

# New Approaches to the Study of Chinese Economic Decision Making

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## Introduction and Literature Review

Ever since the People's Republic of China joined the WTO in 2001, the currency controversy surrounding the value of the Renminbi (RMB) has been a popular topic in the media. Even though at first sight this is an economic disagreement, the currency dispute and China's reluctance to give in to international demands for appreciation have to be considered in the broader context of the foreign relations of China and its trading partners. Against the background of China's supposed economic and political rise to great power status, the question of the appropriate value of the RMB became central to Western and Chinese policymakers, scholars and journalists (Bowles and Wang 2006; Bergsten 2010).

This paper argues that the approach taken by the vast majority of the literature on this topic is not adequate. First, it tends to disregard the complexity of Chinese domestic economic decision-making processes. The literature tends to treat China as one coherent unit, with the leaders of the politburo standing committee being the major and often sole decision-makers that can make and implement decisions with little outside interference. Such an elitist understanding is problematic and misleading since it ignores important actors that are involved in the process, but whose influence is not institutionalized and therefore more difficult to trace. The ways in which interest groups lobby, pressure and influence governments can be quite diverse, and I will argue here that this is also the case in China, thereby rejecting the common approach of literature on the currency dispute.

A second common problem of the literature is that most articles exhibit a strong bias towards suggesting adequate and successful measures to confront the Chinese currency regime (or defend it), overall creating the image that the authors know what's best for China and its economic development. However, when for instance authors like Goodfried and Prasad (2008) state that "China has a better reason to adopt a more flexible exchange rate: It would be good for China" (84), it effectively deprives Chinese actors from making their own judgment as well as their own sovereign economic decisions. This, coupled with the misrepresentation of the power distribution in economic decision making in China, can actually obstruct meaningful attempts at decreasing tensions in e.g. trade disputes. Due to these problems with the literature,

this paper calls for a new approach to studying economic decision making in China, one which pays more attention to the complicated reality of competing domestic forces and changing power distributions.

In particular, this paper will focus on one of the groups that has not been adequately considered as an influential entity in the making of the Chinese exchange rate: private entrepreneurs. The embrace of the communist party of the private sector is well documented (Dickson 2007), yet so far it is not clear how their rising importance might be reflected in economic decision-making. As both the number of private entrepreneurs as well as their success grows, their content with the government becomes increasingly important. While there is some truth in the analysis of authors such as Breslin (2010) and Dickson (2007) that maintaining support of entrepreneurs is an important task for the government for a continuous acceptance of the regime, I will provide suggestive evidence here that private entrepreneurs have taken on a more active role than these authors account for. This paper suggests that private entrepreneurs gained more influence on monetary policy making by 2008.

In order to illustrate this, the decision making process of 2008 is taken as a case study. In contrast to earlier instances, private entrepreneurs had organized themselves and pressured the government to pause the policy of RMB appreciation, steering the currency value away from the influence of the market towards more control by the government, effectively revoking a policy that had been adopted in 2005 with the establishment of a currency basket. Thus, the purpose of this paper is to establish that decision making processes in China are more complex than accounted for and, representative of this, that private entrepreneurs are gaining more power in an even more pluralized Chinese decision making process.

This research is limited in that it provides suggestive evidence rather than hard facts for the influence of private entrepreneurs on the decision-making process. It is in the nature of research on decision making processes that testing of claims is obstructed by limited access to data and decision makers, more so even in authoritarian regimes. However, one should not be discouraged from such complications, and the findings of this research are valuable in themselves, as they present a more comprehensive understanding of Chinese politics than the majority of the literature does, thereby offering a new approach to the study of Chinese decision making.

### **The structure of Chinese decision making processes**

In order to understand the means through which private entrepreneurs were able to exert more influence on policy making, it is crucial to look more into the general pattern of decision making in China. This process is on the one hand elitist and clustered around a small group of leaders, the members of the Politburo standing committee, but on the other hand increasingly complex as many different actors have emerged, whose “input” to policy making is more and

more impacting the final outcome. Thus, while the overall decision making process pluralized alongside economic reforms, the weight and support of individual leaders of this committee can be crucial in advancing certain policies, as the final decision is made in the politburo standing committee (see for instance Lampton 2001; Jakobson and Knox 2010; Pearson 2001, 338).

