

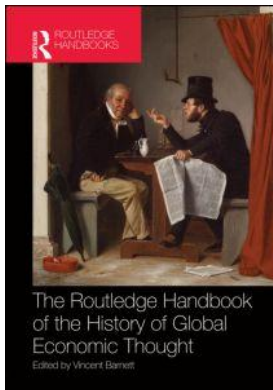
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Vincent Barnett

### **China**

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# 26

## China

### 2,500 years of economic thought

*Zagros Madjd-Sadjadi*

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There is a strong Eurocentric belief that Western civilisation represents the pinnacle of success that all other cultures ought to emulate. Even a cursory glance at most texts in the history of economic thought would erroneously suggest that China had little to contribute. An anti-Eastern bias is found in Weber's (1951) argument that Confucianism and Taoism, while not antithetical to wealth accumulation, lacked the work ethic and the drive to innovate of Protestantism. This is all the more curious when one considers that China had the most advanced economy on the planet prior to the Industrial Revolution, and thus must have had something positive to contribute.

In Beijing today, we find evidence of Western 'cultural imperialism' with children eating McDonald's for lunch, going to watch the latest Disney film, and listening to Chinese popular music with new lyrics superimposed on American melodies. Yet if we reversed our cultural lens, we would see Western culture has long been influenced by China: moveable type, paper money, gunpowder, the crossbow, the decimal system, vaccination and the suspension bridge all trace their origins to China (Temple, 1998). Chinese martial arts through the Hong Kong studios are seen widely around the world and their stars (Jackie Chan, Jet Li, and Michelle Yeoh) have entered the global mainstream. Chinese cuisine is found in every middle-American town and the extent of Chinese cultural influence ranks with only Japanese, French and Indian culture as being able to compete on the world stage with the American variety.

Yet culture has a profound influence on economies and many problems we see in imposing supposedly superior Western solutions onto other regions lie in a failure to understand this basic principle. Capitalism in the United States has been shaped by culture just as capitalism in Europe and Asia are different because of cultural differences, and it is to the Chinese business culture we now turn.

#### **Cultural and business traditions**

Harrison (2013, 83–5) uses a neo-Weberian analysis to argue Confucian-based Chinese and East Asian cultures score well on those dimensions of what he terms 'cultural capital', and that this leads to economic growth. An emphasis on merit and education, as exemplified by the Mandarin system of examinations of old and current *gaokao*, are seen in a positive light. Ancestor

reverence implies not only a duty to the past but also one to the future, leading to a work ethic, future focus, pragmatism, innovation and entrepreneurship, since one will become the ancestor in whose memory others gather. This makes for a curious blend of collectivist and individualist culture quite unlike that of the West.

The West, especially the United States, is typified by an individualistic culture, and neoclassical economics takes the precept that society is composed of atomistic individuals who, in seeking only their own rational self-interests, end up serving those of society. Yet it is rather strange that neoclassical economics has evolved in this manner, given that Adam Smith in his *Theory of Moral Sentiments* never envisioned an atomistic individual abstracted from society.

If we think of rational self-interest as purposefully driven by cultural constraints, we can see why the Chinese version of capitalism is different. There are four fundamental strands of thought that make the Chinese who they are: the legalist, Confucian, Taoist and, in mainland China, Maoist traditions. Achievement is seen in the context of societal need as opposed to individual desire. Nowhere is this more evident than in attitudes towards parenting. Westerners believe that Chinese ‘authoritarian parenting’ stifles the independence of the child, while Chinese parents are disapproving towards Western ‘permissive parenting’ with its negative effect on the harmonious relationship between parent and child (Chao, 1996).

The European passion for individual liberty derives from the Enlightenment. American exceptionalism is a product of the Protestant work ethic, the American Revolution and the drive to conquer the ‘wild west’. Chinese exceptionalism begins with the Yellow River. Confucius (founder of Confucianism) and Lao Tzu (the founder of Taoism) grew up on the river as near contemporaries, but their geographic distance brought about different solutions to the problem of flooding. Confucians seek to ‘control the dragon’ of the Yellow River through a levee and dam system, while Taoists prefer a more *laissez-faire* approach of simply not building on flood plains (Guo, 2010).

