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The state-constituted market economy:
A conceptual framework for China's state–market relations

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Abstract: China has created a distinct economic system. Yet despite a growing literature with valuable contributions on the institutional arrangements under 'capitalism with Chinese characteristics', the precise economic mechanisms underpinning China's state–market relations remain undertheorised. In this paper we develop a conceptual framework of what we call China's state-constituted market economy. We define essential as 'systemically significant from the perspective of the state'. We argue that the Chinese state 'constitutes' the market economy by creating, participating and steering markets for essentials in order to stabilise and guide the economy as a whole. We draw on China's statecraft tradition as well as on proposals for financial policy reform in the US to conceptualise the state market-constitution in China.

Keywords: China; state-market relations; varieties of capitalism; state capitalism; economic stabilisation; market creation

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Introduction

China has deeply integrated into the global economy. Yet China's experimentalist reform path has created its own distinctive economic system (Zheng and Huang 2018, Naughton 2021, Weber 2021). An increasing number of studies set out to discern the specific nature of China's capitalism (e.g., Huang 2008, McNally 2012, ten Brink 2019, Chen 2020, Nölke *et al.* 2020). China is found to be sui generis, but the specific state–market relations that characterise China's variant of capitalism remain theoretically vague (de Graaff 2020, p. 884).

Some scholars describe China as neoliberal, but this does not reveal much about the more specific nature of China's system (Weber 2019, 2020). Others, pointing to the important role of the state, suggest China's system is state capitalist (Naughton and Tsai 2015, Pearson *et al.* 2020, Petry 2020b). But a recent literature review finds that '[d]espite the widespread mobilization of the concept [state capitalism] for both categorization and explanation, there is neither consensus about what it exactly means nor about its implications' (Alami and Dixon 2020, p. 71). On the surface, it appears contradictory that China could be described as both neoliberal and state capitalist. This conflicted state of the literature points to a key characteristic of China's system: the *strong state* is deeply entwined with a fundamentally *marketised economy*. Depending on which of these two aspects of China's system one focuses on, it may appear as either neoliberal or state capitalist. The precise nature of the *relation* between this strong state and far-ranging, deep markets requires further conceptual clarification.

In international political economy (IPE) literature the concept of state-permeated capitalism (SPC) is widely applied to capture the nature of China's economic system. By highlighting the *political* frictions and often diverging interests across different business and state actors as well as the reliance on relations of loyalty and trust within the Chinese system, SPC overcomes the false concept that the Chinese state is a unified monolith (ten Brink 2019, Allen *et al.* 2020). SPC has also initiated rich case studies that characterise important economic institutions in China. Yet the *economic* mechanisms underpinning state–market relations remain vague on a conceptual level. Moreover, the concept of state permeation implicitly relies on a separation between state and market that does not reflect their mutually constitutive nature. After all, for a thing to 'permeate' another, one thing has to be external to the other. As such, Massot's (2020) recent critique, that the IPE literature analytically relies on starting from state and market as separate sphere, applies. A binary conception of state versus market, however, conflicts with the fact that China's market economy has been constituted by the state since the very beginning of re-marketisation in the late 1970s, as argued by Zheng and Huang (2018) and Weber (2021).

A similar critique applies to the concept of a developmental state. Here the emphasis is on the independent nature of the state in relation to the market which also amounts to conceptualising the two as autonomous spheres (Fine 2013, p. 5). Furthermore, the developmental state has been derived through an inductive study of East Asian development successes such as Japan (e.g., Johnson 1982), Taiwan (e.g., Wade 1990) and South Korea (e.g., Amsden 1989). We propose that the Chinese case requires a similar inductive treatment to derive a conceptualisation of its state–market relations rather than a simple importation of the concepts derived from the experience of the Asian Tigers. This would amount to a reimportation of some sort, since the developmental state as it emerged in the neighboring cases has deep roots in Chinese history (Helleiner 2021b). Beyond these shared origins the different scales of the development challenges of the Asian Tigers compared with those of China have led to different economic models. As influential reform economist Deng Yingtao (2014 [1991]) argued, while China can use exports as one element of its development strategy, the challenge of economic development on the scale of China goes far beyond the task of (re-)integrating China into the global economy in a state-led fashion and involves the creation of a new kind of domestic economy.[1]

In this article, we develop the concept of a *state-constituted market economy* as an analytical framework to unpack a set of economic mechanisms that underpin state–market relations in China. We use *constituted* in three meanings of the word as defined in the *Oxford English Dictionary*: (1) 'to make, set up or establish something', (2) 'to be the elements or material of which the thing spoken of consists', and (3) 'to frame, form'. Each of these meanings points to one dimension of the state's constitutive relation to essential realms of the market economy. The first meaning corresponds to the Chinese state's activist role in market creation both historically and as a continued process. The second meaning captures the idea that the state is a key participator in essential markets. The third meaning points to the state's efforts in steering markets for essentials. We refer to a market economy rather than capitalism since our analysis in this short paper is limited to conceptualising modes of state–market

[1] Also see Ang (2016) for a critique of interpreting China's development as an instance of the East Asian developmental state.

constitution rather than providing a full-fledged analysis of China's entire mode of production. We define a market economy as an economy in which production is predominantly for sale on the market and organised through market relations such that all members of society depend in important ways on markets in fulfilling their needs and desires. Market relations are not accidental but engrained in the social relations and mediated through money.

