

Inflation, Welfare, and the Political Business Cycle

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Since April, China has focused on the inflationary challenge. The months of delay before strong measures were taken allowed inflationary pressures to become established, and inflation increased through July despite tight monetary policy. Politicians have resorted to price controls, including in the sensitive housing sector. The lack of success in fighting inflation has fed an unsettled mood in the population, which complicates the power transition set for next year. In particular, the position of Li Keqiang, premier designate, has been weakened.

Since April, Chinese policy-makers have maintained a consistent focus on fighting inflation. April 2011 marked an important turning point from the policy stance maintained through most of 2010, during which policy-makers delayed tough action and adopted a wait-and-see attitude on the dangers of inflation. Although policy has been resolute since April, the delays had real costs. Inflationary pressures have been allowed to take root, making the effort to control inflation costlier and more difficult than it needed to be. The consumer price index grew 5.4 percent in March, which surpassed China's traditional 5 percent "red line" and immediately triggered the more resolute policy line. Despite the new seriousness, the inflation rate has remained high, and even drifted upward to 6.5 percent in July.

These economic conditions have an immediate effect on the political environment. Inflation is very unpopular in China, and when price increases are this evident, it provokes frustration and anger, particularly among middle-class urban dwellers. Indeed, immediately after the inflation figures for March were published, Shanghai truck drivers staged a three-day strike over soaring fuel prices and port charges. Although the protest was defused with concessions on port charges, it seemed to initiate a season of discontent. As the summer passed, a series of incidents (covered in the official press) contributed to the unsettled public mood: two bridges collapsed; the offshore oil industry encountered spills and fires; and the new Beijing-Shanghai high-speed rail line encountered four separate "glitches" in the first 10 days of operation. All these incidents were overshadowed by the shocking crash of the high-speed train near Wenzhou that killed 40 passengers on July 26. Until open reporting was halted by propaganda officials four days later, an outpouring of shock, grief, and outrage gave eloquent expression to the public mood.

This type of economic environment is precisely what policy-makers would have preferred to avoid on the eve of a leadership handover. Inevitably, widely perceived economic failures discredit policy-makers and make their succession choices seem less inspired and less inevitable. This piece first briefly examines inflation policy, emphasizing some of the shortcomings of policy implementation. Then it examines some of the broader changes in policy alignment that, over the last few years, have altered the environment of elite policy-makers. Finally, it puts these economic and political changes

into the context of the political transition looming in late 2012. One important conclusion is that the position of premier-designate Li Keqiang has been substantially weakened. While Li will probably ride out these challenges and assume the premiership as scheduled, it is by no means inconceivable that he will lose out in the coming scramble for power.

Anti-Inflation Policy

A key feature of the relationship between inflation and monetary policy is that there are significant lag effects. Overly expansionary monetary policy causes inflation, but with a lag, which is typically estimated at 14 to 20 months. Thus, the huge expansion of credit and money supply in early 2009 was bound to cause inflationary pressures by late 2010. However, Chinese leaders wasted all of 2010, hesitating and putting off necessary actions. Wen Jiabao stated in his press conference after the 2010 NPC meeting, “if there is inflation, added on to the inequitable distribution of income and corruption, it would be enough to threaten social stability and the consolidation of political power.”¹ This did not in fact signal a shift in policy. It was not until October 2010 that the PBC (People’s Bank of China) was allowed to raise interest rates for the first time since the global financial crisis began. Even then, it was not until December, at the Economic Work Conference, that inflation-fighting was raised to top priority. Almost a year had gone by with little action. It is more than a little ironic that at *this* year’s press conference after the NPC, Wen Jiabao declared that inflation would top the government’s agenda this year, stating, “Inflation is like a tiger; once it gets free, it is difficult to put it back in the cage.”² Why, if China’s leaders know that it is difficult to put inflation “back in its cage” once it is unleashed, did they nevertheless open the cage and let the tiger out? The lack of decisiveness in fighting inflation displays a sharp contrast with the extreme decisiveness that Chinese leaders displayed in combatting the global financial crisis at the end of 2008. The price that policy-makers have paid is that anti-inflation policies now (finally) in place are also working with a lag, and have not yet begun to bring inflation down. July inflation was the highest so far this year, pushed along by a continued surge in food prices.