Coupled with these traditions are legalism and Maoism. The legalist philosophy is a rule of equality under a stable (though often harsh) legal system. Individuals have no rights under legalist doctrine for the law exists as a mechanism for ensuring social control (He, 2011). Emperors were obliged only to uphold equitable treatment under the law so as to ensure compliance with it.

Maoism, the political philosophy of Mao Zedong, holds the agrarian peasant class as the standard-bearers for a new China. The Agrarian Reform Law of 1950 reformed China’s semi-feudalistic land tenancy regime by nationalising agricultural land and collectivising it into communes comprised of a few hundred households. Private industry was nationalized and progressive five-year plans were introduced to create a ‘Great Leap Forward’. However, China was not ready for everyone to live in a communal fashion. The process destroyed the work ethic, thus ensuring no needs were met in what ordinary Chinese labelled the ‘Great Leap Backward’ (He, 2001, 57–9). Shortly after admitting the programme had been a failure, market liberalisation began under Deng Xiaoping and Liu Shaoqi, but increased social inequality scuttled this project. The resulting about-face led to Deng and Liu’s removal as part of the Great Proletariat Cultural Revolution, a rebellion against traditional Confucian values as part of a rejection of ‘the Four Olds: old thought, old culture, old tradition, and old custom’ (Zhang and Schwartz, 1997, 197). The Cultural Revolution was a disaster but it was only the death of First Vice Premier Lin Biao, in what some believe was a staged plane crash in 1971, that allowed Mao to save face. Lin had been part of a failed coup that had shaken the Chinese leadership and led to the resignation of several high-ranking officials, and Premier Zhou Enlai was able to personally intervene with Mao to bring back Deng Xiaoping to the government as First Vice Minister.

As the health of Mao and Zhou deteriorated, the battle for China's soul emerged between the Gang of Four (Mao's widow Jiang Qing, Wang Hongwen, Yao Wenyuan and Zhang Chunqiao), who favoured a return to mass revolutionary movements, Hua Guofeng, who wanted a Soviet-style planning system, and Deng Xiaoping, who embraced market reforms. When Zhou died in January 1976, Deng lost his principal backer and the Gang of Four sought to discredit him. Mao's death, a mere eight months later, stopped Deng's persecution. He was again brought back into the leadership by the newly installed premier, Hua Guofang. Deng worked behind the scenes to consolidate power but did so with finesse. Even after engineering the removal of Premier Hua, Deng did not purge him from the party apparatus.

China turned towards economic reform once again and Confucianism and Taoism were again allowed to blossom. Maoism remains an important strand of thought within the Communist party and the public at large, especially in the minds of those who see corruption as endemic to the economic reform process.

Confucianism teaches of a reciprocal duty between subject and ruler, between friends, and between family members, as well as conveying the desire for stability. This reciprocity is epitomized by *guanxi* or, to the Western mind, 'connections'. *Guanxi* is more properly thought of as a network of individuals with whom each has an affinity to whom reciprocal duties are owed (*renqing*, literally meaning 'a favour') and for whom failure to exercise these duties leads to a loss of social status, known as *mianzi* or 'face' (de Mente, 2009).

Chinese are reticent to voice displeasure openly with authority so as to avoid trouble, a lesson they learned during the Cultural Revolution, when those who openly criticised the regime were attacked. Still, foreigners who think Chinese are pushovers are forgetting the use of *mei yu ban fa*, which means 'there is no way' as a tactical strategy to prevent things by arguing that others will not allow it, *bu zhidao*, literally, 'I don't know' and *kaolú kaolú*, which means 'I'll look into it'. These phrases mean the same thing: it isn't going to happen, and are often used to dismiss those who lack good *guanxi*. Essentially, Chinese value relationships more than the rule of reason (Macleod, 1988, 162–5). They embrace a dualism that baffles the Western mind, as exemplified in the *yin yang*. Night cannot exist without day, male without female or, taking an economic example, maximisation of profit for business cannot exist without maximisation of utility for the consumer. These dualities are interrelated principles rather than contradictions, leading to an emphasis on situational ethics, whereby one always keeps one's options open.