This paper makes two contributions beyond its main aim of providing a new theoretical lens for the study of China's state–market relations. First, we respond to Helleiner's (2021b, p. 10) recent call: 'It is long past time for [the] intellectual bias [of Western-centrism] to be transcended, including for the very practical reason that the ideas of non-Western thinkers – including the Chinese ones … – have left important legacies that endure to this day.' The comparative capitalism research program has been criticised for its neglect of domestic historical foundations and its tendency to use Western experience and models as standards against which other regions of the world are measured.[2] In this paper we draw on the Chinese intellectual tradition referenced by Helleiner and show how China's state-constituted market economy is deeply rooted in China's own statecraft tradition. In drawing on China's history to make sense of its present political economy we built on a nascent trend in the literature (e.g., Arrighi 2007, Heilmann and Perry 2011, Zheng and Huang 2018, Nolan 2018a, 2021, Huang 2019, Helleiner 2021a, b, Weber 2021).

Second, we connect the study of China's market economy to conceptual scholarship on the US economy to avoid essentialising China or creating an unnecessary binary of China versus the West. It is beyond the scope of this paper to conduct a comparison of state–market relations in the US and China. But by showing that a conceptual framework developed for the US case can be integrated into our conceptual framework for the Chinese case we establish the possibility of theoretical cross-fertilisation. To this end we employ concepts of state market-participation and strategically significant prices devised by Hockett and Omarova (2015, 2016). This is possible thanks to a shared 'explicit recognition of the fact that states and markets … are inseparable and deeply interconnected parts of the nation's economic organism' (Hockett and Omarova 2015, p. 122).

[2] See Schedelik *et al.* (2020) for a critical review of the state of the literature in comparative capitalism research.

It is noteworthy that these two contributions are intellectually connected. Omarova and Hockett developed their concepts building on Keynes's work on buffer stocks. Keynes's work in turn has been inspired by the Chinese traditional granary system as brought into the interwar policy discourse by Henry Wallace (Chaomin Li 2016, Weber 2021, p. 50) and Benjamin Graham (1937). We readapt and extend their concepts to the Chinese context by drawing on China's history of statecraft, the Communists strategies of economic warfare and the history of economic reform as well as by using examples of China's contemporary political economy including China's response to the ongoing COVID-19 pandemic.

Essential versus nonessential: Distinguishing economic spheres

Our analysis of modes of state–market relations in China is based on a distinction between essential and nonessential spheres of the economy. The modern Chinese state focuses its market-constituting governance on the essential as a way to govern the economy as a whole. State–market relations vary radically between essential and nonessential spheres. Both essential and nonessential spheres are organised through the market, but in the essential sphere the market is continuously and actively constituted by the state.

In China's tradition of statecraft, a clear distinction between the essential and the nonessential has long occupied a prominent place in principles of government. An early example is the so-called *qingzhong*, or light–heavy, theory of the ancient government manual *Guanzi* (Weber 2021). Ye (2014, p. 98) translates the art of *qingzhong* (轻重) as 'weighing and balancing economic forces'. The task of economic policy in this theory is, in the words of the *Guanzi*, 'To use the thing that is "heavy" to shoot at that which is "light," to use the cheap to level down the dear' (*Guanzi* as in Hu 2009, p. 127). From this perspective, all economic phenomena can only be understood in relation to their social context; things can be heavy or light only in relation to other things. Heavy commodities are considered essential to production or human well-being, and light commodities are seen as inessential. While some things are by their nature important to production and human well-being, such as grain, salt and iron to use the examples in the *Guanzi*, the economic weight of commodities is also subject to continuous change and reflects the season of the year, production practices, technologies and market dynamics, among other factors.

Our definition of *essential* derives from this relational logic and draws on the experience of the COVID-19 pandemic. When faced with the need to impose lockdowns, the question of what and who are essential has become a central policy question around the world (Stevano *et al.* 2021). It was settled in an ad hoc fashion based on what governments perceived as essential for the basic working of society and economy. Taking a lead from this experience, we refer to *goods, assets and services as essential when they are systemically significant from the perspective of the state*. We are not arguing from a normative standpoint what ought to be essential and our understanding of 'essential' is historically contingent; evolves with changing material, social, political and economic conditions; and is shaped by the contestation between state actors and the interplay with social forces outside the state. A change in circumstances such as during the outbreak of a pandemic can shift the boundaries between essential and nonessential.

In using the notion of 'systemically significant' we build on the concept of Hockett and Omarova (2016). They define as 'systemically significant' all those prices of commodities that are ubiquitous in production; of investments that are ubiquitous in certain asset classes; and that are ubiquitous as benchmarks for other prices. We go beyond their focus on ubiquity. Taking inspiration from the shutdown experience and Chinese statecraft, we define as *systemically significant all those economic activities, assets or commodities the absence of which are considered by the state to undermine financial, social or political stability or economic security or which are crucial in the pursuit of economic development and other major policy goals*. Since we focus on analyzing state–market relations, we limit our analysis to systemically significant aspects that are organised primarily through market mechanisms.[3]

Scholars have emphasised that economic governance in China is based on an institutional hierarchy that divides the economy into tiers (e.g., Pearson 2015). The most strategic industries (e.g., metals, energy, pharmaceuticals) are tightly controlled by the state and dominated by central state-owned enterprises (SOEs). Businesses on lower tiers are governed through regulations rather than direct oversight by the government. In parallel to such a tier-based business system, scholars emphasise the importance of central-local relations, local experimentation and competition between different localities (e.g., Heilmann 2008). Our definition of essential is in accordance with such a hierarchical view of economic governance in China, but we structure our analysis around the time-variant systemic

[3] Importantly, we thus exclude all the systemically significant care work that happens within households and beyond markets. We believe care is so important, while operating based on different principles, that it requires a separate analysis.

significance or essentialness of economic activities, assets and commodities to open up a new dimension of analysis. Scholars have also used a Polanyian framework that emphasises the essential factors of production, labor, credit and land (Zheng and Huang 2018, p. 275). This approach overlaps with ours, but in addition to the time-invariant Polanyian factors of production, we consider a dynamic element: certain assets, activities or goods can become essential on account of changing circumstances (e.g., the COVID-19 pandemic) or structural environments (e.g., climate change).

