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Ten general principles**

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# Redefining Beijing Consensus: Ten general principles

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## Abstract

We argue, due to the conspicuous failure of Washington Consensus-guided reforms in most part of the developing world in 1990s and the outbreak of the current global financial crisis, Washington Consensus, as a general term of the neoliberal free market economic thinking, has been withering. In the meantime, Chinese economic model has gain wide recognition and praise worldwide. Joshua C. Ramo coined the term of Beijing Consensus as an alternative approach to economic development for developing nations. There has been hot debate on the notion of Beijing Consensus. We argue even though there are some problems in Ramo's original definition of Beijing Consensus, we should not reject this notion altogether. Instead, we should try to come up with better conceptualizations of this term. In this paper, we sum up ten general principles of the Chinese development model as our new definition of the Beijing Consensus.

**Keywords:** *Washington consensus, Beijing consensus, China, development model, economic reform.*

## 1. The fall of the Washington Consensus

In the 1960s and 70s, in order to finance their ambitious industrialization, many Latin American countries, notably Brazil, Argentina, and Mexico, borrowed hugely from international creditors, much of which were short-term loans. When the accumulation of their foreign debts reached a dangerous level at the end of 70s, the world economy went into a serious recession during 1979-1982, in which, recorded high interest rates in the US and Europe made Latin America's debt payments unbearable. In August 1982, Mexico declared a moratorium on debt service, which within weeks caused the whole region immersed in later we call the debt crisis. Since then, Latin America has had a 'lost decade': although different efforts were made, they had not succeeded in either reducing foreign debt or growing their way out of debt (Vásquez, 1996).

In 1989, when George H. W. Bush became the US president, his Treasury Secretary Nicholas Brady announced a new plan to resolve the debt crisis, which urged Latin American debtor countries to implement market liberalizations in exchange for a 'voluntary' reduction of the commercial bank debts (Vásquez, 1996). In order to understand to what extent Latin American policy reforms were being implemented, a conference under the title 'Latin American adjustment: How much has happened?' was convened by the Institute for International Economics in November 1989 (Kuczynski, 2003). As the organizer of this conference, John Williamson wrote a background paper 'What Washington means by policy reform' to guide the commissioned country studies of individual Latin American debtor countries. In this paper, Williamson laid out ten major policy reforms he believed to have reached 'a reasonable degree of consensus' in Washington as needed to restore Latin American economic growth (Williamson, 1990).

The list of ten policy recommendations that was termed by Williamson as 'Washington consensus' included fiscal discipline, reordering public expenditure priorities, tax reform, liberalizing interest rates, a competitive exchange rate, trade liberalization, liberalization of inward foreign direct investment, privatization, deregulation and property rights (Williamson, 2004). However, as Williamson later lamented that the concept of Washington Consensus had

become 'public property' (Williamson, 2000:252) and 'has been used to mean very different things by different people' (Williamson, 2004). He identified two versions that are very different from his original Washington Consensus. One version refers to the policies the Bretton Woods institutions applied towards their client countries, or perhaps the attitude of the US government plus the Bretton Woods institutions (i.e., the International Monetary Fund (IMF) and the World Bank). Another version uses Washington Consensus as a synonym for neo-liberalism or market fundamentalism (Williamson, 2004).

Williamson pointed out in the early days after 1989 there was not much difference between Bretton Woods Institutions policy package applied to their client countries and his original concept of Washington Consensus. But overtime their policy package deviated substantively, for instance, their adoption of a bipolar doctrine of exchange rate, according to which countries should either float their exchange rate cleanly or else fix it firmly, is directly counter to Williamson's original call for a competitive exchange rate implying an intermediate regime. Another terrible deviation Williamson singled out is that Bretton Woods institutions, or at least the IMF, came in the mid-1990s to urge client countries to liberalize their capital accounts, which, Williamson believes, bears the major responsibility for causing the Asian financial Crisis of 1997. With the disastrous performance of the 'Shock Therapy' reforms in Eastern European and former Soviet Union countries (EEFSU) in 1990s, strongly advocated by the US Treasury and IMF, Bretton Woods institutions' version of Washington Consensus was widely discredited.

Williamson regards the association of Washington Consensus with neo-liberalism or market fundamentalism as 'a thoroughly objectionable perversion' of his original version (Williamson, 2004) because neither he included most of the neoliberal innovations of the Reagan administration in the US and Thatcher government in the UK, except privatization, nor he believes that any of those distinctively neoliberal policies, such as supply-side economics, monetarism, and minimal government, commanded much of a consensus (Williamson, 2004). However, the association of Washington Consensus with neo-liberalism or free market economics eventually has become the most widespread usage of the

term. The current global financial crisis rooted in the US is widely seen to have announced the fall of the free market or neo-liberal economics. Following the 2009 G-20 London summit, British Prime Minister Gordon Brown declared 'the Washington Consensus is over'. Williamson believes Brown's critique on Washington Consensus actually refers to this neoliberal reinterpretation, rather than his original version (Williamson, 2009).

