Chinese Politics in the Global Financial Crisis

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Summary

- This year’s financial crisis not only has had an impact on China’s growing international influence, but also its domestic politics.

- The state has assumed a stronger role, both in supporting state-owned companies and with respect to the provinces. So far this has enhanced the authority of the Wen Jiabao government.

- Government stimulus packages may boost the economy, but also carry the risk of aggravating the recent boom-bust approach. Bad loans made now could create future political problems. Corruption is a major political problem.

- China’s development strategy is likely to shift to a more self-reliant, less export-dependent model.

- The threat of social unrest is manageable, with security forces taking on increased importance.

- Despite the current political stability, the Party is entering a key period ahead of the next leadership transition starting in 2012.
**Introduction**

There has been much discussion on the political implications of the global financial crisis in many parts of the world. What about China? China has politics too, not of the electoral kind, but in broader terms of addressing questions of where domestic power lies and who has access to the different political and economic resources.

To date, much of the international commentary on the political impacts of the economic crisis on China have centred on the question of social stability. In effect, whether the party-state can deal with increased unemployment, particularly among migrant workers and young graduates, or whether any tensions might pose a serious threat to regime stability (although this debate tends to treat China and the Chinese state as a monolith without looking at the diversity within the country). Other discussions have focused on whether China’s economic growth will be enough to lift the world out of the recession, and how the crisis will affect China’s international standing, with plenty of commentary (rightly) seeing this as a moment bringing greater Chinese clout in world affairs. There are other domestic political issues in China which might be affected by the economic crisis, and this paper attempts to examine some of them.

**The impact of the economic crisis on China**

The full economic impact on China will only unfold with time. What is known is that the impact includes a huge hit in overall GDP growth, down to 6.1% (yoy) in the first quarter of 2009 (the lowest since 1992), although growth has revived in the second quarter. Other figures both support and challenge indications that a further resumption in growth can be expected. There is regional variation in how badly China has been hit, and the government has responded accordingly.

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1 This paper is based on extensive reading of Chinese and international media and other sources on recent events.
Within the Chinese economy, export industries have suffered the most and consequently some of the toughest economic and social challenges are in the coastal export-oriented provinces. At the beginning of the year, up to 20 million migrant labourers returned to rural villages from burgeoning cities without jobs, some have found employment elsewhere and others are beginning to return to the coast. Graduate unemployment has increased, not just by the increase in university graduates. The Party is particularly concerned about the potential for social unrest. It has become further aware of the country’s economic (and hence social) reliance on the global economy, feeding further into the desire to rebalance the economy towards domestic consumption, a desire which is already part of the government’s economic strategy.

To help examine the political implications of the economic crisis, this paper attempts a preliminary examination of how the interests of particular groups within China are being affected by the crisis.

For the central Party apparatus and the senior leadership, the economic crisis is being seen as both a threat and an opportunity, with the sense of crisis tending to dominate. The rapid drop in GDP growth is of serious concern to a leadership whose legitimacy depends largely on continuing to deliver economic and social development, and whose strategy for dealing with challenges has been heavily dependent on easing people out of social and economic problems. The way the financial crisis has unfolded, and in particular the massive hit to Chinese exports, raises questions about the current Chinese development model (see below).

There is also a serious concern about social instability, particularly in a year which sees the anniversaries of the iconoclastic May Fourth 1919 movement, the May and June social movements in 1989, the public eruption of Falungong protests in 1999, as well as the sixtieth anniversary of the establishment of the People’s Republic. Although social unrest since 1989 has remained localized and generally related to specific issues, the total

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2 There are of course many ways of profiling Chinese society, and the impacts on different groups will vary not just between but within any individual grouping
number and scale of ‘mass incidents’ has increased, and the fear has been that this year’s anniversaries might bring risks of larger-scale movements.

As well as challenges, the economic crisis also brings opportunities. As seen by the central party-state, these opportunities have arisen firstly in the international arena as Beijing promoted its views more strongly in a number of fora (such as the IMF and G20), and also domestically. The Centre has pushed through increased subsidies to rural communities and taken forward another round of infrastructure development (such as railways) which could enhance long-term domestic growth prospects and address current bottlenecks. The concerns about social instability present a challenge for the security forces, whilst at the same time strengthening their hand politically as their work has moved to centre stage.

For provincial and local officials, social stability is of major concern too and not just because of the Centre’s strict instructions to avoid allowing incidents to get out of hand. The cut in growth provides challenges in creating jobs, reduces provincial government revenue, and makes the implementation of centrally-mandated social programmes, such as those in education, health and social welfare, more difficult. On the other hand, the major stimulus package gives local officials (like their central counterparts) opportunities for investment in growth and to improve their infrastructure; it also opens up space for graft, which is likely to increase in spite of the anti-corruption drive which has accompanied the package.

