

# 'Deepening Reform': The Organization and the Emerging Strategy

Barry Naughton

The Chinese leadership has set up an elaborate top-level apparatus to advance the reforms announced at last year's Third Plenum. This apparatus extends down to local governments, and strongly incentivizes local governments to push forward with local reforms as well. However, these reforms are still not well defined, and specific guidance from the top level has lagged behind the creation of "reform leading groups." The resulting pattern is one of broad movement but relatively slow delivery of actual reform measures. As proposals percolate up from below and "top-level designs" are further fleshed out, we can anticipate an additional protracted stage of bargaining, conflict, and slow consensus-building. Important reforms will emerge over the next few years, but there are also risks that irreconcilable conflicts may emerge or that botched reforms may incite a backlash.

Xi Jinping has continued to push an extraordinarily broad and complex political agenda, characterized by deeply contradictory elements. On the one hand, Xi is strengthening direct Communist Party power and emphasizing top-down leadership, beginning with his own. He is tightening political repression and ideological control, and emphasizing nationalism. At the same time, Xi is driving economic reform forward and continuing a powerful and popular campaign against corruption. There is little doubt that the economic reform component of this policy offensive is significant and substantial. In this piece, I will demonstrate the gathering momentum of the reform process.

With so many initiatives moving forward at once, it is difficult to discern the logic or coherence of the whole project. The contradictions lead some pundits to claim they have found the key to, or the "real" meaning of, Xi's initiatives in some kind of simplifying framework. In my view, while none of these interpretations can be ruled out, there is not enough information available to outsiders to allow any of them to impute simple coherence to Xi's program. Instead, the apparently contradictory elements of Xi's agenda will ultimately turn out to be just that: contradictory. These contradictions may never be resolved, or they may be worked out by the clash among different elements of the Xi agenda. These clashes will lead to the defeat of some elements at the expense of others; to compromise; and to unexpected twists and turns.

What has already become clear is that economic reforms will be significant. While the overall picture with respect to economic reform is—like Xi's agenda overall—complex and chaotic, so many important initiatives are going forward simultaneously that some combination of them with major economic impacts will certainly be adopted. At this stage, though, we simply don't know where the most important breakthroughs are likely to come in the next year or two.

However, the strategy of economic reform is beginning to emerge. In fact, the economic reform agenda is unfolding in a way that nobody predicted. Instead of beginning with a technocratic “top-level design,” as many, including myself, expected, economic reform is instead progressing through a broad mobilization of agencies and local governments throughout China. Right now, I estimate there are at least 800 “deep reform” leadership groups and specialized reform groups working in China (see below for discussion). Each of these is drawing up a reform program, ramping up research programs and pilot projects, and making lists of priority measures. Moreover, to a certain extent, these “deep reform” entities are competing to demonstrate their commitment to reform and their ability to roll out significant new measures. At the same time, the central Communist Party agencies guiding reform are just beginning to pass on the first reform measures. By the end of 2014, a wide array of bottom-up proposals and top-down reform initiatives will have emerged. This will begin a new phase of bargaining, argument and slow consensus-building. The center has already signaled that it is in no hurry to produce grand overall reform programs, but instead wants to roll out partial and incremental reform measures as they are ready. The concluding section of this piece discusses some of the strong and weak points of this emergent strategy.

## The Central Government Organization of “Deepening Reform”

The current cycle of economic reform clearly began as a top-down process. Moreover, this top-down process has been led by Xi Jinping and by Communist Party organizations from the beginning. The key step was the initiation of the “Deepen Reform Leadership Small Group” (DRLSG), a central party-sponsored leadership group headed personally by Xi Jinping. In its first two meetings (January 22 and February 28, 2014), the DRLSG primarily dealt with procedural issues, setting up organizations, passing by-laws, and drawing up priorities and a work schedule for 2014.<sup>1</sup> Most crucially, the first meeting set up six subsidiary specialized groups (SGs): economic system and ecological civilization system (经济体制和生态文明体制改革); democracy and the legal system (民主法制领域改革); the culture system (文化体制改革); the social system (社会体制改革); the party-building system (党的建设制度改革); and the disciplinary and inspection system (纪律检查体制改革).<sup>2</sup> At that meeting, the DRLSG also ratified a number of procedural documents that regulated the LSG’s operations. It also approved a “Division of Labor for Important Initiatives [举措] from the Third Plenum Resolution.”<sup>3</sup> This document has not been publicly released, but from comments made by participants, we know that it includes a list of 336 initiatives (举措), with each initiative being assigned to a lead agency and, where necessary, to additional participating agencies and “member agencies.”<sup>4</sup> In the previous issue of *CLM*, I referred to the Third Plenum Resolution as a “vision statement plus a to-do list.” The “Division of Labor” represents the next step in the to-do list, disaggregating each task to a responsible agency.