The main orthodox tools of anti-inflation policy are monetary policy and exchange rate policy. For monetary policy, the central bank is now using both quantitative measures (increasing reserve requirements) and price measures (raising interest rates). Shortly after the March inflation data came out, the PBC raised bank reserve requirements again, and then followed up with two more increases through early June. Thus far, the Bank has increased reserve requirements six times in 2011 and 12 times since the beginning of 2010, when the bank began moving away from the super-loose policy of 2009. The reserve requirement is now at an unprecedented 21.5 percent.³ In April and again in July, the PBC raised interest rates, marking the fifth increase since the current tightening cycle began in October 2010. The benchmark one-year lending rate now stands at 6.56 percent, just above inflation, while the one-year deposit rate is at 3.5 percent, still significantly below the inflation rate.⁴ After two years of massive increase in lending, and years of ample liquidity in China financial markets, financial markets have only slowly begun to show signs of across-the-board tightening. Lending rates

charged by small banks and informal “curb markets” have begun to increase, and firms are now reporting increasing difficulty in maintaining access to credit when they need it.⁵ These painful symptoms indicate that the necessary correction is finally under way.

Moreover, the government has begun using the other economic levers at its disposal. Since the beginning of November 2010, the RMB has appreciated just under 0.5 percent per month against the U.S. dollar, very consistent with past practice. Still, this tool is being underutilized: the U.S. dollar has declined dramatically against other currencies of the world during this period, so the RMB’s effective appreciation against global money has been nil. That means that on balance, the Chinese have forfeited an opportunity to use the exchange rate more aggressively to fight inflation. Despite Premier Wen’s declaration, inflation-fighting is still not *that* high a priority for policy-makers.

Finally, it is also important that the government has begun the first steps toward ratcheting back the massive commitment of resources to government investment, and especially to government infrastructure projects. China’s high-speed rail project had originally been budgeted to invest a bracing 700 billion RMB in 2011, but in April it was announced that the figure would be reduced to something over 400 billion. In one stroke, that would cut high-speed rail investment to just below 1 percent of GDP, knocking 0.6 percent of GDP from total investment.⁶ This is a positive development, especially if the cutbacks spread to other areas of government investment. It is also troubling, in that the retrenchment of high-speed rail investment did not occur until after the fall of incumbent Railway Minister Liu Zhijun on corruption charges. Moreover, after Minister Liu’s fall, and even before the Wenzhou crash, the press has exposed an almost Great Leap Forward–like expansion of the scale of high-speed rail construction, with lines penciled in for priority development even in unsuitable places. Overall, the fact that the government is now using the tools of monetary policy (interest rates plus reserve requirements), exchange rate, and direct budgeting of government investment in a consistent direction to combat inflation shows that the inflation-fighting effort is now serious and may begin to see some success by year-end.

The Inflation Circus

Once the fight against inflation was elevated to the highest priority, the government—not surprisingly—decreed a general mobilization, urging everybody to pitch in to “whip inflation now.” The National Development and Reform Commission (NDRC) coordinates this campaign. Since December 2010 the NDRC has required a daily report on prices of primary food products, which it then uses as a way to pressure merchants not to raise prices. The NDRC pressures coal merchants to restrain price increases and also to follow through on existing contracts and supply power plants with the quantities and grades of coal specified. Exports of fertilizer were restricted as well.⁷ These efforts are sometimes trumpeted as successful (for example, in stabilizing food prices before Chinese New Year), but other times clearly fall short of intentions (for example, shortages of coal have been reported at power plants from Hunan to Qinhuangdao).

In April, the NDRC rolled out a series of formal meetings with the private chambers of commerce that are grouped into the All-China Federation of Industry and Commerce. As a result, 24 of the 28 Federation chambers of commerce signed an undertaking to “guarantee supply, stabilize prices, and promote harmony,” in which they promised not to collude to push up prices, hoard, or cause panic.⁸ The vice-head of the Federation, Zang Zongsheng, said that the undertaking is purely an expression of enterprise self-restraint, because the chambers don’t have the ability to force their members to do anything. Participants in the meetings acknowledged that the NDRC did not impose a price freeze, but criticized the meetings as a misguided attempt to suppress market forces, one that would not work and that was unfairly focused on private firms.⁹ As a follow-up, the NDRC had a similar sit-down with the heads of China’s biggest coal mines, all of which are state-owned. Again, the commission only politely asked for self-restraint, but of course the mine heads would not have forgotten that the NDRC froze coal prices for six months during a similar inflationary episode back in 2008.¹⁰

At the same time that it was requesting curbs on price rises, the NDRC demonstrated its own willingness to go the other way on April 7, when it raised the prices of petroleum products. This was the proper policy considering the increase in the world price of oil, but it did not escape notice that the large, state-run oil companies benefited from the move just as the NDRC was jawboning private firms to hold their prices down. Perhaps inspired by this contradiction, an anonymous netizen posted receipts online signed by the Guangdong branch of Sinopec for 1.68 million RMB worth of expensive liquor. The receipts specified bottles of 50-year-old Maotai—much prized and hard to get in China—plus a case of Chateau Lafite 1996 at a per-bottle price of 11,800 yuan (about \$1,800).¹¹ Sinopec’s first response to this embarrassing revelation was to point out that they run a chain of convenience stores at their gas stations, so that there was nothing unusual about beverage purchases by Sinopec branches. However, since no one was ever able to produce a \$2,000 bottle of wine for sale at the local Kwik-E-Mart, this explanation was widely ridiculed, and the manager responsible was suspended.¹² Overall, NDRC has been sharply criticized in the business press for its efforts to stop inflation by administrative fiat: an encouraging sign that basic economic principles are now widely accepted as the benchmark to judge government policy.