Three modes of state–market relations: Creation, stabilisation and steering

This section develops three key modes of China's state–market relations in the essential spheres of the economy: creation, stabilisation and steering of markets through the state. We illustrate empirical examples for each of these three modes in the table in the Appendix.

Mode 1: State market-creation

Market creation in the Chinese context involves 'market making' as defined by Hockett and Omarova (2015) but also an even more foundational task. In their definition a market-making state is one that helps 'to create and maintain market exchange of specific assets—goods, services, financial instruments—by ensuring the continuous availability of, and thereby inducing confidence in, prospective counterparties to every trade'. To fulfill this function 'the market-maker agrees to bear two complementary types of risks': the risk of the seller that the commodity in question does not sell is overcome by the state acting as 'buyer of last resort', while the risk of the buyer of not finding the product they are trying to buy is ameliorated by the state acting as 'seller of last resort'. They propose that the state should ameliorate the uncertainty of exchange inherent in market dependency not only on the aggregate level through macroeconomic stabilisation but through state participation in specific markets.

In this definition of market-making the marketplace and the market players are assumed as being in place when the state comes in. In the course of economic reforms in China the state has and continues to create markets from scratch. Our definition of *state market-creation* therefore posits that *the state constitutes the basic infrastructure for market relations, often including the market players themselves, who are at times created and at other times mobilised by the state*. This infrastructure can take a physical form, such as new transportation that creates new market links, an informational form, as for example the creation of digital marketplaces, or an organisational form, as in the case of the creation of China's national champions. The state can act as both a market creator, when it is establishing entirely new markets, and a market actor, when it is deepening or expanding existing markets. In particular, the state can play a crucial role in what Harvey has conceptualised as annihilating space with time, expanding the frontier of the market by revolutionising means of communication and transportation (Harvey 2007, p. 337). Through market creation the state facilitates a deepening of the division of labor locally, nationally and in relation to the global economy. The state ensures the continued harnessing of the expansive forces of the market while structuring the markets for essentials in a way that enables the state to maintain its power.

Our definition of state market-creation is inspired by Polanyi (2001 [1944]). But while Polanyi emphasises the role of the state in the creation of the national market in Europe's capitalist transformation, we focus on state market-creation in China as both a historical process and an ongoing process. Our concept of state market-creation is closely related to Ang's (2016) theory of market building and the coevolution of state and markets. But where Ang suggests that at a certain stage of development, market building gives way to market preserving, we argue that state market-creation is a continuous characteristic of China's economic system. Mazzucato (2013) develops the market creating and shaping functions of entrepreneurial states in relation to innovation at various stages of development. As Mazzucato illustrates based on the example of the solar energy sector, the Chinese state – like the US in the twentieth century – has become a leading example for an entrepreneurial state. Such innovation-oriented activities are included in our definition of state market-creation and steering (see next section). But our definition of state market-creation goes beyond innovation and includes all essential spheres of the economy.

In China's recent history state market-creation has occupied a central place at two critical junctures: during the Civil War and again during the reform period. At both moments markets had become peripheral. During the Chinese Civil War hyperinflation was rampant and the economy had disintegrated to a degree that many peasants reverted to subsistence production. We can think of this as a collapse of the division of labor. The market had ceased to function as a coordinating mechanism for the economy as a whole as trading routes were blocked by the war. In this context, the Communists reverted to ancient statecraft techniques in their economic warfare. They stabilised the value of their currency through recreating markets for essential goods such as salt and grain and by establishing trading agencies that reinstated commercial links. This involved some of China's most influential economic thinkers and policy makers of the twentieth century, such as Chen Yun and Xue Muqiao (Weber 2021).

During the Mao era markets did not disappear entirely, but they were politically suppressed (Perkins 1966, Zheng and Huang 2018, p. 250–1). At the dawn of reform one key question was how to recreate markets in the context of a command economy. China considered but ultimately rejected the logic of shock therapy that would have relied on destroying the planned economy to make space for markets to emerge spontaneously. Instead, China pursued a path of marketisation that consisted of a combination of liberalising peripheral sectors and using the planning institutions as market creators. This eventually transformed SOEs from units that implemented commands into market-oriented businesses (Weber 2021).

But state market-creation is not only part of China's revolutionary and reform history. Rather, it is a continued practice. This is illustrated in recent case studies (see the Appendix). Some examples are the China Development Bank (Chen 2020), the creation of domestic capital markets and their gradual integration with global markets (Petry 2020a, b) as well as China's massive construction of infrastructure in recent decades such as the Belt and Road Initiative and high-speed railways. The market-creating role of the state was again saliant during the COVID-19 crisis, when the lockdown policy paused the flow of market activities and blocked normal connections between sellers and buyers. In this emergency, the state quickly transformed the norms for the essential food markets and reestablished commercial connections (Weber and Qi 2021).

Mode 2: State market-stabilisation

At the core of our concept of state market-stabilisation is what Hockett and Omarova (2015, p. 137) call the 'government-as-market-actor modality'. The state participates in the market for essential goods to stabilise supply and demand by mobilising whatever side falls short. This is similar to the ways in which central banks open market transactions. It happens both in state and privately created markets and aims to smoothen fluctuations, particularly of systemically significant prices of essential goods. A rapid, large change of these prices would have major ripple effects across the economy and have the potential to undermine stability by rendering key products out of reach or triggering cost-push inflation. State market-stabilisation aims to ameliorate the uncertainties and instabilities inherent in markets. By the same token it enables very wide-ranging market reliance. It also amounts to a different mode of macroeconomic stabilisation.

