The Institutional Balance and
Political Stability of the
Chinese Government in the
Transitional Period

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Political stability plays an important role in contemporary political development and has been an issue of public concern for developing countries. For China, engaged in a period of economic transition, the notion of political stability may prove especially significant. While changes in economic structure require a stable political environment, such changes often lead to contradictions that disrupt stability. Although the principal objective of China is economic development, without a stable political environment nothing can be accomplished (Deng, 1987). In China, the issue of political stability in the period of transition stems mainly from changes in the economy. Consequently, economic issues must be taken into account in order to draw objective, scientific conclusions regarding political stability (He, 2001). As S. P. Huntington observed (1986), political scientists regard politics as a dependent variable, hoping to find an explanation for political phenomena in other social processes and systems. They regard the changes in the nature of society and the economy as more important than political changes.

Hence, the useful part in the theory of institutional analysis has been assimilated to form a framework of analysis on the institution (institutional balance, interest balance, political stability); to develop a rational explanation about the issue of political stability in the transitional period from the institutional point of view; and to draw the conclusion that institutional balance is the solution for political stability in China in the course of market development.

This paper proposes that the government take measures to avoid political instability and strengthen institutions. The government should provide institutions sufficient resources to combine, promote, and reform development and stability during the economic transition period.

Abstract: The problem of political stability in the transitional period of China is a topic of great concern for Chinese and foreign scholars, many of whom have analyzed this topic with different theories and methods. In this paper, institutional theories are employed to investigate the influences of the institutional balance of the Chinese government on the interests of different subjects and possible changes in the political environment. It is believed that the Chinese government plays a dominant role in the process of market development in connection with the economy. The provision of institutions by the government exerts great influences on the interests of different subjects and is closely related to political stability. The practice of the Chinese government of maintaining the balance of interests throughout society by means of institutional balance is the foundation of political stability in China.
As the key to developing and operating the economy, the government is the foremost tool for promoting collective action and introducing changes.

The Theoretical Implication of Institutions: A Precondition for the Analysis of Political Stability

Institutions and Their Constitution

Our understanding of institutions has been steadily developing. Moreover, institutions change along with the social, economic, and political environment. According to Veblen (1899), an institution is a system of thought, a criterion for behavior, and a set of principles of power and wealth common to the majority of people. There is also the belief (Commons, 1934) that institutions consist of the way in which collective behavior determines and controls individual behavior.

As the key to developing and operating the economy, the government is the foremost tool for promoting collective action and introducing changes. Wolfram Elsner (1989) has pointed out that institutions are the rules that govern decision making and that specific rules are usually universally confirmed within a specific range as a basis for decision making. North (1980, p. 225) believed that an institution is a series of formulated rules, procedures based on law, and moral and ethical standards for behavior. None of these viewpoints has deviated from the central idea of rules when making an inductive description of the range of institutions. They postulate that the core of any given institution consists of the rules that restrict human behavior. According to the editorial committee of Ci Hai (1980, p. 185), an institution is a code that requires all members to observe and follow definite procedures. Here it is clear that Chinese scholars concur with their Western counterparts regarding the implications of institutions.

Institutional rules are usually composed of formal rules, non-formal rules, and the implementing mechanism (North, 1994, p. 12). Formal rules, which include political rules, economic rules, and contracts characterized as mandatory, are those that have been consciously standardized. Non-formal rules originate in information that has been handed down and are part of the legacy we call culture. Here culture is understood from the western perspective as something handed down from one generation to the next. Culture influences behavior via the teaching or imitation of knowledge, values, and other essentials, including custom, tradition, morals and ethics, and ideology. The most significant of these is ideology, which encompasses values, ethics, moral concepts, customs, and mores.

The division of rules into formal and non-formal ones is simply a means to facilitate discussion. In practice, the influences of the two on the interests and activities of people can hardly be separated from each other. The implementing mechanism may be defined as the operating system under which the formal rules and non-formal rules are implemented. The effectiveness of any given institution depends not only on the formal and non-formal rules, but also on whether the implementing mechanism is capable of functioning effectively. In this regard, the three parts of an institution may be seen as mutually dependent, since the absence of any one of them would make it impossible to bring their functions into play.

The Theoretical Implication of the Economic System

The economic system is a fairly controversial concept. According to M. Bernstein (1988, p. 7), the economic system consists of what should be produced by society, how society produces and distributes, and the means and method by which resources are allocated. E. Newberg (1984, p. 9) views the economic system as a mechanism by which economic decisions are made in the fields of production, consumption, and distribution established by society, which includes rules governing distribution and the right to economic decision making. While Veblen (1899) believed that the economic system involves a series of cultural factors, F. L. Fryor held the view that the economic system includes such formal and non-formal rules as structure, organization, law and rules, tradition, and values.
Comparison and analysis have shown that the economic system is in essence the standards for economic operation, and these standards are determined by a number of institutional essentials. The essentials capable of distinguishing between different economic systems include the following: the power rules, the manner by which resources are allocated and the preference for cultural value.