Even John Williamson has repeatedly defended his original version of Washington Consensus as 'motherhood and apple pie', he recognizes 'the disappointing performance of many countries that made a conscientious attempt to implement the sort of reform agenda' of his original Washington Consensus and he has identified three defects in his formula: first, his original Washington Consensus did not emphasize crisis avoidance; second, there is incompleteness in his original reform agenda and a second-generation of reforms is needed; third, the objective that underlay the original Washington Consensus was excessively narrow (Williamson, 2002). No matter which version of Washington Consensus people use, Harvard professor Dani Rodrik (2006) has argued that 'the debate now is not over whether the Washington Consensus is dead or alive, but over what will replace it'.

## **2. The debate of the Beijing Consensus**

Among those critics of Washington Consensus, Joseph Stiglitz, a Nobel Prize winning economist, may be the most famous one. In 1998, as the chief economist of the World Bank, Stiglitz criticized 'the policies advanced by the Washington consensus are not complete, and they are sometimes misguided' and called for a 'post-Washington consensus' (Stiglitz, 1998).

China's phenomenal economic growth since its reform and opening up and the sharp contrast to the disappointing performance of most part of the developing world in 1990s (World Bank, 2005) makes China's development model distinctive and attractive. In 2004, a British think tank the Foreign Policy Centre published a paper titled 'The Beijing Consensus', the author Joshua Cooper Ramo, a former editor of Time magazine, argues that China's rise is remaking the international order and what is happening in China is not only a

model for China, but a path for other nations around the world. At the heart of his conceptualization of the Beijing Consensus, which Ramo claimed to replace the widely-discredited Washington Consensus, are three theorems: first, innovation-based development; second, giving sustainability and equality priority; third, self-determination in international relations.

Given China's success and increasing influence, the notion of Beijing Consensus, once created, has generated widespread attention in China and beyond. Many people see Chinese model distinctive and successful and therefore representing an alternative way of development. China's economic miracle is now something that many countries in Africa, Latin America and other parts of Asia would like to emulate (Colley, 2009). Leaders of Vietnam, India, Russia, Iran, Brazil, among others, have shown interests in 'Beijing Consensus' (Huang and Ding, 2006: 29). Professor David Schweickart of Loyola University Chicago even argues that 'of all the countries in the world today, China is one of the best situated to make the transition to' what he terms 'Economic Democracy', a viable, equitable market socialist society beyond capitalism featuring workplace democracy and social control of investment (Schweickart, 2005).

While many people highly praise Chinese experience, many others have expressed their disagreements of the concept of Beijing Consensus. There are five major arguments. First of all, Chinese development model has many problems (Dirlik, 2006), such as high consumption of energy and resources, environmental pollution, income disparity, regional disparity, corruption, etc. Secondly, China's success has many China-specific conditions others do not have, such as abundant rural labor and overseas Chinese who contributed much initial FDI to China, so China's success cannot be easily duplicated. Thirdly, China does not have a step-by-step plan in its reform so there is no consensus at all (cf. Huang, 2005). Fourthly, some people argue the essence of the Beijing Consensus is authoritarian government plus market economy (Nye, 2005). Since regime theory holds that authoritarian systems are inherently fragile (Nathan, 2003: 6), some people believe the rule of the Chinese Communist Party (CCP) may collapse. Thus, the Beijing Consensus cannot

replay the Washington Consensus. Finally, some people argue Ramo's conceptualization of Beijing Consensus is 'relatively incoherent and largely inaccurate (Kennedy, 2008: 10).

We disagree with above arguments. For the charge that Chinese model is flawed, we support Colley's (2009) viewpoint that many people (especially in the West) tend to see China's development as a glass half empty or largely focus on the negative aspects of China's development. Admittedly, there are many serious challenges facing China, but they are problems of the development process. No country can grow without problems. It is not easy to have made such a progress in a short period for a country like China with a 1.3bn population and starting from a very poor basis. Moreover, Chinese leaders have been aware of these problems and switching to a more scientific development strategy. Colley (2009) pointed out 'when Chinese leader like Wen Jiabao talk of "putting people first" and developing a "harmonious society" they tend to mean it'.

It is a fact that China has some unique initial conditions; however, people may have overstated their contribution to the success of China's reform. We believe the more important is the way China has been reforming its economy. For instance, most economists have finally realized that political stability is crucial for a successful economic transition and that prudential financial reform is much better than a 'big bang' financial liberalization, which are part of the Chinese experience and significant contribution to economic thinking. Therefore, even without the similar initial conditions, developing countries can still learn something really valuable from China, albeit a duplicated success cannot be guaranteed.