Controlling Housing Prices

The full-court press designed to control prices has by now extended into the sensitive area of housing. For over a year—since April 2010—the Chinese government has been launching successive campaigns in a more or less continuous war against housing price appreciation. A new campaign (the third, by most counts) was launched in January 2011, and pressure has been maintained, or ratcheted up, in the months since. The latest campaign carries over some of the measures from previous campaigns, but also introduces a much stronger element of price control than any previous campaign. The State Council’s “New Eight Articles,” issued on January 26, called for increased local government responsibility in controlling housing prices, and required local governments to develop and publicize target price limits by the end of March. The New Eight Articles also called for more public housing, greater financial disclosure by developers, and

encouraged localities to restrict purchases to local residents.¹³ The city of Beijing promptly prohibited sales of housing to those without a Beijing residence permit (*hukou*), unless they could produce five years' of tax or social security receipts.¹⁴ Numerous other cities followed suit, despite widespread recognition that the policy would impose burdens on immigrants purely on the basis of *hukou* status, an approach that runs entirely counter to the thrust of central government policy on immigration under Wen Jiabao.

On March 16, the NDRC required that sellers of newly built housing publicly post sales prices, and disclose all other fees and conditions of sale. Housing was brought under the "Price Law," and local price bureaus, which are under the jurisdiction of the NDRC, were for the first time charged with enforcement.¹⁵ In this environment, the target prices that the New Eight Articles had required local governments to publish suddenly took on a new significance. Since local governments are ambivalent (to say the least) about housing price appreciation, they responded by delaying, waiting and watching to see what other cities did, and then during the last days of March published targets that were not too demanding to meet and were relatively hard to monitor. By the end of March, nearly every province and city had published some kind of housing target price.¹⁶ Most of these took the form "the housing price increase will be below the growth rate of household income," but some declared that appreciation would be less than last year, or would be controlled below 10 to 15 percent. Overall, the targets did not strike the market as terribly strict. Most potential home-buyers in fact took them as evidence that home prices would continue to climb.¹⁷ The central government responded by tightening the screws. In mid-April, it sent eight home-price inspection teams to 16 provinces. Each team consisted of about 10 people, and was most often headed by a vice-minister from one of various ministries, including Finance, NDRC, Land and Natural Resources, the China Bank Regulatory Commission, and the State Council Office.¹⁸ Teams stressed the seriousness of the housing task and typically talked down the local government target price by a few percentage points. But most importantly, they emphasized that the target prices are now to be "hard" targets. Local governments had flexibility in the means they chose to implement the rules, but the basic idea was to enforce price limits. Real estate developments are now required to report expected prices when they apply for project permits, and the approval process now explicitly includes examination of proposed prices. Projects that propose prices significantly higher than the average selling price in that district in 2010 are to be subject to close scrutiny. Finally, the posted prices now being monitored by the local price bureaus of the NDRC are required to match the prices in the application. Shenzhen City—often regarded as the pioneer of market reform—was an early adopter in the wake of its inspection team's visit.¹⁹ A full set of price controls was suddenly put in place, and Shenzhen's housing policy has gone from "limiting credit to limiting purchases to limiting prices." The regulations on posted prices went into effect nationwide on May 1.

To be sure, none of these regulations technically freeze housing prices, but they are all designed to increase pressure on developers to limit price increases. One of the tools the NDRC will use is to accuse real estate companies of profiteering. There are no clear standards yet for what constitutes profiteering in real estate, since nobody has been charged with it for many years, but the NDRC promises to come up with some

standards.²⁰ This willingness to directly confront real estate developers comes in part because they have so far been weathering successive government campaigns relatively well. According to most analyses, real estate developers had maintained adequate cash flow while increasing their holdings of land through the first half of 2011, and were positioned rather well for probable future scenarios of land scarcity.²¹ As a result, the government has decided to tighten the screws. Doubtless these interventions will slow the apparent rise of housing prices, but at the cost of introducing new distortions in the market and also making reported prices even less reliable as a measure of housing market trends than they already are.