Businesses across the board have been affected by falling economic growth. Profits at many state-owned companies have been hard hit, with some suffering the impact not just of falling demand, but due to the failure of their financial investment strategies, such as fuel hedging in the airline industry, or state-owned conglomerate CITIC’s massive losses on the Australian dollar. The chances of any major state-owned company going bankrupt is very small, although not impossible – recall the GIGIC bankruptcy in 1998 during the Asian financial crisis when the current Vice Premier Wang Qishan was the Guangdong Vice Governor charged with sorting out the mess created by GITIC overstretch. State companies have so far benefited from the stimulus measures, more so than either their non-state counterparts or the SME sector. Moreover, the government’s position towards the state sector seems to reflect a wider policy assumption: that this sector remains central to the
type of Party-guided development the leadership envisages for the PRC. This supports an important conclusion of this paper - that the crisis marks a strengthening of the state relative to other actors.

The preference for the state sector is despite the fact that ‘non-state’ or people-operated (minying) companies create more jobs and have been bigger contributors to GDP growth over recent years. They too are suffering and will be affected by a further slowdown in continued market reforms. The arrest of Gome Chair Huang Guangyu and other corruption investigations show that private companies are not immune to political pressure at this time. From a broader political perspective, the Party appears to have little to fear from private entrepreneurs who remain largely supportive of the current system even if they are at the same time somewhat constrained by it.

This general political attitude, which might be characterized as ‘conservative’, is largely reflected across the urban white collar workforce. Stock market falls (although these predate the crisis and the index has risen substantially so far in 2009) and cooling property markets, have affected financial interests, as too will the challenges of graduate unemployment. The increase in political activism has been at the local level and in response to specific issues, suggesting that it is not due to the financial crisis, and has been largely neutralized by flexibility in official responses on specific issues.

The urban poor and rural migrant workers have been amongst some of the hardest hit by the crisis, with factory closures and lower demand across the economy increasing unemployment. This potentially increases the risk of social instability among lower classes. But contrary to some reporting which implies that migrant labourers returning to the countryside are an inevitable threat to social stability, there is anecdotal evidence that this is tempered by the willingness of many to take a break from difficult work away from home in the cities, or that they have found jobs elsewhere closer to home. Nor does

\[\text{3 For example the 2007 protests against a petrochemicals plant in Xiamen and 2008 protests against the maglev extension in Shanghai.}\]
there appear to have been a significant increase of unrest in the countryside. Indeed, rural communities may in fact benefit from the emphasis on rural infrastructure development in the stimulus plans and from specific programmes such as subsidies on domestic white goods for rural residents.

**Implications for policy and politics**

Even before the economic crisis hit in the autumn of 2008, there were signs of shifts in China’s political environment. The international disputes around Tibet and the pre-Olympic torch relay strengthened the hands of more conservative elements and of those within the security apparatus who tend to attribute not just Tibetan resistance, but also other political opposition, to ‘western anti-China forces’. Economically, the government slammed the brakes on in mid-2008 in response to an overheating economy and the fear that substantial inflation would induce social dislocation, raising questions about the consistency and sustainability of economic policy making. This in turn highlighted the need for progress on the Party’s existing, but broader, long-term political agenda of improving governance. Some experiments in political reform, such as pilot elections at the township level, were also halted in 2008. With this general background in mind, it can be argued that the following shifts in policy and politics may be the result of the current crisis.

Firstly, the crisis has brought to the fore and strengthened (in relative terms) the state’s role in development and managing the economy. State-owned enterprises may find their bottom lines seriously challenged, but politically they are likely to emerge from the crisis with enhanced influence. This is likely to reduce the pace and scope of any future economic reforms which might lessen the influence of state-owned companies. For example, it is likely that the authorities will continue to emphasise strategic national industries and sectors, take a conservative approach to M&A (both domestic and international), and limit price liberalization or further deregulation in these areas.

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4 It is worth noting that the majority of incidents are connected to the confiscation of land for development or general disputes among rural communities and with officials, not necessarily primarily correlated to any level of employment of growth.
This relates to a second, more strategic, area of policy debate. Since the 1990s neo-liberal-influenced approaches to development (such as pushing free trade or maximizing the marketization of the Chinese economy) have gained substantial ground in China, although their wings have been clipped this decade by the more ‘people-focussed’ approach of Party General Secretary Hu Jintao and Premier Wen Jiabao. The economic crisis is likely to shift the centre of gravity in the formulation of China’s future development model, giving greater priority to social issues and less influence to the voices of those who suggest that further market reform is the best way to resolve the social and developmental problems China faces. This also covers attempts to stimulate domestic demand and reduce dependence on exports (which had risen substantially as a driver of growth since China’s WTO accession in 2001).