Hockett and Omarova consider 'market-preserving' as a sub-case of market-making for emergencies that refers to the specific situation of a panic sell-off when individual market actors cannot afford to wait and see how things evolve but a public instrumentality can step in and countervail a free fall. In China state market-stabilisation includes market stabilising state participation that ranges from counterbalancing normal fluctuations to market-preserving emergency measures such as in the context of the 2015 stock market crisis.

China looks back on a long history of state market-participation. The ancient text *Guanzi* states,

> When things are plentiful, they will be cheap; when they are scarce, they will be expensive. ... Knowing this to be so, the prince pays attention to his country's surpluses and shortages and manages its wealth and goods. When grain is cheap, he exchanges money for food. ... He pays attention to the relative value (*qingzhong*) of things and manages them in order to maintain price stability. Therefore, the expensive and the cheap may be harmonized and the prince reaps his profits. (*Guanzi* as in Rickett 1993, p. 384)

The basic logic of the statecraft techniques of *qingzhong* can be illustrated based on the Ever Normal Granaries that were a core institution in imperial China (Will and Wong 1991). Grain markets are inherently unstable due to the changes of seasons that brings about regular fluctuations in supply and prices. In addition, the bad harvests can create extreme price fluctuations or even famines. The public granaries were meant to add demand around harvest time and lift the price, while adding supply when the private supplies were fading in spring and summer, thus preventing price hikes by private merchants.

During the Mao period state market-participation was replaced with the unified system of purchase and sales for grain and other essential agricultural goods. The state monopolised the grain trade (Ash 2006). In the early years of reform and opening-up, grain markets were re-introduced as households were allowed to produce for the market once they had fulfilled their share in the state-commanded grain output quota. As a result, state market-participation reemerged for grain and has been considerably strengthened in more recent years, especially in the context of the violent world food price fluctuations in the 2000s (Huang and Yang 2017).

China today commands buffer stocks, operated by state agencies or state-owned firms in an analogous fashion, for staple food items such as pork, sugar and oil and essential producer goods such as metals and oil, as well as medical supplies. Some key institutions are the National Reform and Development Commission, the National Food and Strategic Reserves Administration and more specialised reserves such as the China National Cotton Reserves Corporation. The size of reserves is not publicly known for most stocks but is estimated to account for only a small share of the nationwide consumption, with the exception of grain. The key to effectively utilising buffer stocks lies in leveraging reserves at the right time.

Beyond reserves, market participation in a range of essential commodities requires complex state capacity to monitor essential markets on a continuous basis and add supply either through imports or the mobilisation of businesses through informal and formal ties. Critically, the mostly state-owned banking system in China can also facilitate counterbalancing investment through preferential credit treatment or increasing capital requirements, as has been the case under the so-called 'three red lines' in the real estate sector since 2020 (Bloomberg 2020).

In the context of the inflationary pressures that have arisen in the aftermath of the COVID-19 pandemic recoveries, the specific logic of China's state market-stabilisation also became salient. While in the rest of the world the debate around a potential stabilising state intervention has focused on a tightening of monetary policy, the Chinese government focused its efforts on stabilising the prices of key commodities that showed rapid price rises in the first months of 2021. To be sure, interventions that are intended to counter the building up of bubbles can also themselves induce instabilities, as happened in 2015 and might happen again in the ongoing Evergrande debt crisis. In the table in the Appendix we illustrate state market-participation based on recent examples.

Mode 3: State market-steering

The goals of the Chinese state go beyond the act of creating markets as an end in itself or stabilising the economy in its existing configuration. The Chinese government has a long-term agenda and is characterised by the bolt ambitions of an 'entrepreneurial party state' (ten Brink 2019). In the pursuit of broad policy goals such as redistribution, resilience or environmental sustainability, markets are shaped and steered. This practice includes what Hockett and Omarova (2015, p. 129) define as 'market moving' – actively alternating prices through state market-participation towards meeting policy goals – along with the whole realm of policy tools conceptualized in Mazzucato's *Entrepreneurial State*. The basic mechanism is similar to that described in the previous section for stabilisation and can involve market creation. There is an analytical overlap, but rather than aiming to recreate an existing market balance in its steering mode the state participates in the market to create a new balance.

Market-moving has a long history in Chinese fiscal policy. In traditional statecraft the state monopolised the salt trade and limited supply in order to extract revenue from high prices. State commerce was also used as a way to absorb excess liquidity (回笼) by sales of expensive luxury goods. Both techniques were used in the early years of the People's Republic of China. Bringing the salt trade under control was an important source of finance for the Communist revolution (Weber 2021). To counter inflationary pressure after the disaster of the Great Leap Forward, cakes made with imported Cuban sugar were sold at a high price to absorb excess liquidity of high-income households (Lowenstein 2019).

Consciously setting prices in ways that diverge from costs was at the core of the Maoist price system (Perkins 1966, Lardy 1984, Weber 2021). Prices were used as a mechanism for redistribution across sectors. In the 1980s, China's market reforms raised the question of what to do with this redistributive price system. China abstained from a big bang in price reform that would have reset all prices overnight and pursued a dual-track price system instead. The core of the old price system was initially left in place while market prices emerged at the margins (Weber 2021). For most of the economy this dual-track price system is long gone. But for certain essential upstream producer goods such as electricity it continues as one element of China's economic policy. For example, granting producing enterprises access to a cheap energy supply is a way to encourage certain sectors. Importantly, the grain price also continues to be steered by the state in the interest of the rural producers. When in the 2000s urban–rural inequality had become so high that it began to endanger social stability, the Chinese government mobilised and expanded the public grain reserve system. To increase farmers' incomes and encourage production, the state guaranteed a minimum procurement price for a range of major grains, thus steering the market in favor of agricultural producers (Huang and Yang 2017).

