

Economics 970: Political Economy of China**Spring Semester 2012****Instructor:** Daniel Koss, koss@fas.harvard.edu, office hours by appointment**Class Meetings:** Monday and Wednesday, 1 pm to 2.30 pm**Quantitative Level:** 2

Course Description: This tutorial explores China's unique model of economic development, as well as the economic effects of ongoing, rapid institutional transformations. What exactly is the Chinese model of development and is it worth emulation by other countries? To what extent can China be characterized as an "Asian developmental state"? Why has it been so hard to bring development to the hinterland and what can be done about it? Is the presence of the local state in the rural economy beneficial or predatory? Unpacking complexities of China's vast economy takes us from industries in the coastal areas (the "national champions") and informal financial markets (back-alley banking), all the way to the poor rural hinterland.

Given the overwhelming role, which the Chinese state continues to play in the economy, the tutorial focuses in particular on the fascinating interplay between politics and economics. The class addresses pressing challenges ranging from inequality and corruption to environmental issues. As governance issues are increasingly perceived as an obstacle to growth in poorer areas, how to give incentives to local officials, so that local governments become more pro-growth? What are the promises of decentralization and tax reform? How costly are the inefficiencies on Chinese labor and financial markets?

Through readings and discussions, the tutorial will encounter a variety of economic approaches, formal models and econometric techniques, which have been applied to study China's political economy. Many of these can inspire students going forward with their own research. The class will give students a sense of how a simple model can be used to clearly illustrate the logic of an argument. Students will put their econometric skills to use in the context of a larger economic argument. There will be a hands-on introduction to using Chinese data and to making maps.

Requirements:

Class participation. 30% of grade. Attendance is mandatory. Your full participation is expected in the discussion of assigned readings and general course themes. To facilitate our class discussion, you must formulate four bullet points of what you have to say about the readings; send them to the instructor (through email, by 8am of the day of class meeting); and be prepared to elaborate on the bullet points in class.

Map. 5% of grade (map plus 600 words). There will be one session introducing software that allows you to design your own maps, a skill that is easy to acquire and very useful to have. After that you will be expected to create your own thematic map and comment on it.

Model. 15% of grade (1800 words plus in-class presentation). You will consider an economic or political agent's decision problem and then create a simple model to illustrate the logic at work and the tradeoffs involved. The model can be defined using math or using well-defined graphs; it can be a variation of models encountered in class. The purpose is to encourage thinking about opportunities and possibilities of using models to formulate hypotheses.

Empirical Paper. 20% of grade (2400 words). You will run a regression and report your findings.

Final paper. 30% of grade. (6000 words). You will write an economic research paper on a topic related to China's economic development. It should be acceptable to an organization such as the World Bank, as a research paper submitted by a research consultant.

I. China's Model of Economic Development

WEEK 1: Central Challenges.

For our first meeting on January 30th, please answer the following question in about 100 words: "In your opinion, what is the single most important challenge or risk that China's economic and political system are facing going forward?" Come up with one potential crisis scenario. There is no reading assignment for our first session. For the second session, the reading assignment is:

- Whiting, Susan, 2001, "Power and Wealth in Rural China: The Political Economy of Institutional Change", pp.1-29.

II. Two Pressing Issues in China's Development

WEEK 2 Inequality (one session will be dedicated to putting data onto maps)

- Gustafsson, Bjoern and Shi Li, 2002, "Income Inequality within and across Counties in Rural China 1988 and 1995", in *Journal of Development Economics*, vol. 69, issue 1.
- Fleisher, Belton, Haizheng Li and Min Qiang Zhao, 2010. "Human Capital, Economic Growth, and Regional Inequality in China", in *Journal of Development Economics*, vol. 92.
- Dwayne, Benjamin, Loren Brandt and John Giles, 2010. "Did Higher Inequality Impede Growth in Rural China?" *World Bank Policy Research Working Paper*, no. 5483

WEEK 3: Corruption (also introduction to using models in a larger argument)

- The Economist, "The Red and The Black", October 3rd, 2009
- Manion, Melanie, 2004. *Corruption By Design. Building Clean Government in Mainland China and Hong Kong*, pp. 1-26.

- Shleifer, Andrei and Robert Vishny, 1993. “Corruption”, in *Quarterly Journal of Economics*, vol. 108(3).
- Ni, Shawn and Hoang Van Pham, 2006. “High Corruption Income in Ming and Qing China”, in *Journal of Development Economics*.
- Cai, Hongbin, Vernon Henderson and Qinghua Zhang, 2009. “China's Land Market Auctions: Evidence of Corruption”, NBER Working Paper No. 1506

SPECIAL WEEK 4: Chinese Statistics or: Where to find good data?