**The power rules.** By “power rules” we mean the distribution of the right to make decisions, which plays a dominant role in the economic system. Owing to their different aims, there is often friction between the interests of subjects. In a country of multiple interests, the government is both the subject of state power and the behavioral subject of the economic system. The economic power and political power of a government are closely combined. Since the government is the highest representative of public interests, its rational objective is to resolve contradictions among subjects and maximize public interests. Hence, the government naturally regulates the relationship of interests among economic subjects on behalf of the public.

As S. P. Huntington (1968) said, by public interests we mean the interests of public institutions as a result of institutionalization of the government. In particular, the institution of the central government realizes public interests by making possible improvements in the macroeconomic environment. Strengthening the authority and institutionalization of the central government provides a solid foundation for the operation of the economic system. Needless to say, power rules can be regarded as balanced when the specific institutional arrangements contained within them balance the interests of the subjects.

**The manner by which resources are allocated.** Since resources are limited, they must be properly allocated. The objective of resource allocation can be realized through currency circulation and price signals, but it can hardly spontaneously yield optimal effects. Resource allocation may also be regulated by the planning mechanism, but resources may not necessarily flow to highly efficient production departments, which can result in low or no efficiency.

Here the price mechanism and power mechanism come into play. The superiority of a government consists in its ability to do things at lower cost than private enterprises. But the operation of a government mechanism can prove costly. Government intervention is effective only when the cost of the administrative solution is lower than that of the market solution.

In modern society, administrative intervention has already become the basic means by which resources are distributed. Resource allocation in a balanced state requires that the position and role of each of the subjects in resource allocation be made clear. It should also work to maintain the effective regulation and control of economic resources by the central government to enable social development. Resource allocation can be regarded as balanced when specific institutional arrangements enable subjects to balance interests. The limited nature of market regulation occurs when only exceptional marginal income is emphasized at the expense of social marginal revenue. Hence, the government’s regulating role in resource allocation.

**The preference for cultural value.** The existence and development of culture is closely related to the economic system. Economic systems contain preferences for cultural value that constrain the behavior of the subject. If an economic system is not grounded in reason, it will lack the motivation to operate. Once a cultural preference becomes the standard for observable behavior, there is less friction and greater social, political, and national cohesion. Although culture, as a concept, may be incapable of changing the world, it can change people, who in turn can change the world (Jiajie, 1994, p. 93). It should be noted that, in an economic system, the preferences of various economic subjects are in conflict insofar as they are based on different understandings of value.

As far as the government is concerned, the problem
of synthesizing individual preferences appears to be paramount. The preference for cultural value in a balanced state should contribute to the harmonious development of the interests of the subject and society. When providing an institutional framework for values, the government should satisfy the subject’s rational requirement for interests and guide the subject toward positive social development.

The Logic of Association between Institutional Balance and Political Stability

The basic content of politics is the regulation of the relationship of interests among people. It is the function of politics to formulate rules. Therefore, a government should use institutions to standardize the interest-based behavior of people to maintain political stability. Lack of perfect institutional constraints often results in interest-based behavior that is disordered, leading to instability. That is, the state of interests of behavioral subjects affects the stability of political systems and nations. Institutions determine interests as well as the processes and objectives of political behavior.

The economic system represents rules of the greatest ability or inability to conform. In fact, the economic system functions as the origin of social conformability (Lipset, 1993, p. 24). As an organ of political power, the government should not only function on behalf of economic goals but, more importantly, political needs. By means of a series of arrangements with the institution responsible for national economy, the government ensures that the economic sector does not endanger political stability in the form of private monopolies. Analyses of theories of state of the 20th century, especially those developed since the middle of the 20th century, show that the political function of states in comparison to the economic function is relatively insignificant. This is due to the great changes that have taken place in the 20th century regarding how countries are ruled. As a means of maintaining political stability, suppression by violence has gradually shifted to economic and cultural control and management. Thus, the means by which governments arrange economic institutions is closely related to political stability.

As a standard for judgment in economics, the balanced state helps us understand the world. David Easton (1953, p. 139) believed that the theory of balance is a valuable concept for drawing analogies between the political activities of balanced states. When it is thought not worthwhile to change the proportion of authority value allocation of a political system, this moment is called the range of “degree” of the balanced state. Here, balance clearly refers to price balance or interest balance, while institutional balance is the range that marks the “degree” of the state of the institution. Only institutions in a state of balance will display characteristics conspicuous enough to bring the function of political stability into play. An institution is designed to constrain the subject’s behavior so that individual interests will identify with public interests.

As Buchanan pointed out (1989, pp. 285-286), the full meaning of the study of institutions lies in the importance of ensuring that all constraints, practices and organs will be capable of reducing selfish political behavior. The two are inseparable insofar as both are necessary to form a balanced institutional state and realize the balance of interests. Obviously, institutional balance implies the harmonious unification of individual and public interests. Otherwise, political stability will be affected. On the one hand, when the economic interests of the subjects of a society are balanced, people lead peaceful lives. On the other hand, when interests among subjects are unbalanced, they often destabilize the political sphere in the form of social upheavals (Guoguang, 1988, p. 10).