The ceremonial-instrumental tension of the Veblenian dichotomy is found throughout China, which relies more on cash than credit, the Chinese viewing debt as something inherently negative in keeping with Confucian tradition to eliminate debts with each new year. This self-reliance on internal financing and desire for familial control was noted by Chen, Kiani and Madjd-Sadjadi (2007, 79–80) in a study of 300 publicly traded Taiwanese companies: 'Firms in Taiwan mostly . . . avoided usage of borrowed funds for firm growth. This is crucial in understanding why Taiwan did not suffer much when compared to the other economies in the region in the 1997 Asian Financial crises.' Following up on that study, Kiani, Chen and Madjd-Sadjadi (2012, 1299) noted 'long-run solvency was negatively related to firm growth', suggesting long-term strategies emphasising sustainability and balance, key Taoist and Confucian elements.

China is no monolith. There are critical regional differences. There is greater emphasis on legalism and Confucian values in the north than in the south, which incorporates Taoism: the Cantonese are fond of saying, 'The mountains are high and the emperor is far away'. Similarly, Singapore's regime is more legalist than Hong Kong's or Taiwan's. These tendencies mean that policies that work in one region may not work in another. Indeed, differences within a culture outweigh differences between cultures. However, if one is to speak meaningfully of culture,

one must examine it through a long lens and generalise, even while warning against turning generalisations into stereotypes (Sun, 2010).

As we turn to the history of Chinese economic thought, we should look at how Chinese culture interfaces with the main challenges of achieving an equitable society as well as a sustainable one. All East Asian countries have very high levels of savings, which have translated into low interest rates. Yet Taiwan, Japan and South Korea all have a more equitable distribution of wealth using the Gini Coefficient than China, which is nominally still Communist, and all of the above referenced countries, along with Hong Kong and Singapore, have a lower ratio of wealth held by the top 20 per cent of society as measured against the wealth held by the bottom 20 per cent of society (World Bank, 2013).

### Economic ideas over the long-term

Taoism reflects a basic belief in non-interventionism and Taoists have been called ‘the world’s first libertarians’ (Rothbard, 1995, 23). In Chapter 3 of the *Tao Te Ching*, written by Lao Tzu (604–531 BC), governments are counselled to ‘do that which consists in taking no action, and order will prevail’ (as translated by Lau, 1963, 7). In Chapter 9, the ruler is advised ‘To be overbearing when one has wealth and position is to bring calamity upon oneself’ (as translated by Lau, 1963, 13), and in Chapter 17, to be ‘but a shadowy presence to his subjects’ (as translated by Lau, 1963, 21). Later, in Chapter 57, Lao Tzu provides this warning against what would become legalism: ‘The more taboos there are in the empire the poorer the people . . . The better known the laws and edicts the more the thieves and robbers there are. Hence the sage says, I take no actions and the people are transformed of themselves . . . I am not meddlesome and the people prosper of themselves’ (as translated by Lau, 1963, 64).

These sentiments are echoed by Chuang Tzu (369–286 BC): ‘Let things be what they are. Have no personal views. This is how everything under Heaven is ruled’ (as translated by Palmer and Breuilly, 1996, 61). Yet little economics appears beyond these simple aphorisms. There is simply nothing there (which might be the best concise summary of Taoism). This does not mean Taoism had no influence. Instead, its influence was more to temper the importance of the state in the minds of the populace rather than having any real impact on policy.

In contrast, the Confucians had a definitive system of economic thought. Confucius (551–479 BC), writing only a few decades after Lao Tzu, founded Confucianism and took a low-regulatory but mixed-state approach, as opposed to the pro-state legalism and asceticism of Taoism. Confucianism is concerned with the place of an individual *within* society rather than the atomistic conception of self found in modern economics. Everyone within society has reciprocal obligations, including the emperor, which puts it at odds with legalism. Yet, this reciprocity is practical, as well as moral, as indicated when the Duke of Ai asks how to raise revenues for the state, to which the reply given is to set the tax rate at 10 per cent. The duke is indignant. His tax is currently set at 20 per cent, so wouldn’t lowering it reduce revenues? The reply, from the *Analects of Confucius* 12:9 (Legge, 1893, 255) is pure supply-side economics: ‘If the people have plenty, their prince will not be left to want alone. If the people are in want, their prince cannot enjoy plenty alone.’

