figures throughout the empire. Near the end of his life, he wrote *Leisure Notes* (*Xianqing ouji*, 1671), a collection of essays full of designs and suggestions that promised to make the reader's everyday life extraordinary, without significant expenditure. One essay teaches readers how to install a pulley system to rig stage lighting; another describes a design for retractable eaves that allow one to enjoy a garden, rain or shine. In genre, subject matter, and tone alike, Li Yu pushed the limits of what was considered acceptable writing for educated men of his day.

Li Yu's work is also entrepreneurial for the creativity and flexibility with which he embraced market-oriented cultural production. Unlike many of his fellow literati who might quietly receive remuneration for standard literary products like prefaces or calligraphy-adorned fans, Li Yu exploited the more obviously commercially oriented publishing business. He printed books at his garden residence in Nanjing where he marketed and sold books and stationery. He also undertook a range of non-literary commercial ventures such as designing gardens and directing a theater troupe that he toured to the homes of wealthy patrons. Garden designers and actors were still very lowly social positions, even though a few aficionados had become famous for their association with them.

The most distinctively entrepreneurial aspect of Li Yu's work is his experimentation with writing and print as technologies. Li Yu stands out among his compa-

triotis for the sheer range of products he developed, but he nevertheless maintains and even extends earlier types of social hierarchy by producing and enforcing new modes of consumption. He experimented with the ability of writing and print to transport new kinds of cultural products to a broader reading public, and in doing so, he generated cultural objects that blur the boundaries between production and consumption. Instead of approaching a purchaser as a pure consumer, many of Li Yu's cultural products encouraged interactivity and personalization, demanding, for example, that you stop reading to go and paper your walls. It's hard to get lost in a novel when Li Yu's narrator is constantly interrupting you, just as it's hard to live in a study with bare walls after you've read about Li Yu's design for crackle-glazed wallpaper that will make you feel as if you're living inside a teapot. In this way, he invited consumers to share the burden of the production of culture, even while the final product retained his brand name.

*Both Technologically Reproducible and Singular:  
Who Owns a "Li Yu" Fan Painting?*

To illustrate this point, I will present just one of the innovative products Li Yu developed at the intersection of innovation and technological reproducibility: his solution to the problem of how to make a technologically reproducible painting that nevertheless retains something of the uniqueness of a fan painting produced on commission for a customer (or friend) that boasts the traces of the artist's brush. The problem Li Yu aimed to solve in this case was how to make a reproducible fan painting that is not simply a *picture* of a fan painting.

For a writer or a painter in the preindustrial patronage system of the early Qing, fame came with incessant demands for new products. Li Yu had given much thought to what it would be like to make a living selling traces of one's brush. His 1653 play, *Ideal Love-Matches* (*Yizhong yuan*) depicts two pairs of well-known late-Ming poet-painter-calligraphers: cultural giants Dong Qichang (1555-1636) and Chen Jiru (1558-1639). The play opens with Dong and Chen complaining about the burden of requests for their works; they plan to spend the day in disguise so that potential customers will not approach them. Instead of refusing buyers, however, the painters of Li Yu's play embrace falsehood in advertising: they each end up marrying a woman who forges their paintings for a living, thus doubling the production capacity for their brands.

But "doubling" was not a sufficient scale for Li Yu. He focused on woodblock

printing, whose simpler technological reproducibility ensured faster production. He reconceptualized print, forging a new path as a designer who made easily reproducible books work in new ways. Whereas connoisseurship manuals had long profited by commodifying knowledge about the proper consumption of luxury goods, Li Yu's essay collection, *Leisure Notes*, is full of reproducible designs that commodify everyday life, as well as new valuations of old luxury goods, like paintings, bronzes, and tea. In his play, *Ideal Love-Matches*, accomplished artists suffer in their dealings with uncouth customers, even as they profit from them.

Li Yu resolves this inconvenience by marketing unique "Li Yu fan paintings" for each reader that could be distributed without extra effort or individualized attention on his part. Instead, the reader makes the painting based on instructions for its design in his purchased copy of *Leisure Notes*. In one of the essays included in that text, Li Yu suggests that readers carve a window shaped like a fan into the wall of a boat, and then completely seal every other opening, so that light can only enter through the fan-shaped window opening. Li Yu's fan-shaped window offers two fan paintings in one: Those on the boat enjoy a scenic landscape painting, while anyone walking along the shore would see a fan painting depicting a lively party. Even at home, he suggests, one can capture a scene in a similar fashion, using old branches, or rocks, or birds to create a diorama on a board outside a window.

With this "fan painting," Li Yu solves the problem of authenticity – he is the designer, but readers capture the view – and the problem of labor – performed by readers per his instructions in the easily reproduced woodblock printed book they have purchased – mobilizing a brand name in new ways and using it to claim technical designs that have yet to be realized. He uses the old technologies of writing and print to produce, reproduce, and profit from such designs, many of which he never saw constructed. This essay, combined with each reader's paper, glue, labor, and time, produces an original "Li Yu fan painting."

With designs like this one, marked with his brand name, Li Yu borrowed readers' labor to commodify their everyday lives as he saw fit: from objects, like chairs or drawers, to such mundane activities as sweeping or even walking. This particular combination of innovation and technological reproducibility makes print work in new ways: it offers a personalized, tailored, and interactive experience, by requiring readers to provide their own resources – materials and labor, alike – to make their own "Li Yu original." In this way, Li Yu used books to spread his brand name throughout the empire, attaching it to windows, incense tamperers,

theatrical performances, and even beds, all without ever encountering those material objects.

Li Yu gained a wider clientele, and required less financial support from each client, than he would have as a painter or calligrapher: by forming a peculiar hybrid of writing and design, his works could be mechanically reproduced by his servants and widely disseminated at an urban point of sale. But in order for him to profit, he needed to find a way to convince readers that he had rights to each copy of those easily reproduced records of his designs – his books. Li Yu's books were reproduced without authorization – that is, pirated – as early as the 1650s, but his most interesting statement about his sole right to produce copies of his books appears in an essay on stationery in *Leisure Notes*.

Permission is granted to copy all the new designs in this book except the stationery designs, which I get my servants to manufacture and sell as an alternative to making a living by my brush. These may not be reprinted. (Li Yu 1992, 3.229; adapted from translation in Hanan 1988, 14)

Stationery, for which he also offers several novel designs, is the only design in *Leisure Notes* that can be easily reproduced on a mass scale. Concerned for his livelihood, Li Yu declares:

As for those who reprint my books in the belief that their wealth and power will protect them, [...] they are living off my labor, and that is a situation I cannot tolerate. I swear that I will fight them to the death, and hereby give notice to the authorities that this book marks a new policy on my part. [...] Heaven and Earth endowed every person with a mind and it is up to each of us to develop our intelligence. I have done nothing to stultify their minds or prevent them from developing their intelligence. What right do they have to take away my livelihood and prevent me from living off my own labor? (Li Yu 1992, 3.229; adapted from translation in Hanan 1988, 14–15)

Here, Li Yu argues fervently against the unauthorized reproduction of his books and stationery precisely because he knows that consumers lose nothing when they purchase a pirated edition of these technologically reproducible products. Li Yu's printed books and his stationery have always been copies, and their popularity and lack of any authentic traces of a brush, seem bound to invite further copying.

According to Stephen Owen, the literati practice of claiming that “a singular style or a text that memorably represents an experience or a place” is a “more secure” form of “ownership” than actual possession of land dates to the mid-Tang (Owen 1996, 31–33). Li Yu has fully embraced this notion, using his style and writing to claim “ownership” over a broad range of things, not only places he has visited or objects he owns, but things he has never seen, things that belong to every one of his readers. Li Yu’s vociferousness regarding his rights to his designs and written works draws on this literati practice of using language to claim moral and spiritual ownership of land – in the absence of, and as superior to, financial ownership. Because Li Yu, unlike these earlier literati, also depends on the profits from his cultural production to survive, he finds a way to inscribe economic value within this conception of textual, or “spiritual,” ownership, insisting that money should be spent only to acquire what is actually valuable: that which is as far from the materiality of the objects in question or their actual owners as possible. Readers pay for their fan paintings, after all, by giving up their right to claim ownership of them.

### *Conclusion*

By way of conclusion, I would like to return to the question with which I opened: What can be gained through historical contextualization of entrepreneurship in China today? In order to address this question, I have also explored the broader question of when, and why entrepreneurship happens, and how it changes social relations.

In Li Yu’s case, the impetus for entrepreneurship is very clearly the dynastic transition. Without political, social, and economic upheaval, Li Yu’s career would doubtless have turned out differently. The disappearance of cultural giants from the major cities of Jiangnan, the loss of faith in the ruling family, the lack of desire to continue to pursue success in the examination, and the very physical uprootedness that many educated young men experienced in this period combined to make possible the serious pursuit of a different sort of path. These new paths that opened for a few decades in the early Qing dynasty were characterized by the pursuit of broad commercial success through the diversification of production and continual expansion of the consumer base. As I have shown, many men at this time opted to remain on a more traditional path, but Li Yu’s ambitions were too great for a profession in decline.

In branding himself, Li Yu inflated his ego to an almost unprecedented degree. He constantly praised himself, his ideas, his writing ability, and his creativity in writing. Patrick Hanan has argued that this is a “persona” that Li Yu created to sell his books (Hanan 1988), but it might also be interpreted as the personality, or set of traits – restlessness, creativity, curiosity – that led him to pursue an entrepreneurial path. Prior to the fall of the Ming, these personality traits had very little chance to be developed as Li Yu was bound to the traditional Confucian education regimen and path to official success.

How does entrepreneurship change social relations? In this case, Li Yu challenged many of the foundational moral principles according to which Confucian-educated men understood themselves. Although he certainly had detractors in his day, he found creative ways to present compelling alternatives to a range of long-held beliefs. He was committed to considering all sorts of situations and things from multiple perspectives, pointing out those aspects that others had missed by relying on common sense or received wisdom. If we consider the effects of Li Yu’s work over the course of the Qing, it cannot be argued that he revolutionized Confucian thought or social relations. In fact, as the Qing rulers solidified their control over the empire and educated men got back to the business of ruling, there was not social or cultural space for the sort of entrepreneurial activity that made Li Yu famous and (at least a little) rich.

In addition to challenging the moral values of the Confucian educated, Li Yu also sought to broaden the scope of his readership, expanding the realm of the literate and the literary to include a larger group than had previously been included. Li Yu sought to accommodate a broader public comprised of a multiplicity of readers who come to his texts with disparate levels of education and divergent desires. Through careful observation of early Qing society, Li Yu sought to welcome and cater to both erudite scholars and less educated readers. In this way, his works differ from most of those written by other literati (*wenren*) – a category usually rendered in English as “scholars,” “literati,” or “intellectuals.” As outlined above, in this period educated men asserted their identities as intellectuals in order to distinguish themselves from merchants and artisans, regardless of whether they had attained an official position or were engaged in the same for-profit activities as those from whom they sought to distinguish themselves. Li Yu’s extensive classical education made him unmistakably part of this group of intellectuals, but he never passed the examinations or held an official position, using his intellect instead to make a living marketing his entertaining books and plays to a range of people that

included women, merchants, artisans, and others.

Our final lesson from entrepreneurship in early modern China lies precisely in this capacity for entrepreneurial activity to break down social barriers and bring previously excluded groups into the dominant cultural sphere. One of Li Yu's key – and most controversial – interventions was his willingness to challenge the elitism of the literary world. In *Leisure Notes*, Li Yu deflates the prestigious category of “*wenren*” by subjecting it to a literal interpretation. Noting that *wenren* means “literary people,” he claims that rather than include “just those scholar-officials or gentry (*caishi*), anyone who can recognize characters (*shizi*) should be included in the group” (Li Yu 1992, 3.351; see Hanan 1988, 199). In another essay, on the importance of teaching women to read, he calls literacy “the key that unlocks every door,” and suggests, somewhat radically, that it has the potential to benefit everyone: men and women, young and old alike (Li Yu 1992, 3.143). The proposal here is provocative: in his understanding of literature and language, Li Yu's interest in marketing his own writing results in a veritably democratic proposal for universal literacy. In seeking profit, this early modern entrepreneur ended up promoting inclusiveness. Perhaps entrepreneurship “with Chinese characteristics” can and still does draw on this vision of the entrepreneurial role.

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# Divine Entrepreneurs: Buying and Selling (the Same Thing, Over and Over) on China's Southern Sacred Mountain

**Robert André LaFleur<sup>1</sup>**

## *I*

### *Entrepreneurial Worlds*

#### *Flowing Trade*

Consider one of the most significant works of art in all of Chinese history. It is called the Qingming scroll [清明上河圖], and has remained an iconic representation of flowing commerce and commercial activity in China for the last thousand years. Inch-by-inch the scroll unfurls to show a powerfully flowing commerce in eleventh century China—carts laden with goods, boats filled with products heading to market, and everywhere a teeming concatenation of people coming together to buy, sell, haggle, and, in time, disperse. The *Qingming* scroll and its representations of commercial sociality underlines a point that is largely uncontested among Chinese historians—China is, and has always been, a society of entrepreneurs.