- The Economist, “On the Poverty Line”, May 24th, 2008
- The Economist, “Clipping The Dragon’s Wings”, December 22nd, 2007
- Rawski, Thomas, 2002, “What is Happening to China’s GDP Statistics”, in: *China Economic Review*, vol. 12.
- Holz, Carsten, 2003. “‘Fast, Clear and Accurate’: How Reliable Are Chinese Output and Economic Growth Statistics?”, in *China Quarterly*, no. 173.
- Walfish, Daniel, 2001. “China’s Census: National Count Reveals Major Societal Changes”, in *Science*.

III. The Chinese Local State: Predatory or Pro-Growth?

WEEK 5: Local Governance in China (preparatory readings for modeling assignment)

- Oi, Jean and Shukai Zhao, 2007. “Fiscal Crisis in China’s Townships: Causes and Consequences”, in Perry, Elizabeth and Merle Goldman. *Grassroots Political Reform in Contemporary China*. (chapter 4, pp.75-96)
- Fock, Achim and Christine Wong, 2008. “Financing Rural Development for a Harmonious Society”, *World Bank Policy Research Working Papers*, no. 4693

WEEK 6. Local Cadres’ Incentives.

- Edin, Maria, 2003. “State capacity and local agent control in China: CCP cadre management from a township perspective”, in *China Quarterly*, vol. 173
- Guo, Gang, 2009. “China's Local Political Budget Cycles” in *American Journal of Political Science*, vol. 53 (3).
 - Kung, James Kai-sing and Shuo Chen (2010): “The Tragedy of the Nomenklatura: Career Incentives and Political Radicalism During China’s Great Leap Famine,” unpublished paper.

SPECIAL WEEK 7. Student Presentations. Read other students’ papers.

WEEK 8. Decentralization.

- Cai, Hongbin and Daniel Treisman, 2006. “Did Government Decentralization Cause China's Economic Miracle?”, in *World Politics*, vol. 58 (4)
- Feltenstein, Andrew and Shigeru Iwata, 2005. “Decentralization and Macroeconomic Performance in China: Regional Autonomy has its Costs”, in *Journal of Development Economics*, vol.82, issue 1
- Qiao, Baoyun, Jorge Martinez Vazquez, Yongsheng Xu, 2008. “Tradeoff between growth and equity in decentralization policy: China’s experience”, in *Journal of Development Economics*, vol. 86.
- Zhang, Xiaobo, 2007. “Fiscal Decentralization and Political Centralization in China: Implications for Growth and Inequality” in *Journal of Comparative Economics*, vol. 34(4).

IV. Two Challenges for the Long Run

WEEK 9: Environmental Issues

- Dean, Judith, Mary Lovely and Hua Wang, 2005. “Are foreign investors attracted to weak environmental regulations? Evaluating the evidence from China,” in *World Bank Policy Research Working Paper*, no. 3505
- Wang, Hua and Yanhong Jin, 2002. “Industrial Ownership and Environmental Performance: Evidence from China,” *World Bank Policy Research Working Paper*
- Fisher-Vanden, Karen, 2007. “How Do Market Reforms Affect China’s Responsiveness to Environmental Policy?”, in *Journal of Development Economics*, vol. 82, issue 1.

WEEK 10: Taxation

- Bahl, Roy, 1998. “Central-Provincial-Local Fiscal Relations: The Revenue Side”, in Donald Brean, *Taxation in Modern China*.
- Bernstein and Lu, 2003. *Taxation Without Representation in Contemporary Rural China*. (chapters 1, 3, 4 and 6)
- Fisman, Raymond and Shang-Jin Wei, 2004. “Tax Rates and Tax Evasion: Evidence from ‘Missing Imports’ in China”, in: *Journal of Political Economy*, vol. 112(2).

V. Continuing Inefficiencies on Factor Markets

WEEK 11: Labor Markets: Migration and off-farm employment

- Meng, Xin and Junsen Zhang, 2001. “The Two-Tier Labor Market in Urban China: Occupational Segregation and Wage Differentials between Urban Residents and Rural Migrants in Shanghai”, in *Journal of Comparative Economics*, vol. 29.

- Whalley, John and Shunming Zhang, 2007. "A numerical simulation analysis of (Hukou) labour mobility restrictions in China", in *Journal of Development Economics*, vol. 92 (1)
- Au, Chun-Chung and Vernon Henderson, 2006. „How migration restrictions limit agglomeration and productivity in China", in *Journal of Development Economics*, vol. 80.

WEEK 12: Financial Markets

- Shih, Victor, 2004. "Dealing With Non-Performing Loans: Political Constraints and Financial Policies in China", in *China Quarterly*, vol. 180
- Boyreau-Debray, Genevieve and Shang-Jin Wei, 2005. "Pitfalls of a State-Dominated Financial System: The Case of China", NBER Working Paper No. 11214.
- Li, Xiaoming, 2000. "Reforming China's Financial System and Monetary Policies: A Sovereign Remedy for Locally Initiated Investment Expansion", in *Journal of Development Economics*, vol. 62 (2)