It took a challenge, known as Mohism, to Confucian thought by Mo Tzu (490–403 BC) to get Chinese philosophy to go beyond axioms and platitudes and towards systematic analytical reasoning. Mohism was a utilitarian-based ethical system that dispensed with what was seen as wasteful expenses, such as the largesse that Chinese spent on the dead. It has now been largely incorporated into Taoism, but Mo Tzu is noteworthy as being the first to distinguish between use value and exchange value, using the same commodity/example used by Aristotle a century

later, leading one to wonder if the Greek philosopher knew of Mo Tzu's argument: 'A straw sandal used as a medium to buy something else is a straw sandal no more' (Hu, 1984, 10).

The Confucian scholar, Mencius (371–289 BC), discusses at great length the division of labour and why the exchange of goods is the only way society can get all that it needs: 'Why does [the farmer] exchange things in such confusion with the various artisans [rather than] avoid all this trouble [by doing it himself]? . . . The activities of the various artisans inherently cannot be done along with farming' (as translated by van Norden, 2008, 70). He also counselled that a 'benevolent government' was one that 'lessens punishments [and] reduces taxes', while traditional commentator Zhu Xi stated 'the people will be able to fully apply their strength in farming the fields' (as translated by van Norden, 2008, 6). The rationale was two-fold: first, it increased prosperity and second, it ensured a loyal populace.

Confucianism was not always amenable to the free market. Indeed, with one exception, it soon took a more centrist position. Scholars such as Xun Kuang (312–230 BC) pushed against limited government. In contrast to Mencius, who viewed man as inherently good, Xun Kuang believed 'Human nature is evil [and] he is born with a love of profit' (as translated by Knoblock, 1994, 150–1), leading him to argue that government must create laws that will lead individuals to become good. His students, Han Fei and Li Si are considered two of the founders of legalism, which heavily influenced Confucian thought as it jockeyed for favour with the ruling elites. These two philosophies, though derived initially from the same principles, ended up being at odds with one another in a battle over China's soul. Nowhere was this more in contrast than on the advice to governments. Whereas Confucianism would stress having few laws and keeping the punishments light, legalism taught punishment should be heavy but equally applied to the powerful and the weak.

During these battles, legalism tempered Confucianism and it was left to the great historian, Ssa-Ma Chi'en, to reassert the original Confucian conception of a *laissez-faire* attitude towards the economy, even if it was only short-lived (Spengler, 1964). China would show a Confucian face over its legalist character for most of its history, a policy known as *rubaio falì* (Wang, 2011, 110).

Coupled with the philosophical traditions, there was a lot of practical economic advice. According to Hu (1988, 17–18) 'The Tribute System of Yu', a fifth century BC document, details the first exposition of the doctrine of equal sacrifice in public finance. Land quality was the dominant rationale for assessment of taxes, although it was modified by factors such as the distance from the central authority and the locality's relative level of wealth.

*The Art of War* by Sun Tzu (544–496 BC) is a military classic still studied around the world. Yet buried within its text is a clear understanding of key economic concepts. For example, the idea of diminishing marginal returns is found in this passage: 'When you do battle, even if you are winning, if you continue for a long time it will dull your forces and blunt your edge' (Cleary, 1988, 57). This point was refined by Jia Lin, a Tang Dynasty (AD 618–906) commentator: 'Even if you prevail over others in battle, if you go on too long there will be no profit' (Cleary, 1988, 57). A ninth-century commentator to the text Du Mu states 'When provisions go for three hundred miles, the country is out a year's supplies; when provisions go for four hundred miles, the country is out two years' supplies' (Cleary, 1988, 61). Sun Tzu notes the military drives up prices in its vicinity, demonstrating an understanding of how demand affects prices. Karagiannis and Madjd-Sadjadi (2007, 183) argue passages such as these show '[a]lthough theoretically dealing with warfare, the book is really about maximising gain in all arenas'.

Huan Kuan in the *Discourses on Salt and Iron* documents the debates in the imperial court in 81 BC on whether to keep government monopolies on salt, iron and liquor. The debate on iron centred on the efficiency of government enterprises, with Confucian scholars (who were

arguing for a return to *laissez-faire*) stating that the quality of state production was inferior since it was ‘produced to meet quotas rather than to provide for real needs’ (Wagner, 2008, 187). Government officials pointed out that having the iron and salt monopolies in the hands of the government had greatly expanded production due to economies of scale, giving a case of natural monopoly some two millennia before Smith and Mill formalised the concept (Hu, 1988, 266–7). The court was convinced of the correctness of this line of reasoning for both iron and salt, but returned the liquor industry to private hands, though it imposed heavy taxes on its production to offset lost revenue.