Goods have always been flowing; merchants have always been strategizing. And they have been doing it all over (and well beyond) the territory that today we call “China.” From the Silk Road to the local and regional markets dotting both

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the Chinese countryside and urban centers, China's markets have always been filled with a plethora of goods that have flowed from, as the old saying goes, "the four quarters of the realm." Consider this description of mercantile activities in a sixteenth century north China gazetteer.

The merchants who transport commodities within Hejian prefecture deal in silk fabrics, grain, salt, iron, and wood. Silk merchants come from Nanjing, Suzhou, and Linqing. Grain merchants travel the imperial thoroughfare from Weihui and Cizhou and go as far as the region along the river at Tianjin, buying up grain when the harvest is good and selling it when the harvest is poor. Iron mongers deal mostly in agricultural implements, coming here in small carts from Linqing and Botou. The salt merchants come from Cangzhou and Tianjin, the wood merchants from Zhending. Those who sell porcelain and lacquerware come from Raozhou and Huizhou. As for local merchants, most come from the prefectures and counties north of the Yellow River: they are known as "shop households."<sup>2</sup>

From river waters filled with boats to mountainside markets, a complex series of markets have dominated Chinese social and economic life for well over a millennium. The range of enterprises is staggering, and some of the most fascinating entrepreneurial activities can be seen in what people buy and sell in the pursuit of an emotional satisfaction that is part "religious," part "economic"—and always profoundly *social*—what I call the "microeconomics of sacrality." How do religious pilgrims make purchases "around" religious actions? And how do entrepreneurs provide materials (not to mention information) they will need in their journeys? The questions combine ethnography, history, literary study, sociology, psychology, and economics.

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2 Timothy Brooks, *The Confusions of Pleasure: Commerce and Culture in Ming China* (Berkeley: University of California Press, 1998), 117-118.

## II *Mountain Worlds*

### *Five Peaks*

About a decade ago, I began what was at first intended to be a modest examination of the eastern sacred mountain in China—the iconic Mt. Tai, or Taishan [泰山]. In the autumn of 2006, I spent a week on Mt. Tai, and began to ponder its central locations, especially the base temple in the city of Taian and the many-acre “peak” 1,500 meters above sea level. I joined thousands of tourists who made their ways up the mountain employing a wide array of transportation possibilities. Some hiked, others took buses to the midway point and hiked from there, and a few just took the bus and the cable cars all of the way, skipping past almost every temple between base and peak.

A hundred years ago, travelers had fewer choices—among them, to walk on foot or be carried up in a sedan chair. And travelers, from emperors and poets to everyday people, have congregated on the mountains for many centuries. Confucius climbed Mt. Tai 2,500 years ago. Reaching a level only 200 meters above the mountain base, he was said to exclaim that, even from that relatively low position, his home state of Lu seemed small. Reaching the summit, Confucius’s humility was even greater. From there, all of the world [天下] seemed small. Only “a mile” into the heavens, the mighty intellect of the great sage had met its match on the peak of a local mountain.

Over the centuries, Mt. Tai and the other four “sacred mountains” have played an outsized role in Chinese cultural and political life. Any student of Chinese history and culture will note the manner in which people from ancient sage kings and culture heroes to prime ministers and presidents have made their way to the sacred mountains for everything from pilgrimages to political photo-ops. They have been, for centuries, teeming centers of tourism, commerce, and religiosity in many forms, from Buddhist and Daoist to Confucian and beyond.

I was enthralled, and turned my research energy toward Mt. Tai. For the next year, I spent every moment that I could—spanning the seasons—on and around the mountain, studying the social, cultural, and religious forms of pilgrimage there. Through the winter, spring, summer, and into the fall of 2007, I traveled to China during every teaching break. I talked to shopkeepers, interviewed monks and nuns in their mountain temples, and studied the city of Taian at the foot of the mountain. Day-after-day, I climbed the mountain and took down the textual

details from more than a thousand “rock inscriptions” [石刻] all of the way up the slope—poems and phrases carved by some of the greatest writers in Chinese history. I talked with fellow travelers about their reasons for being on the mountain, their purchases, the expenses they had incurred, and their intentions for being there.

### *Changing Places*

And yet, stimulating though it was, I was living out an ethnographic version of the film *Groundhog Day*. Every morning, I awoke, had breakfast, and made my way up the mountain. But something was wrong. There were four other “sacred mountains,” and I was, at that point, none the wiser about them. So, in the third week of October 2007, I watched the sunrise from Mt. Tai, chatted with the gathered pilgrims, and started down the mountain. From there, I boarded a train at the Taian Station, arriving many hours later in the central Chinese city of Luoyang. I climbed the central mountain, Mt. Song [嵩山], and then traveled farther, to the western mountain, Mt. Hua [華山]. Two months later, I returned to China and made my way up the southern mountain, Mt. Heng [衡山] and the northern mountain, another Mt. Heng, but with different Chinese characters [恆山].

In that flurry of mountain climbs, I learned something valuable for my historical and ethnographic research. Fascinating as the mountains were for their elegant calligraphy and beautiful temples, I began to internalize something that had been harder to grasp when I focused intently upon historical texts and religious culture. The mountains are (and have always been) centers of bustling social activity that I had not fully appreciated until I had actually climbed each of their, on average, seven-thousand stone steps, from base temple to the temple on the peak. That I had not come even close to thinking of that “social” or “cultural” activity as profoundly *economic*...or, more particularly, *entrepreneurial*, says much more about who I was as a researcher than it does of the mountains and the activities around them.

Entrepreneurial activity—it was everywhere. Like the commercial world depicted in the *Qingming* scroll, the mountains were teeming centers of travelers, social gathering, spending, consuming, and dispersal—back home, or off to other tourist destinations. Every day, travelers arrive and travelers leave. Something was going on, and I suspected that it was profound. I realized at that point that what I had come to think of as “bustling social activity” ran much deeper in its implication than people merely happening to come together. It combined all of

the elements of the social sciences and humanities as we study them today, with not a little bit of what we might call the “natural” or “hard” sciences on top of it.

### III *Getting Down to Business*

#### *Down South*

For many reasons that go beyond the scope of this essay, I focused my attention on the southern sacred mountain, Mt. Heng, located about two hours from the provincial capital, Changsha, in the southern province of Hunan. The southern mountain is better known to many Chinese travelers as “Longevity Peak” or “Longevity Mountain” [壽嶽]. The latter term speaks to the intense devotional traditions that have grown up around this pilgrimage destination for the better part of the past two millennia—from base to peak, and everywhere in-between. The most striking thing that the visitor accustomed to the other four sacred mountains will notice is the intensity of devotion expressed on Longevity Mountain, which has been consistent for more than a millennium.<sup>3</sup>

While it is, of course, difficult to quantify outwardly (and inwardly) emotional states such as “religious intensity,” the connection is palpable. As difficult and, frankly, uncomfortable as such vague concepts can be, matters such as “religious intensity” still matter as we strive to grasp concepts that fall between the lofty silos of academia. Few people have articulated the need to double-down on vague-but-hardy notions that seem to “fit” something “out there” as C. Wright Mills in *The Sociological Imagination*.

The sociological imagination, I remind you, in considerable part consists of the capacity to shift from one perspective to another, and in the process to build up an adequate view of a total society and of its components. It is this imagination, of course, that sets off the social scientist from the mere technician. Adequate technicians can be trained in a few years. The sociological imagination can also be cultivated; certainly it seldom occurs without a great deal of often routine work. Yet there is an unexpected

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<sup>3</sup> For historical context, see James Robson, *Power of Place: The Religious Landscape of the Southern Sacred Peak (Nanyue) in Medieval China* (Cambridge: Harvard University Asian Center, 2009).

quality about it, perhaps because its essence is the combination of ideas that no one expected were combinable—say a mess of ideas from German philosophy and British economics.

There is a playfulness of mind back of such combining as well as a truly fierce drive to make sense of the world, which the technician as such usually lacks. Perhaps he is too well trained, too precisely trained. Since one can be trained only in what is already known, training incapacitates one from learning new ways; it makes one rebel against what is bound to be at first loose and even sloppy. But you must cling to such vague images and notions, if they are yours, and you must work them out. For it is in such forms that original ideas, if any, almost always first appear.<sup>4</sup>

As an ethnographer, I have only seen such intensity of “religious” expression (in a mountain context) on the four “Buddhist” sacred mountains, Emeishan [峨眉山], Wutaishan [五台山], Jiuhuashan [九華山], and Putuoshan [普陀山]. These Buddhist mountains cannot compete, however, with the five “cosmological” sacred mountains for cultural supremacy—few locations in all of China rival Mt. Tai for its central place in the cultural tradition. And yet the Buddhist mountains absolutely bury the sacred five mountains in human interest, and have done so for well over a millennium. The number of travelers to the Buddhist mountains is enormous, and their purposes for being there are fundamentally devotional.

Only the southern mountain, Longevity Mountain, rivals the “religious care” that pilgrims exert on the Buddhist peaks. From my first day in the base temple of Longevity Mountain, I watched, enthralled, as pilgrims poured into the temple. For the traveler well-versed in the cosmological architecture of Chinese temples, the journey through the South Peak Temple begins with a bit of irony. It so happens that almost everyone enters the southern mountain temple through the north gates, which are the closest convenient drop-off location for cabs, buses, and other forms of tourist transportation. The “proper” cosmological direction requires beginning from the south and proceeding to the north. Regardless of direction, though, pilgrims made for the large incense burners, bowed, and burned their incense and “hell money” amidst belching smoke and many hundreds of other travelers.

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4 C. Wright Mills, *The Sociological Imagination* (Oxford: Oxford University Press, 2000), 211-212.



And so I set out to understand the emotional intensity that I was seeing all over the city of Nanyue (South Peak), and all of the way from the temple at its base to the Zhurong Temple at the very top. I clearly saw that pilgrims expressed a sophisticated blend of “syncretic” worship that merged what we might call the “Confucian” tradition with Buddhist and Daoist strains. Indeed, upon entering the great Nanyue Temple [南嶽廟] in the proper, southern direction, the entire right side of the temple complex is devoted to Daoist quarters and offices. The entire left side is reserved for Buddhist compatriots. Everything else in the temple blends Confucian, Daoist, and Buddhist teachings. The sprawling location presents a magnificent unfurling of religious and cultural complexity in a world only decades removed from the Cultural Revolution, when such devotional actions were harshly condemned, and mountainside temples closed for the better part of three decades. Beginning in the 1980s and 1990s, and with growing interest by the year in the last decade, the reintroduction of devotional practices into Chinese life has gained increasingly wider appeal. Much of the domestic tourism focuses initially on historical appreciation and pride. From that foundation, a population that had been significantly cut off from a millennia-old tradition of temple worship has begun to learn it all over again—and in a completely new, ostensibly secular context that would make practices in the early nineteenth century look quaint.

### *Stocking Up*

Tourists arrive in South Peak from all over China, mostly from places far more “secular” than the mountainside cities themselves. There are few logical stops for tourist breaks nearby in the region, so travelers in cars, on buses, and on trains (arriving fifteen minutes away and requiring a taxi cab ride) find themselves in town with depleted supplies, ranging from food and drink to the divinatory commodities that tourists will need to have an effective divinatory experience from the base temple to the Zhurong peak. And waiting for them in South Peak are hundreds of stores *that all sell virtually the same things*.

It is common to eat a post-travel meal and buy religious “necessities” all in the same shop. The vast majority of the stores near the temple are “three wall” arrangements with the equivalent of a garage door to pull down at night to seal the premises. Many have a kitchen in back and living quarters on the second floor. Tables dot the main floor, and products for sale line the walls. Although there is ample room for variation, such a store might qualify as a kind of Weberian “ideal type” for commercial activity in South Peak. Let us imagine that our fictional

travel group enjoys a hearty lunch, right there on the premises, before making their purchases.

When buying devotional products, travelers begin with a sturdy red shopping bag—virtually the same one sold in every other store in the city. On one side of the bag is a large picture of the incense burning point at the base temple, often just a few steps from where they are purchasing their wares. Burning incense at the base and the peak temples is the key experience that links the actions of today's tourists with kingly and imperial devotions that stretch back into Chinese history and mythology. On the other side of the bag is a picture of their ultimate destination, the peak temple. Making the “double devotion” at the base and peak temples links the devotional practices of early rulers with more commonplace gains ranging from “bragging rights” to the expectation of divinely sanctioned aid that can only come from linking base and peak. As I have emphasized in other writings,<sup>5</sup> these two locations are the key to religious tourism on the southern sacred mountain, and, indeed, lie at the core of all “mountain religiosity” in China. The vast majority of travelers go from the base temple straight to the peak temple, employing a variety of transportation forms, from tour buses to cable cars. Fewer than a tenth of travelers hike the 7,000 steps from base to peak.

