To account for the recent spectacular regime transitions in state socialist countries, many have rediscovered and revitalized the concept of "civil society." The societal interpretation traces a direct causal chain from the resurgence of civil society into the rapid disintegration of state socialist systems in East Europe. The other side of the coin, however, has been largely ignored, that is, state capacity to govern. In Poland of the early 1980s, Z. A. Pelczynski found that political opposition owed its existence not so much to an infrastructure of genuinely autonomous social organizations as to "the strange weakness" of the communist state apparatus. This observation seems to hold true elsewhere in East Central Europe and the Soviet Union as well. Why have those once nearly monolithic Leninist states become so vulnerable to pressures from below?

In comparative discussion of regime transition in general, attention has also been focused on the insurgent side (including some ruling factions which cooperate with outside groups for one reason or another) rather than on the incumbent side. From this perspective, the key questions to ask in searching for common causes of regime demise are who compose insurgent political forces, why they want to replace the existing regime with something else, and how strong they are in relations to the besieged old regime, thus leaving another crucial question unanswered, that is, under what conditions the incumbents can hold on their power, preserve the status quo, or even impose their collective will on the society without much opposition, and under what conditions they cannot. It seems to me that a political system is unlikely to be destroyed unless its ruling power has been exhausted, no longer able to guide socioeconomic development, to resolve the political challenges of legitimation, and to maintain social order in old ways. In other words, only when a system begins functionally to break down does it become possible to bring it down. I will argue that our understanding of regime transitions will be greatly enhanced if the concept of "state capacity" is to be introduced into the study of the phenomenon.

Just as we may judge a person by her/his character as well as her/his ability, we should examine a political system not only by its "regime type" but also by its capacity to govern. A good person is not necessarily a
capable person. Similarly, a democratic regime may not be strong enough to govern effectively. In the recent decades, we have observed the demise of not only authoritarian regimes but also democratic regimes. If the regime type of a system doesn't determine its fate, perhaps we should investigate the issue the other way around, that is, whether the changes of a system's capacity to govern, regardless the manner in which the system intervene in its society and economy, is in any way related to its destiny. A quick review of the cases of regime transition in this century seems to suggest that if not every weak regime invariably falls, at least all those that did fall had become very weak before its death knell.

The distinction I emphasize here between state capacity and regime type is by no means a noble one. Any sensible political analysts would notice that "regime type" and "state capacity" are the two defining characteristics of a political system. The regime type defines the range and manner of the state intervention into its society and economy, while the state capacity measures the effectiveness of the intervention. Obviously, a political system which intervenes into its society and economy extensively and in a merciless manner is not necessarily able to carry out the tasks imposed upon it by its own political elite, by other important national actors, or by the pressures of the international environment. And, a highly capable political system needs not to be intrusive in every aspect of social life. In one word, political capacity is not related conceptually to forms of regimes.

The distinction between state capacity and regime type is not a new one either. Many theorists have made efforts to distinguish them from each other, particularly those who are devoted to investigate "state capacity." Scholarship on comparative political economy has recently turned toward systematic evaluation of the effectiveness with which states intervene in their economies and societies. Numerous studies have showed that the success or failure of a domestic or international policy depends largely on the institutional resources that the state has available to secure its implementation. Thus, when suggesting that states make a great difference in the lives of the people they seek to govern, they are less concerned with the differences in policy orientation or the degree of state intervention between countries than with the ability of state leaders to get people in those societies to do what they want them to do.

In searching for a way to predict the outcomes of international conflicts, some theorists of international relations have also noticed the importance of state capacity. They define state capacity as "the effectiveness of a government in doing its job," which is in essence not very different from the one introduced by those international political economists
mentioned above. But the two groups (IR and CPE) seem to have rarely communicated with each other, despite the fact that they are following a similar line of inquiry. The IR group is more explicit in singling out the distinction between "regime type" and "state capacity," because its quantitative researches all lead unequivocally to the conclusion that totalitarian, democratic, and authoritarian regimes do not determine the level of the political performance of governments.

In spite of the proliferation of scholarship concerned with "state capacity," no efforts have been made to link the concept with the issue of regime transition. If we recognize that the incumbent side is as important as the insurgent side in understanding regime transition, a combination of the two bodies of study should be fruitful. One of our objectives of this chapter is to bring these two fields of scholarship together. It will first modify the concept of "state capacity", tailoring it for the purpose of discussing regime transition in a general sense. Then it will apply the modified concept to the authoritarian state socialist system, trying to identify the key determinants of state capacity under that particular sociopolitical system. Thirdly, how changes in state capacity are related to regime transition will be investigated. Finally, the theory developed in the three sections will be tested by using it to discuss the political changes in the People's Republic of China in the last forty years.

I. State Capacity as Fiscal Extractive Capability:  
The Measurement of State Capacity

Though there is already a substantial amount of good scholarship on the issues concerning "state capacity" from various perspectives, it is a literature that badly needs integration and synthesis; and if the concept is to be used to understand regime transition, it needs to be carefully modified.

One of the most serious problems with the CPE strong state-weak state literature is that it fails to offer measures of state capacity that are operational. To determine a state capacity, it requires a thorough review of the overall government structure and state-society relations at a particular historical conjuncture, which can be very arbitrary. Where one reviewer see a strong state, another may find severe constraints on the capacity of the state. Some critics have recently called for a more differentiated conception of state capacity in order to capture the nuances and variations in the capacity of the state in different policy arenas. However, the differentiation would not be able to eliminate analysts' arbitrariness if there is no accepted criteria for measuring state capacity. The net result
of the proposed differentiation without the establishment of proper measurement thus would be a denial of the relevance of "state capacity" as an analytic tool.

Indeed, state capacity is more easily asserted than measured. Nevertheless, a direct measurement of state capacity is necessary if we are to understand the causes of the variance of state capacity across nations and/or over time, and the effects of the variance in a systematic way. In this regard, the IR literature on "political capacity of the state" seems to have filled the gap. This literature assumes that a highly effective political system should be able to extract resources from society, aggregate those resources into a national pool, and use them for national purposes; and that state which is not able to generate sufficient resources for realizing its policy goals cannot be effective. Based upon the two assumptions, the IR literature transforms the concept of state capacity from defining it as the effectiveness of a government into defining it as the government's ability to mobilize and direct the resources of the society toward the ends chosen by the political leadership. The revised definition has two merits. First, the state's extractive capability captures the infrastructural capacity of the state. It is the availability of resources that permits a government to carry out its tasks. Since the extractive capacity is so critical to the overall capacity of any state, it can serve as a proxy measure of the overall state capacity. Second, the extractive capacity is measurable. Unlike the original definition, the revised one is operational.

Furthermore, the IR literature on state capacity chooses revenue extraction as an "unambiguous and continuous derivative of political capacity." Indeed, the public finance is one of the best starting points for an investigation of state capacity. Kautilya, writing several centuries before Christ, already recognized that effective government had to be fiscally viable. In the sixteenth century, when the modern nation-state was rising, Jean Bodin asserted that "Financial means are the nerves of the state." As a matter of fact, the history of the evolution of the modern state is the history of state revenue production. Thus, Esmund Burke did not exaggerate the importance of the revenue for the state when he argued:

The revenue of the state is the state. In effect all depends upon it, whether for support or for reformation...Through the revenue alone the body politics can act in its true genius and character...

Just like a human being cannot be alive without blood, a state cannot function without revenue. The extraction of fiscal resources is a precondition for the implementation of all other government programs. Even
though a state's ability to intervene may vary in different areas of
socioeconomic life, as many have pointed out, we still have good reason to
believe that its fiscal capacity is the infrastructural one which can serve as
the best possible indicator of the state's overall capacity. For "fiscal
events are an important element in the causation of all changes," and
"everything that happens has its fiscal reflection."  

To measure political capacity in a comparative way, the IR literature
develop a ratio which is constructed between the actual resources extracted
and an expected resources estimated on the basis of a number of key
socioeconomic factors among a group of comparable nations:

$$\text{Relative political capacity (RPC)} = \frac{\text{Actual Extraction}}{\text{Expected extraction}}$$

Nations whose actual extraction is larger than expected display high
political capacity. Those whose actual extraction cannot reach the norm
reflect low political capacity. When actual and expected extraction are
similar, RPC reaches unity to reflect that the government's political capacity
is average in the comparison group.

Expected extraction is critical to this equation, because the IR
literature is primarily concerned with the comparison of political capacity
among nations. From a comparative point of view, the absolute revenue level
reflects not only political mobilization capacity but also socioeconomic
factors. Non-political factors such as the natural endowment, the level of
economic development, and the openness of the economy to outside world may
greatly affect the absolute revenue level of a government. Rich countries,
for instance, can tax larger amounts from their population than poor ones. To
control the effects of non-political factors, the developers of this model use
multiple regression to yield a value of expected extraction for a group of
comparable nations. The political capacity of a government relative to that
of others is obtained by calculating the ratio of its real extraction to the
expected extraction of the sample group.

For our purpose of studying regime transition, however, what is
important is not the measure of the strength of a state in comparison with
others but the measure of the political capacity of a state in comparison with
that of its own past. Is the political capacity of a given government
consistent over time? If not, what variables affect longitudinal variation in
the extractive capacity of the state, and what consequences are likely to be
present if the capacity scales up or down? More specifically, is regime transition in any way related to the decline of a government's political capacity? Those are main questions we want to investigate. To answer them, what we need to do is an analysis of dynamic, longitudinal development of state capacity. In such an analysis, we have good reason to assume that the denominator of the right side of the above equation—expected extraction—will either remain constant or increase very slowly. Even in the latter case, we may still choose to treat it as a constant because the increase of the denominator wouldn't inflate the RPC unless actual extraction grows faster. Thus, the actual extraction becomes the only independent variable in the equation, which is solely responsible for the changes of the RPC:

\[ \text{RPC} = f(\text{actual extraction}) \]

Finally, in order to take into consideration the changing size of national economy and to make longitudinal comparison possible, we need to redefine the meaning of "actual extraction." Rather than defining it simply as the absolute value of the actual revenue obtained, we define it as the aggregate of direct and indirect taxes plus profits from government enterprises as a percentage of GDP or national income:

\[ \text{Revenue collected} \]

\[ \text{Actual Extraction} = \frac{\text{Revenue collected}}{\text{Available Resource}} \]

The actual extraction thus defined can be a good indicator of state capacity. Even though not everyone believes that taxation is theft, few taxpayers volunteer to be taxed. There are always many who attempt to evade taxes by smuggling, by misrepresenting, or by hiding production, income, and profits. Sometimes, some taxpayers even organize themselves into groups opposing state extraction. Thus, levels of extraction scale the variation of a government's ability to legitimate its rule, or coerce people into accepting its rule.