Market steering does not always require the direct participation of the state as a buyer or seller. It can also guide the expectations of non-state players about new frontiers of expanding markets. China has transferred the legacies of the planning system, particularly the five-year plan system, into indicative planning (Heilmann and Melton 2013). A five-year plan proposes a variety of social and economic goals, including aspirational rather than mandatory ones that serve to align expectations of non-state players. This involves large-scale public investments and channels private investments into frontier technologies and innovations. The state shapes profitability expectations with political commitments on industry and macroeconomic levels as well as through financing by state-owned banks. The table in the Appendix illustrates this point through the example of the electric car industry.

The state-constituted market economy

Bringing together the three modes of China's state–market relations, we conceptualise the Chinese economy as a state-constituted market economy that is characterised by the active state creation, participation and steering of markets for essentials. China's history of thought on markets goes back to ancient times. It has a long tradition of considering the market as a 'two-edged sword' (双刃剑), a progressive force that can unleash an enormous potential for an enhancement of the material foundations of society but also dangerous in its potential to create vulnerabilities, instabilities and crises (Nolan 2021, p. 35, 2018b). This resonates with Karl Marx's analysis of capitalism as both the most progressive and most crises-prone stage of development. For Marx this dual nature implies that capitalism prepares its own demise and gives rise to revolutionary forces that should eventually overcome the reliance on money and markets. In contrast to such a revolutionary solution attempted in China under Mao, a strand of Chinese statecraft addresses the need to balance the regressive and progressive sides of markets through state market-participation. Some of these techniques of economic governance have been revived in the reform era (Weber 2021). As we will show, this resonates but also goes beyond Keynes's or a Keynesian vision.

The dual nature of capitalism is to some extent reflected in competing strands of scholarship in comparative capitalism. This literature is divided into critical approaches that emphasise power dynamics, social relations, uneven development, crises and *instability* (e.g., Peck 2007, Bruff 2011) and contributions in the tradition of Hall and Soskice's (2001) Varieties of Capitalism (VoC) approach that emphasize different forms of corporate governance as *stable* institutional arrangements that make capitalism *function*. The framework of an SPC derived for emerging market economies takes on some elements of critical political economy scholarship but is ultimately rooted in VoC and focused on the question of how capitalism has enabled these countries to rise. SPC stresses the importance of business–state elite networks grounded on personal relationships, competition between local alliances, and the role of the central state in providing an overarching institutional architecture for this competition in characterising 'China's mode of coordination' (Nölke *et al.* 2020, p. 49). We consider all these elements to be important but believe that the question of how the Chinese state tries to reconcile the dynamic power and the inherent instability of markets remains undertheorised. By focusing on this balancing act, we contribute to attempts to provide a dynamic view in contrast with the often-static analysis inherent in VoC and its offshoots.

We share VoC's critical stance towards a neoclassical framework (Coates 2015, p. 19). In neoclassical economics, markets are one-dimensional, self-regulating spheres where the competitive interaction of private buyers and sellers intermediated by the free movement of prices brings about an equilibrium. In contrast, in practice, all market economies are sustained by some form of state action that ameliorates at least some of the uncertainty and instability that arise from the reliance on market exchanges. These mechanisms differ in degree and mode of operation. The state-constituted market economy is characterised by a particularly intensive and extensive form of such uncertainty-ameliorating policies as well as by a commitment on the part of the state to actively harness and channel the progressive powers of markets. A brief comparative discussion on a conceptual level will help us to develop this point.

On the most basic level all states provide a legal framework that sets rules for market behavior and police those rules. Beyond that, on at least three levels the state can ameliorate the uncertainty of exchange inherent in a market economy, corresponding with different schools of economic thought: (1) by stabilising the value of money, (2) by stabilising aggregate demand, and (3) by stabilising individual, important markets.

All modern states issue a fiat currency. All states also aim to stabilise the value of money to some degree through monetary policy which can limit the uncertainties stemming from the monetary sphere (1). Central banks create and participate in markets for fiat money to regulate the price of holding money (the interest rate). From the perspective of Friedmanite monetarism or the neoliberal tradition, self-regulating market forces dominate over the inherent instability just outlined. Hence, stabilising the value of money is the key to stabilising market economies as a whole (Hayek 1966 [1929]). Conversely, the free market economy facilitated by stable prices is seen as the best arrangement to unleash the virtues of the market. The free market does not mean a market free of the state. The state polices the freedom of the market and encases it to protect it from the intervention of society or state (Bonefeld 2013, 2017, Slobodian 2018).

From the angle of the postwar neoclassical synthesis, the state further has to stabilise aggregate market relations through fiscal policy (2). Here, the inherent stability is mainly located on the macro level and so are the ameliorating policies. Fiscal expansion adds to aggregate demand when effective demand is falling short to prevent a deflationary contraction. The main task of the state is this macro stabilisation. Keynes went further in his vision for an activist state. He argued for the socialisation of investment which would serve to overcome substantial, inherent instability in a capitalist economy as well as to unleash the full productive potential through industrial policy (Crotty 2017).

Later, Keynes added public buffer stocks for essential commodities to his proposed stabilisation policies (Dimand and Dimand 1990, Fantacci *et al*. 2012) (3). Keynes was not the originator of such a state market-participating policy. Benjamin Graham (1937) and Henry Wallace had previously introduced this idea into the interwar policy debates, drawing inspiration from China's Ever Normal Granaries system and traditional statecraft (Will and Wong 1991). In fact, in China theories of state market-participation go back to the aforementioned *Guanzi* and were revived, discussed and perfected in imperial times (Zhao and Drechsler 2018, Zanasi 2020, Weber 2021). Keynes was aware of this tradition of theorising since he reviewed a Ph.D. that surveys China's history of economic thought and covers state market-participation (Chen 1911, Keynes 1912).