A key role in this disaggregation process is played by the six specialized groups. Unfortunately, we don’t know very much about these SGs; very little information—and no systematic information—has been disclosed about them. However, recently some important information was revealed about the most important of these, the “economic system and ecological civilization system reform specialized group” (“Economic Reform

SG” for short). At a May 16–17 meeting on 2014 economic reform tasks, the keynote addresses were made by two men who were identified as the *joint* heads of the Economic Reform Specialized Group. The first co-head, not surprisingly, was Liu He 刘鹤, office head of the Finance and Economics Leadership Small Group (FELSG), and identified in earlier issues of the *Monitor* as Xi Jinping’s main economic adviser. The other co-head, more surprisingly, was Xu Shaoshi 徐绍史, the head, since March 2013, of the National Development and Reform Commission (NDRC).<sup>5</sup> The role of this Economic Reform SG was described clearly in remarks made by Yang Weimin in an earlier interview: “there are a total of 336 initiatives [举措] from the Third Plenum resolution that were separated out for implementation; of these, 181 were delegated to one of the six specialized groups for coordination. Our small group is responsible for 118, or 65 percent, of those entrusted to specialized groups.”<sup>6</sup> Yang’s comment underscores the preeminent importance of the Economic Reform SG.

As of this writing (June 30, 2014), the only other SG to have revealed the name of its leaders was the Culture System Reform Group. The Culture SG is headed by Liu Qibao 刘奇葆, Politburo member and head of the Party Propaganda Department; the vice-head is Liu Yandong 刘延东, Politburo member, vice-premier, and head of the Technology and Education Portfolio in the State Council. As was the case with the Economic Reform SG, the leadership of the Culture SG was revealed, in passing, in the course of reports on a working meeting, in this case the Cultural System Reform Work Conference in Beijing March 25–26.<sup>7</sup> The office head is Sun Zhijun 孙志军, vice-head of the Party Propaganda Department since 2007. In an interview, Sun described an agenda for this year of over 80 items, most having to do with the management of the culture industry.<sup>8</sup> The Culture SG is quite different from the Economic Reform SG in that both its head and vice-head are Politburo members: the group itself is led by the top politicians with responsibility for that issue area, while the Economic Reform SG is led by technocrats, albeit of relatively high bureaucratic rank. We will see later that the Culture SG pattern is repeated at the provincial level, and the Economic Reform SG is very much the exception. As for the other four central-level specialized groups, they toil away in obscurity for now.

The third meeting of the (main) DRLSG, on June 6, 2014, for the first time took up substantive issues, discussing three major topics, although no documents were publicly released. The meeting approved three documents relating to the court system (not discussed here), and considered major reform programs relating to the fiscal system and the household registration system. Both were discussed in depth, and revisions were requested to incorporate suggestions made during the discussions.<sup>9</sup> In fact, three weeks later (June 30, 2014), these two reform documents were approved by a Politburo meeting.<sup>10</sup> A general idea of the contents of these documents has been disclosed, but no detailed description is yet available. For now, the point is simply that these measures are the first formal products of the economic reform apparatus set in place over the last eight months. As such, they are just the first wave of what will likely be a flood of proposals emerging from the DRLSG over the coming months (and indeed years). The strategy is explicitly to have many items under discussion simultaneously, in many different agencies. As a degree of consensus is reached on any particular initiative—or, alternately stated, as a political judgment is made that an issue is ready to be moved forward—it is to

be advanced to the full DRLSG. As one source puts it, “as one [initiative] is mature, consider that one, and roll it out.”<sup>11</sup> We should anticipate the continuous, steady rollout of multiple substantial measures.

## The Economic Reform Specialized Group: A Closer Look

The standard rule for Leadership Groups is that the Group is composed of top-level politicians, and the real work is done by the Office. Office heads are expected to work hard but keep a low profile, allowing the politicians to make the important speeches and get the credit (or blame). Most of the SGs function like Leadership Groups, but the Economic Reform SG is different. The *Office* of the pre-existing Finance and Economic Leadership Small Group (FELSG), headed by Liu He, has now largely *become* the Economic Reform SG.<sup>12</sup> In a sense, then, the Economic Reform SG acts as the substantive office of the DRLSG, coordinating and designing the most important economic piece of the overall reform program. The formal Office of the DRLSG, headed by the Central Party Research Office, presumably has its hands full coordinating the six different SGs.

The appointment of Xu Shaoshi as the co-head of the Economic Reform SG along with Liu He represents an obvious effort to bring NDRC into the coordination process. While Xu, the head of NDRC, is nominally the superior of Liu He (a vice-head of NDRC), this is unlikely to reflect the true relations between them. In the first place, Xu is not a career NDRC person, never having served in the NDRC before his appointment as head in 2013. In turn, Liu He’s appointment at NDRC has been from the beginning a courtesy appointment: according to reports, he has never been to his office there, working instead at the offices of the party center to be close to his boss. NDRC is being brought in as a transmission belt, to coordinate with the multitude of government departments that are involved in the reform process. Indeed, many government departments have already established their own Deepen Reform Leadership Small Groups, including the Ministries of Transport, Agriculture, and Environment, as well as the State Asset Supervision and Administration Commission (SASAC). These departments are expected to coordinate through NDRC with the Economic Reform Specialized Group.<sup>13</sup> Even some large state-owned enterprises have set up Deepen Reform LSGs and are drawing up reform initiatives. Thus, the Economic Reform SG, and the NDRC, must coordinate among many different agencies to which specific reform tasks have been delegated. In a later section we will describe one particularly important case, the creation of diversified ownership systems for state-owned enterprises, in which responsibilities were assigned to both the Ministry of Finance and SASAC.