The Political Situation in the Traditional Economic Structure

An Examination Beginning with the Power Rules

Observation of the relationship between the central government and local government shows a unidirectional order that may be described as a relationship of obedience. The central government relies on political authority to ensure that the local governments carry out all its instructions. In the nearly 30 years from 1949 to 1976, there were no definite rules for income allocation between the central government and the local govern-
Despite the four adjustments of power made by the central government, the institution of power operation is inadequate, resulting in repeated disordered power relationships as soon as power is delegated to lower levels, and a standstill when taken back. Although power was twice delegated to lower levels, local governments did not obtain real power because these were only expedient measures taken by the central government to decrease economic pressure. Even during the period of the “Great Leap Forward,” the central government still controlled 80 percent of the profit of the enterprises handed over to local authorities (Fang, 1984, p. 459-472).

In addition, under pressure from a structure of highly centralized power and ideology, the economic functions of the local governments were restricted, which made it impossible for them to seek the political support of the central government.

Analysis of the relationship between the government and the enterprise shows that, when deprived of autonomy and subjects who maintain independent interests, the enterprise has to submit to national planning with products allocated by the state. It has neither the function of investment making nor the function of management. Although the collective enterprise has a certain degree of autonomy, it lacks the market mechanism; its source of material, product marketing, and credit all depend on the national plan. The economic relationship among enterprises is not regulated by the law of economy but is established and adjusted by administrative orders of the government. The government exercises unified state control over the income and expenditure of enterprises, forming a state monopoly of the purchase and marketing of products and unifying the allocation of labor, materials, and techniques.

Furthermore, the phenomenon of “isomorphism” exists between the government and enterprise. That is, an enterprise is required by the government to set up an organ corresponding to that of an administrative department. The government controls the production and management of an enterprise, the distribution of property, the hiring and firing of staff and workers. The enterprise “eats from the same big pot” of the government and is not responsible for either gain or loss. The government department responsible for the work decides the appointment and dismissal, promotion and transfer of officers of an enterprise. Rather than extending to the social domain, the adjustment of power between the government and an enterprise is confined to relationships between the central and local governments. An enterprise can only passively be attached to the central government or local governments. The subordinate relationship of enterprise to the government has not fundamentally changed.

Examination of this structure shows that it establishes a power relationship between the government and the individual that stresses public ownership. It prevents individuals from owning the assets of an enterprise, thus weakening the association between the behavior and responsibility of the individual. In principle, the people have ownership of the means of production, but in reality they do not have the right to use or dispose of it. The government that exercises ownership on behalf of the people also owns the right to use and dispose of the means of production.

Consequently, producers become indifferent to their right to use and dispose of it. The government prioritizes uniformity as one of its objectives. People are not permitted to behave beyond the boundaries established by the government, even to the point that they cannot choose their own profession or job. The initiative and creativity of individuals are suppressed, which may lead to feelings of passive antipathy and antagonism. When a relation of attachment is formed between an individual and his affiliation, the affiliation has the right to control an individual, who, apart from it, may have no way to survive or develop. The attachment of an individual to his affiliation is in essence his attachment to the government.
As Lucian Pye has pointed out (1991), no country other than China praises the state to the neglect of the individual. The Chinese invariably endow the state with supreme authority to which the individual remains subordinate.

The rigid system of traditional centralized power lacks flexibility and initiative, which leads to ineffective control and sharply reduced efficiency. This is manifested in, first, the monolithic nature of the administrative hierarchy. Since the government cannot effectively control minor economic activities, the administrative power of the state and the administrators erode in the operating process. Consequently, the state lacks effective constraint over the enterprises, the constraints over the budget soften, and large amounts of state-owned assets, for which no one can be held responsible, get lost.

Second, the traditional centralized power reduces the efficiency of administration. Direct control by the central government over a behavioral subject above the middle level amplifies control so that the rationality, accuracy, and effectiveness of control are all reduced. Mistakes in the policies of the central government mushroom into national disasters because the middle levels are missing, as the “Great Leap Forward” and “Cultural Revolution” clearly demonstrated. Furthermore, the centralization of power leads to decision making that depends in large measure on fortuitous individuals’ qualities, hence the mistakes.

Third, the traditional centralized power leads to a dislocation of the function of administration. The government has exercised control over things that it should not control, could not successfully control or are beyond its capability to control. On the other hand, public affairs such as social administration, social security, and social welfare that should be undertaken by the government have been handed over to organizations at the grass-roots level. Such institutional arrangements are bound to confuse the functions of the government and the grass-roots organizations — leading to the erosion of social functions and affecting political stability. The government’s power rules of hyper-control have not only restrained the vitality of development of China’s economy, but have hampered state functions from being brought into play and impaired the authority of the government. Insofar as the power rules of the traditional system have ossified the relationships between the central government and local governments, the government and the enterprise, enterprise and the individual, control is of primary importance. It is clear that the traditional system of the nation is a non-optimal order, a structure whose superficial stability stems from shallow roots. If control is weakened, there will be neither order nor stability.

An Examination from the Perspective of How Resources Were Allocated

Under the traditional system, the government monopolized the greater part of the essential resources. The government took on the function of controlling essential resources in a direct and all-encompassing manner. The resources were supplied through the systems of the commune, affiliation with a workplace, and the ID card to ensure the implementation of a plan.

