THE PRICE OF COMPETITION: PRICING POLICIES AND THE STRUGGLE TO DEFINE CHINA'S ECONOMIC SYSTEM*

Scott Kennedy

Although China formally announced in 1992 that it was adopting a "socialist market economy", the shape of the market economy that China wishes to adopt has remained unresolved.[1] Some believe that firms, business associations and the government should all promote unfettered competition, while others advocate a combination of competition and cooperation, both among firms and between firms and the government.[2] Today the Chinese are struggling with issues, including the appropriate norms of competition, that have long been the subject of controversy within and between capitalist systems.[3]

* The author thanks the George Washington University for the financial assistance that supported the field work in China upon which this article is based, the Peking University Research Center for Contemporary China and the Pudong Institute for the US Economy for their logistical assistance while in China, and Andrew Barnes, Anita Chan, Kenneth Foster, Jason Kindopp, Jonathan Unger, Yu Hui and two anonymous reviewers for comments on earlier drafts. An earlier version of this article was presented at the 2000 Annual Meeting of the American Political Science Association in Washington, DC.

1 Opponents of markets *per se* have strongly criticized the reforms and have fought against privatization in particular, but they have offered no detailed alternative program. See Feng Chun, "An Unfinished Battle in China: The Leftist Criticism of the Reform and the Third Thought Emancipation", *The China Quarterly*, No. 158 (June 1999), pp. 447–67.

2 For an example of the view that there is a consensus in support of free-market principles in China, see Dali Yang, "Survival of the Fittest", *Worldlink*, March/April 1998, pp. 50–3.

3 David Lane applies this framework to the Russian case in his "What Kind of Capitalism for Russia? A Comparative Analysis", *Communist and Post-Communist Studies*, Vol. 33 (December, 2000), pp. 485–504. On the variation among capitalist states see Andrew Shonfield, *Modern Capitalism: The Changing Balance of Public and Private Power* (London: Oxford University Press, 1970); Peter J. Katzenstein (ed.), *Between Power and Plenty: Foreign Economic Policies of Advanced Industrial States* (Madison: University of

The intensity of the debate in China was heightened by the attempt to mobilize business associations to check the pervasive deflation that emerged in the latter half of the 1990s. Because of excessive investment, over-expansion of production and reductions in foreign trade barriers, prices were falling in numerous sectors. Heeding calls from increasingly powerful large firms, both state-owned and private, and pushed by its own interests, the government condoned and encouraged the formation and enforcement of price cartels organized by firms, associations and industrial ministries.[4] This effort climaxed in 1998 with the government's announcement of a policy in which industry associations were to set "self-discipline prices" (*zilüjia*), a program which was bitterly contested and then partly rescinded. The consequence was a reduction in the associations' already limited authority and legitimacy in the eyes of both their members and the government.

The story highlights the myriad forces shaping China's political economy. National and local-level officials are often portrayed as driving the agenda to define China's economic system, and, by implication, non-state actors are assumed to be responding to, rather than shaping, the policy environment.[5] But in reality, the final decisions and programs do not always reflect straightforwardly

---

Wisconsin Press, 1978); Peter Evans, *Embedded Autonomy: States and Industrial Transformation* (Princeton: Princeton University Press, 1995); and Peter A. Hall and David Soskice (eds), *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage* (Oxford: Oxford University Press, 2001). Paul Hutchcroft also distinguishes states by, and their bureaucrats' relative commitment to, the general interest (as opposed to their self-interest). See his *Booty Capitalism: The Politics of Banking in the Philippines* (Ithaca: Cornell University Press, 1998). On differences across sectors, see Wyn Grant, Alberto Martinelli and William Paterson, "Large Firms as Political Actors: A Comparative Analysis of the Chemical Industry in Britain, Italy and West Germany", *West European Politics*, Vol. 12, No. 2 (April 1989), pp. 72–90. Variation across states and sectors is shown in J. Rogers Hollingsworth, Phillipe Schmitter, and Wolfgang Streeck (eds), *Governing Capitalist Economies: Performance and Control of Economic Sectors* (New York: Oxford University Press, 1994); and Suzanne Berger and Ronald Dore (eds), *National Diversity and Global Capitalism* (Ithaca: Cornell University Press, 1996).