It is also not precise to say China does not have a step-by-step plan in its reform, in two ways. For one thing, it is impossible for businesses to make detailed action plans, needless to say for a country. But this does not mean there is no plan at all. In fact, China regularly make five-year plan, ten-year plan, and long-rang plan. For another, people like to quote Deng Xiaoping's famous saying 'crossing the river by groping the stones' to prove China does not have

any plan. In fact, China did rely on trial and error at the early stage of its reform due to lack of experience, but Chinese leaders have gradually reached a common vision and grand strategy which was made national guiding policy – building a socialist market economy with Chinese characteristics. We believe, even if there were a step-by-step plan in China, no country should blindly copy it. One important experience from China has been that a country should adapt any best practice to its own conditions.

It is true that China is an authoritarian regime because China is still a party-state in which the CCP penetrates all other institutions and makes policy for all realms of action (Nathan, 2003: 13). However, as Nathan (2003) has clearly illustrated that, by institutionalizing norm-bound succession practice, meritocracy-based promotion and institutional differentiation with the regime, Chinese authoritarian system has proven to be resilient, therefore it is too-hasty to argue that Chinese regime cannot adapt and survive. Nathan (2003) even argues the Chinese case may suggest that authoritarianism is a viable regime form even under conditions of advanced modernization and integration with the global economy. We share this prospect. In the mean time, we also share Zhao's (2004) viewpoint that Beijing Consensus should be a complement rather than a substitution to the Washington Consensus. Williamson (2009) rightly points out 'most of the governments of the world seem to be determined to follow the precepts originally enshrined in my ten points under the Washington Consensus heading, irrespective of the ritual condemnations by their leaders'. We appreciate that the original Washington Consensus represents conditions under which a mature economy can operate more efficiently. Then, the Beijing Consensus can provide a viable route towards there. This is the value of the Beijing Consensus, i.e., enriching our thinking on development economics.

We agree that Ramo's conceptualization of Beijing Consensus has some problems. On the one hand, his three 'theorems' are not accurate. Clearly, China is not yet an innovative country and China's economic success has not been innovation-driven so far, although Chinese leaders have long realized innovation is very important and made efforts to build its national innovation system (OECD, 2007). On the other, its three 'theorems' do not parallel those

ten policy reforms of the original Washington Consensus (Kennedy, 2005: 10). Williamson's Washington Consensus is only about economic reform while the third theorem of Ramo's Beijing Consensus, using asymmetric power projection to achieve global balance of power, is according to himself 'a new security doctrine'. The fact that the term consensus has a hegemonic connotation (Dirlik, 2006) is because the Washington Consensus was put forward deliberately and systematically (Wu, 2005). As China has repeatedly promised to rise peacefully and not to pursue hegemony and Chinese government does not say much on exporting China's developmental model (Colley, 2009), we think Ramo's third theorem can hardly achieve a consensus in Beijing and should not be promoted as something the developing country can learn.

We believe the flaws of the original conceptualization of Beijing Consensus should not be used to justify the rejection of the notion altogether. What we need to do is instead to come up with a sound new configuration. We intend to contribute to the redefining the concept in this paper. In the following section, we lay out ten general principles that we believe command a moderate degree of consensus in Beijing. We acknowledge there might be more factors than these ten principles that have contributed to Chinese success, but we believe these ten principles are more widely accepted and represent more general policies rather than China-specific or technical factors. We are also very aware that these ten principles should be viewed as a flexible guidance rather than rigid recipe for any other country to copy. At the end of the day, what really makes a difference is how a country creatively adapts the best practice learned from other place to its own national situations.

### **3. Ten principles as the Beijing Consensus**

#### **Principle one: Localization of best practices borrowed**

Chinese leaders firmly believe that, due to the different stages of development, developing nations face very different conditions and many constraints in economic construction, compared with developed countries (and differences also exist within developing world), therefore, any textbook

economic theories and other countries' experiences should be adapted to their local situations, rather than copied without caution. Blindly imitating the so-called best-practice theories and policies without taking local conditions into consideration may result in unexpected outcomes.

During Mao Zedong's era, Chinese leaders were aware of this localization or adaptation principle. Mao himself wrote an important policy paper 'On Ten Great Relationships' in 1956 to warn his Party not to blindly imitate but to adapt Stalinist model to Chinese domestic conditions. Some scholars argue that due to this cautious approach China adopted an M-Form<sup>1</sup> (Qian and Xu, 1993; Yusuf, 1994: 75) instead of Soviet U-Form economic administration structure, and therefore Chinese local governments had much autonomy and incentive in building their local economies. This facilitated a fairly rapid GDP growth even with the political disorder and disrupt during the ten-year Cultural Revolution.