If we add in macro-stabilisation, a substantial degree of socialisation of investment and public buffer stocks for essential commodities, we move towards our concept of a state-constituted market economy, but in our analytical framework for the study of China's political economy, the state takes on an even more constitutive role than that envisioned by Keynes. The state-constituted market economy *stabilises the value of money and the relation between aggregate supply and demand not only through indirect* *macroeconomic means of fiscal and monetary policy, but it also actively creates, participates in and steers markets for a range of essential goods, activities and assets in pursuit of developmental goals*.

The relation between the state and the market is subject to constant calibration and contestation in China's state-constituted market economy. Deng Xiaoping famously reinstated the market in the late 1970s to be a tool to serve the socialist state (Zheng and Huang 2018, Weber 2021). This is the Smithian view of 'markets as instruments of rule' (Arrighi 2007, p. 8). But the market is not a simple instrument, it takes on a life of its own. Active stabilisation of the market is a way to keep the market dynamic under control. Commodity-level state market-participation does not erase the uncertainty inherent in a market economy. But as the state acts as buyer and seller of last resort in a range of markets with wide-ranging linkages across the economy, the uncertainty is more directly alleviated than when relying on macro-interventions alone. To be sure, the economic precariousness that is endogenous in being dependent on selling one's labor for a living is not overcome and there is a possibility of bankruptcy for individual firms. But the state smoothens fluctuations in essential markets to contain risks that can lead to systemwide crises.

Esping-Andersen (1990) categorises welfare states by the degree of decommodification of essentials, following Polanyi (2001 [1944]), who saw the laws of motion in the struggle over the (de-)commodification of the so-called fictitious commodities land, labor and capital (Işıkara 2021). While the Chinese state governs some essentials such as compulsory education and medical services through decommodification, it governs other essentials such as grain and crucial raw materials through state-constituted markets. Consequently, China's economy is deeply marketised, and more state does not mean less market (Zheng and Huang 2018). China's economy is fully commodified in that basically all production is for the market and large parts of everyday life are organised through exchange. But this commodification is constituted by the state in the sense that the state organises the commodification through market creation and pushes the boundaries of marketisation by internalising uncertainties inherent in the commodity form.

An analogous assumption to the focus on decommodification is that more market means less state capacity. The literature on the regulatory state of the neoliberal era, for example, emphasises ruling through 'governance' as a result of marketisation. The regulatory state lacks state capacity beyond its functions of setting and policing rules. This is juxtaposed with the state of the postwar era of advanced economies characterised by 'government' defined as 'statecraft based on hierarchical, command-and-control systems which authoritatively mobilises resources and intervene directly to secure desired social and economic outcomes' (Jones and Hameiri 2021, p. 3). Similarly, the developmental state model is often seen as relying on an all-powerful, centralised bureaucracy and state mobilisation through command-and-order (Allen *et al.* 2020, p. 2). An opposition is drawn between more hierarchical command-and-control and more market rather than between different ways and degrees of the state's engagement with markets that correspond with different forms of state capacity. In line with Massot's observations (2020), the market is thought of as a pure sphere of private actors, so that more market always implies less state capacity. In contrast, in our framework of China's state-constituted market economy, intensified marketisation increases the uncertainties and instabilities inherent in market dynamics and requires more, not less, state capacity. At the same time the state in China is not an all-powerful, monolithic, centralised bureaucracy that penetrates the market on its own terms as in the classical developmental state (Hui 2017, Zheng and Huang 2018, p. 31–2, Nogueira and Qi 2019).

The concept of an SPC provides an answer to the conundrum of China's marketisation under an expansive state. The focus as regards state–market relations is on the firm level and on fragmented interests in business-state alliances and cooperation within elite networks. These networks are grounded on personal relations (*guanxi*) and a shared social background (Nölke *et al.* 2020). This 'non-market mode of coordination' (ibid., p. 49) is thought of as key to understanding China's state–market relations. This analytical lens resonates with approaches that emphasize crony capitalism.[4] In addition to informal ties, the rich literature on SOE governance illustrates the importance of bureaucratic design by stressing the role of the State-owned Assets Supervision and Administration Commission (SASAC), cadre management systems that facilitate the rotation and dual assignments of executives and state officials, party committees inside companies, and political campaigns to mobilise businesses (Chen Li 2016, Leutert and Eaton 2021). Our framework is consistent with the importance of informal business-state alliances as well as of bureaucratic design.[5] But beyond coordination through such formal and informal non-market ties, we stress the importance of market-based coordination of businesses through the state's mobilisation of market dynamics. Formal and informal networks serve as institutions that the state can draw on in its market-constituting activities.

[4] See Ang (2020) for a critical review of accounts that use crony capitalism as analytical lense to analyze China.

[5] See Zheng and Huang (2018, p. 378–424) for a detailed discussion of such personnel rotation.

SPC emphasises fragmentation in China's system as a result of competing interests of the various state-businesses alliances and competition between different localities. Complementary to this, we argue that the non-monolithic nature of the Chinese system also reflects a clear distinction between essential and nonessential parts of the economy (Weber 2021). If we focus on only the nonessential spheres of the economy, the Chinese state appears neoliberal. The Chinese economy can even be considered more marketised than some of its European counterparts since it only marginally adheres to the principle of decommodification at the core of European welfare states (Qi and Li 2018, Zheng and Huang 2018, Weber 2019). But in the essential spheres the Chinese state actively constitutes the market operating in an explicitly non-neoliberal fashion. A growing number of case studies on state–market relations in China stresses that the state 'permeates' and 'penetrates' the market, but there is no consensus what this means for the nature of China's political economy. The diverging conclusions on the degree and modalities of state control are to some extent due to a focus on a range of points on the essential to nonessential spectrum.[6] By taking the essential–nonessential distinction into account analytically, we can help resolve the contradiction of China's internal variety of state–market relations.