The role of the Economic Reform SG was also brought into sharp relief when, on June 13, 2014, it was announced that the FELSG had met for the sixth time since the 18<sup>th</sup> Party Congress, and that it was chaired by Xi Jinping. This was the first time in decades that a meeting of the FELSG had been publicly announced, and it was the first formal announcement that Xi Jinping was the head of this party body, although the fact was widely known among Beijing policy circles.<sup>14</sup> Moreover, for the first time, the entire membership of the FELSG was revealed, as the CCTV cameras panned across the meeting site.<sup>15</sup> Such coverage clearly indicates a new level of visibility for the FELSG,

and certainly a heightened role in the policy process as well. It provides one more administrative channel through which Xi Jinping can exert influence over policy-making, and gives him direct voice earlier in the policy process. This is a major difference from policy-making over the past 15 years, in which economic policy has been made predominantly in the State Council, by the premier as head of the government. (Both Zhu Rongji and Wen Jiabao had dominant voice on economic policy, subject to ratification by the Politburo Standing Committee. Xi Jinping now exercises his voice directly through the FELSG.) A little-noted consequence of this change is that the Office of the FELSG has now been elevated to a position unprecedented in Chinese economic policy-making. Functioning *both* as the Economic Reform SG *and* the Office of the FELSG, this small group of technocrats has become a kind of economic policy secretariat. The broad range of issues they handle was clearly demonstrated by the subject matter of the first publicized FELSG meeting, which was to lay out a five-point long-term energy agenda.<sup>16</sup> To be sure, members of the FELSG Office are staff, not decision-makers, and their influence depends on how effectively they work with their superiors. Still, they clearly occupy a critical node in the economic decision-making process.

### The Local Government Organization of “Deepening Reform”

Immediately after the Third Plenum, local party organs were signaled that they should also set up leadership small groups. In a November 19, 2013, *People’s Daily* article, Liu Yunshan, propaganda chief, Standing Committee member, and vice-head of the DRLSG, said, “Party committees at each level should set up a leadership small group and associated bodies, and get to work as soon as possible.”<sup>17</sup> At the first meeting of the national DRLSG (January 22), provinces were told to set up LSGs “as soon as possible.”<sup>18</sup> By the end of February, the formation of DRLSGs had been announced by every province-level party committee.<sup>19</sup> Province-level DRLSGs have a relatively uniform structure: In every case, the provincial first party secretary is the head, and the governor is the vice-head. Some provinces have announced additional vice-heads, in the persons of the deputy party secretary and the executive vice-governor.<sup>20</sup> In nearly all cases, the office of the province DRLSG is established at the Provincial Party Committee Policy Research Office (省委政策研究室), typically as “one organization with two different titles” and with the secretary-general of the provincial party committee as the head of the DRLSG Office. This makes the provincial support staff directly parallel to the national level (where the LSG Office is placed in the Central Party Policy Research Office, headed by Politburo member Wang Huning.<sup>21</sup> This means that the party is in firm control of the reform process, at the local as well as the central level.

Each provincial DRLSG has established subordinate specialized reform groups. In most cases they mimic the six specialized groups set up at the national level, but a few provinces have adapted the structure of SGs to their own particular needs. Some quite reasonably divide economy and environment into separate groups; Hebei added an agricultural reform specialized group, while Shanghai added a group on social security and [income] distribution reform and separate groups on environment and reform of the “system of economic and social undertakings” (经济社会事业体制). Beijing set up 14 specialized groups, allowing it to introduce groups on regional coordination, pollution

and environment (separately) and technology and education reform.<sup>22</sup> The provincial DRLSG draws up a program of reform initiatives, disaggregates them to responsible agencies of specialized groups, and sets up a timetable that includes priority tasks for 2014. The specialized groups are then responsible for coordinating relevant government departments to carry out the actual work.

The typical staffing of the specialized reform groups in those provinces with six SGs shows how the system works: the Economics and Environment Specialized Group is typically headed by the vice-governor in charge of the economy; the Cultural System SG is overseen by the head of the Provincial Propaganda Department; the Social System SG is headed by the secretary of the Politics and Law Commission; the Discipline and Inspection SG is headed by the chief of the Provincial Party Discipline Commission; the Party Building SG is headed by the Organization Department head; and the Democracy and Legal Arena SG is typically headed by the Party Committee member in charge of United Front work. All these individuals are generally members of the Standing Committee of the Provincial Party Committee.<sup>23</sup> This lineup reveals a great deal about the reform process. First, at the local level, the reform process is 100 percent insider controlled: The provincial party committee completely runs the agenda-setting process for local reform. Second, at the local level, the Politics and Law Commission continues to be very important, as evidenced by its leadership of social system reform, even though at the national level, the head of the Politics and Law Commission no longer has a “seat” on the Politburo Standing Committee. Third, intensive design of the overall reform process is important at the national level in a way that it can never be at the local level. As described earlier, Economic Reform SG at the national level is headed by the technocrats Liu He and Xu Shaoshi (rather than the executive vice-premier in charge of the economy, Zhang Gaoli). At the provincial level, the executive vice-governor in charge of the economy (Zhang Gaoli’s analogue) typically heads the Economic Reform SG. While locally the Economic Reform SG is tasked with coming up with innovative reforms, it does not have to design a new economic system, which the national SG arguably does. Finally, the local SGs draw our attention to the fact that nationally the head of the Discipline Commission, Wang Qishan, is not even on the DRLSG (presumably because he’s so busy with the anti-corruption campaign). In short, the composition of the provincial-level LSGs and SGs is relatively formulaic, consisting of the existing party leadership. This tells us that the purpose is not to bring in new people, but rather to change the incentives of the existing leadership groups.