The government established the commune system, an organizational system of political power at the grass-roots level in rural areas, to prevent agricultural and sideline products from competing and to ensure that agricultural produce would first be allocated to the industrial field. This quasi-militarized control system conformed with the economic requirement of the state that peasants be stabilized on the land. The government became the authority and beneficiary of the land, labor force, and capital through institutional measures, such as instructional production plans, the unified purchase and marketing of products, strict prohibition of long-distance transport of goods for sale, and restrictions on free commercial trade. The government also wielded authority by closing down the markets of essentials in the countryside and controlling the flow of urban and rural area populations, thereby monopolizing and controlling the essential resources of the rural areas.

However, the stability brought by the highly centralized communal system was fragile, achieved at the
expense of stagnating socio-economic development in the rural areas. The operation of economic resources in the rural areas entered into a closed state, which restricted the rational flow of production essentials, causing faulty resource allocation. In spite of 30 years of development, China’s rural areas have not been able to overcome poverty and backwardness, which seriously threaten the foundation of political stability at the grass-roots levels and make it difficult for the state to realize its aims for rural area leadership.

The state had members of urban society join various organizations called affiliations. Each affiliation had administrative affinity relationships and administrative ranks and was subordinate to government organs according to these relationships. The organizational system of the Party, too, was extended to the grass-roots units along with the administrative system, creating the dual system of political power characteristic of China (He, 1998). Through the unit system, the state took possession of essential resources and strengthened control at the grass-roots level, in effect depriving the grass-roots units, especially enterprises, of resources and the right to decide how to allocate any resources they did possess. Thus, the state did not gain control of society by directly confronting members, but by the unique phenomenon of the unit system. The stability of the unit system remained inherently superficial. Specifically, the assets of the units, which were permanently possessed by society, dwindled as a consequence of the central state. If the unit suffered losses, the state could only assimilate the losses through subsidiary, additional input, or by permitting the unit to raise the price of products. Since the state, due to the bankruptcy of the unit, had no way to bear the political and social consequences, it could only cover up the latent factors of instability.

In terms of the “system of identity” of the planned setup, members of society were artificially divided into three major categories, namely the state cadres, workers and peasants. The status they held in the economic struc-

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An Examination from the Perspective of Preference for Cultural Value

The transformation of the values of the traditional system by the government had an impact on the essentials of traditional culture. Occurring at a moment of transition, the impact reflected the value preference of the period and can be distinguished from both traditional culture and modern culture.

First, in traditional Chinese society, the interests of the group had the greatest value: The individual regarded the interests of the family as his/her own, and the interests of family were considered inseparable from
The integration of politics and culture in traditional Chinese society determined the unidirectional character of how people understood value. After the founding of the republic, the economy was unified by the planned structure of the central government, providing the institutional condition for the formation of unidirectional thinking. Leaders determined the standards for judging the value of things. A mentality of "leadership above the truth" prevailed, and the desire to seek truth from facts vanished. With respect to value behavior, the enterprise, which functioned as a unit of the state's network, cultivated an inertia that forced excessive reliance on the state plan. Higher unidirectional reliance resulted in lower individual independence. While ensuring the thorough implementation of the will of the state, this dynamic has also created ossification and lowered the efficiency of the economy.

A Systematic Analysis of Political Stability in the Transitional Period

Changes in the Power Rules and Political Stability

In a sense, changes in the economic structure redistribute power and alter the framework of interests. When pushing market reform, political stability depends on whether institutions can adjust and balance power rules.

With regard to the integration of central and local powers, the central government adopted a fiscal responsibility system characterized by decentralization. The system lacks a power limiting mechanism for the local government, however, leading to local protectionism, limiting market competition, and reducing the ability of the central government to balance the development of the economy with national integrity. Hence, the expansion of narrow local interests has weakened the financial and material capabilities of the central authority as never before.

The changes in China's financial system decreased yearly the government's revenue as a percentage of...
GDP. That percentage in China was 30.9 percent in 1978, decreasing to 14.14 percent by 1992 and 13.3 percent by 1995. It was expected that by 2000, it would be reduced to 11.3 percent. On the other hand, this ratio was 34.6 percent for Britain, 45.9 percent for France, and 41.1 percent for the U.S. during the same period (Hu, 1997, p. 45).

The fiscal responsibility system led to the unprecedented expansion of the power of local governments. Local governments bargained with the central government, lowered the base figure for the assigned task, handed over less financial revenue, and fought for funds, projects and goods and materials. The weakening of its financial capabilities rendered the central government powerless to address the problems of serious economic and social imbalance. The accumulation of these problems endangers the foundation of the political power system, threatening the political process operation and the stability and legality of the central government. The local economy that carved up the market was detrimental to the political unification of the state. Local governments held back state revenue, took administrative measures to blockade the regional market, set up trade barriers, imposed technological restrictions, stored resources, and withheld the truth. That is, they filtered the policies of the central government or adapted and revised the provisions that conflicted with local interests. By distorting instructions, they overstepped the power rules formulated by the central government and impaired its central authority.