This adaptation thinking is also evident in post-Mao reform and opening up. Although being called by Mao as 'the number two top leader walking the capitalist road in the Party', Deng Xiaoping from the beginning of his reform rejected the idea of wholesale westernization and firmly chose a strategy suitable to China's real conditions, thereby successfully avoiding the disastrous failure of the Shock Therapy reform the EEFSU had suffered. Jiang Zemin and Hu Jintao also followed this principle consistently. Although the general direction of China's reform after Deng is moving towards a liberal market economy, as many scholars have pointed out, Chinese socio-economic system has always kept its own characteristics.

This very first principle of localization clearly indicates that the Beijing Consensus is fundamentally different from the Washington Consensus in that China does not promote universal application of its development model and therefore China does not pursue hegemonic power of the Beijing Consensus vis-à-vis the Washington Consensus.

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<sup>1</sup> M-form and U-form are concepts of Organization Theory. In M-form organization, there are multiple autonomous divisions and the headquarter does not interfere much in the decision-making of individual divisions. In U-form organization, the general manager exerts tight control through different functions, like finance, sales, operations, and marketing, etc.

## **Principle two: Combination of market and plan**

Every nation should not be fettered by extreme ideology, i.e., free-market capitalism or fully-planned communism, in its economic construction. Any economy inevitably is or should be a mixed one in which both market and plan have a role to play. Either market or plan in isolation will ultimately fail due to information asymmetry<sup>2</sup> and economic calculation problem<sup>3</sup>. Greenwald and Stiglitz (1986) argue that it is only under exceptional circumstances that markets are efficient. Stiglitz (2002) also recognizes that the government is not always able to correct the limitations of markets. Therefore, the remedy to the doomed failure is to find the right balance between the market and government, i.e., a combination of market and plan.

The essence of using market is to induce competition for an efficient allocation of resources and effective mechanism of survival of the fittest. It is for this purpose that Deng Xiaoping made the decision of opening China up to the world and returning to the GATT and later joining the WTO. One key success factor of China's market reform and opening up is the sequence and emphasis of liberalization and competition. It is obviously important to import investment and technology while giving proper degree of protection to some strategically important industries, such as financial industry and agriculture.

Mao and especially the Gang of Four tried to completely abolish the market mechanism as they saw it as an attachment of capitalism. An extreme example of this purely Communist thinking was to put all people into People's Communes where the central administration of the Commune had the power to decide everything concerning the life and work of commune members. With its huge failure, Deng Xiaoping realized that it was meaningless and misleading to debate whether a policy is capitalist or socialist and the final judgment should be 'the Three Helpfuls', i.e., whether such a policy is helpful for developing

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<sup>2</sup> In 2001, the Nobel Prize in Economics was awarded to George Akerlof, Michael Spence, and Joseph E. Stiglitz 'for their analyses of markets with asymmetric information'. Source: [http://en.wikipedia.org/wiki/Information\\_asymmetry](http://en.wikipedia.org/wiki/Information_asymmetry)

<sup>3</sup> Hayek (1944) argues that central planners will never have enough information to carry out resource allocation reliably. Source: [http://en.wikipedia.org/wiki/Economic\\_calculation\\_problem](http://en.wikipedia.org/wiki/Economic_calculation_problem)

socialist productivity, for enhancing socialist comprehensive national power, and for improving people's living standard<sup>4</sup>.

On the other hand, free-market economy evidently failed in 1930s's Great Depression. In helping to understand and overcome the crisis, the Keynesian Revolution of economics helped the world to appreciate that macroeconomic intervention is necessary at some point in time and in some economic context. The most recent lesson we had of blindly believing 'free-market will maximize public welfare' (Adam Smith's (1776) 'invisible hand' theory) is the global financial crisis caused by the US credit crisis. The US 700bn bailout plan and a called-for global coordinated rescue plan once again prove government planning and market mechanism are both viable and necessary.

Chen Yun once used his by now famous bird cage allegory to describe the desired relationship between plan and market in Chinese economic development trajectory (Brødsgaard, 1991). According to Chen Yun the plan is the cage and the market the bird in the cage. If the cage is too tight the bird cannot move and will eventually suffocate. If there is no cage the bird will fly away. Chen Yun used his position as the second most important leader in China, only next to Deng Xiaoping during the 1980s and 1990s, to push for a reform of 'caged marketization', which proved to be prudential and successful.

### **Principle three: Flexible means to a common end**

Western economic theories and policies have their merits, but they are based on the better conditions of developed markets. Hence, even though the general direction for developing countries' economic transition is to converge to those theories and policies, the route and pace of the transition or convergence will be much more complex than what the Western economic theorists have imagined and expected. Therefore the reform should be gradualist in design and flexible in execution.