The Big Picture

In her analytic work, Susan Shirk has written about the division of responsibilities at the top levels of the Chinese regime in terms of a “performance coalition” and a “control coalition.”²² This is a useful way to conceptualize the Chinese regime over the long term. For the past 30 years, the performance coalition has consisted of a diverse set of officials united by their desire to find solutions for China’s economic problems. Thus, financial, industrial, and commercial bureaucracies worked toward economic reform, even as they pursued their own particularistic interests. “Reform” was the greatest challenge, because without it the economic system would not be productive enough to survive and grow. Distribution of the benefits of growth was to some extent an afterthought. The control coalition was more concerned with stability, and consisted of the propaganda and discipline inspection sectors, as well as intelligence, public security, police, and the military. For most of the past 30 years, the control coalition was willing to go along with the policies of the performance coalition in pursuit of the broader goal of national strengthening.

In recent years, the orientation of what used to be the performance coalition has changed. As politicians, Hu Jintao and Wen Jiabao seem more concerned with the distribution of the benefits of growth than they are with the underlying system that generates wealth. Within the economic management agencies, they have given increased authority to those organizations that attempt to shape the distribution of wealth, such as the Ministries of Finance and Labor, and especially the NDRC. Their objective has been to provide the resources to fund the “harmonious society” and the rebuilding of the social welfare networks that collapsed during the earlier stages of reform. At the same time, the NDRC, along with the Ministry of Industry and Information Technology (MIIT) and the Ministry of Science and Technology (MOST), has been given responsibility for altering the trajectory of industrialization toward higher technology sectors, as well as implementing the energy conservation agenda. Increasingly, the Wen Jiabao administration seems to be a “welfare” government, focused on distribution of the benefits of growth, social security, and shaping the development trajectory. “Welfare” is a worthy objective, but the ultimate ability to achieve it depends to a substantial degree on the continuation of the reform agenda. This is so both because it is technically difficult to craft effective policies to achieve redistributive goals, and because any

redistributive agenda depends in the long run on the continued health and productivity growth of the economy as a whole.

The internal makeup of the performance coalition has shifted: the constituency for continued fundamental reform has shrunk, while the constituency for an activist welfare orientation has grown. Today, it is really only in the financial sector that there exists a critical mass of experienced, knowledgeable officials committed to serious reforms.²³ Wang Qishan, Politburo member and vice premier at the State Council, represents this group in the highest political councils. But Wang Qishan is the only member of the 25-person Politburo clearly associated with the need to continue market-oriented reforms.²⁴ Instead, the Politburo is filled with provincial Party heads who are certainly concerned with economic issues, but primarily from a politician's standpoint, that is, with the distribution of the benefits from growth and the building of patronage and support at the local and central levels. The orientation of these local politicians blends in smoothly with the welfare orientation that has been the most important achievement of the Wen Jiabao administration thus far. At the highest level, on the Politburo Standing Committee, there is no one with an unambiguous commitment to push forward on market reforms. To be sure, most of the top leaders continue to support a market economy, but they tend to take it for granted, and focus their attention on shaping the market economy to get the outcomes they prefer.

Given this orientation among the top leaders, it is not surprising that recent Chinese internal economic policy debates have tended to be resolved in favor of "redistribution" or "welfare" outcomes rather than further reforms. This has been true with respect to macroeconomic policy debates as well, which often come down to arguments between the PBC and the NDRC, with each side seeking to bring Premier Wen Jiabao and other top politicians to its point of view.²⁵ Since the eruption of the global financial crisis in 2008, the NDRC has consistently won those debates. The crisis itself weakened the reformers, who gain credibility from the performance of the U.S. market economy, and inevitably lost credibility along with the U.S.'s economic failures. More specifically, the PBC was focused on inflation-fighting in the 2007–2008 period just before the onset of the global financial crisis, which turned out to be a piece of spectacularly unfortunate timing. Conversely, the NDRC was the driving force behind the initial stimulus package that ultimately carried China through the crisis. The PBC never overcame its misgivings about the massive credit growth in 2009, which the top leaders view as having been basically successful. Thus, not surprisingly, the top leaders pursued their inclinations to focus on distribution and welfare, choosing to believe the NDRC's analysis, while ignoring that of the PBC. This surely is an important part of the background in understanding why China's response to the obvious inflation threat was so tardy. The long-standing warnings of the finance group about excess liquidity were ignored, because the top leadership did not really want to hear what they had to say.

