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September 2018

POLITICAL ECONOMY RESEARCH INSTITUTE

WORKINGPAPER SERIES

Number 467

State and Capitalist Class in China's Economic Transition: From Great Compromise to Strained Alliance

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Abstract

This article contributes to the debate on the role of the Chinese state in economic transition by shedding light on the relationship between the state and the emerging domestic capitalist class. In contrast to the literature that regards the state as a supra-class developmental state, we argue that the relation between the state and a new capitalist class is the product of a two-way movement of top-down forces and bottom-up forces over the course of a transition from a stage of what we call 'Great Compromise' to a stage of what we call 'Strained Alliance'. The state-class relation has evolved with the dynamics of class conflicts, external constraints, and contradictions within regimes of accumulation.

JEL Classification: O10, O53, P16

Keywords: Chinese state, formation of a capitalist class, two-way movement, accumulation regime, developmental state

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1 Introduction

Over the past four decades, the Chinese economy has undergone a transition from a state-socialist to a capitalism-dominated economy. This transition has given rise to not only the great transformation of the working class but also the formation of a domestic capitalist class. The economic transition has made the resurgence of the bourgeoisie particularly entwined with state structures. What role did the Chinese state play in the formation of the capitalist class? What was the impact of the new class into the state? How do state-class relations evolve with the dynamics of internal class conflicts, external constraints and contradictions within the regimes of accumulation? These are the questions to be addressed in this article.

It is vastly recognized that the state continuously played a significant role during China's economic transition. At the beginning of that transition, the state firmly controlled the economy via the central planning system. While capitalist firms play a crucial role in the economy today, the state continues to command the economy via a large state-owned, non-financial enterprise sector, a financial system dominated by a few giant state-owned banks, and a land ownership system largely controlled by local governments. State interventions in the economy are also made through industrial policies and control over crucial prices such as interest rates, exchange rates, and minimum wages. Some scholars argue that the state has gained stronger capacity of controlling the economy, and they express concerns over the prospect of marketization. These scholars point to recent studies showing that the fiscal revenue as a share of GDP has significantly increased since the mid-1990s (Naughton, 2017; Piketty et al., 2017). Therefore, from the perspective of a state-market dichotomy, China appears as a puzzle to the conventional wisdom, since it has witnessed both the rise of the market and a significant role of the state.

The literature largely explains that puzzle by emphasizing the specificity of the Chinese political economy in terms of the relation between the state and emerging capitalists. These studies posit that the Chinese state created the new bourgeoise so that it has adequate capacity to maintain control over it (So, 2003; Dickson, 2008; McNally and Wright, 2010; van der Pijl, 2012, 2016; McNally, 2017). In pursing their economic interests, new capitalists seek to participate in the state and to establish interpersonal relationships with officials, rather than seek an alternative political regime. Similarly, but coming from a neo-liberal tradition, Yao (2010, 2011) argues that China has a neutral government that pursues the goal of development without endorsing the interests of any class. This picture of a neutral government also implies a state with adequate power over the capitalist class or any other class or group so that it can maintain neutrality. Finally, it is noteworthy that these studies somehow mirror the official ideology of 'Socialism with Chinese Characteristics' in that they all contend that capitalists are merely instruments for achieving the fundamental goal, no matter it is economic development or a particular version of socialism.

For critical approaches such as Marxian political economy, capital accumulation would not have taken place without the political power of the state, neither the state has a supra-class role over the emerging bourgeoisie. A proper perspective is not a state-market dichotomy, but rather a dialectical relation in which the dynamics of capital accumulation are vitally entangled with the accumulation of political power. Not only does the state provide the regulatory, legal, and repressive framework for private ownership, contracts, and competition to occur, it also tries to contain crises, reduces uncertainty on the return of capital, and guides the accumulation of capital in varied forms (de Brunhoff, 1978). On the other hand, the state also depends on the accumulation of capital for its functioning, either mechanically, through the collection of taxes, or through the more abstract relationship between the accumulation of wealth and the increase of the state's capacity. Generally speaking, class conflicts, capitalist competition, international forces, and the contradictions generated by accumulation not only shape the state, but are also shaped by the state (Jessop, 2008; Cox, 1981).

In this article, we examine the role of the Chinese state in the historical formation of the capitalist class and the changing patterns of the relation between the state and this emerging class with a Marxian political economy methodology. We provide a systematic account of the dialectical relation between the Chinese state and the new capitalist class, and argue that the formation of the new domestic capitalist class is a two-way movement: the top-down forces of the state interacts, conflicts, and compromises with the bottom-up forces of the new economic elites or capitalists. This two-way movement remains a prominent feature of the relation between the state and the capitalist class in China today. In contrast to the studies that talk about classes or interest groups without analyzing class relations,[1] we argue that this two-way movement is a process affected by

[1] Fine (2013) and Chang (2013) have provided comprehensive evaluation and critiques of missing class relations in the developmental state literature.

class conflicts, international constraints, and the contradictions within the changing regimes of accumulation. As a result, the relation between the state and the capitalist class has undergone a transition from a stage of what we call 'Great Compromise' to a stage of 'Strained Alliance'. We evidence the dynamics of this relation and suggest how this dynamics links with the regime of accumulation in a broader way. With this, we hope to contribute to the debate on the role of the state in the process of economic transition.

In what follows, this article is organized into four sections. In Section 2, we briefly review the literature on the subject and present our approach. Section 3 discusses the relation of the state and the capitalist class *during* primitive accumulation after Deng Xiaoping's famous southern tour. There were two main mechanisms for the concentration of capital in private hands: the privatization of state and collective assets, and the expropriation of rural lands. Section 4 discusses the interactions between the state and the capitalist class *after* primitive accumulation by focusing on the state's indigenous innovation policies and responses to the accelerated process of financial expansion. Section 5 discusses the further implications of the two-way movement and concludes the article.

2 Literature Review: From the Developmental State to the State as a Social Relation

A recent research agenda has proliferated around the complex relation of the state and the new domestic capitalist class in China. A significant part of this literature understands the state as the creator of the new capitalists and that it maintains strict control over the new class (Dickson, 2008; van der Pijl, 2012, 2016). To a large extent, this literature reverberates the notion of the Weberian developmental state as an autonomous, rational actor endowed with a talented bureaucracy with a long-term, coherent, and well-intentioned view of economic development. As Hui puts it in her broad review of the literature on the Chinese state, the state is treated as an actor which is free-standing from society, leaving state-society relations secondary, if not marginalized (Hui, 2017). In a sense, the state in this literature resembles the 'epistemological entity demanded by the strategies of development' referenced in Fiori (2003, p. 101)'s critique of Latin American national-developmentalism, where the state is detached from both class interests and capitalist accumulation.