II. A Theory of Local State: State Capacity as a Dependent Variable

The IR literature treats state capacity primarily as an indicator of national power. Power in international politics refers to the ability of one
nation to exercise control over the behavior or fate of another. Given the importance of predicking nations' ability to impose preferences on each other or withstand demands by their opponents, which in turn is essential for predicking the outcomes of possible international conflicts, it is understandable why the IR literature pay little attention to issues other than the measurement of state capacity.

As a dependent variable, what are the determinants of state capacity? The CPE literature complements well the weakness of the IR literature in this regard.

The central hypothesis of the CPE literature, which was originally advanced by Peter Katzenstein, is that a strong state should be able to set its policy objectives and command sufficient number and broad range of policy instruments to achieve stated objectives in the process of policy implementation. The definition of policy objectives is shaped, and the number and range of policy instruments are conditioned, by so-called policy networks, which is featured by a particular combination of centralization in state and society as well as differentiation between them. In plain language, a state's capacity is a function of the internal coherence of the state apparatus itself and the power of the state in relation to its own society.

Although everyone agrees that "the existence of an extensive, internally coherent bureaucratic machinery is the first prerequisite for effective state action," in discussing the conditions underlying effectiveness of governments emphasis has been laid on "state autonomy" or its absence. Many believe that state autonomy and state capacity for effective socioeconomic intervention go hand in hand. In this perspective, the state is seen as a monolithic entity which is constantly involved in a competition with the society composed of diverse and changing groups over the allocation of resources. This is a zero-sum game of two players. The more governmental resources---the share of the gross resources extracted by the government, the less societal resources---the pool of resources maintained by the population; and vice versa. Thus, societal resistance is considered the primary obstacle to the effectiveness of state actions. The reduced pressure of all societal groups outside the state necessarily increases ability of a bureaucratic state to realize internally generated goals; conversely, the existence and persistence of well-organized social groups with control over the disposition of politically relevant resources implies a less effective state. Without a degree of autonomy from dominant and subordinate classes and from politically active and potentially mobilized groups, the state can hardly formulate its preferences, much less imposing them on the society. Some even go so far as to define state capacity in the terms of the historical balance of power.
between the state and society alone. In their view, the weakest kind of state is one which is completely permeated by pressure groups, and a strong state can resist private demands but is unable to transform private preferences. The strongest state may act at its will, having power to change not only the behavior of private actors but also the economic structure itself. While there is no doubt that autonomy is necessary for effective state intervention, however, it is mistaken to think that autonomy is in itself sufficient for effective state action.

Rueschemeyer and Evans emphasize that an effective bureaucratic machinery is the key to the state's capacity to intervene. To be effective, the bureaucratic machinery must be characterized by internal features fostering not only insulation from its social environment, but also instrumental rationality and activism, differentiation, unambiguous location of decision making and channels of authority, and corporate cohesion of the organization. The more developed the bureaucracy, the stronger the state's capacity to intervene. The worst thing that can happen to a state is that the bureaucratic machinery is not efficient. The inefficiency can be caused by the lack of the expertise and knowledge required for effective state action on the part of individual bureaucrats, or the lack of coherence and coordination within and among different state organizations, or the both. Interestingly, despite their emphasis on the importance of state structure itself, Rueschemeyer and Evans view the problem of corporate cohesion and coordination in the context of the competition between the state and society. According to them, this problem occurs mainly because strong and divergent forces in civil society are bent on capturing parts of the state apparatus and using them for their purposes.

Neither the degree of state autonomy nor the rationality of the state bureaucratic apparatus can adequately explain changing state capacity in the state socialist setting, however. Having intentionally destroyed all competing centers of power within society, the communist states were no doubt much more autonomous from their societies than countries in the West and the Third World do. And, as the time came by, those states' apparatus have been gradually and steadily rationalized. Given those two features, we should expect that communist states had much greater capacity to intervene and bring about socioeconomic changes they desired than their counterparts in non-communist countries, and that such capacity had significantly expanded in the several decades before the crisis of the late 1980s. It is true that state intervention in communist countries was extensive, penetrating into almost every aspect of social and economic life. But it doesn't follow that their interventions were always effective. As a matter of fact, after the 1960s
inefficiency became the stigma of communist economies and social disillusionment was mounting. And in 1989, many of the communist states suddenly collapsed and the rest of them are struggling for survival. One is led to speculate that the authoritarian statism may not correspond to a univocal strengthening of the state.

If the weak point of the state socialist system doesn't lie in its relations with civil society, where does it lie? In an essay of 1975, Philippe C. Schmitter gave a clue. He asserted that "the sources of contradiction, necessary if not sufficient for the overthrow of authoritarian rule, lie within the regime itself, within the apparatus of the state, not outside it in its relations with civil society." We may advance Schmitter's finding one step further by suggesting that the state socialist system is vulnerable not because its bureaucratic machinery is not sufficiently rationalized nor because parts of the state apparatus are infiltrated by societal forces, but because its agents tend eventually to become its rivals. This is the paradox of authoritarian state socialism.

As Krasner once pointed out, communist systems came into being generally with extraordinarily powerful states, because previously dominant social forces were very likely to have been significantly weakened in the course of the revolutions." With great capacity to intervene, the communist states started to make fundamental changes in economic, social, cultural, and even familial relationships soon after their revolutions, while making efforts to eliminate all potentially competing centers of power within their societies. To carry out socialist transformation, and to enforce their authoritarian rules, those states had to construct elaborate set of state agencies throughout the nations. All of those agencies, whether central ministries or local governments, were supposed to be central decision makers' deputies, who should have no preferences of their own. As the center's agents, their missions were to implement whatever orders they received from the top. The irony here is that the greater the expansion of state intervention, and the greater the sprawl of its administrative apparatus, the more difficult the center have to impose a unified course or vision, for a centrifugal tendency tends to develop within such a system.

First, the longer the political structure exists, and the more established the intermediate agencies, the more likely those agencies become aware of their interests distinctive from others, including their overlord---the center. Second, the more the state wishes to penetrate social and economic life, the less can the center afford to deprive subunits of taking initiatives of their own and using the information about particular conditions available to them by insisting the highly centralized system initially
created. More or less, some degree of decentralization is inevitable. To decentralize its activities, however, the center had to allow subunits to have control over some resources.

The distinctive sense of identity and the independent source of resources tend to reinforce each other. The growing consciousness of self-interests is likely to enhance subunits' desire to grasp more resources into their own hands. With more resources under their control, the subunits are inclined to develop new independent preferences. The process of the mutual reinforcement results in a centrifugal tendency among the subunits.

The centrifugal tendency of state agencies exist under every political system, but only under an authoritarian rule it may become the main threat to the coherence and, indeed, the stability of the state. Like under other types of political systems, authoritarian rulers have to find centripetal forces to counteract the centrifugal tendency of their agencies if they are to keep the state organizations together, acting more or less cohesively. At the national level, state leaders may manage to balance two or more trouble agencies against one another. But it is more difficult to overcome the centrifugal forces of local governments (provincial and below). Playing two local governments against each other would do more harm than good to the stability of the whole system. Under an authoritarian system, local governments are no less authoritarian than their overlord so that the center cannot mobilize support from the population to check the centrifugal tendency of the local lords. Furthermore, under the state socialist system, governments at every level are entitled to oversee every aspect of social and economic life in their respective jurisdictions. Thus, it is natural for them to have much stronger desire than their counterparts in market economies to keep as much resource they mobilize in the name of the central government as possible. And, situated at strategic position between the center and the population, they generally are able to play at hide-and-seek over the allocation of resources with the center: When the center imposes centralization, they can withhold their efforts in mobilizing resources; when the center chooses decentralization for maximum efficiency, they would take the opportunity to expand their own pools first.

The literature of state socialist system has depicted local governments as either "central agents" or "local defenders."21 The above analysis contradicts these views. For the local population, the local government is a part of the state representing public authorities, not distinguishable from the central government. But for the central government, the local government could be infected with dangerous "localism" threatening the whole state structure. It is obviously wrong either to reduce the local government simply
to an outpost of the central government, or to treat it as the mouthpiece of local societal interests. The local government is both a nominal agent of the central government and an independent and competitive actor in its own right. The analytic problem is that one label, the state, embraces two meanings. On the one hand, the state can be understood as an abstraction, which transcends any and all of its component factors. As an abstraction, the state is useful as a concept for getting hold of a complex reality and for explaining it. When we discuss state-society relations, we usually use the concept of the state in this sense. On the other hand, the state can be treated as a concrete complex of disparate components. The recognition of disparate elements gives us insight into incoherence, contradictions, dilemmas, and tensions within the state. We use the concept of the state in this sense when we discuss such issues as bureaucratic politics and central-local relations. What causes confusion is that we cannot use the concept of the state solely in one sense or the other. The both are needed for our discussion. The only thing we can do is to point out that no state is a monolithic entity. Instead of "the state", we may speak of a "state system" composed of a "central state" and a certain number of "local states." The concept of local state is valuable in that it enables us to distinguish local states from the central state, from each other, and from society.

Several points are central to this concept. First, the state, even in unitary system, is not a single unified institution; rather it is composed of various hierarchical elements that constitute a state system. Second, a local state has, or comes to acquire, its independent preferences, which may converge with, or diverge from, those of the central state, other local states, and/or the local society. Third, central- and local-state bureaucracies are consistently in conflict, with each striving for control over more resources to pursue and sustain its own policy objectives. Fourth, there is a possibility of the fragmentation of political authority. Local states may acquire a high level of independence. They can, under extreme circumstances, become a state within a state---highly immune from central control. High level of local power and autonomy could pose a serious threat to the central state, and, for that matter, the state system as a whole, by balkanizing the nation.
Figure Four Situations in which the Local Government Translates Its Preferences into Authoritative Actions

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<th>Local and central preferences converge</th>
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<td>Local state and local societal preferences</td>
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But why does the local state acts sometimes as a "central agent" and sometimes as a "local defender?" This is because the local state's preferences are not always diverge from the central state's and the local society's. The figure 1 depicts four possible situations in which the local state may translate its preferences into authoritative actions.