The shopping bag itself lays out the key economic parameters. Inside the bag goes incense sticks in red cardboard containers bearing the phrase “Request and Response Will Follow Incense” [有求必應香]. The cost for each cardboard incense package is ¥8 (\$1.30). The pre-packaged version of the shopping bag, which many people purchase, contains eight boxes, for a total of twenty-four incense sticks. The rest of the bag contains yellow and red boxes of “hell money,” which is meant to pair with incense sticks in a full devotion. Although it is possible to buy “real” hell money<sup>6</sup> in temples all over China, Hong Kong, Singapore, and Taiwan, a quick peek into the cardboard containers show either scrap paper or woodchips. The real goal is, quite literally, to fan the flames of the temples' incense burners. Ignition fuels this economic religiosity, and busy days always see frequent hosing down of the burners and environs before the forces of social-economic devotion heat up again.

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5 Robert André LaFleur, “Religiosity Spent: The Cultural Economics of Divination on China's Southern Sacred Mountain,” in *Unterwegs im Namen der Religion: Pilgern als Form von Kontingenzbewältigung und Zukunftssicherung in den Weltreligionen*, ed. Klaus Herbers and Hans Christian Lehner (Stuttgart, Germany: Franz Steiner Verlag, 2014), 129-146.

6 Te-Ping Chen, “In Hong Kong, Inflation Worries Spook the Spirit World,” *The Wall Street Journal*, August 19, 2013.

*Devout Observances*

Many travelers have told me that their rule-of-thumb for incense purchases is ¥200 (about US \$30). In fact, one young woman told me that her father instructed her before her trip that less than ¥200 lacked seriousness, while more than that amount lacked perspective. In fact, the ¥200 amount proves to be a very useful tool for measuring divinatory consumption. Excluding, for purposes of this example, those travelers with a secular outlook who do not buy any incense—a surprisingly small group, as I found—there is little relationship between total wealth and the amount of incense purchased. I have seen only a handful of people spending many hundreds of yuan on incense during their travels. I have also seen relatively few examples of people trying to “cut it close” and spend only a few tens of *yuan*. ¥200 is an extraordinarily stable number when it comes to assessing divinatory commerce on Longevity Mountain.

Almost every traveler, then, buys the same thing, over-and-over, and the foundational purchases are incense and hell money. A complete bag of incense and hell money costs about ¥100, and there are two main temples to cover. For most people, that means buying two pre-packaged bags. One is stored in the hotel room (or car trunk), and the other is carried straight to the temple after lunch. For the enterprising pilgrims wishing to spend more—and perhaps distinguish themselves with a bit of conspicuous divinatory consumption—one of the most popular options is found in sturdy, golden boxes of “dragon head” incense sticks [龍頭香]. These are often used individually at key temples.

If a traveler wishes to show a bit of personal or family wealth in the course of praying for longevity, dragon head incense plays a significant role in the equation. Thorstein Veblen's words from a chapter titled “Devout Observances” echo the larger themes of his *Theory of the Leisure Class*.

The most obvious economic bearing of these observances is seen in the devout consumption of goods and services. The consumption of ceremonial paraphernalia required by any cult, in the way of shrines, temples, churches, vestments, sacrifices, sacraments, holiday attire, etc., serves no immediate material end. All this material apparatus may, therefore, without implying depreciation, be broadly characterized as items of conspicuous waste. The like is true in a general way of the personal service consumed under this head...At the same time the observances

in the execution of which this consumption takes place serve to extend and protract the vogue of those habits of thought on which an anthropomorphic cult exists. That is to say, they further the habits of thought characteristic of the régime of status.<sup>7</sup>

Any visitor to a Chinese temple can observe a remarkable array of “social spending,” and it is all the more fascinating in that the activities have, at their seeming source, a deeply personal and even private compulsion. The brilliance of Veblen’s insight was to pinpoint the profoundly social and economic nature of even very personal expressions of devotion. Veblen teaches us that motivations as diverse as a deeply personal sense of homage to the spirits and “showing off one’s wealth” can happen at the same time, and both can shape a complex combination of economic and cultural activity.

#### IV *Through the Temple Gates*

##### *Temple Entrepreneurship*

Our “ideal-type” travelers find themselves on a bustling road between the entrance to the mountain and the north gate of the base temple (having arrived there a few hours earlier after their journeys from afar). The north gate faces the foot of the mountain, and—sandwiched between them in that area—lie hundreds of shops, lining the street on left and right.<sup>8</sup>

Inside the temple, the core divinatory “move” is simply to make obeisance (execution of this varies widely) and to “offer” incense and hell money by tossing them into the burners. Everything else in the temple is peripheral to the goal of cementing the divinatory process in the base temple. This goal is shared by all but a small number of “cultural” travelers (and, perhaps, a stray anthropologist). We have seen that almost everyone enters the temple with a shopping bag of incense and hell money, but what else happens *inside* the temple? The question is an important one, because buying and selling is happening from the moment one buys an admission ticket until one leaves through the exit gates.

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7 Thorstein Veblen, *The Theory of the Leisure Class* (New York: Oxford University Press, 2007), 200.

8 One of the topics for my future research will be to examine questions surrounding the ownership of stores, business plans, and distribution of goods.

As we have seen, the vast majority of travelers enter the temple from the “wrong” direction. Mountain temples are designed to “move” toward the north. Buses and cabs bring people to the strategically rich location that links the mountain entrance, the temple exit (which also functions as an entrance), and the rows and rows of shops along that run between them. For those who do enter “from the back,” it is the cosmological/architectural equivalent of seeing the end of the Super Bowl and watching it all of the way back to the beginning. If a traveler does enter the temple in the “correct” way, however, it will require a fifteen minute walk around the walled temple perimeter to the much smaller ticket booth at the (cosmologically correct) south end of the temple. After purchasing the ticket, it takes only a few steps before one sees the first commercial venture—a kind of overture to unfolding commerce within the temple from that step forward. Right there, a temple entrepreneur “sells” the fundamentally Buddhist message of “releasing life.”

For a fee, the pilgrim can pick a little fish trapped in a small bucket and give it new life in one of the large, square, stone pools that frame the entrance, on left and right. A brown sign notes the ways in which such acts of compassion can benefit individual, family, and society. Doing good in this manner comes with a price, depending on the size of the fish. It functions as a kind of cosmic insurance, with a low price and vaguely positive goals.

*Releasing Life—A Public Spirit Without Compare*

What is releasing life? It is giving living things a chance, and also giving yourself a chance. Releasing ten thousand lives eases the eight difficulties... release a hundred thousand and happiness and a “round” life is attained. Release several million, and the circle returns, everlastingly unbroken.

Hurry, hurry and release life—fish, shrimp, turtles, birds, and so forth. All can be given release. Yesterday’s release of life today will bring good luck and positive karma.

- |                                       |   |
|---------------------------------------|---|
| Releasing life is saving life.        | Releasing life is extinguishing disaster.   |
| Releasing life is gaining longevity.  | Releasing life is responsibility.           |
| Releasing life is fortunate and good. | Releasing life is compassionate and caring. |

*Bang the Drum Slowly*

Following the south-north path, travelers reach a structure with stone “round-square” symbols that are often associated with traditional monetary currency. And there, a strange kind of cultural and anticipatory economic gathering takes place. Each traveler carries a shopping bag. One after another they rub—physically rub, with their hands—the traditional stone “cash.” It is a kind of tactile religiosity that frames the entire divinatory process and, indeed, links it to the entrepreneurship all around them. And never forget that the shopping bags in the other hand are filled with another kind of divinatory currency—incense and hell money.

A little further down the path more cultural commerce beckons from left and right. On the left is a small edifice the size of a single college dorm room, containing just enough space for a great drum and the desk for a ticket seller. For the low price of ¥5 (US \$0.75) the traveler can bang the temple drum. On the right side is an equally modest structure containing a magnificent iron bell. For another ¥5 (US \$0.75) it is possible to strike the bell with a thick log tied to the ceiling by a rope. In each of the buildings stand signs with rather pedestrian sayings telling what good might come from drumming or ringing, as the case may be. The bell must be sounded six times, and each holds a different meaning.

Spiritual Compassion Vast and Unending

Virtue Swamping Multitudes of Life

——Strike the Bell of Auspicious Luck

Successful Dreams Will Come ‘round

One—Life of peace and calm, ten thousand of auspicious luck

Two—Dragons play the pearl, a famous name will be attained early

Three—Stars shine on high, wealth and fame, health and peacefulness

Four—Seasons bring wealth, the hundred occupations rise brightly

Five—Luck enters the gate, the heart reflects work completed

Six—Roads are great and smooth, wealth and longevity unfurl like a brocade

It is not lost on the reflective traveler that the rubbing, drumming, and bell-sounding are profoundly social activities for most visitors, who arrive in groups and share the experience. At the same time, no matter how large the travel group, it is equally true that such “magical” practices are personal, individual. The quest for divinatory fortune is a complex blend of the solitary and the social.

So here, even a mere hundred steps into the temple, the traveler has encoun-

tered Buddhist compassion (for sale), rubbing for wealth, and the physicality of iconic instruments of Chinese culture in the form of drums and bells. More than a few travelers have already spent twenty *yuan* (US \$3.00) by this point, and (let us not forget) each is carrying at least ¥100 (US \$15.00) of incense and hell money. And everyone is heading for the main event—the incense burners at the social and economic center of the temple.

## V

### *Getting to Work*

#### *Research Modes*

So how can we possibly approach the social, psychological, literary, and surely historical details of divination on a Chinese sacred mountain? No single discipline is adequate. Better put—no single discipline as narrowly conceived in today's academy is adequate. The best practitioners in all of them have always exercised a pan-disciplinary “imagination” that juxtaposes questions and data from what others think of as “separate fields.” And it is not just a matter of working with different “fields” that is necessary in this kind of work. The researcher must proceed in a manner that is often exasperatingly “subjective” to the casual observer, even though the goal remains the same kind of deep understanding that a more “rational” colleague might desire.

Few academic disciplines merge these seemingly contradictory challenges as well as history. I once heard a story about how difficult it is for historians to explain their work—in this case, as a faculty presentation to a room filled with scholars in the natural and social sciences. The historian explained his method something like this (I paraphrase).

First, I begin with a roughly-formed question, and think about it, clarify it, and jot down some notes. Then I begin reading, and take more notes. After doing this for a while, I write a bit, and try to understand the problem better. Then I read some more, think some more, write some more, and repeat the process until I think that I have it just about “right.” Then I type up the final draft and send it to my editor.

The room was aghast. “That’s not a *method*” was the majority rejoinder. “Where are your variables? Your controls? That’s not how *we* work.” Another vic-

tory seemed within the grasp of the practitioners of more rigorous disciplines. But then an experienced physicist in the back of the room stood up and said, “No, that is *exactly* how we work.”

The physicist was not merely defending a seemingly gullible humanist. He was tapping into the very nature of real scientific research and discovery, almost all of which takes place on the margins of established knowledge. He was echoing a strain from the philosopher of science Thomas Kuhn and his *Structure of Scientific Revolutions*.<sup>9</sup> There, Kuhn notes the ways that paradigms shift in the sciences (indeed, all disciplines). The physicist understood that—no matter how we carry out the detailed stages of our work, from library research to laboratory experiments, social scientific questionnaires, or ethnographic fieldwork—we all research, ponder, clarify, research some more, and finally “write it up” in some form or another for our peers and the public.

At least that is what we do when we are doing it right.

### *Another Twist*

I would like to add another twist to the research challenge because I think that many of us working in the social sciences have been exceptionally clumsy in the way that we approach research design. Either by making certain unexamined assumptions about “culture” or in minutely defining what we think to be the key variables in our research, social scientists all too often limit their fields of vision and miss at least part of their investigative forests by looking at only a small portion of the trees.

It happened to me on the southern sacred mountain in the following way. So enamored was I by a 3,000 year tradition of emperors, esteemed poets, and ordinary pilgrims climbing the mountains, writing about them, and even inscribing their words onto the very rock face, that I was certain that my own research mission was straightforward. “All” I needed to do was study the history and ethnography of a mountain that led me, as I have often described it, to pursue ethnographic fieldwork in a cavern of carved, mountain text—from poems and aphorisms to full imperial edicts. I needed, in short, to merge the historical and literary traditions of the mountain with the teeming, bustling, pilgrimage all over it today. I talked to travelers, filled notebooks with their opinions about history

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9 Thomas Kuhn, *The Structure of Scientific Revolutions*, 4th ed. (Chicago: The University of Chicago Press, 2012).



and literature, and read every book that I could find about the mountains. I used my digital camera as a mnemonic tool geared toward helping me write my historical ethnography, and the collection was formidable—40,000 images, with a third of that for just the southern mountain.

And all the while I ignored the teeming commerce that surrounded me.