Both for Dickson (2008), who calls this new class 'red capitalists', and So (2003), who describes the emergence of a 'cadre-capitalist class', the Chinese state has adopted a rationally articulated process in order to create capitalists from its own rankings or to co-opt emerging capitalists. Both authors discuss the disproportionate participation of entrepreneurs in the political structures of local and central governments, as well as the enrichment of the families of traditional political elites at all levels. In the same vein, for van der Pijl (2012, 2016), the state has anticipated and guided class formation, leading to a 'contained capitalist class', quite harmonious in its relation to political power and disinterested in a broader process of political and economic liberalization. On the contrary, 'there seems to be a convergence in strengthening the state politically, even in its authoritarian lines' (van der Pijl, 2012, p. 513). The entry of entrepreneurs into the Chinese Communist Party (CCP) is interpreted as 'a sign that the political class can absorb upward social forces in the structures it controls' (van der Pijl, 2012, p. 512).

Even more emphatically, McNally and Wright (2010)argue that the party has been successful in co-opting its emerging capitalists via benefits of privatization and subjective bonds of reciprocity, making the Chinese bourgeoisie deeply encrusted to the party-state apparatus for links that range from objective material interests to affective ties. In a more recent article, McNally (2017) argues that the Chinese political economy has been driven by a dialectic of a top-down, state-centered mode of governance interacting with bottom-up modes of entrepreneurship based on market competition; this dialectic is a constant in the evolution of what he calls 'Sino-capitalism'. However, McNally still portrays private capitalists as uncoordinated individuals without political power.

'Neutral government', proposed by Yao (2010, 2011), is another influential and representative interpretation of the state as standing above class interests. Yao argues that the Chinese government has been a neutral government since the beginning of the reform era in the sense that it does not endorse any 'interest group' and it is able to discriminate any 'interest group' for its own purpose; this disinterested government sets economic growth as its main goal in order to maintain political legitimacy. Yao further argues that thanks to the neutrality of the government, China, like some other East Asian economies, has successfully avoided the formation of either a populist government or an elite government, both of which are believed to be harmful to economic growth. While praising the state for its favorable role in economic growth, Yao contends that the government achieved economic success by following the Washington Consensus. While from a neo-liberal tradition, this theory resembles above-mentioned studies because the 'neutral government' is in nature a Weberian state isolated from society, and because the neutrality of the government implies that the state has adequate power over any particular class or interest group.

Although from very different traditions, all the above-mentioned studies discuss classes or interest groups without discussing class relations that evolved during the transition of the social relations of production. Therefore, their analyses fail to interpret the Chinese state in the face of class struggles, and they do not trace the state-class relation to capital accumulation. Put differently, the literature underscores the specificity of the state but ignores the historical class relations that gave rise to this specificity. Thus, in these cases, the state is not descriptive of the concrete struggles of the classes in formation and in transformation.

To address this important issue, this article conceives of the state as a social relation. The political and the economic orders, despite their formal institutional separation, may come to be structurally coupled to produce a relatively unified historical bloc (Jessop, 2008, p. 25). The modes of exercising state power are the result of complex social relations which are historically determined by the forms capital assumes (ibid.). This article highlights the dialectical nature of the relation between the Chinese state and the new capitalist class. This relation should be understood as a historical-concrete process. The state played an active role in the formation of the new class, whereas this formation in turn affected and shaped the state. The state is not invariable but evolved through its interactions with the formation of the new class, as did its goals, strategies, and actions. This dialectical relationship between the state and the new class evolved with changes in social relations of production.

In the following sections, we will show how the pressure of the new privileged elites who emerged in the reform of the 1980s played a role in the concentration of wealth in private hands, a consideration which is often ignored in the literature. Put it differently, the institutional shifts that the state initiated to support the new class were at the same time influenced by pressures from the new privileged elites. The state's political power was constantly impacted by the newly privileged as well as by its clashes with the working class. The next two sections are devoted to detailing the relationship between the state and the capitalists by separating history into a stage of primitive accumulation and a stage after primitive accumulation, respectively. They show how this relationship is intertwined with the regime of accumulation, class struggles, and domestic-foreign conflicts.

3 Great Compromise: The State and the Capitalist Class in Primitive Accumulation

3.1 Privatization for the insiders

The privatization of state-owned enterprises (SOEs) and collective enterprises in the mid- and late 1990s was the first massive movement of primitive accumulation in China since the beginning of the reform era in 1978. Inaugurated with the policy 'grasp the large and let the small go' (*Zhuada Fangxiao*),[2] privatizations entailed a broad and diverse movement of reorganizing the ownership structure of the enterprise sector, leading to not only the emergence of a domestic private capitalist class, but also to the strategic positioning of large state-owned companies. Privatization also led to the dismantling of the social security system and full urban employment, thus laying foundations for the dominant role of the capitalist relation of production and the regime of accumulation led by both investment and exports.

For the new capitalists who became owners of the former state or collective assets, privatization occurred via a process that often resembled asset transfer rather than sale. The beneficiaries were often 'insiders' with connections at privatized factories or in local governments, mainly ex-factory managers and local officials. Generally, these insiders were able to affect the pricing of the assets, either by virtue of their advantage in knowing the information about particular assets or their personal connections with local governments, which resulted in asset losses, debt forgiveness, and subsidized credit for investors without sufficient capital. There are many records of ex-managers or local officials who did not pay anything but became owners of privatized enterprises by means of loans to be paid with future profits. The literature summarizes this process as a 'privatization for the insiders' (Lau, 1999; Li and Rozelle, 2004; Chen, 2006; McNally and Wright, 2010).

It is often noted that it was the state that initiated privatization and thus that this process was a state-led, top-down one; however, this view has neglected the bottom-up pressures and the contradictions of this historical conjuncture. In our view, privatization formed part of the 'Great Compromise' between the state and the new elites whose rise was a result of the reforms of 1978-

[2]The central government has always opposed the term 'privatization' and instead uses the term 'restructuring' of state-owned enterprises. The state also never made the sale of state assets a coherent official policy, and there was no national legislation to regulate the process beyond a few intentionally unclear general lines. In the absence of national regulation, local and provincial authorities were left with considerable discretionary power to decide how industrial property should be transferred to private hands (Chen, 2006; Cao, 2000).