Obviously, the local state should have no problem at all in translating its preferences into authoritative action in the situation I. Under authoritarian rule, it should also have little difficulties to do so in the situation II because the local state acts as if it is a "central agent." If the local state can manage to translate its preferences into actions in the situation III, it would be seen as a "local defender." Only when it is able to act at its own preferences in the situation IV does its autonomy become apparent. There are two decisive variables in determining whether the local state is able to pursue its preferences: the degree of the congruity between local and central states and the level of resources concentration in the hands of the local state. In an authoritarian polity, the congruity between local state and societal preferences is not quite relevant. Only when local and central preferences are divergent, it is harder for the local state to act at its own preferences than otherwise. As pointed out above, the local state's sense of distinct identity tends to be strengthened as the time goes by. Thus, we should expect that local and central preferences clash more often as the system mellows. But it doesn't follow that the local state would have less and less chance to pursue its preferences, because, while the local state clashes more frequently with the central state in the terms of their policy preferences, its pool of resources tends to expand. When the local state is able to identify and pyramid resources from the central state, it is likely to be more able to resist the policy objectives of the center and to pursue its
independent goals. The four situations present a continuum along which the autonomy of the local state ranges from weak to strong. When local states become more autonomous from the center, those supposed central agents become more and more like independent centers of power competing with the central rulers and with one another over the control of human and material resources, which would inevitably enervate the system as a whole. Without independent power centers in society, we may hypothesize that state capacity in the authoritarian state socialist system depends to a great extent on the weight of the central state vis-a-vis the local states. The local states could constrain the central state's freedom and forms of action and thereby confound the capacity of the whole system. The more autonomous local states are from the center, the weaker state capacity is.

Here, we need to refine our definition of state capacity once again. Local states are parts of the state. But, the strengthening of local states' capacity to intervene in economy and society could weaken rather than fortify the capacity of the state system as a whole if local policy preferences are at odds with national ones. Thus we find that it is too vague to define "state capacity" simply as a state's ability to formulate and implement its policies because the state is not a monolithic entity and local states don't always act as the agents of the central state. "The state" in the concept of "state capacity" should be understood as the state system as a whole. Thus, "state capacity" doesn't refer to the capacity of any particular state agency or to the sum total of the capacities of the all components of the state system. It is deserved for the capacity of the state system functioning as a whole. A state system could be very weak even though its agencies (local states) are authoritarian and intrusive, able to penetrating and dominating the society.

The central state is the center of gravity of the state system. Its preferences set the reference point by which the deviation of local preferences it to be measured. The capacity of a state system cannot be strong unless the local states within the system have no power of immunity from the central state.

In sum, a strong state is characterized by a high degree of "local stateness" as well as a high degree of "central stateness." Local stateness involves horizontal concentration of resources in the hands of the public authorities of each and every locality. This is a process of state penetration. Central stateness refers to the vertical concentration of all authorities in the hands of the central state. This centralization can be realized only when local states across the nation act as (not necessarily "think" as) "transmission belt" and "agents" of the central state, and deviations from central policies are minimized by extensive coordination by
the central state. The second process is one of political integration. The decline of state capacity may take either form of less extensive state penetration (low degree of local stateness) or less effective political integration (low degree of central stateness), or both. Figure 2 depicts various possibilities in a simplified way.

**Figure** Two dimensions of state

<table>
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| Hig                  | Low               
| The degree of central stateness | I | I\ | V |  
| Hig                  | I | I\ |   |   |   |
| Low                  | I | I\ |   |   |   |

The central hypothesis of this study is that under the authoritarian state socialist system, the local state tends to develop centrifugal tendency, which could be very bit as undermining of central stateness and thereby corrosive of the capacity of the whole state system to realize its goals. It is not merely "state-society" relations that we will have to look in order to see how and why a state system is strong or not-so-strong. In studying political changes in the state socialist system, it it to the amalgamation of the state that we must give more attention.

It needs to be noted that, composed by hundreds of agencies and tens of thousands of bureaucrats, the central state as such is also internally fragmented, and that conflicts between different central agencies, like ones between the central state and local states, could limit the ability of the central state to pursue cohesive policies. But for the sake of convenience, in this study, we treat the central state as a homogeneous entity represented by what Levi calls "the ruler," what Zysman calls "the national political executive," what Rueschemeyer and Evans call "State elite" or "State managers," what Krasner calls "central decision makers," or what Chinese call "the center" (zhongyang).

III. State Capacity and (Un)governability:
State Capacity as an Independent Variable

In the CPE literature, "state capacity" is used as independent variable in explaining why a common challenge, such as the oil crisis, elicit different national responses in the international political economy. In the IR literature, "state capacity" is used as an independent variable to predict which of the combatants will win and which will lose in an international conflict. Can "state-capacity-as-fiscal-extractive-capacity be used to explain a regime's governability, or more specifically, to predict the probability of regime transition? Some scattered studies seem to suggest "yes." Schumpeter argues:

"The full fruitfulness of this approach [fiscal politics] is seen particularly at those turning points, or better epochs, during which existing forms begin to die off and to change into something new, and which always involve a crisis of the old fiscal methods. This is true both of the causal importance of fiscal policy (in so far as fiscal events are an important element in the causation of all changes) and of the symptomatic significance (in so far as everything that happens has its fiscal reflection)."

O'Connor claims that the state's inability to make both ends meet is likely to aggravate the underlying social crises. In a comparative study of the governability of contemporary Western European and North American politics, Schmitter concludes that main macroaspects of the political-economic performance of the modern states are all connected with the magnitude and mode of financing its fiscal crisis. More specifically, he finds that fiscal ineffectiveness is very positively and strongly associated with the instability of regime, which is the predecessor of ungovernability. Bates notes the correction between monarchs' fiscal crisis and the rise of parliaments. According to his reading of the literature on the origins of parliaments, it was the monarchs' attempts to raise greater levels of taxes that led to the creation of forms of political representation in England, France, and throughout historical Europe. In Of Rule and Revenue, Levi argues that resources are the basis for power. But there are always constraints on a ruler's capacity to produce revenue. In order to overcome these constraints, rulers are willing or forced to alter forms of government to suit their purpose if they can. Levi confirms Bates' findings about the importance of fiscal pressures in creating the basis for parliament but pinpoint the divergence between France and England which distinguish them for centuries into the future. Due to the relative weaker bargaining position of English monarchs vis-a-vis their constituents, from the Magna Carta on, the
English Crown was forced to trade privileges for revenue, which resulted in a relatively powerful parliament. There was no such development in France, however. What is crucial to the explanation is the greater relative bargaining power of France monarchs vis-a-vis their resource-rich constituents. The comparative lack of bargaining power closed off certain options in England that were available in France and compelled English monarchs to make concessions not expected of France monarchs.

Why is the decline of state capacity often accompanied by the weakening of governability, and sometimes followed by regime transition? The enfeeblement of the state-capacity-as-fiscal-extractive-capacity is both the symptom and accelerator of the underlying crises existing in society. It is the symptom of crises because, as pointed out in the above section, unless there are tensions between the state and society or within the state apparatus, the state should be able to mobilize sufficient amount of resources to support its programs. It is the accelerator of crises because, without sufficient supply of revenue, the rulers would find it difficult to sustain the institutions of the state, to bring more people within the domain of those institutions, and to increase the number and variety of the collective goods provided through the state. When the state cannot fulfill its basic functions, delegitimation follows. What else can we expect except political crises? Short of funds, the state may even not able to survive the crisis.

To the extent that there has always been more of a demand for imperative coordination and authoritative allocation than the state is capable of supplying, it has never been an easy task for the state to make both ends meet. But the state may be more able to fill the "gap" between demand and supply by physical repression and symbolic manipulation at one time than at other times. The variation in a state's existing capacity over time may be one of the most important structural features to recognize in understanding the governability-ungovernability syndrome. When a state is strong, it should have no difficulty to absorb temporary or sporadic socioeconomic disorder and foreign challenge. When the state's capacity is weakened, it would begin to have trouble adjusting to internally and externally generated disturbances. Because the state lacks political capacity to extract sufficient resources for allocation and redistribution, the domestic social structure would become at best immobile, which in turn would further weaken the state's mobilization capacity, unless remedies can be found to reverse the trend. Then, unable to deliver what it has intended or promised to deliver, the effectiveness of the state is called into question. If the state's extractive capacity continues to decline, political leaders may find that the volume of demand placed on the state by elites and various social groups exceeds its ability to meet it to
the point that the legitimacy of the regime is shaken. By this time, not just opponents but some of those within the regime would come to the conclusion that the experience of the regime is resounding failure ever according to the standards the regime itself has established. Opponents are stimulated to act because the failure is so obvious, and their rank is expanding. Meanwhile, ruling elites become less and less confident of their own capacity so that internal conflicts break out over who should be responsible for the regime's failure. Unable to retain their position of dominance or to reproduce preexisting coalitional arrangements, rulers are now troubled by the instability of their regime.

However, the situation can be turned from bad to worse, if the deterioration of state capacity doesn't stop. In the extreme, the state may become so weak that it is not able to sustain its basic social control mechanism. The regime then is literally exhausted, powerless to maintain civil order and to stop the dissolution of existing institutions. By this time, regime transition is in order. We may conclude from the above discussion that there is no transition whose beginning is not the consequence---direct or indirect---of the declining extractive capacity of the state.

Even the subsequent trajectory of regime transition is likely associated with state capacity. If a regime starts transition before its capacity is exhausted, regime reformists may be still able to help steer the transition and define the boundaries of the new system. By contrast, if a regime doesn't start transition until its capacity has been exhausted, the stage is prepared for social revolutionary mobilization, provided that revolutionary actors are available.

**IV. State Capacity, Local State, and Ungovernability in China**

In this final section, we use China as a case to test two hypotheses developed in the sections II and III:

1. Under the authoritarian state socialist system, state capacity is circumscribed mainly by the balkanization of state apparatus, especially the centrifugal tendency of local states.