With respect to integration of the powers of government and enterprise, it is important to resolve the contradiction between stability and efficiency. For the transitional period, the state has made clear the position of enterprises. Nevertheless, as the management mechanisms undergo transition, some enterprises have diverted depreciation funds and over-borrowed at the expense of state interests, leading to serious deficits in state-owned enterprises, the loss of state-owned assets, and the phenomenon of spontaneous privatization, all of which contribute to political instability. Neither simply reducing the number of government cadres and delegating powers to lower levels, nor centralizing of powers by the government, helped adjust the power relationship between government and enterprise. While the former jeopardized political stability, the latter sacrificed efficiency. Furthermore, in the transitional period, the government burdened state-owned enterprises with economic, political and social functions. If the government relegated enterprises completely to the market while lacking the associated institutions, the enterprises would certainly abandon certain social functions, e.g., running schools, hospitals, nurseries, and social insurance. At the same time, the government was unable to undertake the social functions alone, leading to the loss of part of the social functions. In recent years, organs of state power have suffered from assaults by staff and workers who object to endowment insurance, unemployment, and medical care. If unresolved for long, these problems will seriously affect the normal operation of the political order.

Regarding the integration of government power with individual power, at the beginning of reform, the institution of the government met the institutional demand of individuals to become the subject of interests. But the unbalanced institutional provision generated political instability. This occurred because, on the one hand, the government solved the problem of the motive force for economic development through its institutional arrangements, while, on the other, it generated the kind of egoism that can disrupt the order of social life and threaten the political system of society.

Second, the government introduced the principle of competition into economic life through institutional provisions, but competition was very like a “double-edged sword.” If government control was not strong enough, undesirable competition and chaos would damage the operating order of the political system.

Thirdly, during the transitional period, the government made it possible for individuals to unburden
themselves of the yoke of the planned structure and freely develop. But the “rigidity” of interests in the market economy, in turn, narrowed the attention of people at the expense of the future, goading them to engage in speculation while keeping them from consciously observing social standards. Valuing material gains above justice led to friction between their immediate and long-term interests, increased contradictions among interests, and ignored the operation of the political system.

Changes in the Allocation of Resources and Political Stability

According to Peter Brawer (1988, p. 116), as a political system rationally distributes resources, it wins the affirmation and support of the people, balancing interests and thus ensuring social and political stability. For China’s rural areas, however, the government has provided autonomy to allocate resources, inadequately controlled rural resources and intensified the problem of stability in those areas. In particular, the shift en masse of surplus labor to non-agricultural sectors, and the flow of people from rural areas to cities and towns, has become the biggest problem of China’s economic and social transition in the new century.

As the government did not have sufficient time to adjust and adapt, peasants developed feelings of vindictive estrangement toward society. This estrangement presents a serious challenge to social order. The floating agricultural population and the rate of criminal and other anti-social behavior has become an apparent cause of social disorder.

In addition, given the current uncertainty regarding ownership of land, the government finds it impossible to monitor land and those engaged in land management effectively. At the same time, numerous forced changes have occurred in the ownership of land. For instance, in the invitation for bid, lease, or auction of the right to manage four kinds of wasteland (abandoned beaches, barren mountains, uncultivated land, and wasteland), the government stipulated that anyone who made the highest offer would be given the right to manage. The stipulation caused an uneven concentration of wealth in the rural areas. Stability in the rural areas in China threatens political instability (Deng, 1987).

A look at the cities shows that separating the functions of the Party branch from that of enterprise management does not mean that owners and managers share the same interests and value objectives. If the government’s monitoring of and control over state-owned assets is not strong enough, the manager may steal state-owned assets. For instance, an enterprise may take advantage of imperfect tax law to evade taxes in the course of changes in property rights, vaguely defined property rights, and changes in revenue structure. This opportunistic situation can destroy the value of state-owned assets and weaken the material foundation by which the government adjusts and controls society.

As state-owned enterprises reduce staff to increase efficiency, Party and government institutions also cut down on staffing, increasing unemployment in cities and towns. The surplus force will be difficult to transfer and absorb; there will exist more people waiting to be employed or reemployed than there are opportunities of employment. As the number of impoverished people increases, disparities between the rich and the poor will grow, aggravating an unfair distribution of resources in society. If the government fails to take adequate measures, the imbalance will bring with it a series of problems, such as the “unbalanced state of mind of social strata,” theft and robbery, pornography, gambling and drug addiction, criminal syndicates, and anti-government behavior. The cost of government operation will increase, worsen the social environment for reform, and render society vulnerable to abrupt instability.

China’s decision to pursue progressive institutional changes and economic reform, while dominating the means of resource allocation, may lead to friction and contradiction in the distribution of interests. To begin
with, there is the problem of unbalanced allocation of resources. According to statistics, the sum total of the difference between nominal and market prices of goods and materials in short supply, added to nominal and market differences in interest rates and exchange rates, reached 200 billion yuan in 1987 and 350 billion yuan in 1988, accounting for over 20 percent of China's gross national product (Hu, 1989, pp. 36-43). During the transitional period, institutional changes scattered the power to allocate resources.