4 A cartel is an agreement among market participants (companies or governments) to reduce competition to their collective benefit by setting price or production targets, with such targets being a specified amount, a range around that amount, or an upper or lower limit.

5 Kenneth Lieberthal and Michel Oksenberg, *Policymaking in China: Leaders, Structures, and Processes* (Princeton: Princeton University Press, 1988); Kenneth Lieberthal and David M. Lampton (eds), *Bureaucracy, Politics and Decision-Making in Post-Mao China* (Berkeley: University of California Press, 1992); Susan Shirk, *The Political Logic of Economic Reform in China* (Berkeley: University of California Press, 1993); and Joseph Fewsmith, *Dilemmas of Reform in China: Political Conflict and Economic Debate* (Armonk: M. E. Sharpe, 1994).

the interests or preferences of political leaders. As will be seen, non-state actors, and business in particular, are having a greater influence today on policy than ever before.[6]

The information in this article derives from two types of sources. Most important were in-depth interviews with participants and close observers of the debates, including officials in the State Economic and Trade Commission, the State Development and Planning Commission and other national-level ministries; officials in coastal local governments; representatives from national business associations; executives from Chinese companies of different sizes and ownership forms (that is, small and large, private, collective, and state-owned firms); Chinese journalists; and industry experts.[7] These interviews were supplemented by primary documents provided to me by various interviewees and by articles from the Chinese press. Although the Chinese media has a well-deserved reputation for hewing to the Party line, the debate over competition policy made headlines in major Chinese newspapers and magazines.

The article will first lay out the conflicting views in China about competition and the market and show how this has led to compromises in pricing policies and laws. The different conceptions coloured interpretations of the recent tide of deflation and the question of how, if at all, to respond. A brief introduction to the structure of government–business relations in China, including the system of associations, follows in order to give a context to the way in which some associations eventually were mobilized. This sets the stage for the story's 1998 climax, in which the self-discipline price policy was announced and then later partially overturned. After explaining the reasons why the vast majority of price cartels in China failed and the conflicting lessons actors learned from the experience, the article concludes by considering the broader implications for China's political economy.

Contending Views of Competition and Chinese Law

Over the last decade it appears that the neoclassical economics model of free markets, embodied in the United States, has vanquished all rivals. Dozens of developing countries have given up hopes of a New International Economic Order and have instead embraced competition. This is demonstrated in their

---

6 Scott Kennedy, "In the Company of Markets: The Transformation of China's Political Economy", PhD Dissertation, George Washington University Department of Political Science, 2002. Also Scott Kennedy, "The New 'China Lobby'", *Asian Wall Street Journal*, 13 October, 1999.

7 Over 250 interviews were carried out in 1998 and 1999 in Beijing, Shanghai, Jiangsu, Zhejiang and Guangdong as part of a broader project on the rise of business lobbying in China; of the total, 98 were conducted with company executives, 56 with government officials and 61 with representatives from intermediaries (associations and lobbying firms). Several related interviews were conducted in Beijing, Shanghai and northeastern China in 2002. To protect their identity, interview sources must remain anonymous.

creation of antitrust policies derived from the experience of industrialized nations. In an optimistic tone, Susan Sell finds that antitrust sentiment and laws have taken root because of strong domestic political constituencies that favour competition over government control of industry, company monopolies or inter-firm collusion. The post-Communist states of Europe followed suit by adopting competition policies largely modeled on the European Union's Treaty of Rome.[8] Even Latin America has seen an unprecedented growth in support for free markets.[9]

Despite such steps, the chequered implementation of such laws with regard to anti-competitive behaviour, and cartels in particular, suggests that the debate in Eastern Europe and elsewhere has not ended.[10] Such ambiguities are even more visible in China. Different groups have different economic and political priorities, have differing interpretations of China's own recent experience with markets and can draw on alternative external models and experiences to buttress their visions.