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<sup>4</sup> Source: <http://www1.peopledaily.com.cn/GB/shizheng/252/5303/5304/20010626/497655.html> [accessed on 29 November 2008]

Compared with EEFSSU's 'Shock Therapy' reforms based on Washington Consensus, China has chosen a gradualist approach to economic reform. The basic features of such a Chinese gradualist reform are: reforming the easier first and harder latter, experimenting in smaller area first, incrementally moving forward, using dual track for gradual transition (P. Li, 2005). There has been a consensus in Beijing that gradualist reform is an ideal approach to maintain stability and avoid reform risk for a big country like China.

Chinese leaders themselves did not expect the complexity of economic reform at the outset. Their initial plan was to complete the reform within 5 to 10 years or at latest by 1995<sup>5</sup> (Zhang, 2008). Also, during the last 30 years of reform (still not yet completed), China has had three rounds of hot debates on how and whether to reform<sup>6</sup>. In the 1980s, China's reform was seen as 'liberalization in odd years and anti-liberalization in even years' (Zhu, 2007). The most recent reform debate started in 2004 even triggered the anti-reform voices (Zhu, 2007). All of these show the complex nature of the reform process.

Deng Xiaoping was a flexible pragmatist. The very idea of economic reform was a break away from the Maoist economic model. Although many Party leaders wanted to reform, it was a taboo at the early years of reform to spell out the failure of Mao's policies. Deng's flexibility was to uphold the banner of 'Mao Zedong Thought' – the CCP's official theory under Mao's leadership – on the one hand and to reinterpret Maoism as 'freeing your mind and finding the truth from the fact' on the other. Therefore Deng's reform strategy was legitimated as a continuity and development of Maoism, essentially guaranteeing the long-term continuation of the reform process.

Another evidence of the power of the flexibility principle is the great idea and policy of 'one country, two systems', which Deng Xiaoping created for handling the issue of the return of Hong Kong and Macau in 1980s. To many people inside and outside China during that time, capitalism and socialism were as incompatible as water and fire. The British Prime Minister Thatcher even

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<sup>5</sup> Source: [http://www.tianjindaily.com.cn/epaper/mrxb/mrxb/2008-06/24/content\\_5748912.htm](http://www.tianjindaily.com.cn/epaper/mrxb/mrxb/2008-06/24/content_5748912.htm) [accessed on 30 November 2008]

<sup>6</sup> Source: [http://news.xinhuanet.com/fortune/2006-02/13/content\\_4173007.htm](http://news.xinhuanet.com/fortune/2006-02/13/content_4173007.htm) [accessed on 30 November 2008]

used this as an excuse to argue for keeping Hong Kong at the rein of British hands. Facing this knotty problem, Deng devised the 'one country, two systems' theory to unite seemingly conflicting systems.

#### **Principle four: Policy rights**

The Chinese leaders consistently argue that every nation should have the freedom to choose its own strategy and polices of building its economy. Therefore China does not allow other countries to dictate China's domestic policies and in the mean time China promises not to intervene other countries'.

After the beginning of China's reform in 1978-1979, the first time a Chinese leader announced this view in an international occasion was in Premier Zhao Ziyang's speech at the on the International Meeting on Cooperation and Development<sup>7</sup> at Cancun city of Mexico on 22 October 1981. Zhao stated China's Five Principles on International Cooperation<sup>8</sup>, the fourth of which was 'developing countries have the rights to choose development strategies according to their domestic conditions; and developed nations should not make the domestic reform of developing countries as the precondition of establishing the new world order'.

When it comes to international aid, China's no-strings-attached approach is in sharp contrast to that of the Western powers which includes strict aid conditionality. In the 1990s, most of the Washington Consensus-based reforms worldwide failed to deliver the expected outcomes (cf. World Bank, 2005), which helped make the Chinese development model attractive to the Global South. To many developing countries, China offers not only an effective model of economic development but also 'a new model for South-South cooperation' (Wen, 2006) which is based on 'peaceful coexistence, equality, and respect for the social systems, sovereignty, and independence of [other nations]' and China's willingness 'to provide assistance without any political strings attached' (Wesley-Smith, 2007: 23).

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<sup>7</sup> This was the first international conference on cooperation and development where 14 developing countries including PR China and 8 developed nations attended.

<sup>8</sup> Source: <http://cpc.people.com.cn/GB/64162/64165/70486/70508/4943078.html> [accessed on 1 December 2008]

This argument concerning the freedom of choosing one's own domestic policies argument is also supported by many development economists and is referred to as 'policy rights' (Alice Amsden, forthcoming; Crook, 2003; Perales, 2004: 416). Stiglitz (1998: 14) argues 'if policies are to be sustainable, developing countries must claim ownership of them'. Chinese government has been consistently following this 'no interference' approach when dealing with international affairs and 'no string attached' approach when granting international aid.