Firms and individuals, one would expect, take advantage of the double-track pricing system and shortage. Incomplete institutional reform in the transitional period, in fact, has led to widespread rent-seeking, and, in turn, may bring about a crisis of confidence in government that threatens the political stability. Government policy has contributed to instability with an unbalanced allocation of resources. In the transitional period, the government mandated unbalanced growth of regions by promoting the development of coastal areas. As a consequence, essential resources from the less developed mid-western areas flowed into the more highly developed coastal areas. The resource flow created a "gap in expansion" between the economies of the coastal areas and the interior, causing the economic problem to evolve into a political one. In particular, the western areas are regions where China's national minorities live in compact communities. For historical and geographic reasons, the economic growth in these areas is slow, which, coupled with unfair distribution, may further sharpen conflict in these areas. If the government leaves unchecked the broadening gap between areas and income levels, conflict will rise and may jeopardize national unification and territorial integrity.

Changes in Cultural Value Preferences and Political Stability

The introduction of a market economy is bound to conflict with certain cultural value preferences that are deep-rooted and generally recognized by the public. With the quickening of the pace of development to a market economy in China, ethics in economics were shat-tered, which may affect the interests of certain people and result in a crisis of belief, depression, and moral degradation.

The political effects of individuality and value preferences. During the period of economic transition, the government used mandatory regulations to push the economic subject to relatively independent status. However, when the individual with interests broke free from the non-economic fixed relation of reliance, there emerged the possibility of extreme expansion of individuality value preferences, developing the problem of extreme egoism whose negative effects cannot be treated with indifference. If the government does not guide the economic subject's understanding of value and value behavior through appropriate channels, cultural value preferences will be in an unbalanced state. Social and political stability will lack the principle of cohesion.

The political effects of efficiency value preferences. Since the economic subject is keen on efficiency, he/she is bound to require that the market get involved in the domain of distribution to broaden the income gap and create a mechanism of incentives. But this, too, may lead to polarization that can cause fears of instability and crisis in society. When such a social mentality is transformed into extremes by certain incentives, there will be social unrest or disorder that is likely to trigger political crisis. Emphasis on market efficiency is bound to lead to the anxiety to achieve quick success and get instant benefits, which conflicts with the mid- and long-term interests of the state, and may cause the macro-economy to spin out of control and affect social and political stability.

The political effects of gain-seeking value preferences. During the transitional period, some of the subjects of interests value the search for profit and money above all else. Utilitarianism and pragmatism have become the order of the day, and money the basis for measuring the value of things. Hence, such negative
phenomena as swindling, kidnapping and abduction, forgery and fraudulence, smuggling and prostitution, drug addiction and drug trafficking that have been kept in check for a long time have re-appeared. The nascent popular culture still in the process of development is turning into its opposite under the action of speculation capital and a handful of upstarts. In fact, a few people, forgetting all moral principles in favor of profits, tread on the legal system and morality to harm the public and society. Although the institution itself is not completely to blame for these phenomena, the unbalance between provision of and demand for institution is one of the root causes.

**Institutional Balance: The Foundation for Political Stability in the Transitional Period**

**The Government as Institution Providing Subject**

As the representative of public interests, the government has the power to coordinate the interests of all quarters and arrange compulsory institutions. The mandatory power of the government makes it possible to compensate for the interests of the innovator. The marginal income obtained by the innovator for his/her innovative behavior will be close to the social integral income, thus maximizing social welfare. At the same time, the government can also carry out mandatory institution innovation without unanimous agreement of the members of society, saving the high cost of consensus of opinion. The commonality of the government itself lies in that it is the most appropriate producer of public articles and can obtain fairly large-scale benefits. As it is, in the non-Pareto evolution of an institution, more often than not there are some mandatory elements. Furthermore, whatever the political system, the government is always the principal provider of an institution. Whether for the maintenance of an old system or the implementation of a new one, the mandatory power of the government provides the foundation. As long as the character of reform is non-Pareto, the reform is very likely a certain kind of mandatory reform (Sheng, 1994, p. 50). No matter how dissatisfied the subject of behavior involved in the institutional innovation may be with the mandatory changes in the institution, he has to be constrained by the mandatory power of the government. The government can force through a scheme that cannot be solved or is hard to solve through negotiation. The mandatory power of the government originates in its lawfulness and the government will not impose any institution unless it has the support of the majority of the people.

The institution provided by the government takes the balance of the maximization of social interests as its rational objective. To this end, the government takes advantage of its lawfulness and authority to regulate irrational phenomena and provide an institution at the macro level. When pushing forward institutional innovation or providing an institution by resorting to the administrative mandate, the government is the crucial productive resource. The provision of an institution by the government as an embodiment of institution is of importance to the welfare of the country. The operating rules of market economic structure as an institution will not occur spontaneously, and even if they do, there is no way to guarantee that people will observe the market operating rules of their own free will. As Karl Polanyi (1957, p. 140) said, as a result of the steady expansion of centralized interventionism, the road to the free market was opened up and not closed down. By mandatory institutional change is meant changes in the dominant institutions provided by the government, that is, arrangements for new institutions within the statutory range. Not only does the government enjoy absolute superiority politically, it can also constrain the behavior of other subjects of interest in varying degrees. It is thus clear that the government is the subject of the provision of institution.