2. The decline of state capacity contributes to the general crisis of the state socialist system.

**Revolution**

With the inauguration of the People's Republic of China on October 1, 1949, China was unified and at peace for the first time in decades. The Chinese communist state in the early 1950s was extraordinarily powerful not
only because the war and revolution had pulverized the old social formation to the degree that no social group was in position to challenge the new regime but also because recently established state agencies were too young to sprout strong independent policy preferences of their own. In March 1950, the central authorities imposed an unified management over the national financial and economic affairs with little resistance from local governments, despite the fact that during the 12 years from the outbreak of the Sino-Japanese War in 1937 to 1949, the financial and economic affairs in the various communist-controlled areas were managed separately, with each having its own currency and taking care of its own revenue and expenditure. The emphasis was on unifying revenue. The state budget was transformed into a consolidated budget that included the budgets of central, provincial, and subprovincial governments. Except few local taxes approved by the central government, all the tax income should be turned over to the central treasury. As to the expenditure, even small items needed formal approval from Beijing. At a time when the country still faced tremendous economic difficulties and enormous fiscal deficits and there were only a limited amount of funds available for extraordinary uses, planned allocation by the central authorities made it possible for the state to use limited funds according to what it perceived as the nation's priorities.

As the unified and centralized system developed during the First Five Year Plan (FFYP) period (1953-1957), the state's extractive capacity continued to grow. State budget revenue rose rapidly during this period, both absolutely and in proportion to GDP, constituting 22 percent of GDP in 1952 and 29 percent in 1957. Of the rising proportion of GDP captured by the budget, the central government concentrated a large share in its own hands. Throughout the FFYP period, the central government's share accounted for 80 percent of the total revenue while the various localities (at the provincial and county levels) could have access only to the remaining 20 percent. Of the total expenditure, the central authorities accounted for 75 percent while the various localities accounted for the remaining 25 percent. The large share represented a distinct increase in the potential role of the state in support of socioeconomic development compared to the prerevolutionary period, when a lack of revenues had severely constrained state-sponsored modernization programs. According to Lardy, "at the end of the 19th century, the revenues of the central government were only 1 to 2 percent of China's GDP. Under the somewhat more vigorous fiscal program of the Nationalist government after 1928, central government revenues were only about 3 percent of GDP. Even when provincial and local revenues are included, the total government revenue share of GDP was less than 5 percent."
comparison with other less developed countries, the role of the budget in resource allocation in China after 1949 was also significantly greater.\textsuperscript{37} The greater extractive capacity of the state enabled central planners to accelerate the rate of capital formation and allocate investment resources to priority sectors and regions. A tangible result was the overfulfillment of the FFYP in 1957.

Devolution

However, the high degree of centralization of financial resources was not without its problems. After several years of existence, local states began to be aware of their distinct interests. No longer resigning themselves to being merely central agents, they became more interested in establishing independent fiscal base than in serving the center. On the one hand, because there was no functional link between revenues collected and expenditures at any level below the consolidated state budget, local states' initiative in mobilizing revenues was dampened. On the other hand, because of the center's annual redetermination of revenues and expenditures for each and every locality, there was no way for local states to play any role in comprehensive long-run local economic planning.\textsuperscript{38}

Mao didn't like the concentration of political and economic authority at the center either, but for a different reason, namely, his fear of the spread of bureaucratism. For him, the way to retrench bureaucratism was to decentralize economic power. Thus decentralization became an important component of Mao's 1958 program of "Great Leap Forward."\textsuperscript{39}

The 1958 decentralization had three key aspects:

1. The great majority (over 80%) of the central enterprises were transferred to the management of the local authorities. Many of those enterprises, such as airlines, railroads, highways, post service, and the like, by their natures, cannot be effectively managed by local public authorities at any circumstance.

2. Central planning was replaced by local planning. Local governments were given permission to approve medium-sized and even large capital construction projects, to issue construction bonds, and to recruit and deploy labor force as they saw fit.

3. Local governments were delegated greater fiscal power. The provinces received a large fixed portion of a substantially broader revenue-sharing base and their expenditures were to be determined by revenues collected, rather than the other way around.

However, the decentralization of fiscal power didn't result in reduction of the degree of state penetration, which was reflected in the rising ratio of
budget revenue to national income. During the FFYP period, the state budget revenue on average constituted 32.7 percent of the national income. But the percentage rose to 39.6% in 1958, 47.3% in 1959, and 53% in 1960. However, the degree of political integration declined tremendously. Of the rising proportion of national income captured by the budget, the central government's share fell from 80% during the FFYP period to 50% in the GLF period, while the local share jumped from 20% to 50%. The two developments suggest that once local states get greater control over revenue, they tend to extort resources from society more rigorously, but revenue increase doesn't necessarily benefit the central planners.

In addition to taking advantages of the favorable new revenue-sharing system, local states endeavored to increase their extrabudgetary incomes by various legal, semilegal, or illegal means. Extrabudgetary sources of revenue are those funds in public sector which are not subject to central budgetary control. In an ideal centrally planned economy, there should never be anything not subject to central control. Nevertheless, extrabudgetary funds have existed in China since the establishment of the People's Republic. During the FFYP period, funds mobilized annually outside the budgetary control mechanism were pretty small, never exceeding 8.5 percent of total budget revenues. The three years of 1958-1960 saw the first upsurge of extrabudgetary funds. In 1957, there was only 2.6 billion yuan of extrabudgetary funds in the nation altogether. The number was doubled to 5.6 billion in 1958, jumped again to about 10 billion in 1959, and peaked at 11.8 billion in 1960. In a short period of three years, the extrabudgetary funds registered a more than 400% increase. During the FFYP period, the extrabudgetary funds had been on average only as much as 6.5% of the budget revenue, but in 1960 the percentage reached 20.6%.

With more money in their pickets, local states became enthusiastic to display their initiative. One of the results was that a massive campaign to build new industrial projects swept the country. Even in economically backward Gansu provinces, 224,500 factories were built in the six months between January and June of 1958. In 1958, a total of 26.7 billion yuan was invested in capital construction, up 97% from 1957 or equivalent to half of the total amount of 55 billion yuan invested during the entire FFYP period. The over-extended capital construction caused an all-round imbalance between sectors, which pushed the central government to spend more money to fill gaps. The result was large deficits, 14.8 billion in all in the years between 1958 and 1961. With neither market nor central plan to coordinate the economy, the Great Leap Forward ended up with a colossal failure.
The failure of the GLF demonstrate that general state revenue as such doesn't reflect the capacity of the state as a corporate actor. What general state revenue reflects is aggregate extractive capacity of governments at all levels. When local states command a large share of financial resources, they tend to use those funds to pursue their own preferences. Thus, growing general state revenue may weaken rather than strengthen the ability of the state as a corporate actor to achieve the policy goals set by the central planners, whatever the goals are.

Fortunately, the center's flexibility in redeploying resources generated by governments at all level survived the temporary ailment between 1958 and 1960. While the center's ability to manage the national economy was enfeebled by Mao's 1958 decentralization, its ultimate political authority over governments at lower levels remained intact. The center might have become less able to exert positive sanctions (to reward desired actions), but it still kept the power to exert negative sanctions on local governments' behaviors (to prevent undesired activity). The retained political authority enabled the center to transform the techniques of state intervention from decentralization back to centralization, at least partially.

In 1961, the central authorities decided to recentralize the system of economic management. All the rights to manage production, capital investment, materials, labor force, purchase, and financial affairs, that had been delegated to local governments, were taken back into the hands of the center. What was crucial to all recentralization measures was the recentralization of fiscal power. It was declared that subnational governments had no right to issue currency (including construction bonds). At the same time, the central government tightened up control over the management of both the budgetary and extrabudgetary funds.

In the five years of readjustment between 1961 and 1965, while budget revenue as a proportion of national income fell back to the level of 1957 (around 34%), the central government's share of the total increased from 50% to 60%. At the same time, the central authorities took rigorous measures to cut extrabudgetary funds. Extrabudgetary funds declined both absolutely and in proportion to budgetary funds, being as much as 20.6% of the budget revenue in 1960, 20.3% in 1962, and 16% in 1965. The recentralization of fiscal power enabled the center to reduce the scale of capital construction, improve the internal structure of the national economy, and achieve a favorable balance between revenue and expenditure in addition to repaying all of China's foreign debts in this period. By 1965, the entire economy had taken a turn for the better. If resources had remained scattered and at local governments' disposal, it was impossible for the center to fulfill the task of readjustment.
and thus for the nation to tide over the difficult period in a matter of few years.

For Mao, however, the recentralization was merely an expedient measure for tiding over the difficult period. Once the economy recovered from the crisis of 1959-1961, he again decided to smash the Soviet-styled centrally planned system. In March 1966, Mao declared that his ideal was what he called a "republic with a nominal monarch" [xujun gonghe], in which central planners should play only a limited role of providing ideological guidelines. Criticizing that the recentralization of 1961-1965 had been overdone, he ordered that all enterprises which the central government had taken back from local governments should be returned to local governments.

The Cultural Revolution paralyzed not only the central government but also governments at all levels. China was in anarchy from late 1966 to late 1968. While Mao enjoyed absolute personal power, the state lacked the basic ability to erect social control, much less to direct socioeconomic development. The 1967 plan never reached to the provinces, and there was no plan at all in 1968. Budget revenue fell from 55.9 billion yuan in 1966 to 41.9 billion in 1967 and 36.1 billion in 1968.

When public authorities were restored in the early 1970s, Mao initiated yet another decentralization drive. This time, he ordered that all enterprises "suitable" for local management were to be transferred to local governments. Even such giant enterprises as Anshan Steel, Daqing Oilfield, Changchun Auto Works, Kailuan Colliery, Jilin Chemical Industries Company were considered "suitable" for local management so that they were transferred to respective provincial governments in 1970.

Along with transferring central enterprises to local governments, most revenue sources and expenditure categories were shifted to the provincial level in 1971. The provincial governments were allowed to keep and use all or most of remaining revenues after transferring a lump-sum to the center according to agreements set between them and the central government. The aim of the 1970-1971 decentralization was to arouse the initiative of local governments. However, the center soon found that local initiative thus aroused was directed to further particular interests of various localities without regard for macroeconomic rationality. Many problems surfaced in the wake of the decentralization of industrial management and fiscal system. With more resources at their disposal and the rights to use them, local governments ran wild in capital investment. The planned targets for investment were exceeded again and again. Without effective mechanism to coordinate economic activities, the decentralized system brought about blindfolded construction and overlapping construction. The unchecked expansion of the scale of capital
construction was followed by a sharp increase in number of people on the state payroll. It had been planned to employ 3.06 million more people in state enterprises in the two years 1970 and 1971, but the actual increase was 9.83 million, three times as much as the planned figure. Because the big jump in the number of state employees, the year 1971 saw a considerable increase in the total amount of wage payment and scale of food grain consumption, which caused an acute shortage of supply on the market.