Pro-competition forces are led by China's growing stock of economists. All have read the classics on market economics, and over the last decade many have studied at the premier centres of economic theory, including the University of Chicago, and then returned home to take up leadership positions in Chinese universities, research institutes, central government ministries and offices, and financial institutions. In their writings, comments in the media and advice to policy-makers, these economists stress the benefits of the free market and roundly criticize government intervention that does anything but improve market

---

8 Susan K. Sell, "Intellectual Property Protection and Antitrust in the Developing World: Crisis, Coercion, and Choice", *International Organization*, Vol. 49, No. 2 (Spring 1995), pp. 315–49; Russell Pittmann, "Competition Law in Central and Eastern Europe: Five Years Later", *The Antitrust Bulletin*, Vol. 43, No. 1 (Spring 1998), pp. 179-228. One observer writes that such laws are founded on the bankruptcy of the old planning models: "The neoclassical condemnation of monopoly has been adopted—and often extended—almost universally throughout the post-communist world": Ben Slay, "From Monopoly Socialism to Market Capitalism", in Ben Slay (ed.), *De-monopolization and Competition Policy in Post-Communist Economies* (Boulder: Westview, 1996), pp. 1–2.

9 Leslie Elliott Armijo and Philippe Faucher, "'We Have a Consensus': Explaining Political Support for Market Reforms in Latin America", *Latin American Politics and Society*, Vol. 44, No. 2 (Summer 2002), pp. 1–40.

10 Dyker and and Barrow stress the "deep ambivalence of much of Russian anti-monopoly policy" and find that "in many cases established industry interests have been able effectively to hijack anti-monopoly policy, and use it for market-sharing, cartelization, and raising new barriers to entry": David Dyker and Michael Barrow, "Monopoly Competition Policy in Russia", in Alan Smith (ed.), *Challenges for Russian Economic Reform* (Washington, DC: Brookings Institution, 1995), p. 112. It is still too early to tell whether Argentina's debt crisis of late 2001 and the election victory in October 2002 of Luiz Inácio Lula da Silva of the Workers' Party in Brazil will break this consensus.

behaviour and increase competition.[11] These economists are joined in their views by government officials who have been persuaded by the merits of free market principles as well as motivated by self-interest. Many have benefited directly or indirectly from their advocacy of pro-competition policies, either because their bureaus have gained additional responsibilities through this, or by way of their own personal promotion to a higher rank for effectively pushing reforms forward. They are ideologically allied with private entrepreneurs, state-enterprise managers and foreign businesspeople who have successfully competed in markets and/or been subjected to less government intervention in their operations. Biographies of successful entrepreneurs and companies are even more popular than economics texts.[12]

In their consideration of what economic policies to adopt, pro-competition advocates share a commitment to strategies that maximize growth. They highlight liberalizing measures as the key sources to China's economic expansion and prosperity, and they criticize anti-competitive measures as obstacles to efficiency and growth. While other countries are studied and discussed, the pro-competition stance is heavily inspired by the world's strongest economy, the United States, which they perceive as a bastion of free market principles.[13] China has established contacts with antitrust organizations from over twenty countries, held several international conferences and sought advice from the UN Council on Trade and Development on the subject, but Chinese pro-competition forces pay greatest attention to American laws and institutions.[14]

---

11 Although there appears to be a general consensus among economists about the inherent benefits of free competition, a few do disagree. See Sun Tianfa, *Lixing jingzheng: shichang jingjide zhidu quexian yu tiaozheng* (Rational Competition: The Institutional Defects and Adjustment of the Market Economy) (Beijing: Economic Management Publishing House, 1999). Given that members of senior political elites, such as Zhao Ziyang, nurtured economists and gave a policy outlet to their ideas, one cannot understate their role in promoting reforms. See Fang Cai, "The Roles of Chinese Economists in Economic Reform", *China Economy Papers*, No. 2, Asia Pacific School of Economics and Management, Australian National University, (1998).