**The Positioning of the Government's Economic Functions**

In the days of socialist planned economy, the government monopolized all the means of production and economic activities on an unprecedented scale. The decision makers and executives of the planned structure attempted to work material miracles that would surpass the capitalist market in terms of economic achievements. However, such an illusion resulted in poverty and backwardness. When reconstructing a market economy on the unique framework left over by
A state with definite economic functions is the historical precondition for ancient China to step into modern society.

The traditional structure, none of us could avoid rethinking the economic functions of the government.

First, if we adhere to the low efficiency of a planned economic structure, the realization of the interests of the subject of micro-economic behavior and China's overall political stability would lack the necessary foundation of a motive force.

Second, to establish and perfect the economic structure of the socialist market of China, we should ensure that the laissez-faire days of “governing by doing nothing” and of playing the role of a “night watcher” are behind us. We must never revive the unbridled free market economy. The socialist market economic structure combines government intervention with market regulation to enable the market to play the foundational role in resource allocation under the macro-adjustment and control of the country. To this end, it is necessary to establish a system of modern enterprises with clear-cut property rights, distinct powers and responsibilities, separated government and enterprise work, and scientific management as required by the market economy.

Third, to optimize the allocation resources it is necessary to set up a market system open to the whole nation, one that combines the urban market with the rural market, and links the domestic market with the market abroad. In addition, it is advisable to transform the government’s function of administration of economy by continuing to prioritize efficiency while giving consideration to fairness. The transformation should establish multiple forms of systems of distribution, such as the distribution according to work or on the basis of essentials to encourage some people and some areas to get rich first so that all the people will be on the road to common prosperity.

Finally, it should establish a multi-level social security system to promote economic development and social and political stability. As such, the market economy with Chinese characteristics is far superior to the western economic mode, its components being “market economy + government intervention + social security” and its characteristic, the combination of a market economy with government intervention (Yuan, 1999). Making macro-regulation and control the functions of the government is the key to realizing institutional balance in China during the transitional period.

In the several thousand years of China's history, the state has been in the ruling position. Historical experience has shown that the weakening of the powers of the central government can only disrupt the political superstructure and interrupt the progress of economic prosperity and social development. A state with definite economic functions is the historical precondition for ancient China to step into modern society. The practice of China’s planned economic structure continues the tradition of the “concept of state.”

In years immediately following the founding of the republic, the rapid development of China's economy was attributed to the dominant role played by the state in the process of socialist industrialization. The sustainable development of China's economy and political stability was affected by the institutional arrangement for an “all-round type” government. Later, the reality of communist countries required that the influence of the state on economy be combined with the subject of market economy and the self-development of the market relation. But this does not imply that the state would give up its regulation and control of the macro-economy.

If the government neither regulates economic activities nor supervises the economic process, it creates the conditions for social and political instability. The economic reforms carried out in Eastern Europe and Russia have had destructive consequences because the responsibility of the states involved has been too restrained. On the one hand, it is imperative to break the shackles the traditional, centralized system of the state has placed on economic development, and on the other it is important to uphold new forms of national authority and bring the state into the process of establishing the market and developing the economy. In China, no force is more authoritative than the government in promoting the formation of market economy.
If a country gives up its economic functions prematurely, especially the macro-function in the transitional period, the result can only be a loss of control of market reform and political instability.

**Institutional Balance: The Countermeasures for Political Stability during the Transitional Period**

As China develops its economic market, it is crucial to unify institutional provision and political stability. Needless to say, insofar as institutional provision requires a stable political environment, it is conducive to political stability. That is, without a stable political environment, the achievements of institutional provision may be destroyed. Unlike the solid state under the traditional system, the political stability required in the process of operating a market economy is dynamic. In modern society, the objective of political stability is “stability — orderliness — development” (Yuan 1999). The exercise of control over the social and political order is to seek stability with development as its ultimate objective. The means of maintaining order depends on whether the means is conducive to development or not. The key to avoiding political instability in the transitional period lies in whether the government has the ability to control, coordinate and adapt. Unlike western countries, the developing countries did not begin to develop their markets until after they were founded; in western countries, the state emerged in company with the process of market development. The government of the developing country and its provision of institution play a decisive role in the process of development of economy toward the market because a thriving market economy depends on institutional support. Those countries that had centrally planned economies lacked, during the process of transformation, exactly these institutions. The imperfection or lack of an institution has thus led to loss of political order. In other words, political order is the consequence either of a low degree of institutionalization or a low degree of recognition of an institution.

By institutionalization we mean a behavioral mode that is stable, respected and recurrent, while a low degree of institutionalization implies the inability to actively respond to various challenges from the outside world and to effectively perform integration. Of course, when there are people who recognize no institutions, or have even developed antagonism and resistance, it will be impossible to standardize social behavior and hard to maintain a stable political order. Political stability is achieved by relying on the government’s selection and provision of an institution. The development of market requires that the government bring its economic administration function into play to build a balanced institutional structure. The institutional provision by the government includes the provision of law, structure, policies and cultural value.