When I give lectures about the sacred mountains today, I always apologize for the relative dearth of pictures of what people buy and sell all over the mountains when compared to thousands of photos of rock carvings, architecture, and natural scenery. You see, it was only in the last year or so that full comprehension of the bustling entrepreneurship on the mountains was anything but a distraction in my larger “cultural” study. To say that I had it all wrong does not even begin to atone for my error, which originated in a naïve humanism that—ironically—needed a healthy dose of mercantile understanding to bring my studies to an entirely new level.

### *Bourdieuian Strategizing*

It was actually a pair of sociologists who set me straight. Sociologists, anthropologists, and historians who read the writings of economists are often startled by what seems to be a naïve and narrow focus on individual choice, even in matters that have been deeply influenced by “social” and “cultural” forms. Spending in “religious” contexts is one of those areas in which the outsider to the field of economics is often dumbstruck by their failure to notice (as many outsiders see it) starkly “irrational” or even beyond-rational choices. As Thorstein Veblen noted more than a century ago, devotional spending is among the most perplexing forms of economic activity to understand.<sup>10</sup> For many sociologists, anthropologists, and historians, economists have been hopelessly naïve about these “cultural” matters.

What is needed is a form of analysis that combines the analytical power of microeconomic (and behavioral economic) theory with a “thick description” of religious, devotional, and emotive spending. Enter the French sociologist Pierre Bourdieu, who articulated a theoretical framework that grew out of empirical challenges in his own work. Many of those details were similar to the challenges microeconomists and behavioral psychologists study. Bourdieu challenged simple notions of “rules” in human activity. For Bourdieu, there are no “rules,” as such. Rather, Bourdieu thought of “rules” as something like a conceptual grid upon which people made choices within a series of structures ranging from rigidly en-

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10 Veblen, 208.

forced ones to general guidelines.

Bourdieu coined the term *habitus* to deal with the ingrained but ever-changing ways that fully enculturated people live, love, and spend. Bourdieu would likely not have been surprised by the manner in which the vast majority of pilgrims enter the base temple on Longevity Mountain from the rear entrance. People strategize, spend, strategize, and spend some more. Mountain divination habitus has the vast majority of pilgrims buying significant stores of incense and hell money, visiting the base and peak temples, and exploring an eclectic series of shops, restaurants, and secondary tourist sites during their stays. The knowledge that emerges from Bourdieu's approach is textured and, like lived economic activity, somewhat chaotic. Bourdieu's greatest insight came in destroying the idea of social "rules" and replacing it with a kind of "strategizing" that is reminiscent of microeconomic theory, yet far more ethnographically rich. Even so, his approach still falls short when an investigator tries to make sense of the staggering detail and nuanced repetition found in even the simplest study of divinatory spending on China's southern mountain.

### *Becker and Society as a Machine*

The American sociologist Howard Becker has become in France a sort of replacement-hero for Pierre Bourdieu, and the story of his octogenarian superstar status in French academia makes for compelling reading.<sup>11</sup> French academics have not just found the anti-Bourdieu in Becker. They have, far more significantly, found someone whose very empirical instincts helps to push Bourdieu's insights about social and economic strategy even further—specifically in framing the initial research questions in a way that few of the most sophisticated social scientists have any stomach for, given the demands they face for "clean" and "efficient" models.

Since his very first publication sixty years ago until now, Howard Becker has scoffed at the manner in which social scientists have seemingly "just decided" what the important variables are—or how we should view them—without the kind of ethnographic sketching required even to know what those variables should be. A case in point is one of his very first publications, in which he turned the sociological study of deviance on its head. Almost every researcher before

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11 Adam Gopnik, "The Outside Game: How the Sociologist Howard Becker Studies the Conventions of the Unconventional," *The New Yorker*, January 12, 2015.

him, he carefully noted, had begun with the assumption that marijuana smoking was deviant, and—more central to their flawed analyses—an escape. Pot smokers were escapists. Becker showed how enormous misunderstandings flowed from that starting point.

Instead, he “built a machine,” as he would later phrase it, that starts with a counter-intuitive premise.<sup>12</sup> “How would I make sure that someone became a pot smoker?” His answer changed studies of deviance in profound ways. In a phrase, Becker found that you would need to create a community. Pot smokers weren’t alienated individuals off on their own, eschewing contact with others. *They learned to smoke pot.* In a statement that has made the rounds for decades, Becker noted that it takes a village to create a pothead.

As Becker has shown in his more recent writings, the analogy of social life to a “machine” is a powerful one, and it can alter profoundly the way that we study phenomena—such as selling the same thing over and over again—that seem repetitious or even inane.

### *Everything (Really)*

Bourdieu and Becker gave me the tools I needed to make at least a beginning form of understanding when it came to economic activity on the southern mountain. I recall a notion from Becker’s *Art Worlds* in which he notes that, to understand a theater production as a social and artistic whole, it was not enough to study the director, actors, stage production crew, and so forth.<sup>13</sup> If we don’t understand the role of the ticket maker, the ticket seller, and even the person who parks people’s cars, we fail to understand the “world” of the production. Somehow, I found this message to be just what I needed when “stuck” in my own understanding, and it provided my breakthrough. I began to see that there were dimensions akin to the “ticket maker” in the divinatory process that would have been lost as “variables” had I not put the entire machine together as well as my current knowledge allowed. And that changed everything.

Becker frames the process in a way that I find enormously compelling.

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12 Howard Becker, *Tricks of the Trade: How to Think about Your Research While You’re Doing It* (Chicago: University of Chicago Press, 1998), 35.

13 Howard Becker, *Art Worlds*, 25th Anniversary Edition: Updated and Expanded (Berkeley: University of California Press, 2008), 20.

Many people think that the object of [social analysis] and theorizing is to simplify our understanding of social life by finding the underlying laws that govern its operation. I think, contrariwise, that the object is to find out the nature of, and find a place in our thinking for, *everything that observably contributes to producing the results I'm interested in*. I want my analysis, my theory, to contain everything I need to describe and account for what my case study has forced me to see.

If you think [social analysis] should produce a simple model that explains everything, you won't find this way of working attractive. If you think a functioning scientific community thrives less on piling up conclusions than on creating a continuous flow of new problems to solve...this approach will keep you busy long into the future.

It's not just the complexity of social life that guarantees that, but also the fact of historical change, which keeps producing new forms of collective activity that provoke new ideas, new research problems, and new categories of elements whose variation will be at work in these new forms.<sup>14</sup>

Among the “variables” or social nuances that I have come to consider when studying temple activity on the mountains is the outsized role played by the burgeoning domestic tourism industry in China. Echoing Becker, temporal change has profound importance, and two decades ago the dynamic would have been profoundly different. The southern mountain has become a tourist stop in a larger group tourism economy that begins in the provincial capital of Changsha and continues with three-, seven-, and ten-day journeys throughout the province. Linking increased wealth, sophisticated transportation systems with a post-Olympic (2008) and post-World's Fair (2010) nationalism, this tourist economy has grown enormously in the past decade, and is fundamentally different from what existed at any time in the past.

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14 Howard Becker, *What About Mozart? What About Murder?: Reasoning From Cases* (Chicago: University of Chicago Press, 2014), 3-4.

Domestic tourism has changed “everything” in some respects, with a new kind of tourist, one not necessarily motivated first by religious feeling, who is simply “en-route” as part of a larger package. One might well expect a lessening of devotional intensity. The sheer numbers, however, have tended to reinforce the intensity that I perceive in the temples, rather than detract from it. These are just two of the gems that have emerged from taking Becker’s approach seriously. Although his (and Bourdieu’s) approaches influence what we might think of as “methodology” most profoundly, the implications for even individual details in the puzzle are profound.

## VI

### *Market Cultures*

#### *Spiritually Animated Markets*

In his provocative 2013 work *Understanding the Culture of Markets*, Virgil Henry Storr employs a Weberian concept to explore “the spirits that animate markets.” Even in the early twenty-first century, economists have been slow to embrace the concept of culture in analyzing economic activity. Anthropologists, sociologists, and historians have been comfortable with such ideas for many decades now, and many of us wonder at the reticence of economists to acknowledge “culture” as a key element of economic activity. But even the more “humanistic” of the social sciences may pause at the idea of market “spirits.”

That such an idea is difficult to measure is obvious even to the most qualitative of researchers. And yet Max Weber, writing more than a century ago, linked forms of capitalism to specific kinds of “economic spirit.” Storr writes,

According to Weber, each of these forms of capitalism is generally animated by a particular economic spirit. “An historically given form of ‘capitalism,’ Weber explains, “can be filled with very different types of ‘spirit’; this form can, however, and usually will have different levels of ‘elective affinities’ to certain historical types of spirits.” Stated another way, in the actual world, a given economic spirit (e.g. one that stresses creativity) will either fit comfortably or uncomfortably within a particular capitalist form (e.g. in a liberal market economy versus in a socialist economy)...[and] although the relationship between a particular

kind of capitalism and the spirit that is said to animate is not one of “mutual dependency governed by any law,” it is more than just coincidental.<sup>15</sup>

Weber most clearly works out these ideas in his classic *The Protestant Ethic and the Spirit of Capitalism*. It is not difficult to see the manner in which a peculiar form of spiritual animation envelopes economic activity on Longevity Mountain, either. The “feel” found from mountainside and temple-side shops to the temples at base, peak, and all of the way up the mountain are distinctive. The smell of incense is everywhere, and it is not just a metaphorical overlay for more serious activity. In very real ways, it is both the key product and the activity animating market life on Longevity Mountain.

### *Market Cultures*

So what is a “market culture” with regard to the southern sacred mountain? On a very simple level, it is one that supplies incense and hell money (as well as nourishment and rest) to a large array of tourists, many of whom are not at all familiar with the devotional principles that drove Chinese temple life for tens of centuries in the past. They come on their own in cars, in large tour group buses that also include trips to popular sites in Hunan, and (as I learned) in small groups of local students praying for educational success. A relatively small number come for the cultural value—the stone inscriptions and temple architecture on the mountain. As we have seen, what almost all of them need is an average of ¥200 (US \$30.00) of incense and hell money, as well as places to eat and rest.

How can we think of “culture” in this framework?

The economist and philosopher Amartya Sen provides a vigorous critique of rational choice, on the one hand, and the larger conception of “culture” and individual predilection, on the other. Storr provides a useful way to frame the issue.

Specifically, Sen insists...that rational choice defined solely as internal consistency cannot make sense of [cultural considerations]... As Sen explains, “one way of defining commitment involves individuals acting counter-preferentially [in ways that] cannot be easily reconciled with rational choice...Think of the

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15 Virgil Henry Storr, *Understanding the Culture of Markets* (New York: Routledge, 2013), 60.

religious devotee who offers prayers soon after waking every morning and gets some personal satisfaction from praying but engages in prayer because she views it as a moral obligation and not because she enjoys doing it...

Sen has, thus, argued that any description of human beings that leaves out the potential for [cultural] commitment to sway choices and insists on there being “no inconsistencies in [his] choice of behavior...must [view him as] a bit of a fool.” According to Sen, “the purely economic man is indeed close to being a social moron.” Actual human beings, as Sen suggests, are far more complex...<sup>16</sup>

And social morons these tourists are not. Where they *do* lack skill—and in ways that would almost be laughably so to the experienced temple visitor who grew up in consistent devotional circumstances—is precisely in knowing *what to do* in temple situations. The market culture of today is driven by demand that is socially sophisticated. People know how, at least in general terms, to distinguish themselves from others. What many, even most, travelers on the southern sacred mountain do not know is how to spend strategically in that storied setting in order to distinguish themselves from others. Combining Thorstein Veblen’s devotional conspicuous consumption and Howard Becker’s “social machine” with the culture of markets, we can see that a strange kind of pedagogical divinatory economics is necessary in this market setting. The shopkeepers are busy teaching “what to do” to travelers who have only recently returned to practices that many of their peers still regard as “superstition,” even as they are buying incense and “hell money.” The travelers often need instruction, even as they create their own individualized buying strategies, and shopkeepers need to learn to “teach” without offending them.

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<sup>16</sup> Storr, 86-87.

## VII

*What Is Entrepreneurship?**Opening Shop*

Imagine the following scenario. Halfway up the mountain, there is a famous temple with a tremendously popular “Sending Children Hall” [送子殿], which is known for unparalleled success in creating burgeoning family lines. Incense and hell money are, of course, for sale at the temple, which has a locational monopoly on the products. For one reason or another, most travelers are “tapped out” by the time they find themselves at that point on the mountain.

It is basic supply and demand—the temple sells the same “shopping bag” (which costs ¥100 on the big avenue in South Peak between the temple and the mountain) for at least ¥200 (US \$30.00), and maybe even ¥300 (US \$45.00). But what if a little shop a hundred meters down the mountain opens and sells the very same “shopping bag” for ¥150 (US \$22.50)? The sales pitch would be straightforward. “We’ll sell it to you for less, even before you reach the temple, where it *will* cost more.” This hypothetical situation meets what most of us would think of as an “entrepreneurial” venture. There is potential risk and reward involved, and the old phrase *location, location, location* is apt.