12 For example, Zhang Yongjun (ed.), *Zhongguo baiming youxiu qiyejia fendoushi* (The History of the Struggles of 100 Outstanding Chinese Entrepreneurs) (Beijing: China All-China Federation of Industry and Commerce Publishing House, 1997); Chen Huixiang, *Lianxiang weishenme* (Why Legend) (Beijing: Beijing University Publishing House, 1997).

13 Early in the reform period, when it was too sensitive to cite the United States in defence of economic policy, scholars and officials used, among others, the examples of reforming Socialist countries such as Hungary and Yugoslavia to promote liberalization. See Carol Lee Hamrin, *China and the Challenge of the Future: Changing Political Patterns* (Boulder: Westview Press, 1990), pp. 33–8.

14 Wu Yunhe, "New Law Against Unfair Trade is Being Weighed", *China Daily Business Weekly*, 3–9 April, 1994, p. 1; *Gongshang xingzheng guanli* (Industrial and Commercial Administrative Management), No. 23 (15 November 1998), p. 11; Ding Bangkai, Xu Zhaohong, Zhang Shengcui and Cheng Xuedong, *Jingzheng falü huanjing lun* (On the

As powerful as the ideas of the pro-competition advocates are, they are far from universally accepted. There are many Chinese officials and business people who, while conceding the benefits of free market in ideal circumstances, believe that China is not yet ready for such complete liberalization. To them rapid growth is just one goal that must be balanced against others, most importantly employment and tax revenues in the near term. The officials who regulate state-owned enterprises are likely also to support policies that provide a rationale for their own employment and enhanced authority. They are joined by managers of inefficient state-owned enterprises as well as by state-enterprise managers and private entrepreneurs of relatively efficient operations who nevertheless are willing to use any means necessary, including collusion, to secure and increase their share of the market. Thus, both for reasons of self-interest and what they consider to be balanced public policy, many in China prefer what could be called a "planned" or "controlled" market economy that legitimizes government intervention, monopolies and vertical and horizontal inter-firm cooperation.[15]

Advocates of such a position draw from the experiences of foreign market economies.[16] The nearest example is Japan and the "East Asian model" of development, which stresses the role of state intervention in channeling resources to priority sectors and moderating competition to achieve a variety of goals, including long-term growth.[17] Japan's Ministry of International Trade and Industry has encouraged, or condoned, hundreds of production and price cartels to help industries through difficult periods, to promote industrial restructuring and to maintain domestic supplies of certain goods.[18] These cartels have not

---

Environment for Competition Law) (Shanghai: Shanghai Finance and Economics University, 1999).

15 The distinction between free and controlled markets rests on the assumption that most markets have some level of state involvement. Markets are not just economic phenomena, but are also social, cultural and political constructs that can vary in terms of ownership rights, barriers to entry, access to capital and credit, rules for pricing and rules of exchange. And each of these factors can be shaped by state and non-state actors alike. See Neil Fligstein, "Markets as Politics: A Political–Cultural Approach to Market Institutions", *American Sociological Review*, Vol. 61, No. 4 (August 1996), pp. 656–73.

16 Jiang Bo, "Hang you hang gui" (Industries Have Industry Standards), *Jingji ribao* (Economic Daily), 4 August 1998, p. 2; Ai Jun, "Jiage zhan che kaichu migong" (The Price War Car Drives Out of the Labyrinth), *Zhongguo jingying bao* (China Business), 18 August 1998, p. 4.

17 Chalmers Johnson, *MITI and the Japanese Miracle: The Growth of Industrial Policy, 1925–1975* (Stanford: Stanford University Press, 1982); Robert Wade, *Governing the Market: Economic Theory and the Role of Government in East Asian Industrialization* (Princeton: Princeton University Press, 1990).