A strong argument is that the policy rights or freedom was fully enjoyed in the history of industrialization of today's developed countries, e.g., UK, France, US, Germany, Japan, and the Newly Industrialized Countries and Economies (South Korea, Singapore, Hong Kong and Taiwan) (Wade, 2004). Therefore, it is not right for the developed nations to 'kick away the ladder' (Chang, 2002) for the developing countries and force them to accept some international rules designed for protecting the interests of the advanced nations (Stiglitz, 2000, 2003; Wade, 1996, 2001, 2002).

### **Principle five: Stable political environment**

Chinese leaders have been well aware that a stable political environment domestically and internationally is a precondition for economic development<sup>9</sup>. So while economic reform has taken big steps forward, political reform has proceeded much more cautiously<sup>10</sup>. According to 'Jiang Zemin's Thought of Three Representations'<sup>11</sup>, one party ruling is not the problem as long as the Chinese Communist Party represents the development needs of advanced production forces, the direction of advanced culture, and the basic interests of

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<sup>9</sup> Even the anti-socialist and anti-collectivist economist and political philosophy Friedrich Hayek once admitted 'Well, I would say that, as long-term institutions, I am totally against dictatorships. But a dictatorship may be a necessary system for a transitional period. At times it is necessary for a country to have, for a time, some form or other of dictatorial power' (source: [http://www.fahayek.org/index.php?option=com\\_content&task=view&id=121](http://www.fahayek.org/index.php?option=com_content&task=view&id=121) [accessed on 29 November 2008]).

<sup>10</sup> Deng Xiaoping called for political reform in 1980 and in 1986 he wanted to have a substantial start of political reform, however, the conservative forces within the Party succeeded in putting off such a bold move.

<sup>11</sup> Source: [http://news.xinhuanet.com/ziliao/2003-01/21/content\\_699933.htm](http://news.xinhuanet.com/ziliao/2003-01/21/content_699933.htm) [accessed on 1 December 2008]

the majority of Chinese people. In China, the official slogan is 'stability overwhelms anything else'. Many scholars now agree that one important reason behind China's fast economic growth in recent years has been its relatively stable domestic political environment (Naughton and Yang, 2004; Brødsgaard and Zheng, 2004; Nathan, 2003). The increased stability and predictability of Chinese politics was evidenced in China's rule-based and orderly transition from the Third to Fourth generation of political leaders (Brødsgaard, 2004).

Some Washington-Consensus-minded scholars prescribed that political reform must precede economic reform because political institutions will directly impact on every economic transaction (North, 1990), therefore getting the institutions right first can ensure minimized transaction costs (cf. Coase, 1937; Williamson, 1975). However, what they did not understand about the dynamics of the relationship between political environment and economic development is that these two are essentially mutually dependent and mutually constraining and reshaping one another.

An example of the positive mutually-reshaping relationship is the Chinese reform performance where Yusuf (1994: 73) notices 'a cycle of economic and political reform has become apparent'. China started off reform firstly in the economic domain, and thanks to the relatively stable domestic political environment, the successful economic performance now enables China 'gradually engineering political adjustments' of 'a process of managed democratization' (Gosset, 2006). To Chinese, a vivid case of the negative dynamics between political and economic reforms was the disastrous outcome of the EEFSU's 'Shock Therapy' reform which was based on the idea of 'political reform comes first'.

### **Principle six: Self-reliance**

Chinese leaders always emphasize and encourage diligence and self-reliance. Mao enthusiastically praised the great potential of Chinese people's wisdom and creativity. In Mao's thinking, only people are the main source of generation of material wealth, scientific technology, and social progress. Chinese leadership after Mao inherited this self-reliance principle. Deng

Xiaoping in 1984 pointed out 'in order to develop, we must mainly rely on ourselves while opening up can attract foreign capital and technology as a supplement to our socialism' (cited in Q. Li, 2008: 37). On 17 November 2006, Chinese President Hu Jintao expressed at the APEC CEO Summit 2006 that 'China's development is mainly based on self-reliance and Chinese people's hard-work. In the meantime, China unshakably implements the opening-up policy, and executes reciprocal and win-win opening-up strategy'<sup>12</sup>.