Especially in the early phase of decision making, input in the form of information, analysis and policy suggestions of relevant ministries and bureaus is crucial (Liang 2009, 24) as the few members of the standing committee cannot take control of the whole process. Bargaining, consensus building and compromises play an important role in narrowing down different policy choices. For this purpose, the politburo standing committee relies on so-called leading small groups (LSG) that are positioned between politburo and state council. They are the primary organs to coordinate information and policy recommendations of several other entities. Leading members of the standing committee are usually in charge of these LSGs, and members are usually representatives of the entities that are affected by such policies (Liang 2009, 24). Like this, coherency between LSG and standing committee can be ensured, and uproar against policy outcomes is less likely since policy input and different interests have been seriously considered. Zeng (2009), Jakobson and Knox (2010), Liew and Wu (2007) and Pearson (2001) have analysed which groups contribute to the input phase of policy making until mid-2000s, such as local governments, think tanks, PLA etc. Strikingly, private entrepreneurs are either way not analysed there or considered to be uninfluential, as Pearson's analysis underlines: "no evidence that private interests, including private business ..., [acted] independent of the government [and] weighed in on the WTO issue in China" (2001, 352). Based on this, one can infer that private entrepreneurs cannot have been very influential in policy making processes.

The exchange rate policy of 2005 is an illustration of both the bargaining and consensus style distinct for Chinese decision making as well as an illustration of the absence of private entrepreneurs in the policy process. According to both Yi (2011) and Liew and Wu (2007), it is the LSG called Central Leading Group on Finance and Economics (CLGFE) that is the major organ to decide foreign exchange rate policy. Both accounts argue that the policy process leading to the adoption of a currency basket in 2005 included the input of representatives of for instance the Ministry of Commerce, NDRC, and PBC. These entities were included in the phase of policy input through their membership in the CLGFE. Accordingly, the eventual adoption of a currency basket with a trading band represented a compromise between these entities. As a matter of fact, the decision to de-peg the RMB in 2005 and allow its appreciation disadvantaged export-oriented companies, and cannot have been in the interest of a significant group of private entrepreneurs. From this one can infer that the position of private entrepreneurs cannot have been very powerful on the issues of the currency reform. Noticeably, there is no evidence that particular leaders of the standing committee weighted in on the matter, and the final deci-

sion seems to have been formulated as a compromise of those on the side of policy input.

All in all, until 2005, one can observe that many actors are involved in decision making processes through the input phase, nevertheless, private entrepreneurs are not among these actors.

### **The rising influence of private entrepreneurs**

When the global financial crisis hit China in the middle of 2008, the government had to make a decision on how to respond to the global financial crisis. Two options were considered: sticking to tight macroeconomic policies or a relaxation (China News Service Hong Kong 2008). Eventually, after a period of intensive negotiation, research, traveling and meetings in July 2008, the leadership decided to relax macroeconomic policies. This time, private entrepreneurs had not been passive but rather took an active stance in this process through both providing more substantial policy input as well as through actively engaging with the top leadership.

Three important differences with regards to private entrepreneur's' impact on the input phase of policy making had occurred since 2005. (1) organization of many private entrepreneurs into the so-called China Association of Small and Medium enterprises (CASME) (2) extensive research on the economic situation of private entrepreneurs (3) private entrepreneurs acted as a consultative body in the "hot phase" of decision making in Mid-July 2008.