1989, the initial stage of the reform era. While the 1980s witnessed some success of reforms, it was in general a crisis-ridden decade, especially during the second half of the decade, when the state launched urban reforms (Qi, 2018). Significant growth in peasants' income failed to persist, as high purchasing prices set by the state eroded fiscal sustainability.[3] Relaxing regulations on wage distribution led to excessive growth in wages and purchasing power, which, along with price reforms, contributed to inflation that jeopardized economic and social stability. The dual pricing system was established with the purpose of maintaining the planning system while introducing market incentives to firms; however, it offered an historical opportunity for the rise of new elites. Making use of personal ties with officials, these new elites extracted rent out of the dual pricing system by buying at lower planning prices and selling at higher market prices. The amount of rent reached 30 percent of the national income in 1988 (Hu, 1989). Ironically, among the strata participating in the social movement of 1989 were new elites who gained great benefits from the decentralization of the 1980s. These new elites stimulated the rage of the social movement in 1989 but at the same time actively pushed for more radical privatizations and reforms (Wang, 2011, p. 31). By the end of the 1980s, the party had been directly confronted by an emerging bourgeoisie seeking new frontiers for accumulation (Wang, 2011; van der Pijl, 2012).

After the turmoil of the social movement in 1989, from 1990 to 1991, the state was dominated by leaders in favor of stability and more cautious policies, and market-oriented reforms suspended. The conjuncture of a slower economic growth as the result of stabilization policies, the precarious political legitimacy of the state after the turmoil, the demise of the Soviet Union, and international sanctions generated internal and external pressures on the state and threats to state power. Deng Xiaoping hoped all those pressures could be relieved by revitalizing economic growth through further marketization reforms. In 1990, Deng explicitly said, 'Why do the people support us? Because over the last ten years our economy has been developing... If the economy stagnated for five years or developed at only a slow rate... This would be not only an economic problem but also a political one'(Vogel, 2011, p. 668). In his famous southern tour at the beginning of 1992, Deng clearly sent signals to other leaders, including those in favor of stability: 'Whoever is against reform must leave office' (Vogel, 2011, p. 673). Deng secured political dominance in the leadership, thus transforming

[3] Agricultural subsidies rapidly increased from less than 1 percent of the fiscal expenditure in 1978 to 12 percent in 1984, equivalent to 44 percent of the state's infrastructure investments. After 1984, the relative size of the price subsidies consistently fell. Sources: *China Fiscal Yearbook 1999*.

the state's strategy from emphasizing stability to pursing economic growth by further extending the reform path without resolving problems of the crisis-ridden 1980s associated with the rise of the new elites.

Therefore, right after Deng's southern tour in 1992, the 'Great Compromise' between the state and the new elites came into being and persisted until the mid-2000s. The compromise constituted the background for not only the privatization for the insiders mentioned above, but also the symbiotic relationship between local governments and the capitalist class, as we will discuss in Section 3.2. Through primitive accumulation, the new elites recruited the insiders, who were formerly managers of state-owned or collective firms or local officials, and the manufacturing or real estate capitalists, who occupied rent from land expropriation by making use of the symbiotic relationship with local governments.

In order to visually reflect the 'Great Compromise', we measured the shares of the state (governments and SOEs), private capital, and labor in the primary distribution of the net value added in the corporate sector (non-financial corporations and financial institutions).[4] The net value added of the corporate sector is the sum of employee compensation,[5] taxes on production (less subsidies) and corporate taxes paid to governments, the after-tax profits of state-owned capital, and the after-tax profits of private capital. Figure 1 presents the shares of the four parts. It shows that labor's share (the share of employee compensation) experienced a major decline from 1996 to 2008 and recovered moderately after 2010. From 1996 to 2008, the governments' share rose from 21.2 percent to 28.8 percent, while state-owned capital's share rose from 4.2 percent to 10.0 percent. The state's share—the sum of the governments' share and state-owned capital's share—rose by 13 percentage points. Private capital's income also increased dramatically over this period, from 9.1 percent to 17.3 percent. Both of the increases were at the expense of the labor's share.

[Figure 1 inserts here.]

The 'compromise' implies a shift in the state's strategy in the face of the emerging new elites and contradictions of the accumulation regime in the 1980s. But it does not mean a new political

[4]The advantage of using this data source is that they distinguish among the corporate, government, and household sectors, allowing us to focus on the distribution within the corporate sector and the relative positions of the state, private capital, and labor in the primary distribution. It is noteworthy that the primary distribution is a crucial aspect of distribution, although it does not reflect the transfer of income.

[5]Employee compensation includes management salaries, which overestimates the distributional share of labor; however, there is no reliable data source to exclude this effect and this should have no significant effect on the trend.

power was replacing the state. In other words, the compromise did not undermine the state's power but shaped the goals for which and the way in which the state used its power; the state's power was still prominent. In the late 1990s, restructuring of the state-owned sector led to the consolidation of the strategically positioned state-owned enterprises that could control the nodes of accumulation, play a crucial role in technical progress, carry out counter-cyclical macro policies, and seek to ensure natural resources outside the country. Remaining SOEs dramatically dried up their social responsibilities in labor reproduction and focused on the pillar industries with strategic significance, such as energy, chemical, steel, telecommunications, banking, and so on. They are the ones who today lead a good part of the internationalization process of Chinese firms. This combination of the new class's formation and the state's still-prominent power reveals their dialectical relation: on the one hand, the political compromise came into being partially as a result of the contradictions within the accumulation regime of the 1980s; on the other, the economic shifts such as marketization and privatization in the 1990s were premised on the political compromise and the particular structure of the state's political power.

3.2 Expropriation of land

The large-scale expropriation of rural land was a second and powerful mechanism for primitive accumulation that occurred in the background of the 'Great Compromise'. Through the expropriation and commodification of rural land, private capital gained a considerable share of the rent that could be distributed to rural collectives – the original landlords. Although rural land is owned by rural collectives in China, local governments have the prerogative to expropriate a certain amount of rural land for the sake of 'public interest.'[6] However, given the local governments' pursuit of urbanization, the annual land conversion quotas determined by the central government have been explicitly ignored (Zhou, 2008). With land prices skyrocketing in cities,[7] local governments have used their control over the conversion of rural land as a way to increase off-budget income and

[6]Legally speaking, rural land can be converted into urban land under three distinct claims: use for public goods (transportation, irrigation and energy projects, health and education), industrial use, and business development (including commercial and real estate construction).