Sophisticated price supports were proposed by Fan Li in the fifth century BC and implemented by Sang Hongyang in 110 BC (Hu, 1988, 270–1). By having grain trade within bands, so it was bought when it was ‘too low’ and sold when it was ‘too high’, the government could help assure domestic order. These bands were set so they would only be triggered in extraordinary cases, and normal trading did not cause government intervention nor lead to a sustainable black market.

The *Book of Guan Zi*, a legalist policy primer dating from the fourth century BC, provides one of the earliest formulations of the quantity theory of money in the ‘Shan Guo Gui’. After beginning with an example of how to increase prices tenfold by removing coinage from circulation, it advises ‘While cash is in short supply and valued and goods are plentiful and cheap, buy up goods, paying for them with cash. Money will then be in the hands of the people below, but goods will be in the hands of the government and increase in value tenfold’ (Rickett, 1998, 392). There is no indication of rational expectations kicking in where the public realises that they are being duped by the government, which controls the monetary supply. To increase demand, the government is advised to engage in deficit spending during contractionary times and in saving during expansionary times, since an individual’s income provides the basis for his consumption and if there is no income, there can be no consumption. It also states that individuals will find it difficult to do these things even as the state can.

By the ninth century, it was generally acknowledged that hoarding of money had reduced the level of transactions, but Shen Kuo (1031–95) was the first to detail the effect that foreign trade could have. He noted (Hu, 1988, 394) ‘the barbarian lands in every direction all rely on the copper coins of China’, and he believed government monopolies on necessities would exacerbate the situation, since the higher monopoly prices would encourage imports and thus an exodus of Chinese coins. The solution was to ban imports to decrease the outflow of foreign exchange rather than banning export of coins directly, as others advocated.

We conclude this section with a discussion of the Chinese Malthus, Hung Liang-Chi (1746–1809). Writing five years before Malthus, in the *Zhi Ping Pian* (On Peaceful Governance), Hung noted China’s population, which had reached 400 million people and was doubling every two generations, increased at a faster rate through geometric expansion than the land that could come under cultivation (which grew in a linear fashion). He believed unless arable land could be increased by land reclamation, or by altering the tax burden so as to discourage agriculture, the government would either have to intervene with policies designed to curb population growth in the country, or ‘natural checks’ to population growth (disease, drought, murder, war) would occur as resources per person dwindled. The more pressing concern for Hung was not demand outstripping the food supply but rather rising joblessness (Silberman, 1960).

## Recent advances and trends in economics

Western economic thought was first introduced to China by Karl Gutzlaff (1803–51), a German missionary, who wrote two Chinese texts on economics, *Outlines of Political Economy* in 1839

and *Treatise on Commerce* in 1840. By the 1880s the first Western economics texts were being translated and studied in China. However, these texts were modified to reduce what was seen as a bias towards low tariffs, regarded as an imposition of Western thought onto Chinese autonomy. Intellectuals such as Ma Jianzhong, one of the first Chinese educated in the West, viewed Western thought in more mercantilist terms, stressing increased exports to achieve wealth (Trescott, 2007).

The first attempt to directly translate the *Wealth of Nations* in Chinese was made by Yan Fu in 1902. Although not an economist by training, it was the first attempt to translate the classic and is even more important because of the translator's inclination to interpret, rather than merely translate, in a manner that could accommodate, rather than supplant, Chinese intellectual traditions (Lai, 1989). This was part of a trend towards rehabilitation of Chinese thought and only nine years later Chen Huan-Chang (1911) introduced the Western world to Confucian economic principles in his masterwork *The Economic Principles of Confucius and His School*, which contains a brilliant exposition of Confucian economic theory and its relationship to Western economic theory.

From 1920 to 1939, the works of many Western economists were translated into Chinese, including J.M. Keynes, F. List, K. Marx, I. Fisher, H. George, A. Marshall, T. Veblen and D. Ricardo. However, there was a strong anti-imperialist current coupled with the socialist philosophy of Sun Yat-Sen, who was heavily influenced by George rather than Marx. This laid the groundwork, not for mainstream economics, but for the introduction of institutional economics in the Veblen-Ayers-Commons tradition, since institutionalism was not antagonistic to socialism. For example, at Yenching University most of the economics faculty had studied under institutional economists from the United States (Trescott, 2007).