Deepen Reform Leadership Small Groups have been set up below the provincial level as well. Big cities like Wuhan, Dalian, and Shenyang all set up LSGs: Wuhan’s LSG has 20 SGs underneath it.<sup>24</sup> Provinces often set up Deepen Reform groups in a few of the most important provincial government agencies. Many provinces have issued instructions that every municipality down to the prefecture level should set up a DRLSG, and even some counties as well. Many of these local governments set up multiple SGs. Special Economic Zones and other economic development zones also set up reform groups.<sup>25</sup> In the national government, NDRC,<sup>26</sup> SASAC, the Ministries of Environment, Water Conservancy, and many others, have DRLSGs. Putting these all together, there must be over 800 DRLSGs and SGs currently functioning.<sup>27</sup> While each of these groups is

composed primarily of existing leaders, those leaders find that their success indicators have suddenly changed: This year and next, they will be evaluated primarily on their ability to generate reform initiatives that appear to be bold, innovative, and effective. To a certain extent, these officials are in competition with each other to demonstrate compliance and enthusiasm.

## A Key Issue: Mixed Ownership

To get a sense of how this reform apparatus is playing out, consider an important and deeply contested issue: mixed ownership. The Third Plenum document called for the active conversion of state ownership to mixed ownership, defined as state, collective, and “nonpublic” actors simultaneously having ownership stakes in what formerly were 100 percent state-owned firms. At the same time, the government was to establish investment holding companies, and shift its management of assets to management of capital (or wealth).<sup>28</sup> Scores of conversion experiments and programs are going forward. Some of these simply invite private investors to take a stake in SOEs. These are relatively simple measures, but remember that progress in reform has been highly incentivized:

Some localities specify a time table, concrete responsibilities and volume of work, and declare that in mixed ownership firms government ownership need have neither a ceiling nor a floor; and they make detailed regulations specifying that the degree of progress in property rights reform will be a “hard target” in the performance indicators [of local officials]. . . . There is in fact a broad consensus on the need to push mixed ownership reform in general, but on the questions of “with whom to mix” and “what is mixed ownership” and “who will be the principal,” there is still heated debate.<sup>29</sup>

This description is part of an account—widely circulated on *weibo* and other social media—that is relatively hostile to these quick changes in ownership, and tends to reflect the cautious views of SASAC, one of the principal stakeholders (or interest groups) in the existing state ownership system. Nonetheless, the basic picture of competitive and highly incentivized implementation of “mixed ownership” is certainly correct. Shanghai and Guangdong were the first localities to come out with programs for mixed ownership reform. Shanghai introduced some significant innovations with respect to stock incentives, but overall the proposal was not particularly exciting.<sup>30</sup> Second movers have tried to surpass these earlier movers. As an official Anhui Province report put it, “with a faster pace of reform, Anhui will be able to . . . seize the initiative, and carve out a new path to ‘catch up and surpass’ in the current round of deepening reform.”<sup>31</sup> More substantively, in Chongqing, the mayor, Huang Qifan—who survived the fall of Bo Xilai and has played an important role in the design and implementation of Third Plenum reforms—laid out a clear proposal for “mixed ownership” reforms, approved for implementation by the local State Asset Management Agency, that contained many interesting elements. Huang formally proposed five measures including listing all the assets (and liabilities) of individual SOEs on the stock market, and the creation of “Warren Buffet–style, Temasek–style” investment companies.”<sup>32</sup>

Huang's proposal directly touches on a few of the key issues that mixed ownership reforms must confront. To simplify a complex issue area, "mixed ownership" will really make a difference if, and only if, a number of complementary institutional reforms are also carried out. These include: a board of directors that actually represents shareholders (and is not just appointed by the Organization Department); a corporate form for the new corporation that packages all assets and liabilities so that there is no residual parent-child, or mother-in-law-child relationship between the firm and its precursor administrative agency; and a "Temasek-style" agency to exercise the state's ownership share in conjunction with—and in competition with—other investment funds and agencies. Only if major progress is made in these three areas does it make sense to have expectations about mixed ownership reform. Without these complementary reforms, private shareholders won't be able to have a voice on the board of directors of the new mixed ownership firms, and government agencies will continue to have the incentive and the ability to directly intervene in firm management. Furthermore, policy-makers need to make appropriate decisions about which types of firms will be on future "negative lists" that restrict non-state ownership because of national security or public goods considerations. These are old issues, much discussed at the end of the 1990s, but then quietly taken off the table around 2004 when the reform agenda lost all urgency. Now they have returned to the policy agenda.

Without these complementary reform elements, "mixed ownership" can easily deteriorate into old-fashioned deal-making. Despite the pressures of the ongoing anti-corruption campaign, local officials can always find favored private-sector partners with whom they can share the benefits of the "ownership mixing" process. Indeed, there is plenty of deal-making going on. Besides the local governments and locally run firms described in this section, large centrally owned firms such as Sinochem and CITIC have presented recent deals to shuffle ownership, bring in private strategic partners, and put all their assets into more transparent, listed companies. Much of the activity seen so far falls into this "deal-making" category.