[7]The legislation governing urban land ownership is distinct from rural land. In rural areas, there is no concentration of land partly thanks to the collective regime. In cities, the real estate market works as in most capitalist countries. Urban land is owned by the state, but private ownership is permitted in the case of urban real estate, which today is traded according to market rules (including leading to real estate bubbles in large cities in the late 2000s). Once the transformation from rural to urban land, everything that is built on the land 'granted' to the urban entrepreneur can be transacted as private property.

attract investments to their regions.

Since the 1994 tax reform, which helped the state re-centralize fiscal revenue,[8] local governments have sought to overcome budgetary constraints in a number of ways, especially through land expropriation and development. Land expropriation and development improved the fiscal condition and economic performance of the municipality, which is fundamental in the political career of local officials. At the turn of the century, the country went through what Riskin (2008) called an 'epidemic' of expropriation, fueled by both the expansion of the housing market (inflated by rapid urbanization and speculation) and the fiscal needs of local governments. Tao et al. (2010) report case studies showing that fiscal revenue related to the expropriation of land accounted for between 30 percent and 60 percent of total revenue on the municipality level spheres in the mid-2000s. It is estimated that a total of 70 million farmers had lost their land by 2006 and had received 'grossly inadequate' compensation, according to Riskin (2008). The case studies attempting to measure the national mean value of compensation (Tao et al., 2010; Zhou, 2008; Guo, 2003) suggest that compensations to farmers have been between one percent and ten percent of the price paid by those who receive the grant of land. The country's arable land has shrunk to 1.827 billion *mu* by the end of 2008, only slightly above the 1.8 billion *mu* (120 million hectares) bottom line set as the minimum needed for national food security.[9]

The symbiotic relationship between local governments and private capital is obvious. Capitalists as industrial investors pushed local governments to expand the spatial possibility of accumulation via land expropriation and infrastructure building, pressuring for lower land costs and lower environmental standards. Capitalists as real estate developers kept a significant share of ground rent through local governments' infrastructure building that created massive urbanization and population concentration. On the other hand, both industrial investors and real estate developers helped local governments to maintain solvency. In the early 2000s, to attract investments, local governments tended to individually negotiate with investors instead of holding public bids, which was favorable for capitalists to gain the ground rent. In some more radical cases, around the Pearl River Delta, the price paid for land was virtually zero (Tao et al., 2010).

[8] The 1994 tax reform determined that the central government would hold 75 percent of VAT, the value-added tax, the main source of tax revenue, against 25 percent reserved for local government. The system re-centralized revenues but kept spending unchanged, creating a significant fiscal gap in local accounts.

[9] Sources: *China Statistical Yearbook 2009.*

A comparison of real estate profits and net land transfer income reveals that real estate developers' gains have grown much faster than local governments' gains from this symbiotic relationship. From 1998 to 2015, the gross land transfer income to local governments rose from 50.8 billion yuan to 3078.4 billion.[10] Local governments need to spend a significant part of their land transfer income on preliminary infrastructure construction and to a lesser extent compensation for land expropriation; thus, only the net land transfer income can be treated as gains by the state. Figure 2 compares the growth of governments' net land transfer income to that of the real estate enterprises' profits from 2000 to 2015, showing that the profits of real estate enterprises have grown more rapidly than has the net land transfer income of governments.

[Figure 2 inserts here.]

The result has been a distorted system of urban land expropriation that benefits real estate developers and industrial entrepreneurs, alleviates the local budget but leaving the cost of rapid urbanization to ex-peasants, in turn coercing the landless to sell their labor power. Moreover, the concentration of income through price appreciation and speculation in the housing market of large cities was, at the turn of the century, one of the main mechanisms for increasing inequalities in China (Galbraith et al., 2009).[11]

4 Strained Alliance: The State and the Capitalist Class in the Face of Increasing Struggles

4.1 Promoting indigenous innovation

Privatization and the expropriation of land contributed to the formation of an investment-led and export-led regime of accumulation. With support of a state-dominated banking system, SOEs and local governments carried out massive investments, which significantly promoted economic growth. Since restructured SOEs concentrated mostly in industries related to raw materials, energy, and infrastructure, a healthy competition between SOEs and private capital transpired. Low costs

[10] Sources: various issues of *China Fiscal Yearbook* and *China Land and Resources Statistical Yearbook*.

[11] The authors also relate real estate speculation to the changes in the legislation on capital flows in the country, which since 2002, despite maintaining control over the inflow of capital, ended the limits of foreign currency that can be kept in cash by Chinese companies.

of land and labor, coupled with enormous industrial scale and infrastructure, attracted foreign capital to invest and produce mainly for the global market. Favorable domestic conditions and the restructuring of global capitalism made China a world factory. However, this investment-led and export-led regime had contradictions which arose from both internal class conflicts and external constraints. Since the mid-2000s, these contradictions have led to a re-adjustment of the relationship between the state and the new-born capitalist class, leading to what we call a stage of 'Strained Alliance', marked by increased international competitive pressures and clashes with the working class.

First of all, privatization and the expropriation of land gave rise to social unrest and struggles of laid-off workers and landless peasants. Due to the reform in the state-owned sector, about 50 million jobs were lost between 1995-2003 (Chavance, 2017), leading to a reserve army of laid-off workers and an explosive increase in job informality (Lee, 2016). The urban revolts that hatched in China in this context were what Lee (2007) deems 'protests of despair'. Former state employees spontaneously took to the streets, strongly anchored in the Maoist discourse of rights under socialism and public ownership. These protests of despair were also caused by the accelerated commercialization of public services, especially health and education, as privatizations also entailed the dismantling of *danwei* (units), the former socialist system of urban social protection.[12] On the side of the landless peasants, over the course of the 2000s, conflicts over land were the main cause of mass incidents, due to the historical relationship between land use and social protection.[13] This social unrest demanded a more sustainable regime of accumulation to contain internal conflicts.

Secondly, since 2004, the rapidly growing export sector in the southeast region experienced a labor shortage. Wages of migrant workers have witnessed a substantial increase (Lu, 2012). While there was a large reserve army of labor in both rural and urban areas thanks to both demographic reasons and institutional shifts, labor processes in the export sector, characterized by long hours, high intensity, and low pay, meant that only some workers out of the reserve army could meet the needs and accept such working conditions. The disadvantage of Chinese capital in the global value

[12]This vacuum in social protection was only seriously addressed in the second half of the 2000s, after intense conflicts and varied mobilizations promoted by the precarious working class.