Conclusion

China has created a distinct economic system. The conceptual framework developed in this paper aims to contribute to a theorisation of the economic mechanisms that underpin modes of state–market relations. We propose the concept of a state-constituted market economy and argue that through market-constituting activities the Chinese state seeks to ameliorate uncertainties and instabilities in essential spheres of the economy while harnessing the power of market forces. This involves the continuous redefinition of the boundaries of essential and nonessential sectors. The state creates and participates in markets for essentials in order to stabilise and steer the economy as a whole. It thereby

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[6] For example, Jones and Zou (2017), focusing on the involvement of a Chinese SOE in one specific hydropower dam project in Myanmar that is of geopolitical relevance but not essential to China's power grid, suggest that the role of the state in relation to SOEs is fragmented and in line with that of the regulatory state. In contrast, Chen and Lees (2016) examine China's developmental state in their analysis of the essential project for China's overall economic security of building up a renewable energy sector. Similarly, Allen *et al.* (2020), in their analysis of China's solar PV industry which is a key element of the renewable energy sector, find that China's state-permeated capitalism is considerably less fragmented and more closely coordinated than that of India. Zhang and Bray (2017) have demonstrated how the expansion of the public higher education sector has at the same time created a shadow system of private schools and tutoring, whereas the latter is organised based on a logic of what they call 'micro-neoliberalism'.

mobilises private market actors but at the same time aims to retain sovereignty over the essential parts of the economy. This is a constant balancing act. The state enters a Faustian bargain with the market. Market forces, once unleashed, can spiral out of control despite efforts to stabilise or steer them. The state-constituted market economy has a more fine-grained state capacity to counter bubbles and instabilities but is by no means free from crises, as the financial turmoil in 2015 and the attempts to deflate the real estate sector in 2021 illustrate.

While we characterise the essential parts of China's economic system by stressing the active state participation in the market, peripheral spheres of the economy are largely left to private actors alone and are only indirectly steered or stabilised through their links with essential sectors. One key to understanding China's political economy lies in capturing this dual nature. The state-constitution of markets for essentials works not against commodification but rather facilitates a wide-ranging commodification of all spheres of the economy. Further research is needed to conceptualise the channels through which the state market-participation in essential sectors affects the nonessential ones and to study the implications of state market-constitution for the role of fiscal and monetary policy.

Appendix: Examples of state market-constitution in China

Mode	**Examples**	**Details**
State market-creation	Example 1: China Development Bank (CBD) (Chen 2020)	• The state has functioned as the creator of a competitive market for infrastructure financing where the regulator, buyers and sellers are all state actors. As China was transitioning out of a directly planned economy, new mechanisms of finance were needed to facilitate China's strategic development projects, and CDB was designed as a core, fully public institution. The state's guarantee has enabled CDB bonds to receive credit ratings as high as those of government bonds. Hence, CDB can raise most of its funds from the capital market. • Chen summarises, 'The state not only penetrates, permeates or regulates the market; it is a component to the market. China's interbank bond market to a large extent does resemble a "competitive market" … its pricing mechanism is determined by market supply and demand, and the players do react to market signals and seek profits. But the major players that constitute this market are state owned. Such a sui generis state–market relation reflects Chinese policy makers' view of the role of the state in development, that is, the state must rely on market mechanisms to achieve economic development in an efficient manner, but if there is no market out there, the state should create one by transforming existing state actors into market players.' (Chen 2020, p. 464–5)

Mode	Examples	Details
	Example 2: State-owned exchanges (Petry 2020a)	• Petry (2020a) analyses how the Chinese state has created domestic capital markets and gradually integrated them with global markets. The state has set up state-owned exchanges and organises the market infrastructure, but unlike the CDB, the players on the exchanges are profit-driven, speculating investors. • The state has shaped the market in ways that harness the dynamism of private capital but constrain the scope for speculation: 'Instead of placing trust in markets' ability to self-correct and achieve "efficient" outcomes, in China, assessments about the social usefulness of financial trading are made – that "finance should serve the real economy".' (ibid., p. 10)

Mode	Examples	Details
	Example 3: Infrastructure construction (Ang 2016, Lawrence *et al.* 2019, Huang 2020)	• China has pursued massive construction of infrastructure in recent decades, with the goal of extending the original market, building new connections between market players, and deepening the division of labor. Ang's (2016, 173–174) case study of a town in Fujian illustrates the role of the construction of a railway on local investment and local 'market building'. China has built the world's largest high-speed railway network which has drastically intensified original cross-regional connections. • A World Bank report shows that 18 per cent of passengers would not have traveled if the high-speed railway were not available. The high-speed railway has helped relatively remote places such as Guilin, Guiyang and Qufu to attract new passengers and expand their tourism markets (Lawrence *et al.* 2019). • The core motivation of the Belt and Road Initiatives is to facilitate trade and create new market connections through improving infrastructural conditions. As part of the initiatives, the Chongqing-Xinjiang-Europe Railway has made Chongqing, an inland city in southwest China, a major trading hub and an important exporter for Europe, challenging the traditional advantages of coastal cities. Manufacturers based in Chongqing, such as Hewlett-Packard and Foxconn, produced 25 million laptop computers per year for the EU market (Huang 2020).