Until Mao took power in 1949, Marxist economists were removed from their posts due to strong anti-communist Kuomintang policies. After 1949, Marxist thought became ascendant but with a Maoist flavour. Most Western economists were suppressed, but ironically Smith and Ricardo were taught since both were referenced favourably by Marx (Trescott, 2007, 320). Still, while Marx believed the rising organic composition of capital led to a declining rate of profit and to economic crises, Mao did not focus on this aspect since China was predominantly an agrarian society without large-scale industrialisation. Instead, Maoist theory concentrated on the development of the peasantry, and most economics of the time dealt not with theory but rather with practical questions of how to engage in industrialisation without losing China's rural character. However, with China's industrialisation more traditional Marxian analysis has come from the Chinese New Left, including Minqin Li and Cui Zhiyuan.

Minqi Li (b. 1969) attended the University of Massachusetts, Amherst and is one of the foremost Chinese Marxists. He believes the insertion of China into the world economy will hasten the decline of the worldwide rate of profit, bringing about the end of the capitalist world system. His argument rests not on traditional Marxian analysis but on the squeeze between competitive prices and the rising cost of energy due to climate change. He views the coming collapse as necessitating a transition to communism so as to ensure a fair distribution of resources in its wake (Li, 2008).

Cui Zhiyuan (b. 1963) was heavily influenced by John Mill and James Meade, explicitly calling for the creation of a 'shareholder-cooperative system' that would pay a 'social dividend' in a similar fashion as Meade's 'labour-capital partnership' (Cui, 2005). He regards social inequality and uneven regional development as critical issues for China.

The Chinese New Left was a reaction against the reform movement, which was developed by Gu Zhan (1915–74). During the 1950s, he dared, along with Sun Yefeng (1908–83) to argue that the market, not the state, was the proper vehicle for socialist planning. These two



economists heavily influenced Liu Shaoqi and Deng Xiaoping and are the intellectual fathers of Chinese economic reforms (Song, 2013). They, in turn, influenced Wu Jinglian.

Wu Jinglian (b. 1930) is known as ‘Market Wu’ for his unbridled championing of markets. A protégé of Gu Zhan, Wu also cites James Buchanan and Douglas North as his main influences. As someone involved in the decision-making process, he has written the definitive study of the evolution of China’s economic reforms from the 1950s to 2002 (Wu, 2005). He believes China has become a crony capitalist society with high levels of rent-seeking behaviour, and has publicly condemned the Chinese New Left for advocating ‘restarting the Cultural Revolution and establishing a total dictatorship over the bourgeoisie’ (Wu, 2012).

Zhang Weiyang (b. 1959) worked with Wu Jinglian and introduced the ‘dual-track price system’ to China. This system provides a centrally planned price for a predetermined quota amount of production, and then allows all production above that quota to be set by the market. By reducing the quota over time, one can successfully transition to a market economy. In recent years, Zhang has become an Austrian economist, declaring that it is time to ‘bury Keynesianism’ in a speech to the China Entrepreneurs Forum (Bhattacharya, 2012).

Since 1976, a dialogue has opened between China and the West, mostly in the form of orthodox economic thought as well as two strands of heterodoxy: institutionalism and Post Keynesian. However, there are gaps in the knowledge base with J.K. Galbraith and G. Myrdal seen as prime proponents of neo-institutional thought and little attention paid to such important luminaries as Clarence Ayers, Marc Tool or Paul Bush (Zhang and Xu, 2013, 320).

Gregory Chow (b. 1929) is one of the world’s top econometricians and developer of the Chow (1960) test that checks the stability of a regression either over time or across groups. He also demonstrated the superiority of the Lagrangian technique over other more complex dynamic programming methods (Chow, 1997).

Stephen Ng-Sheong Cheung (b. 1935), former Professor of Economics at the University of Hong Kong and a former colleague of Ronald Coase at the University of Chicago, is probably the most important of all contemporary Chinese economists from the standpoint of economic theory. A leading member of the New Institutional School of economics, in his ‘simplistic general equilibrium theory of corruption’ (Cheung, 1996), he argues international competition in private markets limits the ability of officials to obtain bribes. Corruption tends to increase in areas where competition is inherently limited, such as antiquities and state-owned enterprises that have been granted a monopoly. Moving from a hierarchical-based property rights system, where claiming resources depends on your position in the party, to a private-property-based approach opens opportunities for corruption and this can cause institutional sclerosis, preventing a full transition to a market-based economy. This worsens under democratically formed governments since individuals vote themselves opportunities to be corrupt.

