



Institutional Adaptability in China: Local Developmental Models Under Changing Economic Conditions

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Summary. — Distinct patterns of regional development have emerged in China's political economy since the initiation of economic reforms in late 1970s. In particular, the localities of Suzhou, Wenzhou, and Dongguan each achieved dramatic economic growth during the first three decades of reform, earning them national reputations as developmental “models” for other cities in China to recognize and emulate. However, the local states of Suzhou, Wenzhou, and Dongguan responded differentially to changing conditions in the broader domestic and global economy; and the global financial crisis at the end of the 2000s affected the three localities with varying levels of severity. This article thus seeks to explain why previously well-performing developmental models diverged in their performance and capacity to recover from a major economic shock. Drawing on national economic census data, in-depth field interviews, and relevant secondary literature, we argue that variation in the institutional adaptability of Suzhou, Wenzhou, and Dongguan throughout the course of their developmental experiences had a defining effect on how these cities fared during the financial crisis. The process-tracing case studies reveal that a locality's ability to adjust to changing market conditions may be conditioned by structural endowments, but ultimately hinges on agent-centric factors, including *motivated and capable local leadership*, *openness to new policy ideas*, and *state capacity for policy implementation*. Ultimately, our analysis makes the broader observation that in a dynamic environment, factors that promote economic success at one point can become barriers later on. Hence, exploring a region's institutional adaptability and identifying the factors that facilitate or impede such adaptability in local economic governance provides a more nuanced means for understanding a locality's evolving developmental patterns and performance—during normal times, as well as more challenging periods.
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“We have always followed Beijing's directions.”

[Suzhou, Private entrepreneur]

“I have only heard local officials shout slogans, but never seen them actually invest in human capital.”

[Wenzhou, Private entrepreneur]

“More and more foreign companies have moved to other places like Kunshan, Suzhou. We are no longer attractive to them now.”

[Dongguan, Local official]

1. INTRODUCTION

Since the late 1970, China's political economy has been distinguished by its decentralized and experimental approach to reforming socialist-era institutions (Naughton, 1995). This relatively permissive policy stance facilitated the emergence of distinct patterns of regional development. In particular, the localities of Suzhou, Wenzhou, and Dongguan each achieved dramatic economic growth over the first three decades of reform, earning them national reputations as “models” for other cities of China to recognize and emulate (see Table 1). Suzhou developed vibrant township and village enterprises (TVEs), and further enhanced its competitive status through the creation of special economic zones and high-technology parks. Initially impoverished during the Mao era, Wenzhou's developmental path became known for its vibrant private sector when the political status of profit-making activities was still highly controversial (Parris, 1993; Tsai, 2006). Dongguan, located between Hong Kong and Guangzhou, developed an export-oriented manufacturing economy by attracting large amounts of foreign direct investment (FDI). Until the global financial crisis, all three localities yielded growth rates that

were more than double the national average of 8.1% (during 1978–2004) (WSB, 2005). However, the local states of Suzhou, Wenzhou, and Dongguan responded differentially to changing market conditions, and the economic downturn at the end of the 2000s affected the three localities with varying levels of severity.¹ This paper thus seeks to explain why previously well-performing developmental models diverged in their performance and capacity to recover from a major economic shock. In so doing, it traces the reform-era developmental paths of the three localities based on both primary and secondary sources. We also conducted fieldwork by interviewing private entrepreneurs and local officials from different bureaucracies (See Appendix A).

This paper argues that variation in the institutional adaptability of local governments throughout their developmental experiences proved to be a key indicator of how well the respective cities weathered the global financial crisis. Existing explanations for variation in institutional adaptability may be divided into those that emphasize structural versus agent-centric factors. Conventional structural variables include: (1) *natural endowments and historical legacies*; (2) *external resources and opportunities*; and (3) *fiscal conditions*. The agent-centric variables include the following attributes of local leadership and administration: (1) *highly motivated and capable leadership*; (2) *openness to new policy ideas*; and (3) *state capacity for policy implementation*. While acknowledging the relevance of structural conditions, this study highlights the role of agent-centric factors in mediating, and even redirecting pre-existing developmental patterns. Localities demonstrating greater institutional adaptability tend to have ambitious leaders who are well educated and have a progressive outlook

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Table 1. *Developmental characteristics of Suzhou, Wenzhou, and Dongguan*