[13]Equal distribution of land among the rural population was the main social protection since the end of the communes. Universal access was an impediment to the formation of a landless poor class, as is the pattern of so many underdeveloped countries, and was the main guarantee of subsistence for rural workers in the absence of a social protection system. Not only could migrants return to their land in cases of lack of work in cities, but old and sick people could find some form of protection against extreme poverty and destitution (Riskin, 2008).

chain has restricted its capacity to bear wage raises, making the export-led regime unsustainable.

Lastly, the state's 'Trade Market for Technology' strategy had its limitations. This strategy was promoted by the state in the 1980s and 1990s as a replacement for the Maoist self-reliance strategy. While no leader of the state opposed introducing foreign technologies, there was a debate in the leadership about whether the self-reliance strategy should be abandoned in the early 1980s. Supporters of introducing foreign technologies dominated the state; as the result, some crucial projects such as the Shanghai Y-10 aircraft was abandoned (Lu, 2006). The new strategy was to transfer advanced technologies from foreign capital by establishing joint ventures and by allowing it to enter the domestic market and keep some monopoly (Lazonick and Li, 2012). However, this strategy failed to bring about sound technology transfer because these joint ventures only manufactured but did not participate in any R&D activity (Lu, 2006; Zhou and Liu, 2016). The transformation of the global production network also made technology transfer impossible. Criticism of the state's science and technology strategy arose from intellectuals. They were concerned that China's dependence on the unsuccessful technology transfer would jeopardize not only the sustainability of growth, but also economic independence and national security.

Given these internal conflicts and external constraints, the state initiated systematic support for indigenous innovation, seeking to summarize a broad set of policies to stimulate innovation and the formation of global Chinese brands and technologies. These policies gained momentum in 2006 due to the '*Zizhu Chuangxin*' (Indigenous Innovation) program launched by the Hu Jintao and Wen Jiabao administration.[14] This program set up a national plan involving several ministries in ambitious megaprojects. It used both the domestic market and the internationalization of Chinese state-owned enterprises (via use of Chinese equipment, components, and technology abroad) to generate demand for products and innovations developed in China. These policies were expected to help establish a new regime of accumulation marked by the rise of the country in global value chains.

The Indigenous Innovation program adjusted the relation between the state and the capitalist class, which requires that the expansion of capitalism take into account political legitimacy and the social conflicts behind it. Given internal conflicts and external constraints, a consensus arose within

[14] This program further developed into the '*Zhongguo Zhizao 2025*' (Made in China 2025) program in 2015 launched by the Xi Jianping and Li Keqiang administration, which is believed by some analysts to be the real target of Donald Trump's trade war against China (Dodwell, 2018).

the CCP that political legitimacy must be rebuilt and the state could not and should not bear all the social costs arising from the unleashed expansion of capitalism. State support for the emergence of Chinese technologies is associated with the ideal of building a strong China that does not become the subject of external control, which met with general domestic support. The Indigenous Innovation policy, along with the Harmonious Society proposed by the Hu-Wen administration and the Common Prosperity proposed by the Xi-Li administration, sent the signal that the new class should contribute to rebuild political legitimacy.

While the Indigenous Innovation program relied heavily on restructured SOEs, it supported private firms in a selective manner, revealing the state's tendency to adjust the regime of accumulation. Two instruments have been widely used as innovation policies based on domestic demand: public procurement and the choice of technical standards, both much contested by international competitors. Equivalent to 3.5 percent of GDP (2016),[15] government procurement was quickly perceived as an instrument for boosting national brands. A main beneficiary of the program was Lenovo, a private company with state-owned history. The choice of technical standards by the state has often been used in the telecommunications sector to stimulate Chinese firms. Both Huawei and ZTE, two major Chinese telecoms brands, were favored by the choice of the V5.1 standard, used in switching systems for large capacity telephone exchanges and jointly developed by these two private firms. Until the mid-1990s, this pattern was restricted to the rural interior of China, where these companies were able to penetrate without foreign competition. It was at this point that the Chinese government stipulated that all new switching systems sold in the domestic market should be compatible with the V5.1 interface. As most foreign firms did not produce systems in this interface, the expansion of domestic brands was significant until competitors from outside managed to adapt (Zhao et al., 2007; Nogueira, 2015).

The third-generation mobile phone standard is a telling example about the formation of the cooperation between SOEs and private firms. From the mid-2000s onwards, there have been reports of pressure from Chinese manufacturers for protection and defense of indigenous technology via, for example, technical standards for mobile phones. In 2009, the government selected TD-SCDMA as the technical standard for third-generation mobile phones, after intense dispute between domestic state-owned operators, foreign manufacturers and domestic private manufacturers (Lee et al., 2012).

[15] Sources: Ministry of Finance of P.R.C. (2017).

The standard was developed by Datang, an SOE that suffered from open resistance from foreign manufacturers (mainly Motorola and Nokia) and domestic operators but was supported by domestic manufacturers. In 2009, 3G TD-SCDMA was not only adopted nationally, but also accompanied by a national support program through credit and subsidies for domestic manufacturers (Gao and Liu, 2012; Nogueira, 2015).

The central countries' reaction to these instruments has been intense. The Chinese government demanded a specific stamp of independent innovation as a prerequisite for participation in public procurement in 2009. But the measure was repealed in 2011 after threats from the U.S. government (Nogueira, 2015). Similarly, while it was still a proposal, the Trans-Pacific Partnership (TPP) had specific chapters prohibiting, by signatory countries, the use of public procurement as an innovation policy. Throughout its various chapters, the initial draft of the TPP was an explicit case of bans and vetoes on the set of industrial policies, domestic market protection, and innovation support that China has undertaken to promote its indigenous industries and technologies. In sum, the attempts of Chinese firms to take leading posts in the global value chain have intensified inter-capitalist rivalries and international tensions. An increasingly inhospitable world order has raised the level of tensions for China, which has in turn intensified the urge for a re-adjustment of state-domestic capitalist compromise.

4.2 Repressing financialization

Repressing financialization is the second part of the re-adjustment of the relationship between the state and the new capitalist class, and it also serves as evidence of increased tensions in this relation. Financial expansion took place when China's private capitalist sector lost momentum as the global economy was trapped in the Great Recession after the global financial crisis of 2008. The state stimulus package dramatically increased the leverage of both local governments and SOEs, which gave rise to the significant expansion of a shadow banking sector (Ehlers et al., 2018). In this context, a fraction of the bourgeoisie imposed pressures on the state to demand financial liberalization. However, concerned about the independence of the financial system, the state repressed these attempts, which, again, demonstrates a two-way movement between top-down forces and bottom-up forces.