We do not know the exact nature of the debates and deliberations that go on within the Politburo or Politburo Standing Committee. However, a speculative interpretation of recent policy-making would stress that the balance among represented groups has shifted. Instead of a performance/reform coalition calling the shots in economic policy, economic

policy has been set in recent years by those politicians with an interest in redistribution and shaping the development agenda. In other words, under Wen Jiabao, a “welfare coalition” has tended to have the largest voice in economic policy. The efforts of this welfare coalition are perfectly acceptable to the control coalition, which sees progress in the social agenda as reducing discontent and strengthening political control and stability. Neither of these groups wants to get rid of the “reformers” (the rump of the performance coalition), who are seen as having valuable economic skills that are needed to keep the economy on track. But neither wants to subject any of their objectives to a new round of reforms, which they fear might destabilize society and the economy. The end result is a lowest common denominator, consensus politics. In normal times, policy-makers move incrementally toward their goals (now predominantly welfare goals instead of “reform” goals). Decisive action is deferred for as long as possible, but when decisive action is compelled, the whole system has to swing behind it. This is the pattern we have seen playing out in macroeconomic policy during the course of 2011. Yet this process is not well suited to macroeconomic policy, and it has resulted in higher inflation and popular dissatisfaction. Faced with this lack of success, the top leaders have been more or less forced to “bring back” the PBC and rely on its more orthodox approach to monetary policy and inflation-fighting.

The Political Business Cycle

We are approaching the end of the Hu Jintao-Wen Jiabao administration. In a little over a year, a new administration will start to take over. Under these circumstances, it is normal that the incumbent (lame duck) leaders seek to appear successful, secure their legacies, and hand off power to sympathetic allies and especially to their protégés. Hu-Wen have important successes, in improving rural welfare and living standards, in protecting rapid economic growth in the face of the global crisis, and in presiding over China’s rise as a global power. However, some important parts of their agenda are also glaringly incomplete. The “rebalancing agenda” articulated in the 11th and 12th Five-Year Plans is utterly unfulfilled, and China’s growth is still being driven by investment. The housing market is still out of control, and Wen Jiabao’s efforts to provide significant low-rent public housing and stabilize housing prices have not yet achieved success. Health reform is in its infancy. Now, inflation threatens to overturn the apple cart. Can the Hu-Wen administration credibly claim to have succeeded in their social and economic agenda?

The answer to this question is inevitably subjective, but the answer given by politicians and the public in China will directly affect the fate of Li Keqiang. Li Keqiang is the chosen successor for Wen Jiabao, and the personal favorite of Hu Jintao. Li’s choice represents continuity with the economic and social policies of Wen Jiabao and Hu Jintao, and thus with the welfare coalition. By contrast, Xi Jinping, under the norms that currently govern the Chinese succession process, is relatively independent of Hu Jintao, and thus has “wiggle room” when it comes to defining his own policies at the beginning of his term. Indeed, Li Keqiang already plays an important role in implementing policy, and is essentially serving as apprentice—or perhaps probationary—premier.²⁶ While we cannot separate out the precise role that he plays in shaping policy, we can easily see

where the bulk of his efforts are devoted. Li Keqiang has a broad economic portfolio, but this depends in practice on how responsibility is shared with Wen Jiabao. Li's specific domestic portfolio comprises three main areas: health care reform, public housing, and food safety. In other words, he has been made the front man for the pro-consumer, pro-welfare strand of current Chinese policy-making.

None of Li Keqiang's domestic policy arenas are going well right now. To the extent that Li has broad economic responsibilities, he inevitably attracts some of the blame for the unpopular increase in inflation, and the failure to address it more effectively. As head of the State Council Leadership Small Group on Medical System Reform, Li is supervising the challenging transition from a few experiments to a functional national health insurance system.²⁷ While it is still early in the process, one hears grumbling in Beijing that the process is behind schedule and beset with difficulties. A year ago, Li was appointed the head of a food safety commission that includes three out of the four vice-premiers.²⁸ In spite of this attention, a spate of new food scandals emerged in early 2011, indicating how intractable the issue may turn out to be.²⁹ Finally, Li Keqiang has been selected to be the point person in the promotion of public housing.³⁰ It is unclear if Li bears any responsibility for the overambitious public housing targets advanced this year, but it is fairly certain that performance will come in well below widely publicized objectives. Thus, Li Keqiang has no clear policy successes, but can easily be blamed, fairly or unfairly, for subpar outcomes in a number of economic policy arenas, including inflation.

It is not surprising, then, that a recurrent Beijing rumor in the summer of 2011 was that Li Keqiang's ascension to the premiership was "not assured." It is undoubtedly true that Li Keqiang's position has been weakened and his political capital diminished by the mediocre recent performance of economic policy. Moreover, there is an obvious alternative candidate for premier, Wang Qishan. Wang possesses the dual credentials of a strong personal track record plus a distinct policy orientation. A Wang Qishan premiership would be expected to tone down the welfare orientation and perhaps reinvigorate the stalled market-reform agenda. However, Wang Qishan is not a powerful politician with an independent network of supporters. It is inconceivable that Wang could "challenge" Li Keqiang for the job of premier. Such a challenge would be self-defeating, and is quite foreign to Wang's normal behavior. Only some kind of collective decision by the top leaders to replace Li Keqiang could lead to a Wang Qishan premiership, and there is no evidence at this time that any such dramatic action is in the cards.