Mode	Examples	Details
State market-stabilisation	Example 4: Essential goods reserves (Weber and Qi 2020, Bloomberg 2021)	• Even though somewhat less essential than grain, pork has become an important consumption good for most Chinese people, and the price of pork has significant importance in the official consumer price index. The state's control over pork is less strict than its control of grain; nonetheless, the government operates a frozen pork reserve through a state-owned firm, China Merchandise Reserve Management Center. • During 2020, when pork price rose rapidly due to the impact of the swine fever in the preceding two years, the Reserve Management Center constantly released reserves of frozen pork while also importing pork on a large scale in order to increase domestic supply (Qi 2020). • Similarly, when the world oil prices collapsed in 2020, the Chinese state reserves made headlines about their global buying spree, stocking up reserves to ensure greater energy resilience as well as to have leverage to insulate the domestic market from later price hikes (Bloomberg 2021).
	Example 5: Medical supplies under COVID-19 (Qi 2020)	• In the context of the inflationary pressures that have arisen in the context of the COVID-19 post-shutdown recoveries, China has focused its efforts on stabilising the prices of key commodities that showed rapid price rises. The state played a crucial role in meeting the rapid increase in the demand of medical supply and personal protective equipment and avoided a vicious cycle of inflation and infection.

Mode	Examples	Details
		• In the initial two weeks after the city of Wuhan was locked down on 23 January 2020, China mobilised official reserves of medical supply and imported massively (328 million masks and 3.9 million gowns) through both state-owned and private businesses. • The ultimate solution to the shortage was not reserves or imports but the state's mobilisation and coordination of production through two agencies: the Ministry of Industry and Information Technology (MIIT) and NDRC. These state agencies sent officials to key production firms, collecting data daily, coordinating the supply of raw materials and equipment, and helping those firms improve technologies and ramp up output at an enormous pace. By 25 February 2020, the production of medical masks and gowns met the domestic demand (Qi 2020).
	Example 6: Counter-cyclical investments of SOEs (Qi and Kotz 2019)	• In China a complex infrastructure for targeted investments importantly involves the SOEs. Rather than focusing on the macroeconomic dimension of expanding fiscal spending in order to lift up aggregate demand in response to a crisis, China's stabilisation policies for the economy involve the mobilisation of state and private businesses around tailored investment programs. These programs are usually focused on major innovation, infrastructure building, and improving basic living conditions. SOEs, who are more willing to implement riskier investments, are leading investors in these programs.

Mode	Examples	Details
		• Qi and Kotz (2019) find that since the early 2000s the investments of SOEs have been significantly countercyclical and have played a crucial role in stabilising reginal economic growth. SOEs are not only boosting economic growth with counter-cyclical investments but also playing a leading role in major innovations.
	Example 7: 2015–2016 stock market crash (Li *et al.* 2020, Petry 2020a, 2020b)	• As Petry (2020a, b) shows, a complex institutional infrastructure has been designed 'with control in mind' to contain speculation instead of simply assuming that unregulated markets would be self regulating. As for the rest of the economy within the financial sector, we observe the logic of tight control over essential functions and entities: Borrowing Petry's (2020b) terminology, 'pivotal points' are state-controlled, but instead of operating based on a command-and-control logic, they follow market principles – as market designers, participants and managers to ensure that 'finance serves the real economy'. • To avoid the building up of bubbles, transaction-supervision departments monitor trading activities in order to detect potential market manipulation and ensure stability. When such prevention strategies fail, the Chinese state reverts to the same logic of stabilising market participation that we have traced in other essential sectors. This became apparent in the context of the 2015–2016 market crash. • Concerned with the bubble, the China Securities Regulatory Commission (CSRC) strengthened regulations in 2015, which however triggered the burst of the bubble. In

Mode	Examples	Details
		response to the crash, CSRC mobilised state-controlled financial institutions to stop selling and bailout the market by massively buying stocks (Li et al. 2020), thus reversing the panic and stopping the free fall of the market.
State market-steering	Example 8: Urban land (Tao *et al*. 2010, Xu 2011, Knight 2014, Liu 2018, Zheng and Huang 2018, Lan 2021)	• The local government is the only lawful owner and supplier of urban land, but the demand for land comes from a multitude of players, most of whom are private firms. Local governments lease the land to non-state users for a fixed period. Monopolising the urban land supply has allowed local municipal governments to obtain land revenues as an important supplement to local fiscal income, which has financed in considerable rapid and large-scale urbanisation and local infrastructure building since the mid-1990s (Xu 2011; Knight 2014; Zheng and Huang 2018). • A common practice of local governments is to lease land for manufacturing firms through one-on-one negotiation instead of public bidding, which can lower the price and thus attract manufacturing investments (Tao et al. 2010). In this way, local governments are shaping the outcome of the land market to generate a stable income stream and pursue economic development goals. • State-owned investment platforms hold a lot of urban land and have easy access to credit. They not only play a crucial role in municipal infrastructure building but also are the key player in supporting the development of highly risky frontier technologies. Domestic high-tech companies such as BOE and TCL in the LCD industry and

Mode	Examples	Details
		Suntech in the photovoltaic industry have substantially benefited from the financial support of state-owned investment platforms. • Since 2014 local governments have established industrial guiding funds, which are state-owned venture capitals that make investments in high-tech companies. By June 2019, industrial guiding funds amounted to 4 trillion yuan (Lan 2021).
	Example 9: Electric cars (State Council 2012, Altenburg *et al.* 2017)	• By early 2021, the number of electric cars in China had reached 5.8 million; this accounts for 50 per cent of electric cars globally (Xinhua-News 2021). China proposed a plan for the development of electric cars as early as 2012, aiming at overcoming the reliance on oil, countering environmental pressures, and transforming the traditional auto-manufacturing industry into a technological leader. • The state has provided substantial subsidies but, importantly, it also shaped the expectations of potential manufacturers and customers through creating a state-supported ecosystem for electric car innovation, investing in a wide and dense network of charging infrastructure, running a more favorable plate allocation system for electric cars, encouraging the usage of electric cars as taxies, and pledging that by 2035 no new combustion-engine automobiles may be sold in China. • These policies have created a clear expectation that profitability and survival on the Chinese market for car manufacturers will depend on their competitiveness in electric cars – a powerful form of steering the business activities of a whole sector.

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