In the meantime, the most important action is taking place back in Beijing. As part of the process of disaggregating and assigning tasks, described above, design of mechanisms for "mixed ownership" was assigned to two lead agencies: the Ministry of Finance and SASAC.<sup>33</sup> The Ministry of Finance (MOF) has already presented its plan, key points of which are available. It calls for the trial establishment of state investment companies next year, and the full rollout of the system by 2020.<sup>34</sup> In essence, the MOF calls for organizing large investment companies that will replace many of the current functions of SASAC, and will be large funds, oriented toward long-term value maximization (like Temasek, although they do not make the explicit comparison). SASAC's plan will not be ready until September.<sup>35</sup> The fact that its plan is not ready reflects a certain amount of disarray at SASAC, which has been hit hard by corruption scandals, and is having a hard time coming up with a coherent program. Still, the basics of SASAC's approach are known: they would prefer to build existing corporations under SASAC into the new investment companies, creating a three-tier structure with themselves at the top. SASAC and MOF have been intellectual and interest adversaries for years. There is no possibility that their programs will be compatible. The State Council Development Research Center



has also weighed in with a plan, and NDRC will have a significant role mediating between these different approaches.<sup>36</sup>

Much more could be written about the reform of SOEs through mixed ownership and establishment of state investment companies. What is crucial here is that although the ultimate content of the future SOE reform is still highly uncertain, the shape of the process that will determine that reform is now coming into view. By autumn 2014, multiple proposals and pilot projects will be piling up in Beijing. It will be the job of the Economic Reform SG, aided by NDRC, to pick through these elements of a reform and try to cobble together a coherent program. They will have to persuade, and cajole, and pressure recalcitrant agencies, because there is no doubt that underlying disagreements about SOE reform will remain strong and deep. Perhaps the Economic Reform SG already knows the type of reform package that it wants to get out of this process; perhaps it will be forced to settle for the lowest common denominator. Sometime in the fall, the political leadership in the DRLSG will decide what version of the Economic Reform SG's compromise package they want to go forward with. It will be just one—but a critically important one—of the many compromise packages they will be passing on at the same time.

## Evaluation

The word “consensus” (共识) is much used in China today, favored by academics and decision-makers as a way to describe parts of the policy process. A key point, though, is that consensus formation always occurs within the framework of the political hierarchy.<sup>37</sup> What we see in the case of economic reform is that Xi Jinping has dramatically reshaped the incentives of many of the main political actors in the economic policy process. He has created—perhaps “artificially”—an incentive to push reforms, particularly among local government officials, thus shaping and manipulating the consensus formation process. Bureaucratic interest groups who could be expected to oppose reforms (like SASAC) have been dramatically weakened by the new pro-reform line at the top, and by the ravages of the anti-corruption campaign on their erstwhile leadership. As a result, the consensus that “emerges” from the current process will be very different from the consensus that might have existed a year or two ago.

The “strategy” of reform now coming into view is thus to generate an enormous amount of new “reform” activity at every level of the hierarchical Chinese system. That activity is expected to be today's version of “groping for stepping stones to cross the river,” generating ideas, proposals, and pilot projects. As those proposals are funneled upward to the new reform agencies headed by Xi Jinping, he will preside over a process of compromise and consolidation, shaping the proposals into elements of a reform program. Xi will use his political skills, his dominance of the current leadership, and the advice of his technocrats to shape this process, and end up with a program onto which he can stamp his approval.

This process has a certain coherence. Perhaps outside analysts should have expected a messy, disorderly process like this, since this is the way change has usually come to China. In any case, we can confidently predict that it will produce a series of significant

reform proposals, one after another, over the next six to eighteen months. There are so many things that need fixing—and so many different initiatives and pilots under way—that a steady stream of proposals is inevitable. China’s economic reform is not stalling out; indeed, it is gaining momentum.

Nonetheless, this approach has serious shortcomings and carries substantial risk. While many proposals are working their way through the system, and the cumulative impact of those proposals will inevitably be great, it is quite conceivable that every individual proposal will end up disappointing. The consensus-building process may rub the sharp edges off the most important changes, blunting their impact. Alternately stated, there is a definite lack of prioritization in the current strategy, which tries to start everything at once and then finalize things according to the speed with which they move through the process, rather than according to their intrinsic importance. Policy-makers might approve scores of reforms, but never get around to making the most fundamental actions that change the nature of the system.

A related problem is apparent at the local level. Local officials have been incentivized to adopt things that look like reforms. The process has the potential to generate an enormous amount of fake compliance and meaningless activity. Local officials will want to create reform zones and pilot “mixed ownership” enterprises; none of these hothouse flowers will contribute much to building a healthy environment for a more sustainable and fair market economy. With a myriad of overlapping measures, and competition for the attention of top policy-makers, there will be a tendency to overshoot. Overshooting leads to disorder and, more worryingly, to backlash and retreat.