Due to the Cold War international order after the Second World War, Socialist China at its birth faced immense difficulties in its economic development and nation building. During the isolation and blockade by the West led by the US in 1950s, China relied on the Soviet Union for economic help and assistance. However with deterioration of the China-Soviet relations from the early 1960s, China was forced to fully rely on her own efforts. But this forced self-reliance helped unite the whole Chinese people and created a sense of common destiny. In 1978, Deng Xiaoping announced to open door to the outside world in order to import foreign capital, technology and management knowhow. After the 1989 Tiananmen student movement, Western countries led by the US started to block China, and China had to once again rely on herself. One negative case is the policy of 'market exchanges for technology' started in 1992 (Lan, 2005). After more than ten years practice, Chinese leaders realized this policy has almost failed and China has to rely on herself to develop advanced manufacturing industries (Mei, 2009).

Chinese are said to have enormous, what Singapore's ex-leader Lee Kuan Yew commented, 'endurance and stamina needed for sustained efforts' (cited in Ramo, 2004: 65), and whose culture 'enjoins you to endure hardship and have the stamina to struggle on in a cohesive society where the individual subsumes himself for the benefit of the family and his society' (cited in Ramo, 2004: 67). The history of China's reform has proven the importance of self-reliance as well as learning from others.

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<sup>12</sup> Source: News of the Communist Party of China, available at: <http://cpc.people.com.cn/GB/64093/64094/5057874.html> [accessed on 27 November 2008]

## **Principle seven: Constantly upgrading industry**

Chinese leadership knows well the importance of upgrading industrial portfolio. This is exactly the idea of, what Lee Kuan Yew put straightforward in an interview with Joshua Ramo: 'we tried import substitution for a short while, we were making toothbrushes, mosquito coils, some shirts and garments, but it wasn't going to make us a living' (cited in Ramo, 2004: 71). A former Japanese Ministry of Finance official Masaki Shiratori (1993) echoes this wisdom by arguing 'a latecomer to industrialization cannot afford to leave everything to the market mechanism'<sup>13</sup>. The trial and error inherent in market-driven industrialization is too risky and expensive considering the scarcity of resources' (cited in Wade, 1996: 29).

It is beyond the scope of this paper to make a detailed argument why some industries are more important than some others. Briefly put, certain strategic industries, say, capital-intensive, knowledge-intensive and high-tech industries, are more important than others for several reasons. Firstly, these industries offer more space for technological learning, such as electronics, biochemical, and new material industries, etc. Secondly, these industries add more realizable value into their products hence generate more profit<sup>14</sup>, such as software, financial services, designing and marketing industries, etc. Thirdly, high-tech industries will have much more potential for export growth (Fagerberg, Srholec, and Knell, 2007) with a rising terms of trade. Fourthly, technology sophisticated industries may have positive externality or spillover effect to other domestic industries. During the 1950s China adopted a development strategy which focused on heavy-industrial growth and massive investments. During the reform period attempts have been made to channel more resources into agriculture and light industry (Brødsgaard, 1991).

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<sup>13</sup> Stiglitz (1998:11) points out two major market failures in developing countries: 'left to itself, the market will tend to underprovide human capital' and 'technology', which are crucial factors for economic development.

<sup>14</sup> Chinese ex-Minister for Commerce emotionally commented that 'Chinese people need to produce 800 million shirts in order to exchange an A380 plane'. His calculation was based on the harsh reality that the profit margin for a Chinese made shirt was only 0.35 US dollar. Source: <http://www.scol.com.cn/comment/bbsnr/20060208/200628153736.htm> [accessed on 25 November 2008]

It is worth noting that it is necessary to foster competition (Stiglitz, 1998: 7) among firms as well as among industries if a successful industrial upgrading strategy is to succeed. During the reform period, even though China has opened its door to let foreign companies invest and operate in China, there has been a reluctance to open up strategically important sectors such as finance, telecommunication, steel and power generation. However, the current leadership realizes that Chinese industry needs to start competing on the global level playing field and has defined a group of 120 major companies ('national champions') that should be developed into major international players (Nolan, 2001).

### **Principle 8: Indigenous innovation**

A corollary of the need for constant upgrading industry is the demand for indigenous innovation. This point is the first theorem in Ramo's original analysis of the Beijing Consensus (Ramo, 2004: 11). Ramo writes: '[r]ather than the "old-physics" argument that developing countries must start development with trailing-edge technology (copper wires), it insists that on the necessity of bleeding-edge innovation (fiber optic) to create change that moves faster than the problems change creates. In physics terms, it is about using innovation to reduce the friction-losses of reform' (Ramo, 2004: 12).

China has invested heavily in education and technology. China used to rely more on technology import and transfer, but has realized it is crucial to develop the country's own innovation capabilities in order to compete in today's fast-changing world (Fagerberg, Srholec, and Knell, 2007). China has now been geared to develop her national innovation system where her intention and strategy is to gradually transit from a government-centered to an enterprise-centered innovation web (OECD, 2007). Some policy instruments for stimulating indigenous innovation are protecting intellectual property rights (IPR), fiscal decentralization and tax reform which fuelled up the incentives needed to each level of local governments.