So how does this kind of risk-reward entrepreneurship compare to the decision strategies employed by the dozens—hundreds, really—of shops down in the city of South Peak? Is opening the thirtieth store on your street, and selling exactly the same things as another one, *entrepreneurship*, or might we need another concept that more closely allies with the situation?

The thirtieth shop on a street in Nanyue serves the spiritual needs of pilgrims for a price that is matched by every other store. Yet the demand remains enormous, and is growing. It is fueled by a complex tourism industry that is aided by the mountain’s connection in Chinese culture to ideals of “longevity,” but even more so to its location an hour away from a much more recent culturally iconic site in China—Mao Zedong’s birthplace. Tourists pour in after completing their primary goal of visiting Mao’s hometown, and make another stop at the southern mountain. The tourism stops are not always a matter of individual or family choice, either. Tourist destinations (throughout the world) are often clustered, and Longevity Mountain is no different. Because it is closely connected with tourism to Mao’s birthplace, the southern peak has benefited enormously from a changing tourist economy.



Business is booming, but almost all of the core businesses in the city of Nanyue (South Peak) are retail—and they sell exactly the same things to almost exactly the same kinds of travelers. How can an individual business distinguish itself? If what the new store owner sells is exactly the same as hundreds of other stores, what is *entrepreneurial* about it?

### *Retail Winds*

Let us return to the relationship between buyer and seller, and what one of the great philosophers of entrepreneurship, Josef Schumpeter, states about entrepreneurial activity. Despite the fact that he never envisioned commerce on Chinese mountains, he speaks to the very soul of the economic enterprise.

Economic activity can have any motive, even a spiritual one, but its meaning is always the satisfaction of wants.<sup>17</sup>

The “wants” on the Longevity Mountain bridge spirituality and (following Veblen) increased status among peers. Not only do they cost money, but they require “instruction.” Instruction might come from tour group leaders or traveling companions, but it often arrives in the form of “instructional entrepreneurship.” These forms of instruction are too-little understood as a dynamic on the southern mountain. Tourists are often quite sincere about their desires to fulfill their spiritual obligations in a newly re-centered Chinese cultural world now open to such expressions, at least in this sacred mountain context.

That tourists often don't know *what to do* plays into the “market culture” and the strategies of tour group leaders and sellers. Consider just two examples. Following a long-standing tradition in Chinese domestic tourism, tour buses stop at key “loading stations” to stock up on supplies. The tour company forms a relationship with the shop, makes a rest and refueling break of it, and satisfies multiple *wants* in at least a small way. The negatives should also be obvious. The tourism industry shapes the “divinatory” experience from the start, and many tourists have already spent their ¥200 (US \$30.00) before they reach the temple—and before they really know what they are doing. At least in this post-Cultural Revolution transitional period, when many people are becoming reacquainted with a temple

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<sup>17</sup> Joseph Schumpeter, *The Theory of Economic Development: An Inquiry into Profits, Capital, Credit, Interest, and the Business Cycle*, trans. Redvers Opie (New Brunswick, NJ: Transaction Publishers, 2012), 10.

experience that was common to almost everyone a century ago, these incentives (including going to the rest room and combining it with incense purchase) are significant. Schumpeter takes an intriguing angle in analyzing “The Circular Flow of Economic Life.”

The chief source of these gains and losses—and this is the second element that I wish to consider here—is spontaneous changes in the data with which the individual is accustomed to reckon. They create new situations, adaptations to which require time. And before that can happen a great many positive or negative discrepancies between cost and receipts occur in the economic system.

Adaptation always offers difficulties. The mere knowledge of the changed state of affairs is not attained in most cases with the desirable promptness. To draw conclusions from the knowledge is again a big step...But often perfect adaptation relative to the formerly existing products is impossible...<sup>18</sup>

It is the changing nature of “divinatory economics” on the southern sacred mountain that most intrigues me, and—with a combination of Veblen, Becker, Sen, and Schumpeter—it is possible to see the outlines of an economic activity that is fueled as much by traditional knowledge of ritual practice as it is by more “information-driven” market forces. A real problem for the buyer on Longevity Mountain is simply *not knowing what to do*. That social, intellectual, and economic void is being filled in fascinating ways—even as the “products” remain exactly the same, and for almost exactly the same price.

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18 Schumpeter, 33.

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# An Economy of Words: Observations on Fictional Narrative and Entrepreneurship in Early Modern China

Daniel M. Youd<sup>1</sup>

## *Introduction*

This brief essay addresses the theme of entrepreneurship through examples from a selection of fictional texts from China's early modern period, a span of time that I take to run from ca. 1550 to the mid nineteenth century. It explores – through a focus on words and stories – some areas of common concern between economics, on the one hand, and literary and cultural history, on the other. I begin with the supposition that language – as an essential tool for the expression of individual preferences and desires – is a *sine qua non* of economic activity. As the preface to an 1864 Cantonese-English phrasebook aimed at Chinese traders says, “If you cannot understand [each other's] language, how can your desires/sentiments (*qing* 情) be known? If you cannot read [each other's] writing, how can you communicate?” (夫不通語言，情何由達？不識文字，言何由通？)<sup>1</sup>

Indeed, according to economist David Levy, for no less an authority than Adam Smith “trade and language are two aspects of the same process; humans trade because we have language, nonhumans do not trade because they do not.”<sup>2</sup> To quote *The Wealth of Nations*: “Nobody ever saw a dog make a fair and deliberate exchange of one bone for another with another dog.”<sup>3</sup> In Smith's view, moreover, trade is a fundamentally *rhetorical* practice. In *Lectures on Jurisprudence*, he writes: “The offering of a shilling . . . is in reality offering an argument to persuade

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one to do so and so as it is for his interest. Men always endeavor to persuade others... and in this manner every one is practicing oratory on others thro [sic] the whole life.”<sup>4</sup> Not coincidentally, results of a study published in a recent issue of the *Harvard Business Review* stress: “The quality serial entrepreneurs display[] above others . . . [is] persuasion, or the ability to convince others to change the way they think, believe[,] or behave.”<sup>5</sup>

For some, the connection between entrepreneurship – or, more broadly, economics – and persuasive rhetoric will come as little surprise. I suspect many will be familiar with the work of Deirdre McCloskey. Building on the insights of Smith, she has, in a series of well-known articles and books, written compellingly about what we might call the “literary structure” of economic thinking.<sup>6</sup> Others, such as cognitive linguists George Lakoff and Mark Johnson (followed later by literary critic-cum-cognitive scientist Mark Turner), go even further, contending that certain basic features of storytelling underlie all human understanding.<sup>7</sup> For McCloskey, however, it is enough to suggest that economists are actually “not so very different from . . . novelists.”<sup>8</sup> The former simply tend to study things like “the market for rice,” while the latter tend to obsess over “the scarcity of love.”<sup>9</sup> To hold our attention, however, both must tell persuasive stories about their chosen subjects.

These stories are, of course, rooted in specific historical contexts. Recall, for a moment, the phrasebooks cited above. Its author, Táng Tíngshū 唐廷樞 (1832-1892), played an important role in the business history of nineteenth-century China. Educated in Hong Kong missionary schools in the 1840s, Táng pursued an eventful career, working first as an interpreter for the colonial government of Hong Kong, next as a secretary for the Shanghai Maritime Customs Service, and then as a compradore for Jardine, Matheson and Co. Later, recruited by Vice-Roy Li Hóngzhāng 李鴻章 (1823-1901), he managed the China Merchant Steam Navigation Company (輪船招商局) and helped establish the Kāipíng Mines (開平礦務局) and Tángshān-Xūgèzhuāng Railway (唐胥鐵路).<sup>10</sup> Over Táng’s lifetime, business practices in China underwent significant changes as “Chinese merchants in the treaty ports . . . learned about the operation of [Western-style] companies . . . several decades before China enacted a Company Law [in 1904].”<sup>11</sup> Táng himself was an active participant in these changes, seeking ways of transforming earlier forms of business organization and entrepreneurial activity – those that developed and flourished in the commercial economy of the Míng and Qīng – into new ones for a new era. Institutionally, for example, he mobilized merchant

networks to invest in new ventures, such as the *Huibào* 《匯報》 newspaper, which he and Yè Tíngjuàn 葉廷眷 (1829-1886), District Magistrate of Shanghai, established as a joint-stock company in 1874.<sup>12</sup> Ideologically, Táng translated – quite literally as his work on the phrasebook attests, but also more figuratively as a mediator between the business practices of his Chinese peers and those of the Western powers. From this perspective, there is much to be gained by viewing entrepreneurship – whether in Míng and Qīng dynasty China or the contemporary global economy – as, among other things, a narrative activity that is everywhere and always embedded in the value- and desire-making function of language. It is to the elaboration of economic themes in Míng and Qīng period fiction that we now turn.

### *Míng and Qīng Fiction and the Market*

Much has been written about the *bürgerlich* qualities of Míng and Qīng dynasty fiction. In current Chinese scholarship, in fact, such fiction is often referred to as *shìmín wénxué* 市民文學 – that is to say, literature by, for, and about “city folk” (*shìmín*), expressive of their tastes and values, and anchored in those market-oriented modes of production and exchange that were a prominent feature of urban life in early modern China.<sup>13</sup> Significantly, the first character of the compound *shìmín* is *shì* 市 – i.e. “market.” Of course, during the period under consideration, China was an overwhelmingly agricultural society. At the same time, as the economic historian Madeleine Zelin notes: “[It] was a place where, by the late Ming dynasty and into the Qing dynasty, there was a proliferation of markets. Approximately eighty percent of the population lived within a day’s journey of a market town and could take some of their produce to the market and become involved in marketing activities.”<sup>14</sup> Historian Timothy Brook suggests the following relationship between the farming economy and the growth of commerce over the three hundred years of Míng rule: “The Ming became a commercial world . . . not . . . despite the . . . agrarian order . . . but . . . because of it. . . . Enhanced production resulted in surplus that went into trade, and the regular circulation of surplus encouraged a move from surplus-production to commodity-production.”<sup>15</sup>

Notably, in contemporary usage, the Chinese word *shìmín* has varied connotations and plays a key role in debates concerning the nature of Chinese modernity (both economic and cultural). Specifically, *shìmín* serves as the translation of a range of terms from “citizen,” to “bourgeois,” to “urban resident.” It is also closely

tied to the Hegelian – and, by extension, Marxist – idea of “civil society” (*bürgerliche Gesellschaft*, Ch. *shìmín shèhuì* 市民社會), as the realm of liberal individualism – i.e. an “abstract ... association [that] is brought about by [individuals’] needs, by the legal system – the means to security of person and property – and by an external organization for attaining their particular and common interests.”<sup>16</sup> Remarks from a 1948 essay by the Japanese Sinologist Takeuchi Yoshimi 竹内好 (1910-1977) make clear the various thought-provoking associations of these terms. Takeuchi writes:

Civil society existed in the Orient [sic, = 東洋] from long ago, prior to the invasion of Europe. The genealogy of bourgeois literature can be traced back to the Song period (and perhaps even to the Tang period). Particularly at the time of the Ming Dynasty, civil rights had in certain respects extended to the point where bourgeois literature was able to forge a type of free man that was virtually akin to the Renaissance man.<sup>17</sup>

Observe that in Takeuchi’s original Japanese the words for “civil society” *shimin shakai*, “bourgeois literature” *shimin bungaku*, and “civil rights” *shimin-ken* are written with the same sinographs – and thus carry similar connotations – in Chinese.