18 Mark Tilton, *Restrained Trade: Cartels in Japan's Basic Materials Industries* (Ithaca: Cornell University Press, 1996); and Ulrike Schaede, *Cooperative Capitalism: Self Regulation, Trade Associations, and the Antimonopoly Law in Japan* (Oxford: Oxford University Press, 2000). On diversity of competition policy regulatory frameworks within

always been successful and have carried significant costs for the overall economy, but Japan's reputation among some of China's political elite, industry officials and business people has remained strong.

Developed countries beyond East Asia have also utilized anti-competitive measures to promote growth and other goals. Although European Union members have relatively strong antitrust regulations, they do not ban cartels when the firms involved have a combined market share below a certain threshold, and laws often permit exceptions when they promote growth or benefit consumers and there is no harm to others.[19] Even the United States, which has the world's most stringent pro-competition policies, has permitted significant exceptions to competition by occasionally allowing cartels in some industries, instituting price controls in the early 1970s in the midst of the oil crisis and using quotas, voluntary export restraints and anti-dumping laws to manage its international trade.[20] But the most famous example of cooperation by market actors is the Organization of the Petroleum Exporting Countries, which has manipulated global oil prices through agreements on production output since its inception in 1960.[21]

Chinese in government and business are acutely aware of these cartels. Multiple interview sources praised Japan and other countries for their governments' activist role and for attempts by their business associations to promote price coordination among members. Since the late 1970s, the Chinese government and Chinese associations have sent numerous delegations to study the chambers of commerce and other similar associations of countries in East Asia, Europe and North America.[22]

East Asia, see Carl J. Green and Douglas E. Rosenthal (eds), *Competition Regulation in the Pacific Rim* (New York: Oceana Publications, 1996).

19 Edward M. Graham and J. David Richardson (eds), *Global Competition Policy* (Washington, DC: Institute for International Economics, 1997), pp. 1–43; Michael Utton, "Going European: Britain's New Competition Law", *The Antitrust Bulletin*, Vol. 45, No. 2 (Summer 2000), pp. 531–51.

20 On the legality of some American cartels, see Peter C. Carstensen and Bette Roth, "The Per Se Legality of Some Naked Restraints: A [Re] Conceptualization of the Antitrust Analysis of Cartelistic Organizations", *The Antitrust Bulletin*, Vol. 45, No. 2 (Summer 2000), pp. 349–435. On the milk industry, see Michael Grunwald, "Milk Price Fight Again Spilling Into Congress", *Washington Post*, 20 September, 1999, p. A1. Some believe that US law has become more lenient toward monopolies and mergers: Eleanor M. Fox, "Mergers R Us", *Washington Post*, 30 March 1997, p. C1.

21 *OPEC: General Information and Chronology: 1960–1994* (Vienna: Organization of the Petroleum Exporting Countries, 1994); and Shukri M. Ghanem, *OPEC: The Rise and Fall of an Exclusive Club* (London: Kegan Paul International, 1987).

22 Ou Xinqian and Du Jinling (eds), *Guowai hangye xiehui ziliao xuan di yi ji* (Foreign Industry Associations: Selected Materials), Vol. 1 (Beijing: China Commercial Publishing House, 1999); Chen Qingtai (ed.), *Shanghui fazhan yu zhidu guifan* (Development and Institution Regulation of Chambers of Commerce) (Beijing: China Economy Publishing House, 1999); Yu Hui, *Hangye xiehui ji qi zai zhongguode fazhan: lilun yu anli* (Industry

The enduring co-existence of these two contending views on the proper behaviour of government and firms is reflected in the compromises regularly found in the laws and regulations that govern competition and pricing in China. This has clearly been in the direction of promoting greater competition and freeing up prices, but at each point exceptions have been maintained. Between 1984 and 1988, China introduced market prices through a dual-track system in which enterprises' above-quota output could be sold at higher market prices, allowing state-owned enterprises to adapt to market prices at the margin. As Table 1 demonstrates, the proportion of goods sold at market prices, measured by transaction value, rose dramatically. The first effort to broadly institute free prices occurred in 1988, but was reversed because of inflation.[23] A renewed attempt was initiated in 1992 and 1993 and was more widely implemented, and there has been less of a reversal since. Nevertheless, there are still some areas (utilities, energy, transportation and some agricultural products) where prices have continued to be administratively set by the State Pricing Bureau and the State Development and Planning Commission. Pricing authorities have also occasionally intervened to re-set prices for goods that are normally allowed to be determined by the market (for example, airline tickets).[24]