In ‘Irving Fisher and the Red Guards’ (Cheung, 1969), he asserts that Mao’s interpretation of a ‘social contradiction’ between individuals who desire limited resources is inherently superior to Marx, but still fundamentally flawed. Whereas Marx believed a communist state would end competition since man was inherently good, Mao believed it would endure, but in an unstable form, unless something could be done about human nature itself. This presented a rationale for government action: if human nature does not change naturally, it must be forced. The Red Guards, acting on Mao’s instructions to abolish private property, took it to the logical extreme of eliminating all differential rents, even those due to superior intellect or ability, leading to the disaster of the Cultural Revolution.

Two other articles are considered seminal reading in transaction cost economics. Cheung (1983) discussed the problem of defining a firm as a set of contractual arrangements existing to reduce market transaction costs, and notes that piece-rate payment and other endeavours

that treat workers as independent contractors threaten to destroy the notion of what a firm actually is. In ‘The Fable of the Bees’ (Cheung, 1973), he demonstrates the traditional view on reciprocal externalities was inaccurate. So long as both parties could exchange services and benefit from that interaction, a market can develop. Similarly, he has shown that the use of bride prices (payments from the groom’s family to the bride’s) and foot binding served to enforce property rights at a time when children were viewed as an economic good, and this consequently reduced female infanticide (Cheung, 1972).

In 1957, Ma Yinchu (1882–1982) proposed his ‘New Population Theory’, advocating China begin state-enforced family planning (Ma, 1997). Ma had been one of the first Chinese graduates from Columbia University and was influenced by Malthus. Initially decried as a reactionary who did not uphold socialist values, by 1979, his viewpoint had become government dogma with the introduction of the ‘One Child Policy’. Solving one problem may lead to others, as suggestions arise for the Chinese government to re-examine this policy in light of a demographic crisis of too many males and a rapidly aging workforce. After all, Taiwan, Hong Kong and Singapore, none of which have had a population control policy, all have birth rates lower than mainland China. Still, pointing to these counterexamples as a rationale for abandoning the one child policy is problematic, since levels of development differ.

Zhou Xiaochuan (b. 1948), governor of the People’s Bank of China, has argued that using SDRs (special drawing rights) rather than the US dollar as the world’s reserve currency will resolve the Triffin paradox whereby the reserve currency country (in this case the United States) ends up with a permanent trade deficit as it attempts to provide liquidity for the rest of the world (Zhou, 2009), a policy the International Monetary Fund has cautiously endorsed.

Yu Yongding (b. 1948) has been influenced by Nobel Laureates Robert Shiller and Paul Krugman. He argued that China needs to reduce its capital and current account surpluses. The ongoing US budget deficit, the dysfunctional US political system and the aforementioned Triffin Paradox make a rapid devaluation of the US dollar more likely, which will negatively impact China’s investments. He believes diversification, including into gold and away from US treasuries, is beneficial for this reason and will act as a steriliser for the vast amounts of foreign currency coming into the country, so that it does not lead to mal-investment. China suffers from severe overinvestment in the property market (both commercial and residential) and this is causing a major bubble. Indeed, this overinvestment might be masking actual *underinvestment* in productive capital and infrastructure (Yu, 2006, 2013).

Yang Xiaolai (1948–2004), then called Yang Xiguang, spent 10 years (1968–78) in prison after writing a notoriously scathing critique of the Chinese Communist Party from a leftist perspective entitled ‘Whither China?’ It set the stage for the ‘bourgeois democracy’ and the desire for a ‘privatized economy’ (Unger, 1991, 34). In deriding ‘the red capitalist class’, it is cited as a precursor for the backlash against corruption that is now manifested throughout the country (Unger, 1991, 3). While in prison, he taught himself calculus and later undertook a PhD in economics. He contributed to our understanding of infra-marginal economics. Infra-marginal decisions are those that cause discrete future path-dependency that closes off some alternatives while opening others. Infra-marginal analysis also leads to endogenous specialisation, reduced transaction costs, and network effects that contribute to increasing returns in society (Yang, 2001).