Due to the fact that to a large extent, local governments were responsible for the over-extended capital construction, moderate central leaders made efforts in 1973 to restore central control over industrial management and budgetary funds. But this attempt was obstructed by the radical Gang of Four. Mao on the whole sided with the Gang of Four, though sometimes on some specific issues he played a role in checking the Gang of Four's excesses. Because of Mao's insistence on letting each region, locality, or enterprise rely in so far as possible on its own resources, throughout the first half of the 1970s, local governments had greater access to revenues they extracted locally and more discretionary control over their expenditures than they had had in the 1960s. This was true despite the fact that local governments still had to revert most of revenues generated locally to higher levels under the consolidated budget. One of new sources of income for local governments was the so-called "five small local industries." In 1970, the central treasure earmarked 8 billion yuan in the following five years as a special fund to be handled by the provincial, municipal, and autonomous regional authorities for the development of these key industries. As for the newly built "five small industries" run by county governments, the county governments were allowed to keep 60% of the profits made by those enterprises. Even if those within the category of the "five small industries" suffered losses, county governments would not lose, because those enterprises would be exempted for a certain period of time from tax levies, or better, getting financial subsidies.

Extrabudgetary funds, which were beyond the central control, expanded in the early 1970s. From 1970 to 1976, while the budget revenue increased only 17.1%, extrabudgetary funds increased 172.8%. In 1970, the amount of extrabudgetary funds amounted to only 15.2% of the budget revenue, but in 1976, the ratio increased to 35.5%.

As central financial control over regional economic activity weakened, many localities found that they did not have to take central plans seriously; some of them even went so far as to acting contrary to central plans and arbitrarily discontinuing coordination with other localities arranged by central planners.
The late Mao era was characterized by its totalitarianism. Almost every aspect of social life was carefully monitored by state agencies at various levels. However, the very organizational structure which gave the state its power over society also weakened it, so the repressive Chinese communist state was unable to control priority economic activities and to secure inputs for them. By the time of Mao's death in 1976, China's national economy had been very much fragmented along regional lines. The fragmentation of the economy reflected the parcelization of the state apparatus. According to Lyons, the Chinese system in the late Mao era can be characterized as one in which "substantial devolution of authority---intentional or otherwise---was not accompanied by appropriate incentive and information structures, leaving decisions taken by the various planning offices largely uncoordinated."

Mao's decentralization not only aroused local governments' consciousness of their particular interests but also expanded their pool of resources. The self-consciousness and independent source of resources, as expected, reinforced each other, resulting in disintegrative potential within China's political structure. This legacy of the late Mao era created an inertia that Mao's successors would find difficult to overcome.

Nevertheless, the centrifugal tendency in the Maoist era were relatively weak for several reasons. First, that Mao was still alive itself set a limit to the development of localism. No one was in position to challenge Mao's authority as a symbol of unity. Second, while Mao was advocating the decentralization of economic management, he insisted on centralized and unified political leadership. In the early 1970s, most of provincial leaders were just recently rehabilitated after having been in disgrace for several years during the early stage of the Cultural Revolution. They still had lingering fears. In the treacherous political situation of the early 1970s, they had to act as if walking on thin ice to avoid any political accusation, which might destroy their careers. "Localism" was the last thing with which they wanted to be associated. The centrifugal tendency thus was less apparent at the provincial level. At lower levels, local leaders didn't have to deal with the ferocious Gang of Four and their direct superiors at the provincial level were generally irresolute and namby-pamby. Thus they were usually more bold in taking advantages of the central leadership's call for self-reliance and independent system by interpreting it as license to build autarkic "kingdoms" and to protect them with trade barriers.

Third, to reduce the interprovincial differences in level of development, the central government still retained control over a large share of the budget revenue even after the fiscal decentralization. In the 1970s, the provinces collected over 80 percent of total budgetary revenue, but they
were entitled to carry out about 45 percent of expenditure, higher than in the period of readjustment of the early 1960s but lower than in the Great Leap Forward period. Moreover, the revenue-sharing rates with the provinces were subject to annual adjustment, so the center retained a certain leeway to extract more from the provinces if it found it necessary. In fact, the decentralized fiscal responsibility system was modified at the end of 1971, less than one year after it had been put into practice. Localities could no longer keep all the revenue surplus they collected above the targeted amount. In 1973, the percentage of above-target revenue being kept by the localities was once again lowered. Then, the year 1976 witnessed a retreat away from fiscal decentralization to basically the same system that had existed in the early 1960s.

Involution

Since Mao's death in 1976, the Chinese economic system has undergone significant changes. The essence of the economic reform may be summarized by one phrase "fangquan rangli", that is, to devolve control over resources and decision-making power to local governments on the one hand and enterprises on the other. Deng Xiaoping chose the fiscal system as the breach of his overall reform program. Many have interpreted Deng's fiscal decentralization as a voluntary concession, which aimed at narrowing the scope of state intervention and strengthening the role of the market. This is probably right. Indeed, while Mao advocates decentralization as an alternative to both central planning and market, Deng views decentralization as a way through which China would be able to move away from a command economy and to head toward the direction of market economy. But Deng's intention to replace the planned economy with a market economy was only part of the reason why he initiated the fiscal decentralization in 1980 and further expanded local autonomy and enterprises autonomy in later years. As a matter of fact, in 1980 the reformist central leadership hardly had any option other than fiscal decentralization.

In December 1978, the Chinese Communist Party convened the Third Plenary Session of the 11th Party Central Committee. The plenum set out to solve many problems affecting the daily life of the people in city and countryside that had piled up for quite some time. It was decided, among other things, to raise the prices by a wide margin for the purchase of farm products and sideline products, to reduce or remit agricultural taxes for some poor regions, to import a large amount of grain from abroad, to arrange jobs for millions of educated youth who had been sent down to the countryside, to raise the levels of salary for state employees, to restore the bonus system, to
build more houses for urban residents, and the like. All of those measures were imperative for winning popular support for the reform drive, but they entailed great burden on the budget. In 1979, China run a deficit of 20.6 billion yuan, almost triple as large as the previous peak of 7.1 billion in 1960. The next year saw yet another big deficit of 14.2 billion. Together, the amount of deficits in the two years was as high as 34.8 billion, exceeding the total of deficits in the previous 29 years between 1950 and 1978 (24.8 billion). It is not hard to image how anxious the central planners were when facing such big numbers.

How to make up the deficit? One way was to print bank notes. The total volume of new paper money issued in the two years was 13 billion yuan more than normal increase. This, however, entailed the danger of inflation. Ultimately, the government needed either to increase its revenue or to cut its expenditure, or both. Unlike under the capitalist system in which individuals and private firms are tax payers, in China, state enterprises are the main contributors to the budget revenue. Some of enterprises were run directly by the central government, but more were under the control of local governments at various levels. Although it is not recognized as factually existing in China, local governments in effect possess proprietary rights over their "own" enterprises. This is not something which is observed in the Soviet Union or in the former state socialist countries of European CMEA. Thus, most taxes are collected, not from society, but from elements of the state itself (local states). Because of the quasi-ownership, local governments tended to resist the center's encroachment of local source of revenues as much as they could. To increase revenue or cut expenditure, the central government hence had to negotiate with the provincial governments. Because the fiscal system had become very dispersed since Mao's decentralization of the early 1970s, the central government couldn't expect to increase revenue by recentralization without facing strong local resistance. At the moment when the reformist central leadership desperately needed the support of the provincial leaders for their reform drive, it would be no less than committing a political suicide to provoke such resistance. To choose the path of least resistance, the reformist leadership adopted the "eating-in-separate-kitchens" reform in 1980. The scheme had two advantages: having localities to bear more financial responsibilities while at least guaranteeing central income at current levels. The center hoped that as the pie expanded its slice would become larger.

What follows from my analysis is that the 1980 fiscal decentralization was a reflection of constraints on the reformist leadership imposed by powerful provincial forces. In other words, the decentralization must be
attributed not so much to the reformist leadership's voluntary decision to extract below capacity as to its incapacity to extract the greatest amount of revenue in the old way and its desire to increase revenue over time in a new way.

Many authors have discussed the contents of the 1980 fiscal reform and the evolution of fiscal sharing system thereafter in detail, we need not repeat them here. Since it is apparent that Deng's fiscal decentralization was a result of the declining capacity of the Chinese communist state to govern, in what follows, we shall focus on whether and how the fiscal decentralization has in turn affected state capacity, and, if yes, what are the political consequences of the changes in state capacity.

It is widely accepted that Deng's fiscal decentralization has significantly weakened Chinese communist state capacity-as-fiscal-extractive-capability. As a result, the institutional environment within which local states make their own decisions has been changed in a fundamental way.

1. The budget revenue as percent of national income has dropped by a wide margin.

Because of the major government role in the economy, the level of revenue as a share of GNP should be substantially higher in the socialist setting than in the capitalist setting. In 1978, on the eve of the economic reform, the government revenue as a ratio of GNP was 34%, which was already very low in comparison with the Soviet Union and East European countries. After ten years of economic reform, the ratio fell to 19.8 in 1988. This ratio was lower even than that in developed capitalist countries (24.2% on average) and middle income countries (24% on average), and only slightly higher than that in the Third World countries (15.4% on average). It needs to be noted that for all country groups, data refer only to central government revenue while for China both central and provincial revenues were included.

2. Of the budget revenue, the central government's share has dropped by a wide margin.

The central government's share of total budget revenue was above 70% in the 1950s, about 60% in the 1960s, around 55% in the 1970s, but only 50% in the 1980s. In 1988, the central share accounted only for 47.2% of the total budget revenue. Between 1980 and 1986, on average, the local revenue increased annually 8.29%, higher than the increase rate of either the total budget revenue (6.9%) or the central revenue (5.5). During the same period, the local expenditure increased annually 9.2% on average, but the central expenditure only grew at an annual rate of 3.6%. In the Soviet Union and former socialist countries of East Europe, central revenue generally accounted for 70% of the total revenue. Even in capitalist countries, whose budgets are
generally not responsible for capital formation, it is rare for the ratio of the central revenue to the total government revenue to be lower than 50%. In the United States, which is a decentralized fiscal system by world standards, the federal government's tax income accounts for 57% of the total tax revenue while state and local governments together get only 43%. As for expenditure, on average, subnational governments in industrial countries account for about 30% of all government expenditures, compared to 15% in the Third World countries. In China, however, the subnational share of government expenditure is about 55%, well above these averages. No wonder the World Bank exclaims: "only a few countries in the world can claim as great a degree of expenditure or revenue decentralization."