Noteworthy, too, is the broader context in which Takeuchi’s comments occur: an essay entitled “What Is Modernity? (The Case of Japan and China).” In this essay Takeuchi argues for a fundamental distinction between late nineteenth- and early twentieth-century East Asian modernity – the result of Western imperialism – and earlier, indigenous forms of social organization and institutions (evident, for example, in Ming dynasty China and Edo period Japan).<sup>18</sup> Limiting our focus to China, much scholarly energy has been expended on reconstructing the histories of such institutions: from merchant guilds, to native banks, to the evolution of the concept of property rights within the imperial legal system, to forms of knowledge production within the context of Ming-Qing print culture.<sup>19</sup> Although maybe not truly “modern,” this society nevertheless allowed its members certain degrees of “freedom” (Ch. *zìyóu*, Jp. *jiyū* 自由), to use Takeuchi’s word. In turn, the argument goes, such freedom – of movement, of association, of thought, etc. – engendered a spirit of industry and enterprise – something akin, perhaps, to an entrepreneurial ethos – among its population. In accord with this view,



the intellectual historian Yú Yīngshí 余英時 has marshaled significant evidence to suggest a shift, beginning in late sixteenth-century China, in elite attitudes towards commerce and trade as well as a rise in the social status of merchants.<sup>20</sup>

One thinks here, inevitably, of the novel *Jīn Píng Méi* 《金瓶梅》 (*The Plum in the Golden Vase*) and the great late Míng short story collections of Féng Mènglóng 馮夢龍 (1574–1645) and Líng Méngchū 凌濛初 (1580–1644): the *Sān yán* 《三言》 (*Three Words*) and the *Èr pāi* 《二拍》 (*Two Slaps*).<sup>21</sup> Not only are these masterpieces signal products of the great cultural centers of the Jiāngnán 江南 region – the most urban and sophisticated part of the Míng empire; they are also themselves peopled with characteristic *shímín* types. In his study of representations of *shímín* in Míng fiction, the literary scholar Fāng Zhìyuǎn 方志遠 distinguishes the following groups. First, there are the “urban intellectuals,” or “scholars” (*shìrén* 士人), men who use their education and literary talents to earn a living either within or outside of the imperial bureaucracy; consisting of a large number of failed examination candidates, members of this group are just as likely to engage in trade as they are to work as clerks and secretaries to officials. Next, there are the “merchants” (*shāngrén* 商人) and “laborers” (*gōngrén* 工人), individuals with little or no formal education who, engaged in commerce and handicraft industries, form the backbone of the early modern commercial economy. Finally, there are the “courtesans/prostitutes” (*jīnǚ* 妓女) and “vagabonds” (*yóumín* 遊民), people of low social status who inhabit the urban demimonde of tea houses, theaters, and brothels.<sup>22</sup> Tying all of these groups together – and reflecting the expansion of the silver-fueled money economy of the Míng-Qīng period – are complex networks of trade and exchange, in which everything is for sale and everything (and everyone) has a price – or so it often seems.

Of such money economies, the philosopher Georg Simmel (1858-1918) has written: “[They] enforce[] the necessity of continuous mathematical operations in our daily transactions. The lives of many people are absorbed by such evaluating, weighing, calculating and reducing of qualitative values to quantitative ones.”<sup>23</sup> The genius of a novel such as *The Plum in the Golden Vase* is to represent the social anxieties that arise from this state of absorption. While the novel is best known for the promiscuous sexual relations of its protagonist Xīmén Qìng 西門慶, it is just as obsessed with the promiscuous circulation of silver in Xīmén Qìng’s world. Attuned to its anonymous author’s penchant for clever puns and wordplay, readers of *The Plum in the Golden Vase* have often remarked on a parallel in the symbolic economy of the novel between lust (*yín* 淫) and silver (also pro-

nounced *yín* but written with a different character: 銀).<sup>24</sup> As the eminent literary critic Patrick Hanan once noted: “[M]oney is the fabric of the story.”<sup>25</sup> Recently, one scholar has added specificity to this claim: According to his calculations, *The Plum in the Golden Vase* describes no fewer than 456 cash transactions – valued at some 180,000 *taels* of silver – over the course of its 100 chapters. (For some perspective on these figures, a sixteenth-century agricultural manual pegs the per annum wages for a farm laborer at 13 *taels*.)<sup>26</sup> For our present purposes, we should note that, of these 180,000 *taels*, roughly 120,000 – or 67% of the total – relate to business dealings, many of which involve entrepreneurial risk taking of one kind or another.<sup>27</sup>

### *Example One: Something from Nothing*

Ultimately, notwithstanding its scandalous reputation, *The Plum in the Golden Vase* is a morally (and economically) conservative work. From its author’s perspective, both sexual desire and money, in unregulated flow, corrode hierarchy and social stability. To quote Simmel again, it is money that, as “the common denominator of all values[,] . . . hollows out the core of things, their individuality, their specific value, and their incomparability.”<sup>28</sup> Much the same could be said for Ximén Qìng’s voracious carnal appetites. In any event, Simmel’s remarks have a deep resonance with the unyielding sense of “desolation” and “emptiness” (*kōng kōng*) that pervades *The Plum in the Golden Vase*, despite its relentless cataloguing of activity and things.<sup>29</sup> I will return to the moral problem of the individuality and value of “things” (*wù* 物) in my remarks on *Hónglóu mèng* 《紅樓夢》 (*Dream of the Red Chamber*) below.

Right now, however, I would like to look beyond *The Plum in the Golden Vase* and its critique of the money economy to consider an alternate – and substantially more positive – fictional representation of the value-creating possibilities of the Míng-Qīng economic system. Of the numerous tales of entrepreneurial risk-taking and resourcefulness in the corpus of the vernacular literature of this period, a most remarkable example appears in a rather obscure early Qīng collection of short stories called *Zhào shì bēi* 《照世杯》 (*The World-Reflecting Cup*, ca. 1660s). The author of this collection is known to us only by the pseudonym Master of the Zhuóyuán Pavilion 酌元亭主人.<sup>30</sup> The fourth and final story in this collection is entitled “By excavating new cesspits, a skinflint becomes a moneybags” 〈掘新坑慳鬼成財主〉. In it the author prefaces a narrative of intergenerational domes-

tic discord (the details of which need not concern us here) with a brief account of a villager's rise in fortune. To summarize: By converting several rooms of his house into a public cesspit and then selling the collected filth to his neighbors as night soil, Elder Mù 穆太公 (for such is the villager's name) devises a scheme, or "system" (*zhìdù* 制度) (to use his word for it), for extracting profit from shit. To entice people to use his facilities, he has decorated them with pretty pictures and calligraphic scrolls. He also offers the luxury of free toilet paper. In the following excerpt, the episode reaches its droll climax:

Lo and behold! They came, young and old, to admire the new cesspits. . . . Those bumpkins, moreover, liked nothing better than to think they might be getting something for nothing. Thus, when they saw there was [free] toilet paper to be had, they could barely contain themselves, especially since they had only ever before wiped down there with straw and bits of tile. . . . Then, they saw the pretty wall decorations. What wasn't to love! A visit to the new cesspit was like taking in a vision of natural beauty! . . . Next, came the women with their disheveled hair and big feet. "Do you have a women's cesspit?" They asked. So Elder Mù built a new room and dug a new pit exclusively for their convenience and pleasure. Who knew women visitors would outnumber the men? . . . After this, it wasn't long before farmers were at his door to buy [night soil]. For every picul he charged a single copper coin. There were, moreover, those who brought firewood, rice, and oil to exchange with him. Thus, by opening these cesspits, Elder Mù and his family became quite well off.

果然老老幼幼盡來賞鑒新坑 .....。況那鄉間人最愛小便宜。他從來揩不淨的所在，用慣了稻草瓦片，見有現成草紙，怎麼不動火？ .....又且壁上花花綠綠，最惹人看。登一次新坑，就如看一次景致。 .....還有那蓬頭大腳的婆娘來問：「可有女糞坑？」太公又分外蓋起一間屋，掘一個坑，專放婦人進去隨喜。誰知婦人來下顧的比男人更多。 .....一時種田的莊戶，都在他家來躉買。每擔是價銀一錢，更有挑柴、運米、擔油來兌換的。太

公從置糞坑之後，到成個富足的人家。<sup>31</sup>

For its original seventeenth-century readers, I believe, this comic scene was calibrated to provoke a very particular aesthetic response – namely, a feeling of *qí* 奇 in the full panoply of its meaning from “marvelous!” and “original!” to “how strange!” and even “that’s not right!” (i.e. the opposite of *zhèng* 正, or that which is “proper” and “in its appropriate place”).<sup>32</sup> How so? First, the story of Elder Mù’s cesspits is *qí* as a literary artifact. From nothing, the author has accomplished the marvelous – the creation of something: something not only to be read and enjoyed, but also something to be printed, bought, and sold. The author is, in other words, an entrepreneur, trading in originality and filling the demand of his audience for unusual tales. Although, as mentioned above, the identity of the Master of the Zhuóyuán Pavilion is unknown, it nevertheless seems to me not improbable that he may himself have been one of those “urban intellectuals” who, turning away from the examination system and official employment, sought to forge new identities as cultural entrepreneurs in the burgeoning Míng-Qīng commercial economy.

Second, the cesspits and even Elder Mù himself are *qí*, in the sense that they are (it must be admitted) decidedly strange. Through association with the abject – what anthropologist Mary Douglas famously termed “matter out of place”<sup>33</sup> – they present us with an unnerving spectacle (accentuated by the appearance of unruly women), from which readers are only somewhat protected through the workings of parody. Thus, this story reminds us that entrepreneurial energies – such as those embodied, in the fiction, by Elder Mù’s cesspit business and, in reality, by the writing and publishing of vernacular literature – were potentially disruptive of accepted ideas and hierarchies. The social inappropriateness of the upstart merchant Xīmén Qīng – his “out-of-place-ness” – is, after all, a major source of the anxiety that permeates *The Plum in the Golden Vase*. Here it is worth considering just how much the Míng-Qīng aesthetic fascination with *qí* (qua the strange) draws its potency from the socially transformative dynamics of the commercial economy, in which the notion developed.

In this regard, it is Elder Mù’s “system” itself – his *zhìdù* – that is *qí*. Analogous to the text as artifact, this system – the commercial economy in microcosm – also creates something from nothing; and it does so – again, like the text itself – through language. What others call “shit” (*fèn* 糞) Elder Mù calls “precious sludge” (*bǎobèi zhī* 寶貝汁, *bǎobèi* on its own being a word for a treasured

object or possession). In a manner that resembles Táng Tíngshū's phrasebook and his various business ventures, Elder Mù translates and he persuades. His story thus lays bare a basic structure of entrepreneurial narrative: "One man's trash is another man's treasure," as the saying goes. But, that is not enough. To get rich, Elder Mù cannot just collect other people's waste for his own enjoyment. He must represent it to them anew. He must tell them a different story about it. Yes, shit is shit, but, as fertilizer, it is also new life, a commodity of real value, and a source of wealth, not only for Elder Mù, but his customers too.

### *Example Two: Creative Destruction*

Of course, there is something a bit too utopian about this scenario. What happens when the new narrative, at the same time that it creates new value, destroys something of existing value? In other words, how do Míng-Qīng authors construe the ethics of "creative destruction" (*schöpferische Zerstörung*)<sup>34</sup> – an entrepreneurial notion, if there ever was one? To address this question, let us jump from the seventeenth to the eighteenth century and explore some of the details of a well-known episode from *The Dream of the Red Chamber* by Cáo Xuěqīn 曹雪芹 (1715?-1763?). In Chapter 31 of this beloved novel, Jiǎ Bǎoyù 賈寶玉, the young male protagonist, is embroiled in a conflict between two of his maids – Xírén 襲人和 Qíngwén 晴雯. The proximate cause of the drama is a fan, which Qíngwén accidentally damaged by treading on. As the fighting escalates, Bǎoyù, in a fit of pique, threatens to dismiss Qíngwén from his service, a decision that he soon regrets. To mollify Qíngwén's wounded feelings, he then invites her, in a typically flamboyant gesture, to rip as many fans as she likes. She agrees gleefully, claiming that she loves the sound fans make as they are torn. Another maid intrudes and chides them for their wastefulness, and the episode concludes.

Cáo Xuěqīn's focus in these events is, as ever, on the nature of desire. Simply put, although they would be incapable of expressing themselves in these terms, both Xírén and Qíngwén desire to be understood, to be appreciated, and – ultimately – to be *loved* by Bǎoyù. Moreover, it is precisely this perceived "scarcity of love" (to borrow McCloskey's phrase) that instigates their conflict with each other and with their master. "Desire," as the great scholar Wáng Guówéi 王國維 (1877-1927) once wrote in response to *The Dream of the Red Chamber*, "is by its nature boundless, and yet it [always] derives from scarcity." (欲之為性無厭，而其原生於不足。) <sup>35</sup> Undoubtedly, Wáng intended this observation to be a comment

on the philosophical – or, one might say, religious – and psychological nature of Cáo’s masterpiece. It is just as easy, however, to read it as an economic axiom.

In fact, Cáo Xuěqīn seems keenly interested in how the philosophical, psychological, *and* economic aspects of desire intertwine. Consider the fans that play such a pivotal role in the quarrel between Bǎoyù, Xírén, and Qíngwén. As the first half of the title of Chapter 31 – “A torn fan is the price of silver laughter” 撕扇子作千金一笑 – suggests, fan-tearing has meaning as a romantic gesture only insofar as fans have monetary value. To emphasize this point, Cáo goes to great lengths throughout his novel to insert fans – and other such articles that make up the realistic texture of his fictional characters’ material world – into a convincing described system of trade and exchange. In Chapter 67, for example, when Bǎoyù’s older cousin Xuē Pán 薛蟠 returns to Běijīng from a business trip to Sūzhōu, he brings with him trunks filled with all manner of objects, including, of course, fans. Cáo writes: “In the first trunk were mostly materials – silks, satins, brocades and so forth – and various foreign articles of domestic use; . . . [in the other trunk were] writing brushes, ink-sticks, paper, inkstones, different sorts of fancy stationery, purses, rosaries, fans, fan pendants, face-powder, rouge, etc.” (這一箱都是綢緞綾錦洋貨等家常應用之物， . . . [那一箱裏] 卻是些筆、墨、紙、硯，各色箋紙，香袋、香珠、扇子、扇墜、花粉、胭脂等物。) <sup>36</sup>

To gain a sense of what we might term Cáo Xuěqīn’s economic realism, compare this list of commercial goods to those items represented as available in the shops of Sūzhōu in one of the scroll paintings commissioned by the Qiánlóng 乾隆 era emperor (1711-1799, r. 1736-1796) to commemorate his southern tour of the empire in 1751 – i.e. exactly when Cáo was writing his novel: Remarkably, there is an almost one-to-one correspondence, as Figures 1 to 3 demonstrate. Viewing the painting, one can easily imagine that among the merchants and their customers there depicted are Xuē Pán and his agents.