### Dissemination of national traditions overseas

As the Qing Dynasty crumbled under the weight of misguided policies and European colonial expansion, many Chinese emigrated. They sought better opportunities and reacted to greater

despotism among ruling elites who had abandoned Confucian values. The Chinese used familial connections to create an insular network that gave them an advantage in business dealings. They were hated for their successes and were stereotyped as being greedy and having little allegiance to their new countries. Later, overseas Chinese lost their connection to their homeland when, in the 1960s, China revoked their ability to hold two passports, and in 1980 the right to immigrate back to China for overseas Chinese descendants was removed.

Despite this, the Chinese continue to be determined not to assimilate on anything other than their own terms. There are three main reasons why the Chinese remain Chinese and succeed regardless of where they go: education, cultural acceptance and the *huis*.

There is a Confucian saying on a banner in our family's Chinese ancestral home: 'All other occupations are ordinary; only scholarly pursuits are held in high regard'. The Confucian philosophical belief that education is of primary importance has led to success around the world and the Chinese tend to concentrate their endeavours in subjects leading to well-paying jobs (business, economics, engineering, sciences). This is less evident in mainland China due to the Cultural Revolution (1966–77) where *all schools* closed from June 1966 to February 1967 (and in the case of urban schools and universities even longer), and educational attainment was interrupted for millions, sometimes as long as five years. There is still a pronounced reduction in educational attainment for those who came of age during that time (Guo, 2010).

Cultural acceptance is high among the Chinese, who incorporate 'Chinese characteristics' into foreign ways. It is not merely for public consumption that the Chinese describe their economy as 'socialism with Chinese characteristics', or perhaps more appropriately 'capitalism with Chinese characteristics'. The Chinese may dress in Western clothes and use English in business dealings but they do so without abandoning traditional culture or their use of their native tongue at home and with other Chinese.

The *huis*, small credit associations organised under the term 'family association' and found in almost all overseas Chinese enclaves, are, in theory, merely social clubs where those with the same family name can congregate and receive assistance. In reality, they serve as a back-channel banking system that provides credit to Chinese who are often discriminated against (at least the Chinese perceive themselves to be discriminated against) by local banks. Monetary obligation serves to bind the community together and reinforce their identification with other Chinese.

The Chinese have always given their host countries a blend of Chinese and local culture. Fortune cookies (authentic Chinese restaurants would serve oranges as an after-dinner treat instead) and chop suey are unheard of in China, but have made an indelible mark in Western countries. Confucianism and Taoism are studied, as are ancient Chinese classics such as the *Art of War*, in universities around the globe. Still, the biggest influence of Chinese culture on other lands (other than through the emigration of Chinese citizens) is the Chinese written language and the Chinese philosophies sent to other Asian countries, specifically Korea, Vietnam and Japan.

Chinese characters, called Hanja in Korean, Han tu in Vietnamese and Kanji in Japanese, served as the basis for literate society in those three countries for millennia. They came by way of trade and conquest. Buddhism, with its various Chinese literary texts, was incorporated into the cultures of these countries. Legalism and Confucianism in its more state-oriented configuration bridged the gap to Korea and Japan. Taoism influenced ordinary ethnic Chinese rather than elites and there was a great deal of intermarriage between Vietnamese and Chinese due to a long history of rule by China of Vietnam. Taoism, though present in both Japan and Korea for 1,400 years, never became a major philosophical influence and was relegated to folk religion status in Korea and Japan.

Korean and Japanese society ended up with a corporatist form of governance giving rise to Japanese *zaibatsu* and *keritsu* and Korean *chaebols*, the large interlocking industrial conglomerates that control much of the Korean and Japanese economies. Taiwan, Singapore and Hong Kong tend to have smaller companies more focused on single industries, greater emphasis on equity financing due to negative Confucian attitudes towards debt and more economic freedom. It is nonetheless a mistake to regard the Chinese experience as a model for the world stage. Even within Chinese society, the blend of legalist, Confucian, Taoist and Maoist elements causes friction and disagreement. To the extent it works, it relies upon human nature transformed by centuries of philosophy, and it cannot be wholly lifted into another context without considering the cultural foundations upon which it lies.

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