3. Extrabudgetary funds have skyrocketed.

Before Deng's reform, there were two periods in which extrabudgetary funds expanded rapidly: the Great Leap Forward period and the Cultural Revolution period. In 1978, on the eve of the reform, extrabudgetary funds were as large as 31% of total budget revenue. In the ten years between 1979 and 1988, while budget revenue increased 133%, extrabudgetary funds increased five-fold. By 1988, almost as much money was circulating outside the state budget as within it. In many provinces, extrabudgetary revenues have surpassed budgetary revenues. Given their magnitude, some Chinese economists call the extrabudgetary funds "the second budget." On paper, only a small fraction of extrabudgetary funds (2%) are under the direct control of local governments, while most are to be managed by enterprises. But, in reality, local governments have no difficulty in encroaching on the resources of the enterprises under their jurisdictions. As long as funds are kept within localities, they are within the reach of local governments. Since an increase of extrabudgetary income would enhance the autonomy of local governments vis-a-vis the central government, whenever it is possible, local governments always attempt to maximize local extrabudgetary funds even though it may be detrimental to the central government.

To keep as much local resources from central extraction as possible, local governments are often very "generous" to enterprises at the central government's expense. China's tax administration and collection system enable them to do so. In most unitary countries, the central governments directly employ their own tax administration and collection staff who are responsible for levying all central taxes. But in China, the central government has no nationwide tax collection administration. Instead the central government relies on local government for the implementation of central tax policy and for the remittance of tax revenues. If local government had had no their own preferences, thinking and acting as central agents, this system should have
worked fair. Under the new revenue-sharing regime, however, local governments benefit little from higher collections, so that they would prefer to see their enterprises flourish rather than subject them to taxes revenue from which they have to share with the central government. The World Bank believes that no country in the world can claim to have a more decentralized tax administration system than China does.

There are opportunities for them to do so. First, local governments may set a reduced tax rate, authorize a tax holiday, or grant ad-hoc tax relief to enterprises. It was estimated that in 1988 alone, 10 billion yuan of taxes were lost in this way. Second, local governments may wink at enterprises when they evade taxes. The level of tax evasion has reached colossal dimension in the recent years. It is reported that at least 50% of state enterprises were engaged in tax evasions. Every annual tax audit conducted by the central government in the recent years could recover as much as 10 billion yuan of unpaid taxes. Some estimated that about 2% of budget revenue was lost in fiscal fraud. Without local governments giving tacit consent to such practices, it is hard for tax evasion to become so widespread and persistent.

Third, local governments may enter into contract arrangements with enterprises for payment of negotiated amounts of taxes. During the mid-1980s, local governments successfully boycotted the center's "substituting taxes for profit" reform, and forced the center to stay with problematic "contracting" system. Most of experts agreed that the "taxes for profit" would increase central revenue and simultaneously promote economic efficiency in enterprises. But it threatened the financial position of local governments by diminishing their patronage over local enterprises. On the contrary, relied on ad-hoc negotiation of profit or tax delivery responsibilities between enterprises and their supervisory bodies, the "contracting" system allows local governments to continue acting as "patriarchs" in their regions. The success of local interest in this episode demonstrates that local powers are now sometimes able to "veto" central decision. Under the contracting system, whether targeting on tax or profit remittance quotas, such contracts tend to reduce effective tax rates and increase enterprises' chance to retain more profit. Local governments are often lavish in negotiating contracts with their subordinate enterprises because they understand that liberal contracts would help their appropriation of enterprise revenue for their own uses later.

4. Ad-hoc charges run wild.

As Huang Yasheng puts, "[t]he crucial link between [local] bureaucratic largesse and their pecuniary interest is what is known in Chinese as tanpai---the imposition of various fees on enterprises in addition to formal tax obligations." An outgrowth of Deng's decentralization, the tanpai is a sign
that local states have become strong enough to make rival claims over resources extracted from society in defiance of the center's regulatory authority. To enterprises, these ad-hoc charges are exorbitant levies. But the new revenues generated in various forms of tanpai are all arrogated by local governments. Whenever local authorities need funds on a temporary basis, they impose tanpai. Originally, tanpai was put on by rural cadres after the decollectivization because accumulation funds of teams, brigades, and communes were no longer available to them. In the early 1980s, the central government issued repeated injunctions to forbid tanpai in the countryside. Before long, however, tanpai made its way into cities. By the late 1980s, there were literally tens of thousands of forms of tanpai. Chongqing Municipal Public Security Bureau alone imposed over 1,000 varieties of fees. No forms of tanpai has statutory basis, but they are all authorized by local governments or their agencies. It is estimated that local authorities now extract at least 20 billion yuan a year in various forms of tanpai. It probably contributes more to local government revenues than many formal taxes. Due to its quick proliferation and growing magnitude, the central government finds it almost impossible to supervise tanpai. In April 1988, the State Council issued a directive which prohibited local governments from imposing tanpai on enterprises. An economist found in May 1989, however, that the Sichuan Provincial Government had imposed five new forms of tanpai since June 1988. In October 1990, the CCP Central Committee and the State Council jointly issued another directive, but today tanpai is still a headache for the center and for enterprises. It is unlikely that the center will succeed in its battle against illegal tanpai, because local governments, which the center expects to lead the fighting against tanpai, wouldn't act against their own interests.

5. Local control over banking institutions.

Initially, the central decision makers expected that granting some authority to commercial banks in their credit decisions would improve microeconomic efficiency and strengthening macroeconomic control. They haven't gotten either, however. Instead, allocating bank loans is still very much based on political rather than economic grounds. The only difference is that now political interventions have intensified at provincial level and below, which the central government has lost much of its grip over macroeconomic control over credit. The reason for the heavy local hands on bank loans is simple. On the one hand, in the past few years, the interest rate of loans was often lower than the inflation rate, and therefore bank loans were virtually free. Demand for loans was understandably high. On the other hand, because bank managers are in effect under the direct control of
local governments, they have to place their immediate superiors' wishes above anyone else's. An investigation shows that most of problematic loan decisions were made under the pressures from local governments. The pressures of local governments have contributed to the uncontrollable investment drive in the last few years. In 1984, the bank loan for fixed capital investment amounted to only 29 billion yuan but in 1987 it rose to 127 billion, representing an average annual increase of 59% in the four years.

The above discussion of the effects of Deng's decentralization leads to two conclusions. First, the decentralization doesn't reduce public authorities' extractive capacity in general; it only reduces the central state's extractive capacity. If funds generated outside the budget are added to the budgetary funds, we would find that the ratio between resources kept in public sector and national income has actually steadily increased since 1980 [see graph 1]. A Chinese economist estimated that in 1987 the sum total of budgetary and extrabudgetary revenues and *tanpai* totalled 460 billion yuan, accounting for 50.3% of the national income of that year. In comparison with other countries, the ratio was very high. But, of 460 billion the central government could control only 26%, or 120 billion.

Second, as local governments were amassing more resources under their direct control, their intervention in economic life has become more frequent and the range of their intervention has become wider.

In sum, the decentralization doesn't result in the demolition of command economy. What it brings about is fragmentation of the national political economy, which, while effectively weakening the position of central planners, reproduces command economies on smaller scale.

Fragmented command economy is the worst kind of command economy. It doesn't have the advantages of market economy, while losing the advantages of centralized command economy. The central planners not only lose control over a significant proportion of state resources, but precisely because of the expanding role of local states, they also become increasingly unable to solve macroeconomic problems.

How do local states use resources under their control? First of all, they tend to spend more money on themselves. After 1979, administrative expenditure has grown rapidly. Before 1979, administrative expenditure usually accounted for 4% to 6% of total budget expenditure. For most of the 1970s, it was kept below 5%. After 1979, the expenditure on public administration as a percentage of total budget started a steady increase. In 1988, it reached an unprecedented 9%. The increase rate of the administrative expenditure was higher than that of total budget expenditure, national income, grass output value of industry and agriculture, or all budget expenditure.
items but one (scientific research and education). And the local share of
the increase was higher than the central share.

In addition to money from budgetary funds, local governments spent a
growing proportion of their extrabudgetary funds on public administration.
Administrative expenditure outside formal budget registered an increase of
16.7% in 1984, 42.8% in 1985, 25.5% in 1986, and 32.2% in 1987. A large
amount of money was spent on luxurious items such as cars, air conditioners,
refrigerators, modern office equipment, nice office building, and the like.
The extravagant local administrative expenditure certainly runs counter to the
interests of local population as well as the interests of the central
government. It demonstrates that local states now are able to pursue their
own preferences even in the situation IV I depicted in Figure I.

In the situation III, it is easier for local states to translate their
preferences into policy actions. The decade of the 1980s saw that luxury
hotels, the state of art amusement parks, skyey TV towers, modern overpasses,
giant stadiums and many other types of large non-productive projects sprang up
like mushrooms throughout China. Since local residents have no objection to
the improvement of the appearance of their towns, local governments can claim
that they represent local interests by spending money on such projects. But
local bosses intend to kill two birds with one stone. The other aim for
investing in such projects is to build up their personal public images. No
wonder that many projects are called "monument projects of so-and-so."

Of course, local governments wouldn't invest all of their money into
non-productive items. To expand their basis of future revenues, local
governments tend to invest as much money into productive projects as they can
generate. In selecting projects for investments, local governments usually
act very "rationally." They would not invest in infrastructure constructions
such as energy, raw material, highway, railroad, education, and the like,
because such projects generally need large amount of investment, take long
time to finish, run high risk, and worse than all from local governments' view
of point, benefit other localities. Local governments' favorites are high-
profit processing projects which can employ more local laborers and yield
quick returns. Thus, the decade of the 1980s also saw that small cigaret
factories, small breweries, small textile mills, and small home electronic
appliance plants sprang up throughout China.