**The Provision of Law**

In modern society, as special social rules formulated or recognized by the state, law has become a significant tool for political control and the general standards for constraining arbitrariness. Apart from its class character, law has a social character, most obviously the social character of economic law and regulations. The law, rules and regulations provide the criteria for all the activities of an economic subject. It is the task of law to protect all social interests and maintain a certain balance or harmony among these interests (Bottome, 1987, p. 147). The essence of all institutions is interests and, without exception, the precondition for the existence of any laws and rules and regulations is that they can standardize people’s behavior in relation to interests. In the transitional period, the purpose of the Chinese government, which regulates and controls the economy by legal means, is to constrain the behavior of the subject of interests to conform with the common behavioral standards, both promoting reform and development and protecting political stability. Specifically, the purpose is to determine the behavioral standards of the market and recognize its rights and obligations. The market can pursue its interests only on the premise that it will not damage public interests. Compared with legal standards of a restraining character, the present legal standards have a higher quality of guidance and are more balanced with the institutional standards. When an economic subject keeps its behavior in conformity with legal standards of its own accord, the factors of political instability occurring in
As China develops its economic market, it is crucial to unify institutional provision and political stability.

Second, the system of social security should be perfected. The imbalance in interests brought about by restructuring will inevitably cause certain social groups or members of society to lose vested interests or enjoy relatively less social interests for the time being. For instance, the merger or bankruptcy of enterprises in the process of market development will leave certain staff and workers impoverished. If the interests of such groups or members of society remain uncompensated for long, dissatisfaction and indignation will turn into destructive forces for political stability. Therefore, the government ought to redesign the system of social security by providing corresponding institutional arrangements for guaranteeing equal enjoyment of benefits.

Third, the management system of the property rights of state-owned assets should be reformed. This means separating the “four rights” from the government and handing them over to the relatively independent multiple subjects for their exercise. That is, the government exercises the power to manage the economy, and the National People’s Congress exercises the power to own the state-owned assets on behalf of the people, while the power to manage state-owned assets entities should be exercised by the micro-economic subjects. The management of the state-owned assets property rights belongs to companies dealing in state-owned assets. The government should break away from the management of miscellaneous affairs, abandon state-owned assets, and concentrate on administrative supervision to ensure that the rights and interests of state-owned assets will not be encroached upon, thus laying a solid material foundation for China’s lasting stability.

Fourth, the macro-management and coordination mechanism of the flow of population and labor force should be developed. During the transitional period, China is confronted with the enormous pressure from the flow and transfer of surplus labor, which, objectively, asks the government to give guidance and coordination at the macro-level so as to promote the orderly flow and transfer of population and labor. At the present time, the government should accelerate the process of urbanization in a planned way by creating
the corresponding mechanism. It should develop medium-sized and small cities and towns as source of economic growth and the cornerstone of a stable future society, thereby maintaining the sustainable growth of the national economy. At the same time, it is necessary to open channels of population flow to prevent social upheavals caused by abrupt population flow. The government should encourage private and individual businesses so that they can provide positions to the jobless and eliminate discontent among the impoverished.

**The Provision of Policies**

During the transitional period, many contradictions in interests and conflicts cannot be coordinated and solved owing to imperfections in the legal system and institutions. Objectively, this requires that the government fill the vacuum of missing institutions by means of policy provision. The essence of policy is the concentrated reflection of the relationships of social interests. The differences in interests of people directly lead to contradictions in the interests of subjects. The government should intervene and coordinate the contradictions in interests of the subjects to form a rational framework of interests. It should be noted that the market economy takes the direction of interests as its objective and interests as its driving force. The market economy recognizes the difference in interests of the subjects and encourages the subjects of economy to seek the maximum interests. However, coordinated social and economic development requires a unified objective. The government that represents the overall interests of society should intervene in economic life by incorporating independent decision making to encourage the economic subjects to seek interests. The attribute of political value in China’s market economy has determined that the economic development is built on the foundation of political and economic systems different from those in the capitalist market economy. But the spontaneity of the market mechanism will aggravate polarization. The government should adopt balanced economic policies to perform macro-regulation and control. The government regulates the excessively high income of subjects through its tax policies and helps those in the impoverished stratum sustain themselves. The government can also regulate the percentage of tax and strengthen the invigorating function of the impoverished subject by providing special policies. It can encourage investors at home and abroad to develop poverty-stricken areas to help improve the economic habits of the impoverished to eliminate the economic disparities that endanger political stability.

**The Provision of Cultural Value**

The institution of cultural value is the order intrinsic in the economic structure. It has become the precursor of political stability by influencing the mode of behavior. The purpose of the government in regulating and controlling cultural value is to guide the interests-based behavior of the economic individual in a direction helpful to the public interests of society. Such regulation and control of cultural values not only negate and restrain the motive force of individual behavior but standardize and guide it to conform with the principles of public interests. Since market economy needs a fairly high cultural content and moral standards, it is important for the government to push forward reform in the educational, scientific and cultural system through effective provision of institution. Such a provision of institution can strengthen quality education, help popularize science and technology, enable culture to flourish and fashion public opinion into a wholesome and enterprising cultural value.

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