In connection with this liberalization, China has passed several laws to promote competition. The Anti-Unfair Competition Law, enacted in 1993, for the first time forbade selling goods at below cost. However, the law made important qualifications, including a stipulation that it had to be demonstrated that the motivation of sellers was to "squeeze out competitors".[25]

Associations and Their Development in China: Theory and Cases) (Beijing: Economic Management Publishing House, 2002).

23 On the policy process behind the 1988 price reforms, see Cheng Xiaonong, "Decision and Miscarriage: Radical Price Reform in the Summer of 1988", in Carol Lee Hamrin and Suisheng Zhao (eds), *Decision-making in Deng's China: Perspectives from Insiders* (Armonk: M. E. Sharpe, 1995), pp. 189–204.

24 By mid-2001, the prices for all but 13 types of commodities and services were liberalized, down from 141 in the early 1990s. Zhao Cheng and Sun Yubo, "State Council Information Office Holds News Conference; State Development Planning Commission Expounds on Issues Related to the List of Prices to be Determined by the Central Government", Xinhua Domestic Service, 11 July, 2001, in *FBIS-China Daily Report*, FBIS-CHI-2001-0711. Also see Jean-Jacques Laffont, *Price Controls and the Economics of Institutions in China* (Paris: OECD, 1997); Li Huizhong, *Zhongguo jiage gaige de luoji* (The Logic of Chinese Price Reform) (Shanxi: Shanxi Economics Publishing House, 1998); and Nicholas R. Lardy, *Integrating China Into the Global Economy* (Washington, DC: Brookings Institution Press, 2002), pp. 24–7.

25 Exemptions were also allowed for products that are fresh and alive, have almost reached their expiration date, are overstocked, seasonal or are sold to repay debts, transfer assets or go out of business. The Chinese text is in *Zhongguo falü nianjian* (Law Yearbook of China) (Beijing: China Law Yearbook Service, 1998), pp. 265–7.

Table 1: Percentage of Goods Sold at Market Prices in China
(by transaction value)

	Agricultural Goods	Retail Commodities	Producer Materials
1978	5.6	3.0	0.0
1985	40.0	34.0	13.0
1988	57.0	49.3	n/a
1989	40.4	45.5	40.0
1990	42.0	45.0	36.5
1991	57.8	68.8	45.7
1992	81.8	93.0	73.8
1993	87.5	93.8	81.1
1994	79.3	90.4	80.0
1995	78.6	88.8	77.9
1996	79.1	92.5	81.1
1997	80.5	93.2	81.6
1998	83.8	94.7	86.0
1999	83.0	95.0	86.0

Sources: For 1978–1993: Lawrence J. Lau, "Gain Without Pain: Why Economic Reform in China Worked", in Wang Gungwu and John Wong (eds), *China's Political Economy* (Singapore: Singapore University Press and World Scientific, 1998), pp. 66–7; for 1994: *Price Yearbook of China 1995*, p. 17; for 1995–1997, *Price Yearbook of China 1998*, p. 413; for 1998: "Fewer than 20 commodities and services have state-controlled prices, survey says", *ChinaOnline* (www.chinaonline.com), 9 October 2000; and for 1999, Nicholas R. Lardy, *Integrating China Into the Global Economy* (Washington, DC: Brookings Institution Press, 2002), p. 25.