Possibly one of the features that most strongly distinguishes China's accumulation regimes from other economies is in its relative independence in relation to financialization tendencies under U.S. hegemony. This is part of what Lo (2016) called China's resistance to the systemic dynamics of global capitalism. Financialization, which has affected the rhythms and modes of accumulation from developed to developing countries since the beginning of neoliberalism in the 1980s, has not penetrated the Chinese economy in the same way. For the most part, this is hampered by the essentially state-controlled financial system, where the state imposes limits on short-run capital flow and speculation (Vermeiren and Dierckx, 2012). This does not mean, however, that the Chinese economy has not gone through financial overdevelopment in recent years. On the contrary, all three scenarios that we have described earlier have been accompanied by some expansion of finance. But financial expansion in China is centered on the attempt to create a monetary system less dependent on the U.S. dollar and more based on multipolar institutions under Chinese control or influence (Aglietta and Bai, 2016). This includes the consolidation and expansion of development banks as ultimate lenders (such as the Asian Infrastructure Investment Bank), with infrastructure investments funded by such banks being expected to be a dynamic engine of global growth. These attempts also include the expansion of the international use of the Renminbi in transactions, including oil.[16]

This process of financial expansion arose in the mid-1990s and gained spectacular impetus after the global financial crisis in 2008. While the state maintains strict control over capital account, private capitalists have penetrated China's financial circuits in two ways.

First, private capitalists participated in shareholding with state corporations through direct purchase of shares or via financial holding companies, investment funds, and insurance companies. This new bourgeoisie pressed for further capital opening of large SOEs under central management, most of which are now listed in stock markets with limits to non-tradable shares. Investment funds and new holdings were established to allow for the sale of shares and became fast vehicles for the formation of large fortunes (Wang, 2015; Cao, 2000; Lau, 1999). It is this same fraction of the financially-minded bourgeoisie that today leads the call for financial and capital account liberalization. The state has led the process of financial expansion of SOEs, under intense pressure from the new domestic capitalists, leading to what Wang (2015) calls the 'shareholding state'. Virtually

[16]China has established future oil contracts denominated directly in its currency, so these contracts can be traded in yuan, not dollar, on the Shanghai International Energy Exchange (INE). The petro-yuan is a clear challenge for petrodollars, one of the elements that sustain the dollar as the monetary standard of the international system. 'China taking the long road to solve the petro-yuan puzzle'. Asia Times, March 28, 2018, available at: http://www.atimes.com/article/china-taking-long-road-solve-petro-yuan-puzzle/

all major SOEs have been transformed into publicly traded corporations and have undergone an accelerated process of securitization in the last decade, mainly as a way to raise capital and to vent domestic pressures by new frontiers of profits.

Second, private capitalists speculated on real estate. Financial overdevelopment in China mobilized and channeled domestic resources via the financial system for major infrastructure and urbanization works, especially after 2008. And at the same time, it has opened channels for the penetration of private capitalists in the speculative highways, which is one of the causes of the current real estate bubble. Local governments, for their part, have made aggressive use of leverage to finance urbanization, especially through a special purpose vehicle called local financing platforms (LFP). In 2013, more than 7,000 LFPs were accounted for, with loans representing 40 percent of local government debt (Theurillat et al., 2017; Wang, 2015). The LFPs use different state assets as collateral—leasing sliced public services in state-owned enterprises, tax revenues and, above all, mortgaged land. These structured products are then repackaged into securitized products sold by banks to investors.

This process of financial expansion, however, came with contradictions and tensions. A fraction of the new Chinese capitalists is pushing for financial liberalization under hegemony of the U.S. dollar. These rentier capitalists withdraw increasing slices of their earnings from financial activities. Together with foreign interests, they are the ones pushing for the opening of China's capital account. In March 2017, during the 5th Session of the 12th National People's Congress, business executives of the financial and civil construction sectors openly criticized capital controls as instruments that hinder Chinese acquisitions abroad.[17] So far, Chinese financial expansion has maintained autonomy in relation to the power of the U.S. dollar precisely because of the state's control of capital. But internal and external pressures are strong, and China's expressive outflow of capital in 2016 shows its vulnerability to unregulated speculative movements. From 2015 to 2016, during a limited liberalization attempt, China lost almost half a trillion dollars in international reserves (precisely 443 billion U.S. dollars), bringing total reserves down to below 3 trillion U.S. dollars for the first time since 2011(Tsui et al., 2017; Chen, 2017).

The social tension generated by this fracture within the capitalist class became evident in do-

[17] 'China's Capital Control Trigger to Backlash after Scrapped Deals.' Bloomberg News, March 7, 2017, available at: https://www.bloomberg.com/news/articles/2017-03-07/china-s-capital-controls-trigger-a-backlash-after-deals-thwarted.

mestic struggles. Since the anti-corruption campaign launched by President Xi Jinping in 2012, corrupted officials have been arrested and punished, as well as some capitalists and officials who have made a fortune in the financial system. Wu Xiaohui, a financial capitalist with strong ties to former high-level officials, was arrested in June 2017. His arrest comes in the wake of other arrests of businessmen and regulators, and a new campaign to redress financial corruption. Wu Xiaohui's holding company, called Anbang Insurance Group, is one of the largest in the country, and has been notable for its billion dollar purchases of luxury hotels around the world. In November 2016, Wu tried to close a Manhattan hotel deal with Jared Kushner, the son-in-law and adviser to U.S. President Donald Trump.[18] The case is just one glaring example of the connections of a fraction of Chinese capitalists with international capital, which current Chinese leadership is trying to contain via intense internal struggle.

5 Discussion and Conclusion

We deny both that the state firmly controls the new capitalist class, and that the state is a developmental state detached from society. In our view, the Chinese state during the process of economic transition is not invariable; rather, both class conflicts and external constraints affect the state and in turn are affected by the state. The seeming autonomous power of the Chinese state can only be fully understood by taking into account the historical trajectory of social relations. On the one hand, the state's autonomy is a legacy of the revolution and class struggle in history that led to the foundation of the current state form. While the state in the reform era abandoned some goals set by the earlier Maoist regime, it has retained the goals of economic development and enhancing living standards of the people in order to maintain political legitimacy and to contain internal and external conflicts. On the other hand, this autonomy is also the result of a gradualist path of reform. In contrast to a more radical path that led to economic recession and political rebuilding in Russia, the gradualist path assumed by China has enabled the historical trajectory to play the role of generating persistent effects. This also means an analysis of contemporary Chinese political economy should regard the state as a social relation with historical dynamics, rather than reducing

[18] 'Chinese tycoon reportedly caught up in sweeping corruption crackdown'. The Guardian, June 14th 2017, available at: https://www.theguardian.com/world/2017/jun/14/chinese-tycoon-reportedly-caught-up-anti-corruption-crackdown-wu-xiaohui-anbang.

the state to either a neutral supra-class or a servant of the capitalist class.