Having lost control over local governments' purses, the central planners
find it increasingly difficult to control aggregate demand for investment and
consumption. In the past, expansion drive were usually initiated by ambitious
central planners. Now the driving forces for capital expansion are local
officials. The problem is that while there is a self-constrained mechanism
for the center, there is no constraint at local levels. The central planners may start a "great leap forward," but they cannot afford to ignore imbalance in the national economy for long. However, local governments don't have to worry about macroeconomic instability when they launch expansions. Every local government thinks that its investments are smart, rational, and absolutely imperative for local socioeconomic development. If there are problems with the national economy, it is other local governments or the central government to blame. Since no one plans to restrain its own investment fever, the result is an uncontrollably overheated economy. Since 1982, the central government has made countless efforts in vain to cut fixed asset investments, but fixed investment increased 28.6% in 1982, 14.5% in 1983, 33.4% in 1984, 38.7% in 1985. In 1986, it again increased by a big margin. In January 1987, the center convened a national conference of the provincial governor, at which the governors were told that no more new projects was to be permitted. But in the first two months of that year, 1,105 projects broke ground, among which 88.8% were financed by local authorities. In March, the central government issues a strongly worded directive demanding that all new projects were to be stopped. And in July, Yao Yilin repeated the warning. In the end, however, fixed investment went up 20.7% that year. The center failed because it simply does not possess adequate tools to directly control local investment. By the end of the 1980s, only less than 10% of fixed asset investment was financed by budgetary funds, and the rest of it by bank loans, extrabudgetary funds, tanpai, and foreign investment. Under this circumstance, state planning becomes a chimera. The direction and magnitude of local investments have to a large extent been out of the center's reach. What it could do thus was merely to hold down its own spending, while watching the localities continued the expansion of their investment.

The central control over the level of consumption is as loose as its control over investment. In the past, it was as easy for the central government to control the level of consumption as issuing an annual aggregate wage plan to lower level governments, which was in turn to be disaggregated into planned wage quotas for each and every individual enterprises. After the reform, the central government still sets the ceiling of the total wage bill, but it can no longer control the level of consumption, because local authorities have more say about bonuses, which now constitute a very large portion of people's income. In the 12 years between 1978 and 1989, while the total wage bill increased by 460%, bonuses registered a 4,525% increase. As investment and consumption were constantly expanding, aggregate demand persistently exceeded supply in much of the 1980s. The cumulative result was inflation. In the first three decades after the revolution, prices
scarcely rose. From 1951 to 1978, the average inflation rate was 0.7%. In the first years of the economic reform, inflation remained mild, rising annually 2.6% on average from 1979 to 1984. After 1984, the situation got worse every year. In 1988, the inflation rate rose to 18.5%, and in the first half of 1989, it reached 25.5%. The urban cost of living increased even faster. As the inflation rate rose to levels that had been quantitatively unknown, it threw the whole nation into panic, which contributed to the emergence of the 1989 protest movement.

The enormous expansion of local autonomy also resulted in growing regional inequality. During Mao's era, Lardy finds, the central authorities were able to reduce the large initial interregional differences in level of development by redistributing resources from richer to poorer provinces. Today, the center still tries to use differential revenue-sharing rate with the individual provinces as a main mechanism for redistribution. But this old method cannot be effective any more. A World Bank study finds that the development gap in China is bigger than ever since the founding of the People's Republic in 1949. Many of rich provinces make a lower level of revenue collection effort, e.g. Jiangsu, Zhejiang, Shandong, and Liaoning all make below average effort and Shanghai is just about average. It is poor provinces that make a greater collection effort than their richer counterparts. Of the ten provinces with the highest levels of per capita output, six had below average revenue growth during the reform period. Conversely, of the ten provinces with the lowest level of per capita output, nine had above average growth in revenue collection. Why did the richer provinces tend to make less effort to collect revenue? Because under the provincial contracting system of "eating in separate kitchens," rich provinces have to remit a certain proportion of the shared taxes to the central government, while poor provinces can retain all revenue they collected. By authorizing tax exemptions and preferential tax treatment to their enterprises and thereby lowering the total taxable base, rich provinces can keep more resources "at home," thus available for tanpai. Fiscal expenditure differentials have increased in the 1980s as a result of the provincial contracting system. Between 1983 and 1986, for instance, Shanghai's budgetary expenditure tripled, Guangdong's increased 138%, and Zhejiang's 132%; but Tibet's 61%, Qinghai's 65%, Shanxi's 71%, and Ningxia's 73%. Another symptom of the growing inability of the central government to redistribute among the provinces is the declining role the transfer system. Take Ningxia, one of China's poorest provinces, as an example. During the Second Five Year Plan period (1958-1962), the fiscal subsidy from Beijing increased on average 71% annually, and during the Fourth Five Year Plan period
(1971-1975) it still grew over 20% a year. But the increase rate of the central subsidy declined to 14.29% during the Sixth Five Year Plan period (1981-1985), 11.8% in 1986, and 8.4% in 1987.

The budgetary incomes account only for part of fiscal resources the provinces control. As pointed out above, extrabudgetary funds have exceeded budgetary incomes in many provinces. In comparing increase rates of the provinces' extrabudgetary incomes, we find that the rates tend to be higher in rich provinces than in poor provinces. Between 1982 and 1985, the average annual increase rate was 111% in Shandong, 86.5% in Liaoning, 68% in Zhejiang, 57% in Jiangsu; but only 33.9% in Ningxia, and 41.3% in Gansu. In 1985, the total extrabudgetary income of seven poor provinces (Guizhou, Yunan, Tibet, Shannxi, Gansu, Qinghai, and Ningxia) was less than Liaoning's alone.

Even under the capitalist system, the central authorities have to master sufficient fiscal resources to sever three general policy objectives: the provision for social goods (allocation function), adjustment of the distribution of income and wealth (the distribution function), and maintenance of macroeconomic stability (the stabilization function). However, Deng's decentralization has weakened China's central government's extractive capacity to the degree that it lacks adequate resources to perform those basic functions. First, there exists a substantial backlog of infrastructure needs which is believed to be a major bottleneck to growth. The central government sought to allocate more resources to bottleneck sectors such as energy, transportation, and basic raw materials, but local governments' investments in the processing industries have always increased at higher rate. As a result, the sectorial imbalance only deteriorated.

Second, inequality within and between regions has become greater. Traditionally, the communist state didn't use fiscal policy to adjust the distribution of income and wealth. What was considered fair or just was generally set in the primary distribution by wage policy. Thus, when the economic reform generates inequality within regions, China doesn't have an efficient mechanism to adjust increasingly unequal primary distribution. And the central government has no sufficient funds for building new safety nets to replace old ones. The transfer system was and still is a main mechanism to adjust inequality between regions. However, as the central government is losing control over fiscal resources to the provinces, there is simply not much to be transferred. Third, aggregate demand has greatly exceeded the available output in the recent years. In such situation, to stabilize the economy, the central government needs to adept restrictive measures to reduce demand. However, due to Deng's fiscal decentralization, the center was no longer able to control local governments' expenditures. Although China's
increase rate of output value was impressive during the 1980s, the country suffered high inflation, low efficiency, and volatile economic fluctuations.

A modern state has to perform the functions of allocation, [re]distribution, and stabilization. Otherwise, the state would lose its legitimacy to rule. But in China, the central government's ability to extract resources now is very limited, falling far short of the necessary level for performing the three basic state functions. Unable to cut expenditure to match revenue declines, the central government did what it could: it got into debt. China had gotten into debt before. But it doesn't mean that every it ran deficit, it was in fiscal crisis. Between 1950 and 1978, there were 12 deficit years in China, among which four occurred during the decentralized Great Leap Forward period and another four during the chaotic Cultural Revolution period. Except those occurring during the Great Leap Forward period, the magnitude of deficits was generally small, and the government was able to eliminate them every time when it became serious about the red on its balance sheet. After 1979, however, the budget has been characterized by continuously rising deficits. In the 12 years between 1979 and 1990, there was not even a single year in which the government escaped large deficit.

Beijing has made efforts in every possible way to increase revenue in order to keep pace with soaring demand for expenditure, but it simply couldn't make that happen. What the center had been able to do in the 1950s, 1960s, and 1970s, seems to have lost in the course of Deng's fiscal decentralization. After 1985, despite intensified central efforts to curtail expenditures and increase revenue, the government budget deficit began to balloon dangerously and hit a record 50.4 billion yuan in 1990. The center seems unable to recapture control even at high prices. While the center accumulated large deficits in the 1980s, local governments sat on surpluses. Before 1982, the center was still able to force surplus provinces to make extra contributions to the central budget in addition to what they were supposed to remit to Beijing. But it had to stop that practice after 1983 due to strong resistance from those provinces.

Donnithorne once likened the Chinese central government to a medieval king who was not able to live off his own and who had to rely on funds extracted by feudatories. But now the "vassals" begin to feel and act like independent lords of their soil and begin to detach themselves in spirit from the vassalage. They are so powerful and assertive that they can resist the fulfillment of their fiscal obligations. Here we have what Schumpeter calls "the crisis of a fiscal system: "obvious, ineluctable, continuous failure due to unalterable social changes."
A weak state tends to be a corrupted state. The better the quality of rulers' information about the actual wealth, income, and property produced and the more resources in the rulers' hands to be allocated, the more effective their control over the behaviors of government bureaucrats would be. Conversely, the more alternatives there are for local bureaucrats to gain access to resources, the more likely they are to become corrupted under an undemocratical system. In the PRC, there has never been an institutional mechanism to check bureaucrats from below. After Mao's death, the mechanism to check them from above---political campaign---has been set aside. Deng's decentralization thus greatly increases opportunities for those in positions to control resource allocation to profiteer by abusing their power. The result is widespread corruption.

A weak state cannot be a fair state. With limited extractive capacity, a weak state would have little to be redistributed, thus unable to adjust the distribution of income and wealth to assure conformance with what society considers "fair" and "just." Interregional as well as intraregional disparities have been exacerbated as a result of the reform. The increasing variance and inequality entail dangers of social polarization and political disaffection. Tremendous resentment has been building among "losers" of Deng's policy of "letting some people get rich first" against "winners." A 1987 survey of residents in 33 cities found that 88.7% of people thought that social inequalities were "great or very great." It is interesting to note that in 1980 when Solidarity first emerged, a public opinion poll in Poland found 85% of people thought that social inequalities in Poland were "great or very great." The percentage was even lower than what was found in China in the late 1980s.

Macroeconomic instability, skyrocketing inflation, widespread corruption and growing economic inequality have severely shaken people's confidence in the communist state's ability to manage the economy, control its own bureaucratic elites, and ensure social justice, which cast serious doubt on the regime's legitimacy. Were one to single out one factor conditioning Chinese people's support for the communist regime, it would be an expectation of protection from inequality and uncertainty by a strong welfare state. Deng Xiaoping gambled on being able to compensate Chinese people with greater prosperity in exchange for erosion of equality and certainty. In any event, the gamble failed. The state has become so weak that it can no longer "engender and maintain the belief among its citizens that the existing political institutions are the most appropriate ones for the society."