**Figure 1:** *Detail of a stationery store; the sign reads 各色名箋 (Famous stationery in all colors)*



**Figure 2:** *Detail of shops selling satin and brocades; the signs read 漢府貢緞 (Tribute satin from Hanfu) and 八絲宋錦 (Eight-thread Song brocade).*



**Figure 3:** *Detail of stores selling writing brushes; the signs read 狀元名筆 (Famous brushes for prize winning candidates) and 三場名筆 (Famous brushes for sitting the three exam sessions).*

Source of Figures 1 through 3: Xú Yáng 徐揚 (active ca. 1750 – after 1776) and assistants, *The Qianlong Emperor's Southern Inspection Tour, Scroll Six: Entering Suzhou along the Grand Canal, 乾隆南巡圖 (第六卷:大運河至蘇州) 1770, handscroll; ink and color on silk, The Metropolitan Museum of Art. An excellent resource for exploring this work is the website Recording the Grandeur of the Qing, The Metropolitan Museum of Art, Columbia University, Asia for Educators Program of the Weatherhead East Asian Institute & Visual Media Center of the Department of Art History & Archaeology, 2005.*

Social stability and economic flourishing – pillars of the so-called “prosperous age” (*shèngshì* 盛世) of the mid Qīng dynasty – are central themes in this genre of painting, which was intended by emperors such as Qiánlóng and his grandfather Kāngxī 康熙 (1654-1722, r. 1661-1722) before him to immortalize for posterity the achievements of their reigns.<sup>37</sup> Lively scenes of urban life and healthy trade contribute to the creation of the desired effect. A similar impression of stability and prosperity emerges from the repeated descriptions of routine financial transactions in *The Dream of the Red Chamber*. Cáo Xuēqīn’s characters inhabit a fictional world structured by an efficient and sophisticated commercial economy – one that not only embraces the entire empire but also extends well beyond its borders (note the presence of imported goods among the items Xuē Pán purchases in Sūzhōu). In this context fans have a recognized use and an established value. In Chapter 31, however, Bǎoyù’s encouragements to Qíngwén to tear the fans upend this system, revealing, paradoxically perhaps, the unpredictable dynamics of scarcity and desire upon which wealth creation depend.

Devotees of the novel will, of course, recognize unconventional – and, yes, disruptive – behavior as a core component of Bǎoyù’s personality. Elevating this aspect of his character to the mythic plane, Bǎoyù’s own mother famously refers to her son as a “world-confusing demon king” (*hùnsì mómáng* 混世魔王).<sup>38</sup> Here I would like to propose that Bǎoyù’s demonic powers resemble, at least in the episode we are now considering, something akin to what economists term “Schumpeter’s gale.” For readers unfamiliar with this expression, it derives from the work of the Austrian-American economist Joseph Schumpeter (1883-1950). Schumpeter theorized that the “entrepreneur-spirit” (*Unternehmergeist*) consists in the unleashing of a “gale of creative destruction,” the effect of which is to “revolutionize[] the economic structure from within, incessantly destroying the old one, incessantly creating a new one.”<sup>39</sup> He, moreover, cites the identification of “a new quality of [an already existing] good” as an example of this kind of revolutionary innovation.

Already we have seen this kind of innovation at work in the story of Elder Mù’s cesspits, although Elder Mù does not need to destroy anything to create value. In *The Dream of the Red Chamber*, however, Bǎoyù and Qíngwén *do* destroy in order to create. It is for this reason that Shèyuè 麝月, the other maid in the scene, rebukes the pair, admonishing them that their actions will lead to the accumulation of “karmic debt” (*niè* 孽). Premised on the rising popularity of moral account keeping in late Míng and early Qīng China,<sup>40</sup> this warning itself invokes



the “evaluating, weighing, [and] calculating” (following Simmel) of the money economy.

For his part, Bǎoyù offers two rather distinct justifications for his conduct, both of which engage him in the entrepreneurial process of – in the words of the *Harvard Business Review* study – “convince[ing] others to change the way they think, believe[,] or behave.” On the one hand, to Shèyuè, Bǎoyù appeals to the very same procedures of “evaluating, weighing, [and] calculating” that she deploys against him: “How much can a few fans be worth after all?” (幾把扇子，能值幾何？),<sup>41</sup> he asks rhetorically. His point is this: Of minimal value *in themselves*, the fans function as a form of ersatz currency. Once again, the work of Georg Simmel provides useful context. Simmel writes: “Money expresses all qualitative differences of things in terms of ‘how much?’” From this perspective, Bǎoyù’s jǐhé 幾何 – his “how much” – “hollows out the . . . individuality” of the fans with the result that they are no longer fans per se but rather tokens of exchange. Thus, when Qíngwén rips the fans, no value is lost, as their destruction purchases something of equal – indeed, greater – value: her laughter.

On the other hand, in conversation with Qíngwén herself, Bǎoyù offers a considerably different rationalization of their behavior – one that focuses on the use-value, as opposed to exchange-value, of individual objects. He says:

These things are there for our use. What we use them for is a matter of individual whim and desire. For example, fans are made for fanning with; but if you prefer to tear them up because it gives you pleasure, there’s no reason why you shouldn’t. What you mustn’t do is to use them as objects to vent your anger on. It’s the same with plates and cups. Plates and cups are made to put food and drink in. But if you want to smash them on purpose because you like the noise, it’s perfectly all right to do so. As long as you don’t get into a passion and start taking it out on things — that is the golden rule.

這些東西原不過是借人所用，你愛這樣，我愛那樣，各自性情。比如那扇子，原是搨的，你要撕著頑兒也可以使得，只是別生氣時拿他出氣；就如杯盤，原是盛東西的，你歡喜聽那一聲響，就故意砸了，也是使得的，只別在氣頭兒上拿他出氣。這就是愛物了。<sup>42</sup>

One may, of course, read this little speech as a bit of juvenile sophistry typical of a pampered and self-indulgent scion of privilege, as is the protagonist of *The Dream of the Red Chamber*. Even when we take into account Cáo Xuěqīn's tendency to treat with a touch of irony Bǎoyù's attempts at intellectual sophistication, however, these remarks do establish an intriguing ethical framework for considering acts of wealth destruction and creation in the context of early modern China.

The first thing to note here is what we might call Bǎoyù's Schumpeterian attention to the innovative discovery of "new qualities" in already existing goods – e.g. fans, plates, and cups. At the same time, this "entrepreneurial spirit" is firmly grounded in aspects of the Chinese philosophical tradition. In this passage, for example, the influence of Zhuāngzǐ 莊子 (369?–286? BCE) – in whose thought Bǎoyù expresses explicit interest elsewhere in the novel – is especially strong. Briefly, according to Zhuāngzǐ, the perceived quiddity of a "thing" or "object" (*wù* 物) originates, in large measure, from habit and the concretization of habit in language. In Zhuāngzǐ's own words: "A road is made by people walking on it; things are so because they are called so." (道行之而成，物謂之而然。) <sup>43</sup> Similarly, for Bǎoyù, the apparent properties of a fan depend rather more on how it is "used" (*yòng* 用) than on any inherent "nature" it may possess (*wù zhī suǒ rán* 物之所然).<sup>44</sup> The frisson of fan-tearing thus derives from a creative shift in perspective: from the habitual, to the novel; from the use of a fan to fan, to the use of a fan to make a delightful sound. The catch lies in the fact that to enjoy the latter one must destroy the former.

A key question therefore is: How much does Cáo Xuěqīn sympathize with this point of view? In other words, is he satisfied with Bǎoyù's assertion that the world of things exists solely for "our use" (這些東西原不過是借人所用)? Or, do these "things" (both *dōngxi* 東西 and *wù*) have a claim to existence that is somehow independent of human "whim and desire" (你愛這樣，我愛那樣，各自性情)? In this context, it seems crucial that Bǎoyù himself makes two attempts to limit the scope of his argument. First, he insists – however arbitrarily – that one must never tear a fan or break a cup or plate "when in a passion" (在氣頭兒上). Next, and more significantly, he appends to this insistence a suggestive gloss: *ài wù* 愛物 – a phrase that David Hawkes translates in his English version of the text as "the golden rule," but for present purposes I shall render less elegantly, although perhaps more accurately, as "the appropriate care of things/objects."

A well educated Qīng dynasty reader of *The Dream of the Red Chamber* would

have immediately recognized this phrase as a reference to *Mencius* 《孟子》 (7.A.45), in which the philosopher says: “The noble person cares for things [*ài wù*] without being humane [*rén* 仁] toward them and is humane towards the people without being affectionate.” (君子之於物也，愛之而弗仁；於民也，仁之而弗親。) <sup>45</sup> The same reader might have been somewhat surprised by Bǎoyù’s choice of classical reference, given the otherwise more obvious affinity of his argument with the philosophy of Zhuāngzǐ (as discussed above). For this reason, then, its appearance invites further consideration.

On the one hand, of course, Bǎoyù’s allusion to Mencius is little more than a sort of rhetorical legerdemain, whereby the famous “world-confusing demon king” enlists orthodox authority to support unorthodox opinion. Beyond that, it may actually mean very little to our hero. On the other hand, for the perceptive reader, the text’s turn to Mencian philosophy seems to signal a subtle correction to the Zhuāngzǐ-like perspective that use alone determines both the nature and value of an object.

Specifically, in the original passage, Mencius aims to draw a distinction between two kinds of moral regard: 1) the care (*ài*) of things; and 2) the humane treatment (*rén*) of other people. On the surface, this distinction merely reinforces the instrumental status of things: whereas human beings, as ends in themselves, must be treated as such (i.e. “humanely”), things are subject to a different – and lesser – ethic of “care.” Upon closer examination, however, this notion of “care,” particularly as it is defined in the exegetical tradition, entails its own safeguards against the complete instrumentalization of things. As the great Southern Sòng dynasty (1127-1279) philosopher Zhū Xī 朱熹 (1130-1200) writes, “To care [for something] is to gather it up in its season and to use it in moderation.” (愛，謂取之有時，用之有節。) <sup>46</sup> From this perspective, then, things still are primarily “there for our use” (借人所用), as Bǎoyù says; but Bǎoyù is wrong to believe that what we use them for is a matter of indifference. Rather, “the appropriate care of things/objects” establishes definite limits – e.g. of “season” (*shí* 時) and of “moderation” (*jié* 節) – on their consumption. Crucially, moreover, these limits are tied to specific properties of the objects *themselves*. That is to say, these objects exist independent of human “whim and desire.”

If this interpretation is correct, then the fan-tearing episode in *The Dream of the Red Chamber* appears to be more than simply an endearing scene of overwrought teenage emotional conflict that resolves in peels of laughter. Instead, in this deceptively trivial incident, Cáo Xuěqīn demonstrates how his characters are

caught up in an economy of both things and words, the manipulation of which may have far-reaching moral consequences. What is lost through the damaging of a fan? What is gained? Does what is gained outweigh what is lost? Cáo prefers to raise questions rather than to provide answers. All the same, it is intriguing to consider that, through a subtle play on words, he may have hidden an explanation for his reluctance unequivocally to affirm Qíngwén and Bǎoyù's unconventional energies, as the very object they destroy – a fan (*shàn* 扇) – is, in the original Chinese, homophonous with the “moral good” (*shàn* 善).<sup>47</sup> At the very least, Cáo's fiction provides a sophisticated arena in which to consider the moral complexities of creative destruction.