It is worth noting that innovation is not just about technological innovation, but also about institutional innovation as well as. Since the reform in 1978 China

has shown considerable abilities in institutional innovation and reform. As the decentralized social structure and reform leaders support experimentation, Chinese society has rehabilitated the ability to innovate from below. Significantly, Chinese peasants have made several institutional innovations, such as the household contract responsibility system (HCRS), township and village enterprises (TVE), self-governance in village, rural special cooperatives, collective forest rights reform, etc<sup>15</sup>. In respect to the urban reform, Chinese leaders invented the 'dual-track system' which ensured a much more smooth transition from centrally-planned to a market economy compared with the big-bang reform in EEFSU. Some scholars highly praised this institutional innovation as a Pareto-improving method (Lau, Qian, and Roland, 2000).

### **Principle 9: Prudent financial liberalization**

China has been so prudent and cautious when it comes to liberalization of financial market that China still has not yet opened her capital account. This might be partly because China has lacked the experience of managing stock and other financial markets, and partly because Chinese leadership is worried about losing control of her strategic national assets. But the most important reason is that Chinese leaders understand the enormous risk of a rapid financial liberalization.

Chinese leaders' cautions and worries have been warranted by the chilly reality that those countries that have liberalized too quickly or relaxed regulations on financial markets have had to bear painful losses due to unexpected financial crises. One may point to the Latin American debt crisis in 1980s and 1990s, the Asian financial crisis in 1997, the Russian financial crisis in 1998, and most recently the global financial crisis in 2008 caused by US subprime crisis.

What puzzles Chinese leaders is how come the rest of the world (LA, EA, EU, and US) has not learnt a lesson from the string of financial crises in the last two decades of 20<sup>th</sup> century? To Chinese leaders, the main culprit of the global

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<sup>15</sup> Source: China's official Xinhua news agency website, available at: [http://news.xinhuanet.com/politics/2008-10/08/content\\_10165611.htm](http://news.xinhuanet.com/politics/2008-10/08/content_10165611.htm) [accessed on 25 November 2008]

financial crisis was the blind belief in free market. Ironically, in his speech at the Manhattan Institute on 13 November 2008 'on the eve of' of the G20 summit, the former US president George W. Bush 'fervently defended U.S.-style free enterprise' as 'not the cause' but rather 'the cure' for the world's financial chaos (Feller, 2008).

### **Principle ten: Economic growth for social harmony**

Chinese leaders are enthusiastic about building a harmonious society and they believe they can achieve this by effectively growing the economy first. This belief can be traced back to the birth of the New China in 1949. Mao spent his whole life to explore a road toward a prosperous and strong China in which the Chinese people could enjoy a happy and equal life. Harmony in Mao's mind might mean no oppression and no exploitation. Based on this belief, he tried to make the oppressed stand up, the proletariat control the means of production, and the bourgeoisie deprived everything. The way of realizing his harmonious society proved to be wrong and had disastrous consequences, but it could be argued that his vision was clear, for instance, he even believed by cultural revolution he could find a way from total chaos to total harmony (*cong tian xia da luan dao tian xia da zhi*).

Deng Xiaoping inherited Mao's vision but took another direction. Deng allowed part of people to get rich first and reminded his Party never to forget his vision: let the people and regions who became rich first help the less wealthy people/regions to prosper and develop together. Deng Xiaoping and Jiang Zemin have effectively encouraged a part of Chinese people to get rich first, which in fact prepared the material basis for the new generation of Chinese leadership led by President Hu Jintao and Premier Wen Jiabao to take on the task of 'making all Chinese prosper together'. Hu and Wen have so far had a good start – they brought forth a new development plan called 'constructing a harmonious socialist society', which we argue will have far-reaching impact on China's peaceful rise in the 21<sup>st</sup> century. Part of this new development plan would be to correct the big income disparities that have emerged as a consequence of letting some people and regions prosper first.

Although we list this principle as the last one, it actually is very important because it indicates the ultimate purpose of reform and development. Chinese leaders since Mao have never lost their grand vision: to build a prosperous, democratic and civilized socialist country. Many westerners criticize China lacks democracy, human rights and freedom. However, we believe, it takes time for a huge country like China to realize its transformation from an underdeveloped semi-colonized and semi-feudal country to an advanced modernized nation. What we have learned from Chinese story is China has prioritized economic development at the earlier stage and has gradually moved towards coordinated economic and social development when they feel they have accumulated sufficient material resources in the earlier stage. The best evidence is China's strategic switch to a strategy of building a harmonious society domestically and a harmonious world internationally in the beginning of 21<sup>st</sup> century.

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