The weakened state has also proved unable to arrest centrifugal tendencies among local governments. Local states' financial muscles can be
easily converted into political muscles. Throughout the 1980s, local political elites were busy in building up political machines that control local economic monopolies and engage in sometimes fierce competition with the center and with one another over scarce raw materials, goods, and funds. With strong stake in maintaining and expanding their control over resources, local governments spare no efforts to protect local industries. The local authorities in peripheral regions well endowed with natural resources tend to keep the raw materials for local processing industries. They sometimes employed police force and militia to patrol their borders in order to block local suppliers' attempt to "smuggle" raw materials out. Media has reported "silkworm war," "wool war," "tobacco war," "tea war," "cotton war," "coal war," and "wars" on other raw materials in the recent years. To retaliate, core regions depending on import of raw materials tend to block technology transfer to resource-endowed regions. And all local governments have incentive to prevent the inflow of finished products from other localities in order to protect the sale of local products. The local protectionism resulted in the "balkanization" of China's economic system. A number of Chinese economists and political scientists have used the term "feudalist structure" to characterize the situation in the late 1980s. They believe that China has been split into 30 dukedoms (provinces) with some 2,000 rival principalities (counties). Although "vassals" have not been bold enough to openly challenge the ultimate political authority of Beijing, the emergence of local power centers produces deep cracks in the regime.

The mounting socioeconomic problems and political challenges tend to create deep divisions among central decision makers. "Reformers," led by former Party Secretary General Hu Yaobang and Zhao Ziyang, with the support of Deng Xiaoping, believed that the only way out of the current crises is to wage faster and more comprehensive market-oriented reform, while "conservatives," represented by Premier Li Peng, with Chen Yun's support, favored a slower pace and more reliance on central planning. There was yet another dimension of internal division within the political leadership: "hardliners," such as Deng Xiaoping, were willing to protect their authoritarian rule by whatever means necessary, including the use of brutal force, whereas "softliners," such as Hu and Zhao, prepared to tolerate new political actors and introduce certain freedoms. Internal conflicts within the political leadership is the necessary precondition for regime transition. It is not likely that socioeconomic crises themselves bring about such a transition. Comparative studies of regime transition in other contexts have established that "there is no transition whose beginning is not the consequence, direct or indirect, of important division within the authoritarian regime itself." It is so
because the internal divisions increase the fragility of the regime and thereby decrease the cost of transition.

**Conclusion**

As should be evident from the above discussion, there has been a paradox in the Chinese experience of the 1980s: the thickening of local stateness occurred concomitantly with the thinning of central stateness. In other words, the deepening of state penetration in local society was not accompanied by the strengthening of political integration. In many ways, this phenomenon resembles the process of state involution characteristic of the Republican period before 1949. In studying state finances of the Republican period, Duara reveals a similar situation: while the bureaucratic power of the central state was becoming parcelized, the fiscal foundations of local states were actually strengthened in the process. The weakening of central control thus went hand in hand with the unprecedented expansion of state penetration in society. Duara believes that there are direct causal links between state involution in the Republican China and the communist revolution.

The involutionary expansion of the state seems to have been a recurrent phenomenon in Chinese history. In the late Ming dynasty, for instance, Ray Huang finds that "though the imperial government was in theory omnipotent, in practice it was often unable to act." Characterized by its monolithic structure, the Ming fiscal system was designed to impose a unified administration over all the financial resources of the empire. The main concern of the dynasty's founders was to prevent the regions from over-developing any financial potential of their own, and thus from challenging the central government. But fiscal practice diverged increasingly from the original design. Toward the end of the dynasty, tax collectors became more and more intrusive. However, it was not a sign of strength, but of a lack of it. "The arbitrary and excessive demands of the tax collectors...in part reflected this loss of control, and in part represented attempts by officialdom to compensate for its own organizational weakness."

The Qing dynasty started with an effective centralized fiscal system. But, from the late 18th century on, the central government became increasingly unable to extract sufficient resources for sustaining its rule. In the 150 or so years from 1750 until the early 1900s, it suffered an enormous decline (by almost two thirds) in the real values of the revenues collected from direct taxes. The growth rate of indirect taxes did begin to accelerate in the latter part of the 19th century, but much of the increase was siphoned by local states. In retrospect, one has good reason to speculate that there
were also direct or indirect causal links between the degeneration of "state-capacity-as-fiscal-extractive-capability" of the two dynasties and their fall.

The involutionary expansion of the Chinese communist state have certainly aggravated the underlying social crisis that led to Tiananmen. The Chinese protest movement of 1989 marked the beginning of the end of the Chinese state socialism. We assert that the system is moribund not so much because we believe that all undemocratic regimes are doomed to destruction as because we believe that the system's capacity to govern has been weakened to the point beyond repair. In fact, the killing of hundreds of unarmed civilians in central Beijing itself reveals how fragile the system is. If the state were strong, it would have been able either to mitigate grievances before they became the source of instability or to meet political challenges without resorting to military solution. But by the late 1980s, the Chinese communist state has become so weak that it was unable to extract adequate amount of resources for unified state actions, to guide the national economy, to regulate the distribution of economic resources, to garner the loyalty, support, and obedience of the population, and even to direct the behaviors of state bureaucrats. As a result, when a serious political crisis occurred, there was little alternative other than mobilizing the army. Even the military is not reliable, though. Some elements within the People's Liberation Army resisted the military mobilization in the spring of 1989, which was overcome only through the active involvement of Deng Xiaoping and other elder leaders. Once Deng and other aged hardliners pass away, the military could become a force for change. By then, either being forced to initiate transition from within or being overthrown in a revolution, Chinese political system would change for good or ill, but definitely in a fundamental way.
Endnotes


4 Migdal, Strong Societies and Weak States, p. xiii.


7 Zysman, Governments, Markets and Growth, p. 297; Samuels, The Business of the Japanese State, p. 6; and Ikenberry, Reasons of State, p. 43.


9 Ibid, p. 45.


Dietrich Rueschemeyer and Peter B. Evans, "The State and Economic Transformation: Toward an Analysis of the Conditions Underlying Effective Intervention." In Evans et al., eds., Bringing the State Back in, p. 50.


Rueschemeyer and Evans, "The State and Economic Transformation."


Some suggest that in order to make the concept of state capacity unambiguous it should be replaced by "central government capacity." It
should not be forgotten that just as "local governments' capacities" can be a "minus" to the central government's capacity, it can be a "plus" too. The "central government capacity" cannot capture positive or negative effects of local governments on the state system as a whole. The relationship between "state capacity", "central government capacity" and "local government capacity" can be summarized as follows:

State Capacity = Central Government Capacity + Local Government Capacity

where we define:
"local government capacity" > 0 when local governments intervene in behalf of the central government;
"local government capacity" < 0 when local governments intervene to pursue preferences at odds with the central government's;
"local government capacity" = 0 when local governments don't intervene at all.

Thus, we find:
1. State capacity > central government capacity when local government capacity > 0;
2. State capacity < central government capacity when local government capacity < 0;
3. State capacity = central government capacity only when local government capacity = 0.

Obviously, state capacity cannot be reduced to central government capacity.

Levi, Of Rule and Revenue.
Zysman, Governments, Markets, and Growth, p. 298.
Levi, Of Rule and Revenue, pp. 12, 37. and 95-144.


Ibid, pp. 88-89.

Riskin, China's Political Economy, chapter 9.


Ibid, p. 239.

Here I use a definition closer to that found in the other countries, which subtracts domestic and foreign borrowing from the Chinese measure of revenue and foreign and domestic loan repayments from the Chinese definition of expenditure. See World Bank, China: Revenue Mobilization and Tax Policy, pp. 9-10.


Ibid, pp. 380-381.


Lardy, Economic Growth and Distribution in China.

Riskin, China's Political Economy, pp. 213-218.


59 Li Xianglu, "Weishemo shuo fenquan rangli gaige fangzhen shi zhongque de," Zhishi fenzi, (Fall 1990).

60 Zuo Chuntai and Song Xinzhong, Zhongguo shehui zhuyi caizheng jianshi, p. 453

61 Ibid, pp. 431-452.


64 In fact, the 1980 fiscal decentralization was supposed to be accompanied by the return of several thousand large enterprises to direct central government subordination, but due to strong local opposition, the second part of the reform has never been implemented. It also needs to be noted that right before his second purge in 1976, Deng Xiaoping made a decision to recentralize financial resources, which was reversed after his fall. See Allen S. Whiting, "Domestic Politics and Foreign Trade in the PRC, 1971-1976," (Ann Arbor: Michigan Papers in Chinese Studies, no. 39, 1979).


67 In the mid-1960s, the ratio was 76.9 in Czechoslovakia, 62.6% in Bulgaria, 54.8% in Poland, and 50.6% in the USSR. Ibid, p. 42.


70 World Bank, China: Revenue Mobilization and Tax Policy, p. 80.

71 Ibid, pp. 76-80.

72 World Bank, China: Revenue Mobilization and Tax Policy, p. 80.


World Bank, China: Revenue Mobilization and Tax Policy, p. 11.

Huang, "Web of Interests and Patterns of Behavior," p. 450.

Interview with an official from the Ministry of Finance.


Huang, "Web of Interests and Patterns of Behavior," pp. 451-453.


Wang Shaofei, "Zhongyang he difang caizheng guanxi di mubiao moshi."


Zhongguo tongji nianjian 1990, p. 132.


Lardy, Economic Growth and Distribution in China.

See Huo Shitao's chapter in this volume, "The Variation of Regional Inequality and Management Policy of the National Government in China since 1980."


AUDREY DONNITHORNE, "CENTRAL–PROVINCIAL ECONOMIC RELATIONS IN CHINA." Contemporary China Paper, no. 16. Contemporary China Center, Research School of Pacific Studies, Australian National University, 1981.


O'DONNELL, SCHMITTER, AND WHITEHEAD, **TRANSITIONS FROM AUTHORITARIAN RULE**, vol. IV, p. 19.

VIVIENNE SHUE, "STATE SOCIALISM AND MODERNIZATION IN CHINA THROUGH THICK AND THIN," paper for the 1988 annual meeting of the APSA.