### *Conclusion*

In conclusion: a caveat. The texts that I have discussed in this essay come from different historical, cultural, and linguistic contexts than the one we inhabit at this moment. None, however (or, maybe, therefore), is representative of “the Chinese way” of thinking – an *ignis fatuus* of lazy cross-cultural analysis, the gleam of which blinds rather than illuminates. Let us not forget that these texts have varied voices and complex intellectual lineages. My purpose here has been to show how these voices contribute meaningfully to the humanistic understanding of our lives as economic beings, which unfold – not un-problematically – across local, regional, and global networks, and whereby all of us are united, as John Dewey has said, in a concern for “the occupations and values connected with getting a living.”<sup>48</sup>

*Endnotes*

- 1 Anonymous, untitled preface, in Táng Tíngshū 唐廷樞, Yīngyǔ jíquán 《英語集全》 (*Ying Ü Tsap Ts'ün, or The Chinese-English Instructor*), (Canton, 1862), n.p.
- 2 David M. Levy, "Adam Smith's Rational Choice Linguistics," in David M. Levy, *How the Dismal Science Got Its Name: Classical Economics and the Ur-Text of Racial Politics* (Ann Arbor: The University of Michigan Press, 2001), p. 259.
- 3 Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, ed. R H. Campbell and Andrew S. Skinner (Oxford: Clarendon Press, 1976), p. 26. Note: I am aware that Smith's understanding of animal communication is in need of revision. Non-human primates, for example, are capable of engaging in reciprocal exchanges. On this point, see John C. Mitani, "Reciprocal Exchange in Chimpanzees and Other Primates," in *Cooperation in Primates and Humans: Mechanisms and Evolution*, ed. Peter M. Kappeler and Carel van Schaik (Berlin: Springer, 2006), pp. 107-120.
- 4 Adam Smith, *Lectures on Jurisprudence* (Oxford: Oxford University Press, 1978), p. 352.
- 5 Bill J. Bonnstetter, "New Research: The Skills That Make an Entrepreneur," *Harvard Business Review*, (Harvard Business School Publishing, 7 Dec. 2012), Web. 9 Mar. 2016.
- 6 See for example: Deirdre N. McCloskey, *The Rhetoric of Economics* (Madison, Wis.: University of Wisconsin Press, 1985); "The Rhetoric of Economics," *Journal of Economic Literature* 31 (June 1983): 482-517; and "The Literary Character of Economics," *Daedalus* 113 (3, Summer 1984): 97-119.
- 7 See George Lakoff and Mark Johnson, *Metaphors We Live By* (Chicago: University of Chicago Press, 1980); and Mark Turner, *The Literary Mind: The Origins of Thought and Language* (New York: Oxford University Press, 1996).
- 8 Deirdre N. McCloskey, "Storytelling in Economics," in *Narrative in Culture: The Uses of Storytelling in the Sciences, Philosophy, and Literature*, ed. Christopher Nash (London: Routledge, 1990), pp. 20-21.
- 9 McCloskey, *The Rhetoric of Economics*, p. 21.
- 10 Rudolf G. Wagner, *Joining the Global Public: Word, Image, and City in Early Chinese Newspapers, 1870-1910* (Albany, NY: State University of New York Press, 2007), pp. 61-62.
- 11 David Faure, "A Historical View of Chinese Entrepreneurship," in *Comparative Entrepreneurship Initiatives: Studies in China, Japan and the USA*, ed.

- Chikako Usui (New York: Palgrave Macmillan, 2011), p. 25.
- 12 Rudolf G. Wagner, *Joining the Global Public: Word, Image, and City in Early Chinese Newspapers, 1870-1910*, pp. 60-61.
- 13 For an example of this scholarship, see: Fang Zhiyuan 方志遠, *Ming dài chéngshì yǔ shìmín wénxué 明代城市與市民文學* (Beijing: Zhonghua shu ju, 2004).
- 14 Madeleine Zelin, “The Grandeur of the Qing Economy,” *Recording the Grandeur of the Qing*, The Metropolitan Museum of Art, Columbia University, Asia for Educators Program of the Weatherhead East Asian Institute & Visual Media Center of the Department of Art History & Archaeology, 2005. Web. 8 Mar. 2016.
- 15 Timothy Brook, *The Confusions of Pleasure: Commerce and Culture in Ming China* (Berkeley: University of California Press, 1998), p. 10.
- 16 Georg W. F. Hegel, *Philosophy of Right*, trans. T. M. Knox (Oxford: Oxford University Press, 1952), § 157.
- 17 Takeuchi Yoshimi, “What Is Modernity? (The Case of Japan and China)” in *What Is Modernity?: Writings of Takeuchi Yoshimi*, trans. Richard Calichman (New York, N.Y: Columbia University Press, 2005), p. 54.
- 18 For a version of this argument with regard to the development of business practices in China, see David Faure, “A Historical View of Chinese Entrepreneurship,” pp. 15-35.
- 19 For a general overview, see: Richard Von Glahn, *An Economic History of China: From Antiquity to the Nineteenth Century* (Cambridge: Cambridge University Press, 2015). Since the secondary scholarship on each of the topics mentioned here is voluminous, I merely list one representative study on each subject. Merchant guilds: C. Moll-Murata, “Chinese Guilds from the Seventeenth to the Twentieth Centuries: An Overview,” *International Review of Social History* 53, Supplement 16 (2008): 213-247; native banks: Andrea L. McElderry, *Shanghai Old-Style Banks (ch'ien-chuang), 1800-1935: A Traditional Institution in a Changing Society* (Ann Arbor: Center for Chinese Studies, University of Michigan, 1976); property rights: Thomas Buoye, *Manslaughter, Markets, and Moral Economy: Violent Disputes Over Property Rights in Eighteenth Century China* (Cambridge: Cambridge University Press, 2000); print culture: Cynthia J. Brokaw and Kai-wing Chow, ed., *Printing and Book Culture in Late Imperial China* (Berkeley: University of California Press, 2005).
- 20 Yú Yingshí 余英時, *Zhōngguó jìnshì zōngjiào lúnlǐ yǔ shāngrén jīngshén 中國近世宗教倫理與商人精神* (Taipei: Lianjing chubanshiye gongsi, 1987),

- pp. 104-121.
- 21 The earliest printed edition of *The Plum in the Golden Vase* dates to 1610, although there are references, as early as 1596, to a manuscript version of the novel. The *Three Words* and *Two Slaps* are collective terms. *Three Words* refers to Féng Mènglóng's three short story collection – 《喻世明言》 (*Stories to Enlighten the World*, 1620; originally titled 《古今小說》 [*Stories Old and New*]), 《警世通言》 (*Stories to Caution the World*, 1624), and 《醒世恒言》 (*Stories to Awaken the World*, 1627); *Two Slaps* refers to Líng Méngchū's two short story collections – 《初刻拍案惊奇》 (*Slapping the Table in Amazement, First Collection*, 1628) and 《二刻拍案惊奇》 (*Slapping the Table in Amazement, Second Collection*, 1632).
  - 22 Fang Zhiyuan 方志遠, *Míng dài chéngshì yǔ shì mǐn wénxué* 明代城市與市民文學, pp. ??
  - 23 Georg Simmel, *The Philosophy of Money*, trans. Tom Bottomore and David Frisby (London: Routledge, 1990), p. 444.
  - 24 Katherine Carlitz, "Puns and Puzzles in the *Chin P'ing Mei*: A Look at Chapter 27," *T'oung Pao* 67.3-5 (1981): 232-233.
  - 25 Patrick Hanan, "A Landmark of the Chinese Novel," *University of Toronto Quarterly* 30.3 (April 1961): 330.
  - 26 Denis C. Twitchett and Frederick W. Mote, *The Cambridge History of China, Volume 8, Part 2* (Cambridge: Cambridge University Press, 1998), p. 544. The manual in question is the *Bǔ nóng shū* 《補農書》 by Zhāng Lǚxiáng 張履祥 (1611~1674).
  - 27 Zhèng Tiěshēng 鄭鐵生, "Jīn Píng Měi yǔ bái yín huò bì huà" 《金瓶梅》與白銀貨幣話, in *Míng Qīng xiǎoshuō yánjiū* 明清小說研究 86.4 (2007): 267-279.
  - 28 Georg Simmel, "The Metropolis and Mental Life," in *The Sociology of Georg Simmel*, trans. Kurt H. Wolff (Glencoe, Ill.: The Free Press, 1950) p. 414.
  - 29 Andrew Plaks, *The Four Masterworks of the Ming Novel: Ssu Ta Ch'i-Shu* (Princeton: Princeton University Press, 1987), pp. 178-179.
  - 30 For a brief critical assessment of this text, see Patrick Hanan, *The Chinese Vernacular Story* (Cambridge, Mass.: Harvard University Press, 1981), pp. 187-190.
  - 31 *Zhào shì bēi* 《照世杯》. reprint in *Gǔběn xiǎoshuō jíchéng* 古本小說集成, vol. 332 (Shanghai: Shanghai guji chubanshe, 1990), pp. 237-238.
  - 32 On the *qí* as an aesthetic category, see Judith Zeitlin, *Historian of the Strange: Pu Songling and the Chinese Classical Tale* (Stanford: Stanford University Press, 1993), especially pp. 5-6. See also the extensive treatment of this

- concept in the art-historical context in Katharine P. Burnett, *Dimensions of Originality: Essays on Seventeenth-Century Chinese Art Theory and Criticism* (Hong Kong: Chinese University Press, 2013).
- 33 Mary Douglas, *Purity and Danger: An Analysis of Concepts of Pollution and Taboo* (London: Routledge and Kegan Paul, 1966).
- 34 On the origins of this term in late eighteenth- and nineteenth-century German literary and intellectual history, see Hugo Reinert and Erik S. Reinert, “Creative Destruction: Nietzsche, Sombart, Schumpeter,” in *Friedrich Nietzsche 1844-2000: Economy and Society*, eds. Jürgen Backhaus and Wolfgang Drechsler (New York: Springer, 2006), pp. 55-85.
- 35 Wáng Guówéi 王國維, “*Hónglóu mèng pínglùn*” 《紅樓夢》評論, in *Wáng Guówéi quán jí* 王國維全集 (Hangzhou: Zhejiang jiaoyu chubanshe, 2009), vol. 1, p. 55.
- 36 Cao Xueqin. *The Story of the Stone: Volume 3, The Warning Voice*, trans. David Hawkes (Harmondsworth: Penguin Books, 1980) p. 311 (translation slightly modified); Cáo Xuěqīn 曹雪芹. *Bā jiā píngpī Hónglóu mèng* 八家評批紅樓夢. ed. Féng Qíyōng 馮其庸, et. al. 3 vol. (Beijing: Wenhua yishu chubanshe, 1991), vol. 2, p. 1653.
- 37 Maxwell K. Hearn, “Art Creates History: Wang Hui and *The Kangxi Emperor’s Southern Inspection Tour*,” in Wen C. Fong, Chin-Sung Chang, and Maxwell K. Hearn, *Landscapes Clear and Radiant: The Art of Wang Hui (1632-1717)* (New York: The Metropolitan Museum of Art, 2008), pp. 129-183.
- 38 Cáo Xuěqīn 曹雪芹. *Bā jiā píngpī Hónglóu mèng* 八家評批紅樓夢. ed. Féng Qíyōng 馮其庸, et. al., vol. 1, p. 69.
- 39 Joseph A. Schumpeter, *Capitalism, Socialism, and Democracy* (London: Unwin, 1941) pp. 82-83.
- 40 On the relation of this phenomenon to social and economic factors, see Cynthia J. Brokaw, *The Ledgers of Merit and Demerit: Social Change and Moral Order in Late Imperial China* (Princeton: Princeton University Press, 2014 [1991]).
- 41 Cáo Xuěqīn 曹雪芹. *Bā jiā píngpī Hónglóu mèng* 八家評批紅樓夢. ed. Féng Qíyōng 馮其庸, et. al., vol. 1, p. 743.
- 42 Cao Xueqin. *The Story of the Stone: Volume 2, The Crab-Flower Club*, trans. David Hawkes (Harmondsworth: Penguin Books, 1977) p. 116 (translation slightly modified); Cáo Xuěqīn 曹雪芹. *Bā jiā píngpī Hónglóu mèng* 八家評批紅樓夢. ed. Féng Qíyōng 馮其庸, et. al., vol. 1, p. 742.
- 43 *The Complete Works of Zhuangzi*, trans. Burton Watson (New York: Columbia University Press, 2013), p. 11; *Zhuāngzǐ jí shì* 莊子集釋. ed. Guō Qìngfān



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- 郭慶藩, et al. 3 vol. (Beijing: Zhonghua shu ju, 1961), p. 69.
- 44 The phrase物之所然 comes from Guō Xiàng's郭象 (252-312) commentary to Zhuāngzǐ.
- 45 *Mencius*, trans. Irene Bloom (New York: Columbia University Press, 2009), p. 155 (translation slightly modified); Mèngzǐ jízhù孟子集注 (Shanghai: Shanghai guji chubanshe, 1991), p. 109.
- 46 Zhū Xǐ's comment to *Mencius* (7.A.45). See Mèngzǐ jízhù孟子集注 (Shanghai: Shanghai guji chubanshe, 1991), p. 109.
- 47 This pun is suggested by Zhāng Xīnzhī张新之 (1828-1850) in his commentary on *The Dream of the Red Chamber*.
- 48 *John Dewey, Democracy and Education: An Introduction to the Philosophy of Education* (New York: Macmillan, 1922 [1916]), p. 253.

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