The final problem may be the most fundamental one. As Stevenson-Yang and DeWoskin put it in their acerbic commentary:

In today’s China, “reform” means to sideline and squash institutionalized bureaucracy and inject personal power into a sclerotic system. . . . what China has never meant by its use of the word “reform” is the codification in law and practice of rules to govern transparently and at scale a growing economy.<sup>38</sup>

This is a fair judgment. The Communist Party is being mobilized to overcome inertia and get economic reforms moving, and Xi Jinping through this process has pulled much greater decision-making authority into his own hands. This has already disrupted the division of responsibilities that for more than 20 years has delegated control over economic decision-making to the government. At this stage in China’s economic development, it seems unlikely that a process that overrides existing government authority and practice will really be able to produce a more effective, stable, and institutionalized system. Moreover, this fault of execution is compounded by sins of omission: The missing link in China’s reforms thus far has been the absence of programs to build credible and independent regulatory agencies to govern those market spaces from which interventionist government is being rolled back. While Xi Jinping’s economic reform program is serious and real, these shortcomings remind us that it has just begun,

and that future phases will involve sharp conflict between incompatible interests and approaches.

---

## Notes

<sup>1</sup> Gui Tiantian and Zou Chunxia 桂田田 邹春霞, “Central Reform Deepening Group considers household registration reform; Insists on maintaining the Three Rights of Rural People” (中央深改组审议户籍改革意见 强调维护农民三权), *Beijing Youth Daily* (北京青年报), June 7, 2014, accessed at <http://news.qq.com/a/20140607/002652.htm>.

<sup>2</sup> These correspond roughly to the list of reform tasks in the Third Plenum Resolution. Those were organized into 16 broad headings. The economic and ecological group would cover headings 2–7 plus 14; democracy and legal system headings 8–9; culture heading 11; social heading 13; party-building 16; discipline and inspection heading 10. This leaves out military (15, of course) and government social services (12), which may be spread among economic, culture, and social. The first heading is very general. Thus, Econ/Ecology has 7 out of 14 relevant headings.

<sup>3</sup> The full title is “中央有关部门贯彻落实党的十八届三中全会〈决定〉重要举措分工方案。” See Xiao Ming 肖明, “Local Deepen Reform Groups follow divergent paths” (地方深改分组走差异化路线), *21<sup>st</sup> Century Business Herald* (21世纪经济报道), February 18, 2014, accessed at [http://news.ifeng.com/mainland/special/ggldxz/content-3/detail\\_2014\\_02/18/33900261\\_0.shtml](http://news.ifeng.com/mainland/special/ggldxz/content-3/detail_2014_02/18/33900261_0.shtml).

<sup>4</sup> According to Shi Zhihong 施芝鸿, former vice-head of the Central Party Research Office, quoted in Gui and Zou (see note 1); Zhang Xudong and An Pei 张旭东 安蓓, “Yang Weimin, vice-head of the FELSG Office, says there are around 60 major initiatives this year for Economic and Ecological Civilization Reform (中央财经领导小组办公室副主任杨伟民: 经济体制和生态文明体制改革今年要推进的举措大体有60项), *Xinhua* report accessed from *Chongqing Daily*, March 7, 2014 online edition at [http://cqrbepaper.cqnews.net/cqrb/html/2014-03/07/content\\_1724337.htm](http://cqrbepaper.cqnews.net/cqrb/html/2014-03/07/content_1724337.htm).

<sup>5</sup> Xiao Ming 肖明, “Leaders of the Central Economic Reform Specialized Group debut” (中央经改专项小组负责人亮相), *21<sup>st</sup> Century Business Herald* (21世纪经济报道), May 21, 2014, accessed at <http://www.21so.com/content/42-276598.html>. See additional biographical material at “The people in charge of the central economic and ecological civilization system reform specialized group: Xu Shaoshi and Liu He (中央经济和生态文明体制改革专项小组负责人: 徐绍史、刘鹤), *Guanchazhe* 观察者, accessed at [http://www.guancha.cn/politics/2014\\_05\\_21\\_231396.shtml](http://www.guancha.cn/politics/2014_05_21_231396.shtml).

<sup>6</sup> Zhang Xudong and An Pei 张旭东 安蓓, “Yang Weimin, vice-head of the FELSG Office, says there are around 60 major initiatives this year.”

<sup>7</sup> “The national culture system reform work conference opens; Liu Qibao is head of the Central Cultural Reform Small Group.” (全国文化体制改革工作会议召开 刘奇葆任中央文体改革小组组长), March 27, 2014, accessed at [http://www.guancha.cn/politics/2014\\_03\\_27\\_217248.shtml](http://www.guancha.cn/politics/2014_03_27_217248.shtml).

<sup>8</sup> Ibid.

<sup>9</sup> “The Central DRLSG tears down barriers to fiscal reform and sends a clear policy signal” (中央深改小组“清障”财税改革释清晰政策信号), *China News Net* 中国新闻网, June 8,

---

2014, accessed at <http://finance.people.com.cn/n/2014/0608/c1004-25118582.html>; Gui and Zou, “Central Reform Deepening Group considers household registration reform.”

<sup>10</sup> New China News Agency (新华社电), “Politburo meeting approves fiscal and tax reform proposal” (政治局会议通过深化财税体制改革总体方案), *China Securities Daily* (中国证券报·中证网(北京)), July 1, 2014, accessed at <http://money.163.com/14/0701/06/A022290C00252G50.html>.

<sup>11</sup> Gui and Zou, “Central Reform Deepening Group considers household registration reform.”