Locality	Period	Local economy	State–business relationship	Central–local relationship	Type of capital
Suzhou, Jiangsu Province	1980s	Dominated by TVEs and strong collective sector	Local state-led macroeconomic planning	More central-oriented	State and foreign capital
	1990s	Privatization of TVEs and attraction of FDI	Strong local state intervention and stronger social safety net		
Wenzhou, Zhejiang Province	1980s	Dominated by private household factories	Minimal state intervention	More independent and autonomous	Mainly domestic capital
	1990s	Small commodities with more out-migration	More state intervention, planning, and regulation		
Dongguan, Guangdong Province	1980s	Small-scale manufacturing	Close relationship between levels of local state and business	More independent and localized	Mainly overseas Chinese capital
	1990s	Promotion of export-oriented development	More centralized city-level government		

toward developmental strategies, along with the administrative capacity to implement local developmental policies. Leaders in such localities are also more willing to mobilize resources from higher levels of government, and are more likely to be promoted.

The paper proceeds as follows. The first section situates our analysis of local governmental adaptability in the literature on institutional development. We argue that state capacity to adjust to a dynamic economic environment ultimately depends on the agency of local leaders even though structural endowments may condition their policy options. The subsequent sections trace the developmental paths and patterns of institutional adaptability in Suzhou, Wenzhou, and Dongguan, respectively. We then compare the factors accounting for variation in institutional adaptability among the three localities. Each locality established a distinct area of comparative advantage at the outset of reform, which yielded impressive growth rates. Over time, however, they diverged in adaptability to changing conditions in the broader domestic and global economy. Suzhou shifted its priorities to fostering technology-intensive industries prior to the crisis; Wenzhou persisted in its original economic model; and Dongguan attempted belated reforms. We conclude with the caveat that policies associated with growth during a particular period do not guarantee continued success later on, as market conditions shift during the very process of economic development.

2. EXPLAINING INSTITUTIONAL ADAPTABILITY

By definition, “institutional adaptability” has a normatively positive connotation, but what are the sources of such adaptability? The late economic historian and institutionalist, Douglass North (1990, 2005), noted the importance of *adaptive capacity* in his explanation of developmental success, arguing that adaptive capacity facilitated by formal and informal institutions enables actors to experiment with a broad spectrum of options in both political and economic systems. Richardson and Bogart (2008) depict Great Britain’s adaptability in property-rights institutions as a response to the will of the people in fostering economic development during 1700–1830. From an alternative perspective, Nassim Taleb (2010) explores the concept of *adaptive governance* and contends that variations in innovative strength result not from systemic features, but from the opportunities provided through “maximum tinkering.” Such tinkering may occur in non-democracies as long as rulers encourage openness to exploring a wide range

of plausible alternatives among its institutions, processes, and actors.

Taleb’s insight holds particular relevance to China given that its experimental approach to reform reconfigured the country’s socialist political economy within the span of just a few decades. During the 1970s, profit-making activities were illegal, China’s economy was closed to foreign trade and investment, and internal migration/labor mobility was highly restricted. By the 1990s, those key constraints to market-oriented development had been reversed: the private sector was legalized and thriving, China became one of the world’s leading destinations of FDI, and hundreds of millions of rural migrants were working in its cities. Incremental reforms generated unexpected economic transformation.

Within this national macroeconomic context of economic liberalization, localities have exhibited remarkable diversity in their developmental patterns and capacity for institutional adaptation. One of the recurrent themes in studies of China’s political economy is that the interests and policy priorities of central and local governments are not always aligned. Breznitz and Murphree (2011) describe this tension in central-local relations as “structured uncertainty.” This uncertainty has enabled local adaptation of ambiguous central mandates to build an innovation economy through “trial and error based experimentation (p. 19).” Along similar lines, Chen (2014) finds that the choice of global business allies by local governments affected the manner in which domestic firms pursue industrial upgrading, leading to varying levels of success. In a broader analysis of local developmental paths during the reform era, Ang (2016) contends that industrial growth and bureaucratic capacity has occurred in a coevolutionary, rather than sequential manner. Furthermore, local variation in developmental resources and trajectories exhibits a “domestic flying geese pattern,” whereby coastal localities that attracted foreign direct investment earlier in the reform era, now represent a domestic source of investment for interior regions. Unlike Ang’s structured approach, however, this paper advances an agent-centric perspective to explain variation in institutional adaptability, and in turn, divergent economic performance during different stages of development.

Beyond the literature on China’s contemporary political economy, our emphasis on agency departs from conventional explanations for cross-national or regional variation in development. In institutional analysis, the concept of path dependence has generated considerable attention and refinement. Pierson (2000), for example, characterizes path dependence as “social processes that exhibit increasing returns (p. 252).”

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