In the meantime, a rival politician has surfaced, in the person of Chongqing Party Secretary Bo Xilai. Bo Xilai's complex political background, as a "true" princeling and fiercely ambitious politician, will be familiar to many readers of the *China Leadership Monitor*. The one point to mention in the current context is that Bo (aided by the extremely capable Mayor Huang Qifan), has amassed an apparently successful record in Chongqing doing exactly the kind of thing that Li Keqiang is tasked with doing nationwide: providing housing and welfare services to the people. Bo's promoters—and there are many—claim that he is responsible for Chongqing spending 50 percent of its budget on the people's livelihood, and in particular for providing public housing. Indeed,

on the surface it would appear that Bo is having greater success with this agenda than are Wen Jiabao and Li Keqiang. In fact, this is an illusion, since Chongqing has been aided by vast subsidies and policy preferences from the central government, estimated by Huang Qifan to have a total value of 800 billion yuan in the years from 2009 through 2020. This implies that Chongqing gets central government subsidies equal to just over 10 percent of its annual GDP.³¹ A parade of top politicians have made the pilgrimage to Chongqing and paid obeisance to Bo Xilai. The most recent visitor was Li Yuanchao, head of the Organization Department.³² These are strange and somewhat ominous developments. An outside observer cannot help but note that while Bo may be able to plausibly pass himself off as a representative of the welfare/redistribution group, he also has made a strong appeal to the control coalition. Bo's attacks on criminal gangs in Chongqing have earned him popular support and approval nationwide. His invocations of Communist tradition, Maoist authority, and revolutionary nostalgia trigger emotional support from many within the Chinese leadership, but especially from the propaganda officials tied to the control coalition. Thus, Bo's positions appeal to the widest possible spectrum within the top leadership group. Bo, self-confident and extremely ambitious, is clearly trying to turn that appeal into a top leadership position, but whether he can overcome the mistrust of other top leaders remains to be seen.

The transition to a new leadership in 2012–13 will not only bring new people to power, it will also inaugurate a new distribution of power at the top that will be subtly—or not so subtly—different from the current distribution. Based on trends through mid-2011, it appears that power at the top will be, if anything, more diffuse and dependent upon a prolonged consensus-building process than is the case today. Li Keqiang certainly is unlikely to dominate the economic policy-making process as thoroughly as Wen Jiabao has over the past decade, and he will have to make major efforts over the next year to shore up his position. Given the absence of a strong core to the leadership, it is even conceivable that the Politburo Standing Committee could be expanded from its current nine members to accommodate a broader range of powerful politicians. Whatever the ultimate configuration of the Standing Committee, the broad range of influential interest groups represented at the top will give Xi Jinping, the new top leader, an opportunity to shape a new policy equilibrium, even as it places extreme demands on his political skills.

Notes

¹ Wen Jiabao, “国务院总理温家宝会见中外记者并回答提问” (State Council Premier Wen Jiabao meets Chinese and foreign press and responds to questions), March 14, 2010, accessed at http://www.npc.gov.cn/huiyi/dbdh/11_3/2010-03/14/content_1563493.htm.

² Xin Zhiming, “Wen calls inflation a ‘tiger’,” *China Daily*, March 15, 2011, accessed at http://www.chinadaily.com.cn/cndy/2011-03/15/content_12171303.htm.

³ This means that commercial banks have to deposit 21.5 cents with the central bank for every dollar of deposits they have. This locks up funds and prevents the banks from lending them out. For a nice concise description and graph, see Tom Orlick, “Reserving Judgment on PBOC’s Inflation Fight,” *Wall Street Journal*, April 18, 2011, accessed at <http://online.wsj.com/article/SB10001424052748703916004576270323485160858.html>; An Yang and Wang Jing, “PBOC Raises Reserve Requirement Ratio,” *Caixin English*, June 14, 2011, accessed at <http://english.caing.com/2011-06-14/100269277.html>.