Concerning the first point, when the currency basket was established in 2005, there was no organization in China through which SMEs (and thus many private entrepreneurs) could organize themselves and effectively lobby for their interests. With the establishment of CASME in 2006, SMEs gained a better organizing platform. First of all, CASME is an important information provider for SMEs, organizing new policies, ministerial announcements, events, and lectures, helping private entrepreneurs not only to access information, but also get in touch with one another. Second, through CASME, SMEs speak with one voice which increases their bargaining power. According to CASME's web page, CASME is the bridge between government and SMEs (China Association of Small and Medium Enterprises 2014). Representatives of CASME feature prominently in the press and expressed their opinions on the economy clearly, overall creating a much more prominent and representative voice in Chinese decision making processes. For instance, CASME had repeatedly appealed to various ministries for better access to funding in the preceding months (The Economic Observer 2008). Concerning the second difference to 2005, extensive research had been conducted since June 13, 2008, in which particular attention had been given to the effect of RMB appreciation on companies (China News Service Hong Kong 2008). Most likely, CASME's influence has led to such a research effort. Concerning the third point, from July 3, 2008 until July 25, 2008, the alteration of monetary policy, including a pause of the RMB appreciation was decided, and

in contrast to 2005, private entrepreneurs were part of consultative bodies that discussed these policies. The process consisted out of several smaller parts, including trips of the leadership to some provinces and companies, but also the consultation of economic experts on this topic in several consecutive meetings. Between July 8 to July 11, regional leaders, economic experts as well as private entrepreneurs would convene and discuss appropriate measures with the leaders of the standing committee (Xinhua Agency Service 2008). The successive days saw other meetings too, but nonetheless, it is evident here that private entrepreneurs have been included in the list of those that should be consulted before a policy decision is made by the standing committee.

In essence, private entrepreneurs have gained more impact in the preparation of policies. As shown above, CASME facilitated policy input from private entrepreneurs, extensive research was directed towards them, most likely initiated by CASME, and perhaps most important, in the hot phase of policy making, private entrepreneurs were part of consultative bodies. All of these points were non-existent in 2005.

Besides more influence with respect to input to policy making, private entrepreneurs also expanded their direct links to the leadership. Such links can be crucial as the weight of certain leaders can advance or hinder certain policies, given the particular character of the Chinese decision making process. Even before the crisis hit China, private entrepreneurs had, through CASME, repeatedly appealed to ministries and top leaders for more support for their companies. In the beginning of July, several members of the top leadership, including Wen Jiabao and Wang Qishan, both prominent members of the responsible LSG, travelled to provinces and visited companies, an endeavour that many newspapers described as unprecedented and unexpected (China News Service Hong Kong 2008; Hong Kong Economic Times 2008). During these meetings, private entrepreneurs could personally lead top leadership members through factories and explain which problems are most pressing and how they believed the situation could be eased. Such personal contact is rare, giving credence to the suggestion that private entrepreneurs' un-institutionalized channels to top leaders are at this time was very influential for the decision making.

All in all, what this analysis suggests is that through gaining more impact in both the input-phase of decision making as well as through direct channels to the leadership, in the realm of economic policy making, private entrepreneurs have successfully improved their position and ability to influence policy making according to their own interests.

### **Concluding remarks**

This paper set out to suggest a new approach to the study of Chinese decision-making processes, as the current approach of the majority of the literature simplifies the process through treating China as a unit, thereby undermining meaningful attempts to understand and solve

issues such as the currency dispute. This research illustrated how diversified, comprehensive and complicated economic decision making in China is. Rather than being a coherent unit, China's economic decision making process involves a considerable amount of bargaining and consensus-building before a final decision is made, and monetary policy is a trade-off process rather than an elitist decision. As an example of the (changing) nature of Chinese decision making processes, this paper looked into the increasing influence of private entrepreneurs on policy making, based on the analysis of the currency reform in 2008. In fact, these findings could justify more research on the role of private entrepreneurs in China's overall political structure. It is likely that private entrepreneurs are, by now, not only influential on issues such as the currency policy but perhaps also increasingly powerful with respect to other decisions being taken. Thus, ignoring them and their role in decision making risks missing out on important actors.

In order to develop further from here onwards, interviews with top officials, private entrepreneurs and other officials would be necessary. A more conclusive proof that private entrepreneurs have a direct and growing impact on the leadership will remain open for future research. Nonetheless, the revelations this research uncovered are worthwhile in themselves because they provide the justification for conducting more research under consideration of this new approach to the study of Chinese decision making.

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