The consolidation of a capitalist class is among the most fundamental transformation of the Chinese social structure of the last four decades. This urges us to problematize the conventional developmental narrative that states that Chinese success is due to the materialization of a rational and well-intentioned Weberian state. Such a narrative should be problematized not only for its excessive 'methodological nationalism' and disconnection with external constraints, but also because of its detachment from the social structures and class dynamics that characterize the expansion of capitalism.

This article showed how the formation and transformation of the capitalist class was intertwined with the dominant accumulation regime. In the period of 'Great Compromise', through privatizations for the insiders, the state both responded to pressures for reforms and strengthened the strategic positioning of the remaining SOEs. This laid the foundations for a capitalism-dominated economy, including from the point of view of the formation of an urban labor market with an unlimited supply of labor. Likewise, the expropriation of peasants' land and the explosion of investments in housing and infrastructure greatly facilitated the emergence of Chinese billionaires and paved the way for investment-led growth. In the period of 'Strained Alliance', the conflicts generated by primitive accumulation were partially cooled by the 'harmonious society' of the 2000s and by systematic state support of indigenous innovation. However, the fractioning of the capitalist class, rapidly accelerated by financial expansion and the intensification of its attempts at relations with foreign capital, generated new pressures on the state. The state responded by intensifying its repressive apparatus through, among other maneuvers, the anti-corruption campaign of the current President Xi Jinping. Table 1 presents the changing patterns between the state and the new class.

[Table 1 inserts here.]

Current tensions between political power and economic power in China emerge from attempts by a fraction of the domestic capitalist class to connect with international capital. The nationalism of the CCP and its narrative of development as a project of national strengthening is the element of continuity and the deepest amalgam that maintained ideological coherence in the face of the dismantling of the socialist structure. Its questioning by a fraction of the domestic capitalist class is undoubtedly an element of strong tension for a social structure undergoing intense transformation.

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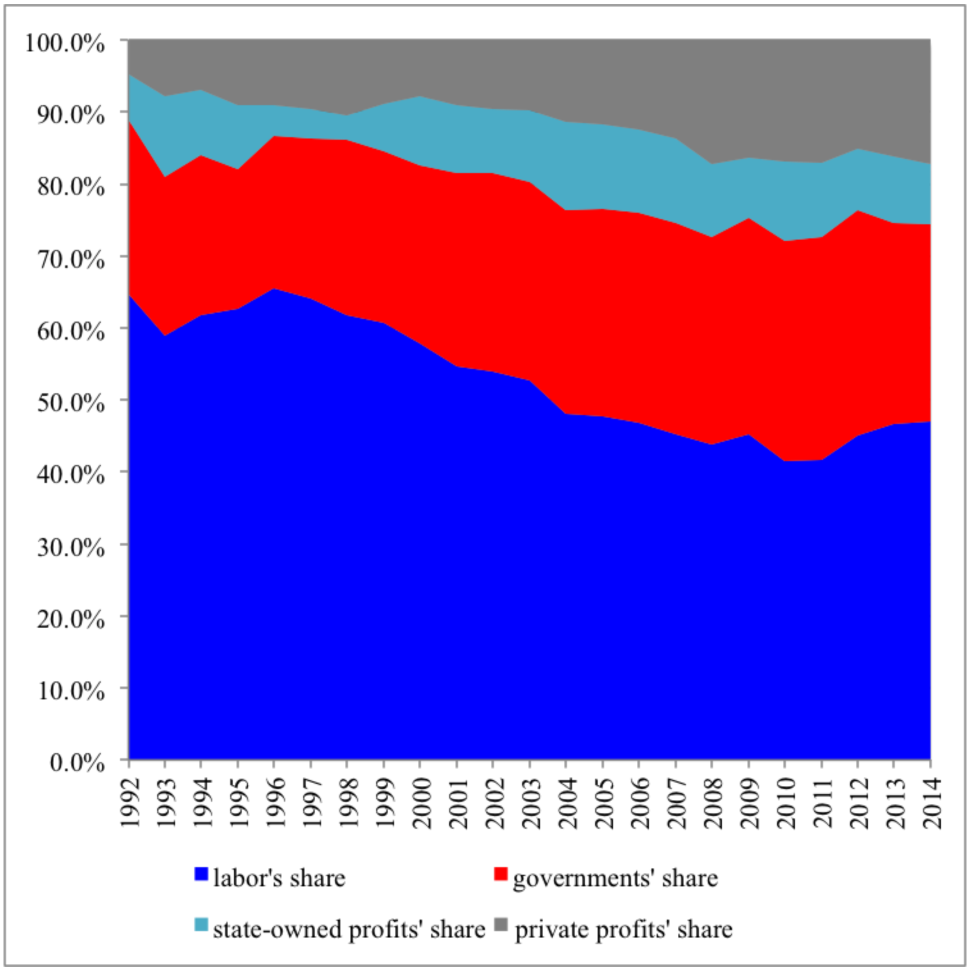
Figure 1: Distribution of Net Value Added in the Corporate Sector, 1992–2014



Source: We use the Flow of Funds Account tables in Data of Flow of Funds published by the NBS (2008) and the *China Statistical Yearbook* 2012–2016 (CSY). The Data of Flow of Funds provides tables for 1992 to 2004, and NBS (2012) revised and published tables for 2000 to 2009 but has not published revised tables for 1992 to 1999. Thus, we revise the data for 1992 to 1999 in the following way:

X1999 = X1999 from NBS (2008) / X2000 from NBS (2008) * X2000 from NBS (2012)

X1998 = X1998 from NBS (2008) / X1999 from NBS (2008) * X1999

We also revise variable X for other years and extend this method to the rest of the variables.

The Flow of Funds tables provide value added for the corporate sector. We use the depreciation data on this sector provided by Piketty et al. (2017) to calculate the net value added of the corporate sector.