- ⁴ A convenient synopsis of interest rate changes is available at <http://www.global-rates.com/interest-rates/central-banks/central-bank-china/psc-interest-rate.aspx>; Li Yuqian, "Analysts: More Monetary Tightening Ahead," *Caixin English*, July 7, 2011, accessed at <http://english.caing.com/2011-07-07/100277019.html>.
- ⁵ Rabinovitch, Simon, "Credit squeeze drives change at China's SMEs," *Financial Times* [English], July 14, 2011, accessed at <http://www.ft.com/cms/s/0/ddb5c048-ae00-11e0-a2ab-00144feabdc0.html-ixzz1VQraMOJn>.
- ⁶ Wen Shuping 温淑萍, "高铁建设 '大缩水' 今年少投2000亿," (Big contraction in high-speed rail; this year's investment down 200 billion) *经济观察报* (*Economic Observer*), April 30, 2011, accessed at http://www.eeo.com.cn/Politics/beijing_news/2011/04/30/200330.shtml.
- ⁷ Zhang Xiangdong 张向东, "发改委有请" (NDRC makes a polite request), *经济观察网* (*Economic Observer*), April 30, 2011, accessed at http://www.eeo.com.cn/Politics/beijing_news/2011/04/30/200332.shtml.
- ⁸ The other four chambers did not deal in ordinary consumer goods, so basically everybody signed. Xu Kexin 许可新, "数万企业同倡稳物价; 参与者称不是喊口号" (Tens of thousands of enterprises undertake to stabilize prices; participants say it's not just sloganeering), *第一财经日报* (*Business News*), April 14, 2011, p. A3.
- ⁹ Xu Kexin.
- ¹⁰ Zhang Xiangdong (NDRC makes a polite request).
- ¹¹ Lin Xiang, Li Zhen, and Lin Xiaozho 林向, 李晨, 林小昭, "中石化高档酒采购惹众怒; 一味提油价不降内部成本难服人," (Mass anger at the Sinopec purchase of expensive booze; hard to swallow the high price of oil without efforts to lower costs) *第一财经日报* (*Business News*), April 14, 2011, p. A1. Assuming the bottles were legitimate 1996 Chateau Lafite Rothschild, this is actually a reasonable price, in a premium market now driven largely by Chinese demand. Strangely enough, Chinese purchasers often pay astronomical prices for Lafite's second label, Carruades de Lafite, which they do not fully differentiate from Lafite Rothschild, though it is a much less impressive wine. If the bottles were this second-tier Lafite, the Sinopec purchaser was not only corrupt, but stupid, too. Andy Xie, "The Puzzle of Carruades de Lafite," July 7, 2010, accessed at <http://english.caing.com/2010-07-07/100158965.html>.
- ¹² 李星文 Li Xingwen, "中石化天价酒事件何时才能见真相?" (When will we get the true story about the astronomical prices paid for alcohol by Sinopec?) *北京青年报* (*Beijing Youth Daily*), April 17, 2011, p. A2. This journal also reports a meal by a Shanghai Luwan District Red Cross that cost 9,859 RMB for 17 people, about four times the 150 yuan per person standard. It's somewhat comforting to hear that this was actually newsworthy and generated outrage. The participants were said to have already reimbursed the over-standard amount. "上海红会: 高额餐费属实已处理" (Shanghai Red Cross: The over-expenditure on meals is true and has already been taken care of), *北京青年报* (*Beijing Youth Daily*), April 17, 2011, p. A1.
- ¹³ "2011年国务院出台楼市新国八条 (全文)" (The complete text of the State Council's 2011 New Eight Articles), January 27, 2011, accessed at <http://news.9ask.cn/Article/sd/201101/1069752.shtml>.
- ¹⁴ Office of the Beijing City People's Government 北京市人民政府办公厅, "北京版 '国八条' 楼市调控细则公布 (全文)" (Complete text of the detailed Beijing edition of the State Council's Eight Articles), February 16, 2011, accessed at http://house.ifeng.com/special/2011jbguobatiao/zuixin/detail_2011_02/16/4702277_0.shtml.
- ¹⁵ NDRC, "商品房销售明码标价规定" (Regulations on posting real estate sales prices), March 16, 2011, accessed at http://www.gov.cn/zwgk/2011-03/22/content_1829108.htm.
- ¹⁶ "部分城市2011年新建房价控制目标一览" (A summary table of control prices for newly constructing housing in some cities in 2011), accessed at <http://finance.eastmoney.com/news/7315,20110401127986655.html>.
- ¹⁷ Zhang Xiaoling and Wei Yi 张晓玲 魏懿, "从限购到限价: 新房均价必然下跌" (From limiting purchases to limiting prices: Will the average price of new homes necessarily fall?), *21世纪经济报道* (*21st Century Economic Herald*), April 21, 2011, accessed at <http://www.21cbh.com/HTML/2011-4-21/wNMDAwMDIzNDAwNA.html>.
- ¹⁸ Lan Yahong 兰亚红, "国务院督察组行程揭秘" (Uncovering the mystery of the State Council inspection teams' itineraries), *中国房地产报* [*China Real Estate News*], April 17, 2011, accessed at <http://finance.eastmoney.com/news/1355,20110417130693888.html>.
- ¹⁹ Zhang Xiaoling and Wei Yi 张晓玲 魏懿.