<sup>12</sup> This is quite apparent in the interview with Yang Weimin, cited above. Although Yang is identified in the article as the vice-head of the office of the FELSG, he talks about the Economic Reform SG as “our group.” Doubtless he has a parallel position as vice-head of the Economic Reform SG, but this has not been officially disclosed.

<sup>13</sup> Xiao Ming, May 21, 2014, “Leaders of the Central Economic Reform Specialized Group debut.”

<sup>14</sup> Zhu Jianhe 祝剑禾, “Xi Jinping: We must actively pursue a revolution in energy production and consumption” (习近平: 积极推动能源生产和消费革命), *Capitol Times* (京华时报), June 14, 2014, accessed at [http://news.ifeng.com/a/20140614/40731846\\_0.shtml](http://news.ifeng.com/a/20140614/40731846_0.shtml).

<sup>15</sup> Li Wei’ao 李微敖, “Central Finance and Economic Leadership Small Group Unveiled (中央财经领导小组掀开面纱), *Southern Weekend* (南方周末), June 19, 2014, accessed at <http://www.infzm.com/content/101628>. The membership is now conveniently available on Chinese Wikipedia, which has been completely rewritten to take into account this new information: <http://zh.wikipedia.org/wiki/中央財經領導小組>, accessed June 26, 2014.

<sup>16</sup> Zhu Jianhe, “Xi Jinping: We must actively pursue a revolution.”

<sup>17</sup> Liu Yunshan 刘云山, “Strengthen and perfect the Party’s leadership of all-around deepening reform” (加强和改善党对全面深化改革的领导), *People’s Daily*, (人民日报), November 19, 2013, accessed at <http://politics.people.com.cn/n/2013/1119/c1024-23581969.html>.

<sup>18</sup> Jiang Yanxin and Li Dandan 蒋彦鑫、李丹丹, “28 Provinces have set up Deepen Reform Leadership Small Groups” (28省份已成立“深改”领导小组), *New Capital News* (新京报), February 24, 2014, accessed at [http://news.ifeng.com/mainland/special/ggldxz/content-3/detail\\_2014\\_02/24/34101032\\_0.shtml](http://news.ifeng.com/mainland/special/ggldxz/content-3/detail_2014_02/24/34101032_0.shtml).

<sup>19</sup> *Ibid.* The last three provinces, Zhejiang, Fujian, and Ningxia, announced their groups in the next few days.

<sup>20</sup> Ren Qi 任琦, “Deepen Reform Leadership Small Groups have been revealed in 26 provinces; the Specialized Groups have attracted attention” (26个省级“深改组”亮相改革专项小组备受关注), *Shenzhen Special Zone News* (深圳特区报), February 24, 2014, accessed at <http://cpc.people.com.cn/n/2014/0224/c64387-24448748.html>; Jiang and Li, “28 Provinces have set up Deepen Reform Leadership Small Groups.”

<sup>21</sup> The nominal head of the office is often the secretary general of the Provincial Party Committee, and the head of the Policy Research Office is often the vice-head, for example in Jiangxi. Xiao Ming, “Local Groups take divergent paths.”

<sup>22</sup> Ma Li 马力, “Beijing has set up 14 specialized groups for Deepening Reform; Controlling pollution and Beijing-Tianjin-Hebei [cooperation] are included”

(北京设14个深改专项小组 治大气、京津冀均在列), *New Capital News* (新京报), April 2, 2014, accessed at <http://legal.people.com.cn/n/2014/0402/c188502-24799736.html>; Xiao Ming, “Local Groups take Divergent Paths.”

<sup>23</sup> Xiao Ming, “Local Groups take Divergent Paths.”

<sup>24</sup> Ibid.

<sup>25</sup> Xiao Ming 肖明, “The establishment of Deepen Reform Offices at the province and below levels has accelerated; Local characteristics are evident”

(省以下深改办加速成立: 地方特点鲜明), *Twenty-first Century Business Herald*

(21世纪经济报道), February 21, 2014, accessed at [http://news.ifeng.com/mainland/special/ggldxz/content-3/detail\\_2014\\_02/21/34026656\\_0.shtml](http://news.ifeng.com/mainland/special/ggldxz/content-3/detail_2014_02/21/34026656_0.shtml).

<sup>26</sup> National Development and Reform Commission (NDRC), “Our views on the main tasks for deepening economic system reform in 2014”

(关于2014年深化经济体制改革重点任务意见), issued by the State Council as 国发[2014]18号 on April 30, 2014, and accessed at [http://tgs.ndrc.gov.cn/zyw/201406/t20140617\\_615437.html](http://tgs.ndrc.gov.cn/zyw/201406/t20140617_615437.html).

<sup>27</sup> If we assume that each of China’s 333 prefectures has a DRLSG, and that the 31 province-level governments and 15 municipalities at the vice-provincial level have on average 10 DRLSGs and SGs each, that implies 793 local government reform agencies. At the central level, besides the DRLSG and its 6 SGs, there are well over 30 ministerial and central SOE LSGs. Therefore, 830 would be a minimum estimate of the number of LSGs and SGs.