Labor income = compensation of employees + allowance + 60% * net interest and 'other' net property income + 80% * 'other' net current transfer

The allowance is provided by enterprises to needy families. 'Other' property income refers to property income excluding interest, dividends, and land rents. We assume that 60 percent of the net interest and 'other' net property income belong to labor for this part of income goes to working-class households and the rest belongs to private capital for the rest goes to capitalists' households. 'Other' net current transfer applies only to the period before 1997 and consists mainly of the pension and medical expenditures of enterprises that were not integrated into the social security system. We assume that, before 1997, 80 percent of 'other' net current transfers belong to labor and the rest belongs to profits; after 1997, all of it belongs to profits. These assumptions do not significantly affect the trend of labor's share.

Government income is defined as the sum of taxes on production less subsidies, corporate taxes, and land rent payments. Since the state is the owner of urban lands, land rents paid by enterprises belong to government income. Note that land rents here refer to the rent paid to use underground resources and are not part of land transfer income.

State-owned capital income is calculated by multiplying net corporate profits with an estimated state-owned share β. The net corporate profits are calculated the following way:

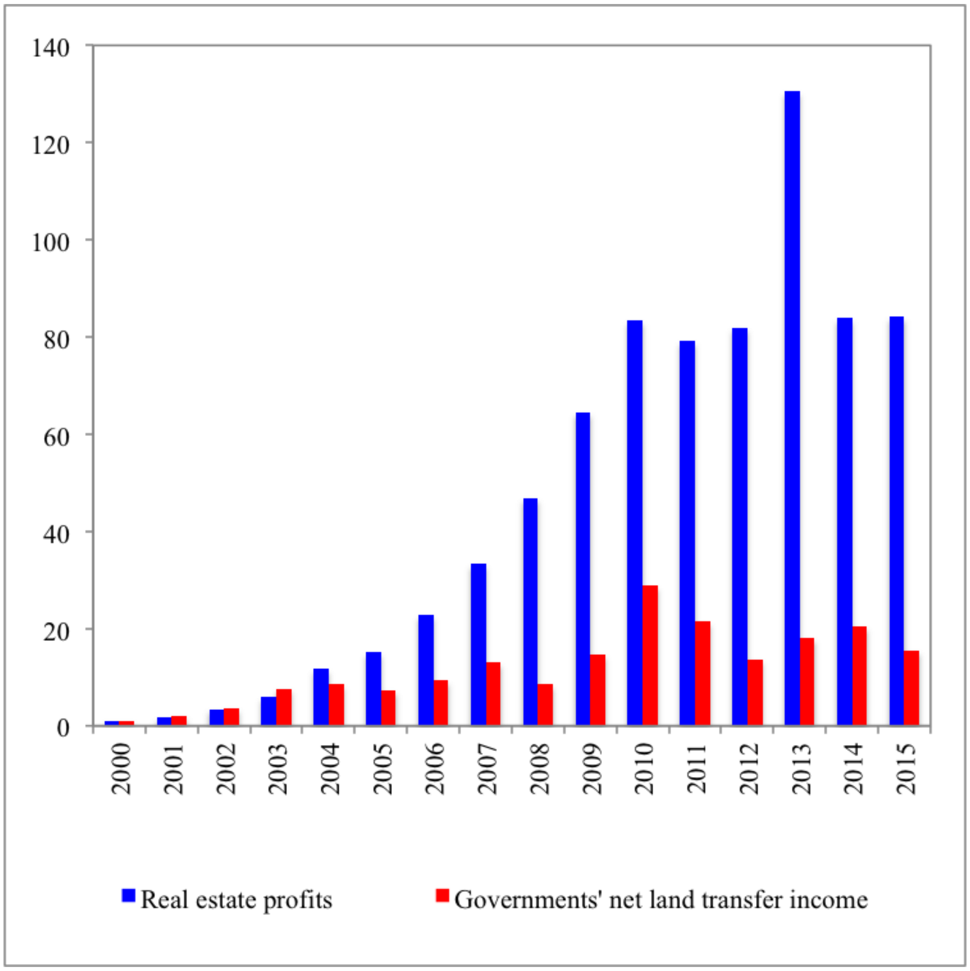
Net corporate profits = net value added – compensation of employees – taxes on production less subsidies – allowance – land rents – the net interest – 'other' net property income – 80%* 'other' net current transfer

The last term appears in the equation only for 1992 to 1996.

Piketty et al. (2017) estimated the public share of corporation equity, finding that it fell from 89 percent in 1992 to 56 percent in 2014. β is estimated by multiplying the public share provided by Piketty et al. (2017) with the ratio of the state-owned industrial profit rate to the above-scale industrial profit rate. This method is better than the method used by Naughton (2017) because it covers profits from both state-holding corporations and non-state-holding corporations with state-owned shareholders. As expected, the estimated profits are slightly higher than those in Naughton's results.

Private capital income = (1 - β) * net corporate profits + 40% * net interests and 'other' net property income

Figure 2: Growth of Real Estate Profits and Net Land Transfer Income, 2000–2015 (2000=1)



Note: Real estate profits are the profits of real estate enterprises. Governments' net land transfer income comprises total land transfer income less land transfer costs. Land transfer costs comprise governments' expenditures for the compensation of land acquisition and preliminary infrastructure construction. All values are in nominal terms. Both values in 2000 are set to 1.

Source: Real estate profits and building costs data come from the China Statistical Yearbook 2016. Land transfer income and land transfer costs data come from the website of the Ministry of Finance. The Ministry of Finance does not report land transfer costs for 2000 to 2007. We thus estimate the ratio of net land transfer income to land transfer income based on a linear trend and then calculate net land transfer income and land transfer costs with the estimated ratio.

Table 1: Relationship between the Chinese state and the domestic private capitalist class

	Privatization of state-owned and collective enterprises	Expropriation of land	Promoting indigenous innovation	Repressing financialization
Period	Mid- to late 1990s	Since early 2000s	Since mid-2000s	Since 2008
Accumulation regime	Export-led	Export-led and Investment-led	Export-led and Investment-led	Investment-led
Key internal class conflicts/external restrictions	Repressing workers' power and creating a reserve army of labor	Squeezing peasants' interests	Conflict between domestic capital and foreign capital in technology transfer	Rentier capital's pressures for financial liberalization
	Workers' struggle	Peasants' protests	Persistent workers' struggle and peasants' protests	
State-domestic private capital relation	Great Compromise	Great Compromise	Strained Alliance	Strained Alliance
Top-down forces	Deng's southern tour	State's pursuit for economic growth	Economic independence in technological progress	Economic independence in financial expansion
Bottom-up forces	Rise of new elites as a result of the 1980s reform	Industrial and real estate capitalists' pursuit for ground rent	Competitiveness in the global value chain	Rise of the rentiers and its relations to international capital