²⁰ Jia Haifeng 贾海峰, “发改委备战五一楼市 囤地房企或成反暴利目标” (The NDRC prepares for a May 1 housing battle; real estate companies that hoard land may become targets of anti-profiteering), *21st Century Economic Herald*, April 27, 2011, accessed at <http://www.21cbh.com/HTML/2011-4-28/5OMDAwMDIzNTM5OA.html>.

²¹ Huang Shuhui 黄树辉, “房企‘不差钱’楼市短期内恐难降价” (Real estate developers are not lacking money, so there’s not that much downward pressure on prices right now), *第一财经日报* (*Number One Finance Daily*), April 14, 2011, pp. A1, A4.

²² Shirk, Susan, “Can the Chinese Political System Sustain its Peaceful Rise?” University of California, San Diego. Unpublished working paper, 2011.

²³ Among the technocrats, People’s Bank of China (PBC) head Zhou Xiaochuan is its most articulate exponent in policy debates. In the earlier years of the Hu-Wen administration, the State Asset Supervision and Administration Commission (SASAC) under its first head, Li Rongrong, was also generally aligned with the performance coalition, but since Li’s retirement SASAC’s position has wavered.

²⁴ By contrast, in the 16th Politburo (2002–2007), Huang Ju (who died in office), Zeng Peiyan, and Wu Yi could be expected to champion efficiency objectives. In addition, although Zhu Rongji had retired, the bureaucracy was still staffed with experienced bureaucrats who reflected Zhu’s generally reformist orientation.

²⁵ For example, this can be easily traced back to earlier cycles of macroeconomic tightening. See Barry Naughton, “Another Cycle of Macroeconomic Crackdown,” *China Leadership Monitor*, no. 19, Fall 2006, <http://www.hoover.org/publications/china-leadership-monitor/article/6355>.

²⁶ Li must of course begin to play a role in foreign affairs, and he spends a fair amount of time meeting foreign dignities.

²⁷ The “office head” of this Leadership Group is Sun Zhigang, one of the NDRC vice-directors.

“李克强：建立健全基本药物制度 拓展公立医院改革试点” (Li Keqiang: Establish and perfect the basic pharmaceuticals system; expand the public hospital experimental reforms), *People’s Daily* 人民日报, February 17, 2011, accessed at <http://cpc.people.com.cn/GB/64093/64094/13937739.html>;

“李克强：统筹谋划 攻坚克难 把医改向纵深推进” (Li Keqiang: Draw up a comprehensive plan and overcome difficulties, push medical reform forward in depth), *Xinhua*, January 20, 2011, accessed at <http://cpc.people.com.cn/GB/64093/64094/13770869.html>.

²⁸ The heavy representation of vice-premiers shows how sensitive the food safety issue is in China today.

Ai Kesi (艾克思, pseud.), “胡锦涛苦心拉拔李克强” (Hu Jintao exerts himself to the utmost to promote Li Keqiang), *动向杂志* (*Dongxiang* magazine, Hong Kong), March 2010, accessed at http://www.aboluowang.com/news/data/2010/0317/article_96484.html.

²⁹ “食品安全事件频出 监管部门被指为利执法” (Many food safety cases have appeared; Regulatory bodies have been instructed to facilitate enforcement), *新京报* (*New Capital Daily*), April 19, 2011, accessed at <http://news.9ask.cn/Article/zbtj/04/1157982.shtml>; see also Laurie Burkitt, “Why China Struggles with Food Safety,” *China Real Time Report* (*Wall Street Journal*), April 25, 2011, accessed at <http://blogs.wsj.com/chinarealtime/2011/04/25/why-china-struggles-with-food-safety/>.

³⁰ Li Keqiang 李克强, “大规模实施保障性安居工程 逐步完善住房政策和供应体系,” (*Carry out the public housing project on a vast scale; gradually perfect housing policy and the housing supply system*), *Qiushi* magazine 求是, 2011: 8, April 16, accessed at http://www.qstheory.cn/zxdk/2011/201108/201104/t20110413_76857.htm.

³¹ Su Wei, Yang Fan, and Liu Shiwen, *重庆模式* (*The Chongqing Model*). Beijing: Zhongguo Jingji, 2011, page 15. This is a rough calculation derived by dividing the (rough) total figure for subsidies by 12 to derive an annual amount, and dividing by Chongqing’s 2010 GDP.

³² Xiao Zhu 肖竹 “中央政治局委员、中组部部长李源潮在渝考察侧记,” (A record of Politburo member and head of the Organization Department Li Yuanchao’s visit to Chongqing), *重庆日报* (*Chongqing Daily*), April 19, 2011, accessed at <http://cpc.people.com.cn/GB/64093/64094/14420834.html>.