<sup>28</sup> Section 6 of Chinese Communist Party Central Committee, “CCP Party Center Resolution on several questions relating to comprehensively deepening reform”

(中共中央关于全面深化改革若干重大问题的决定), November 12, 2013, Third Plenum of the 18<sup>th</sup> Central Committee of the Communist Party, accessed at [http://news.xinhuanet.com/politics/2013-11/15/c\\_118164235.htm](http://news.xinhuanet.com/politics/2013-11/15/c_118164235.htm).

<sup>29</sup> Liang Peng 梁鹏等 et al., “The reform of SOEs has fallen into a trap of mistaken understanding; repeatedly taking the easy way out; mixing ownership just for the sake of mixing is worrisome” (国企所有制改革陷认识误区屡屡“走偏”“为混而混”令人忧), *Economic Information Daily* (经济参考报), June 24, 2014, accessed at [http://news.xinhuanet.com/fortune/2014-06/24/c\\_1111277887.htm](http://news.xinhuanet.com/fortune/2014-06/24/c_1111277887.htm).

<sup>30</sup> Zhang Yu 张瑜 and Qian Hejin 钱贺进, “Shanghai: First city in state asset reform”

(上海: 国资改革第一城), *Liaowang Eastern Weekly* (瞭望东方周刊), March 10, 2014, accessed at [http://news.ifeng.com/shendu/lwdfzk/detail\\_2014\\_03/10/34608238\\_0.shtml](http://news.ifeng.com/shendu/lwdfzk/detail_2014_03/10/34608238_0.shtml).

See also “The full text of the 20 Articles of Shanghai State Enterprise Reform issued (上海国资国企改革20条”正式发布[全文]),” December 17, 2013, accessed at [http://finance.ifeng.com/a/20131217/11291452\\_0.shtml](http://finance.ifeng.com/a/20131217/11291452_0.shtml).

<sup>31</sup> Shi Li 史力, “Deepening Reform can’t wait” (深化改革等不得), *Anhui Daily* (安徽日报), April 9, 2014, accessed at <http://cpc.people.com.cn/pinglun/n/2014/0409/c78779-24861979.html>.

<sup>32</sup> Temasek is the Singaporean government sovereign wealth fund, used to invest in a broad range of firms, some of which are state-owned, like Singapore Airlines, but many of which are not. “Chongqing State Asset Reform proposal envisions two-thirds of SOEs being converted to mixed ownership” (重庆国资改革方案拟出 2/3国企将成混合所有制),

---

*Daily Economic News* (每日经济新闻), April 29, 2014, accessed at <http://finance.21cn.com/stock/hgyj/a/2014/0429/11/27099808.shtml>

<sup>33</sup>“State Enterprise Reform proposals have been submitted; Next year start pilot state investment companies” (国企改革方案已上报 明年将启动试点国资运营公司), *21<sup>st</sup> Century Business Herald* (21世纪经济报道), June 6, 2014, accessed at <http://finance.21cn.com/stock/zjl/a/2014/0606/11/27397216.shtml>.

<sup>34</sup> Yu Li 于丽, “The Ministry of Finance clearly lays out the route for the new round of state enterprise reform: Create state-owned investment management companies of 1 trillion RMB” (财政部明确新一轮国企改革路径: 组建亿元(sic)国有资本投资运营公司), *China Finance and Economic News (Weibo, 中国财经报)*, June 4, 2014, accessed at [http://mp.weixin.qq.com/s?\\_\\_biz=MzA5NTQzNzAzNw==&mid=200664276&idx=1&sn=6af09c63122355d808b1d013c8d7c5b4](http://mp.weixin.qq.com/s?__biz=MzA5NTQzNzAzNw==&mid=200664276&idx=1&sn=6af09c63122355d808b1d013c8d7c5b4).

<sup>35</sup> Kang Yi 康怡, “SOE reform document will likely be promulgated after September” (国企改革方案有望9月后公布), *Economic Observer* (经济观察网), June 13, 2014, accessed at <http://www.eeo.com.cn/2014/0613/261871.shtml>. This news article presents the SASAC proposal as the crucial next step in the SOE planning process, which is misleading: The SASAC proposal is more like one (missing) piece of a complex puzzle, since there are scores of “reforms” going forward already.

<sup>36</sup> “SOE mixed ownership proposal submitted to State Council; no regulation on private ownership shares (国企混合制方案已提交国务院 无民资参股比例规定), *AAStocks* (阿思达克财经网), May 13, 2014, accessed at <http://finance.21cn.com/stock/hgyj/a/2014/0513/16/27213324.shtml>.

<sup>37</sup> Heilmann talks about “experimentation under the shadow of hierarchy.” In a parallel sense, consensus formation takes place under the shadow of hierarchy.

<sup>38</sup> Anne Stevenson-Yang and Ken DeWoskin, “What Beijing Means by ‘Reform’: China analysts who expect a step-by-step blueprint for economic liberalization are missing the whole story,” *Wall Street Journal*, May 26, 2014, accessed at <http://online.wsj.com/news/articles/SB10001424052702304587704579585811299776036>. Compare their view with that of the chairman of Goldman Sachs Asia-Pacific, who says, “My confidence in China stems from the fact that the roadmap has been laid out and the strategy has been determined.” Mark Schwartz, “Reason to Be Optimistic on China’s Economy,” *Caixin Online*, March 27, 2013, accessed at <http://english.caixin.com/2014-03-27/100657637.html>.