However, and thirdly, the immediate emphasis on reviving the economy appears to be coming at the expense of some – though not all – of the broader social goals of sustainable development and a harmonious society which have characterized the leadership’s approach since at least 2002. The most salient of these is in the area of environmental protection, where the rush to push through major stimulus projects risks storing up problems in the medium term (environmental degradation is a major cause of social unrest). Although recent news that two major power companies were ordered to halt work on dam project in southwest China suggests that the Environmental Protection Ministry may be prepared to tackle some of these issues. Secondary to this, it is likely that both corruption and bad debts will increase as a result of stimulus measures. While the short-term consequences of these are manageable, corruption in particular is an area which has driven societal dissatisfaction with the Party in the past thirty years.

Fourthly, for many people the crisis has weakened the authority of western approaches to reform as well as damaged the reputation of the US. The impact of this should not be overstated, but it is likely to lead both to a greater belief in the feasibility of China pursuing its own approaches to development issues and to stronger nationalism particularly in economic areas (including political support for Chinese companies and the government both domestically and overseas).
Fifthly, there is the issue of where power lies within the Chinese system. Here, this refers to the relative power of different parts of the party-state and of leaders or factions within it. On the basis of evidence so far, there are signs of the following shifts within the system:

(i) The authority of Wen Jiabao’s government has been boosted, both domestically and overseas, with the increased role of the state and government under Wen’s leadership quietening talks heard pre-crisis about the government’s limited control over the economy.

(ii) Internationally, President Hu Jintao has been prominent in China’s economic diplomacy (e.g. at the G20). Hu’s protégé and the designated successor to Wen, Li Keqiang, has had a slightly lower profile until he emerged to take charge of the healthcare reform package announced in April. Fellow Vice Premier Wang Qishan has played an important role nationally and overseas. In the provinces, Wang Yang (Guangdong) has shown firm political and economic leadership. Other rising stars, such as Bo Xilai in Chongqing, have faced important tests of their ability.

(iii) The balance between centre and provinces is a constant question in Chinese politics. The economic crisis has strengthened the centre whose financial and policy support has been helpful, if not necessary, in reviving many of the regional economies.

(iv) The central administration responsible for dealing with the financial industries has been extremely powerful over recent years, and still appears to retain substantial latitude within the system. Nonetheless their relative influence is likely to have declined with the obvious challenges met by the international financial sector. Zhou Xiaochuan’s call for SDRs as a new global reserve currency could be seen as an attempt to dip into nationalist sentiment at home in a bid for wider political support, as well as a statement to international audiences on the US dollar. Conversely, the parts of the machine responsible for rural areas or social policy are likely, over the medium term, to find their weight increased as a result of the greater shift to social policy (see above).
Finally, fears of social unrest have strengthened the importance of the Party’s internal security apparatus. The military will also be taking advantage of the more general moves by Beijing to increase China’s international clout, including through further modernization.\(^5\)

**Conclusion**

This analysis suggests that risks of social instability from the economic downturn are not sufficient to pose a serious challenge to Party rule. The leadership, well aware of the problems, is focusing its policy response on addressing them. In the 1990s the Party succeeded in dealing with arguably much bigger social and political challenges arising from an earlier phase of economic restructuring. Nonetheless, the seriousness with which they are taking the current challenges reflects genuine nervousness about the significant social and economic dislocations which exist in China today. If these are not consistently addressed over the coming years, then the risks to continued Party rule will increase.

Previous economic and social crises have had a significant impact on China’s development path and its political makeup: for example, the 1989 protests which saw the rise of political conservatives, followed by the 1992 return to the path of reform; or the 1997-98 Asian financial crisis, which allowed China, to present itself as a responsible and benign regional player. The current crisis will not only see an increase in China’s relative weight in international councils, especially economic ones, but coincides with increasing nationalist confidence to confront domestic challenges. In the short-term, it is likely that there will be a more prominent role for the state, accompanied by a cautious and (where possible) more self-reliant approach to development. With the next major leadership transition in 2012 approaching, delivering results at home will continue to dominate the Party’s agenda. Demonstrating success in this will be a priority for those senior cadres hoping for promotion in the major reshuffles of 2012.

\(^5\) Military ambitions and capabilities warrant separate detailed analysis as the PRC approaches its 60th anniversary.