The 1998 Price Law, which replaced the 1987 Price Administration Regulations, broke new ground in banning collusion and manipulation of market prices. It specifically bans selling goods at unreasonably high prices or, as will be discussed, at prices below cost.[26] And the law provides for significant penalties for violators, from fines to revocation of their business licences. But like the Anti-Unfair Competition Law, the Price Law requires that collusion and dumping be proved by authorities through obtaining a combination of evidence concerning cost, motive and consequence, which creates a very high burden of proof. In addition to having to prove that products are sold under cost (which is still left undefined) and that companies are doing so in an attempt to get rid of competitors or to monopolize a market, it must also be demonstrated that such activities "disturb the normal order of production operations and harm the national interest and the legal rights of other operators". In addition, the Price Law gives similar exemptions to those provided in the 1993 legislation (for example, for overstocked goods). Finally, the law allows for some degree of intervention in market prices by the government, which is permitted to set prices temporarily when "violent fluctuations in general price levels emerge". And the law creates an opening for associations to coordinate prices by encouraging "industry organizations" to help firms "strengthen price self-discipline".[27]

These laws were primarily the result of debates that occurred within the halls of government which heavily drew upon advice offered by experts, particularly economists and lawyers. Though it is unclear to what extent the drafters considered foreign laws or consulted foreign governments and experts, there are some similarities in the principles of these laws and the relevant portions of Japan's antimonopoly and trade association laws.[28] According to government sources, some state-owned and private companies were consulted during the drafting of both laws, but their contributions appear to have been minimal.

Deflation: The New Threat

A sense of urgency sparked firms into pro-active attempts to influence pricing policies in the late 1990s as a result of the deflationary trends in a wide array of sectors. During the planning era and into the early 1990s, industries regularly had faced shortages, and price liberalization therefore usually threatened to produce inflation, which is what occurred after wide swaths of prices were freed in 1988

---

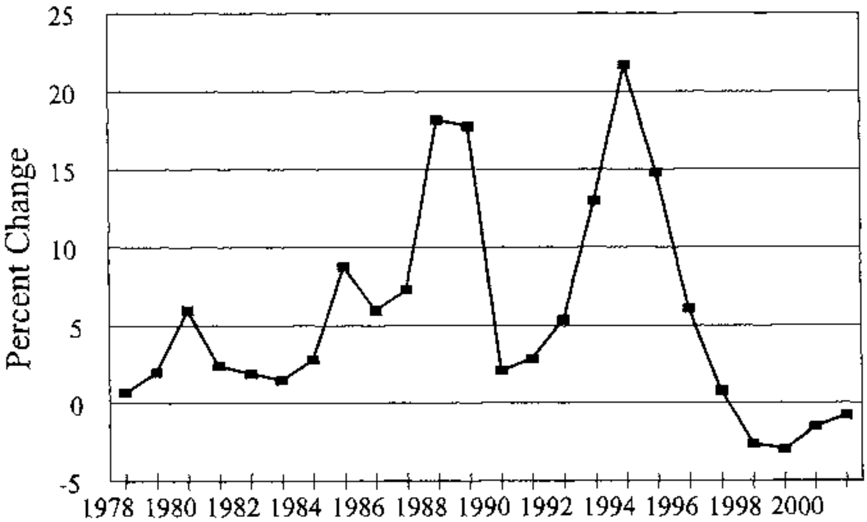
26 Although the law refers to domestically sold goods, it still terms such activity "dumping" (*qingxiao*) or "low-priced dumping" (*dijia qingxiao*).

27 The English and Chinese texts of the law are contained in *China Economic News*, No. 13 (6 April 1998), pp. 9–13, 24–7. Also see Volker Pasternak, "The Right Price", *China Business Review*, Vol. 25, No. 5 (September–October 1998), pp. 40–3.

28 Tilton, *Restrained Trade*, pp. 27–42. It should be noted that China does not have an antimonopoly law. One was supposed to have been drafted along with the 1993 Anti-Unfair Competition Law, but it was shelved because of strong internal government disagreements. Drafting of a completely new version began in the late 1990s, but, in a sign that it will not soon be enacted, it was left off the 1998–2003 agenda of the National People's Congress. See Xue Cheng, "Prices Face Discussion", *China Daily Business Weekly*, 13–19 June 1999, p. 8.

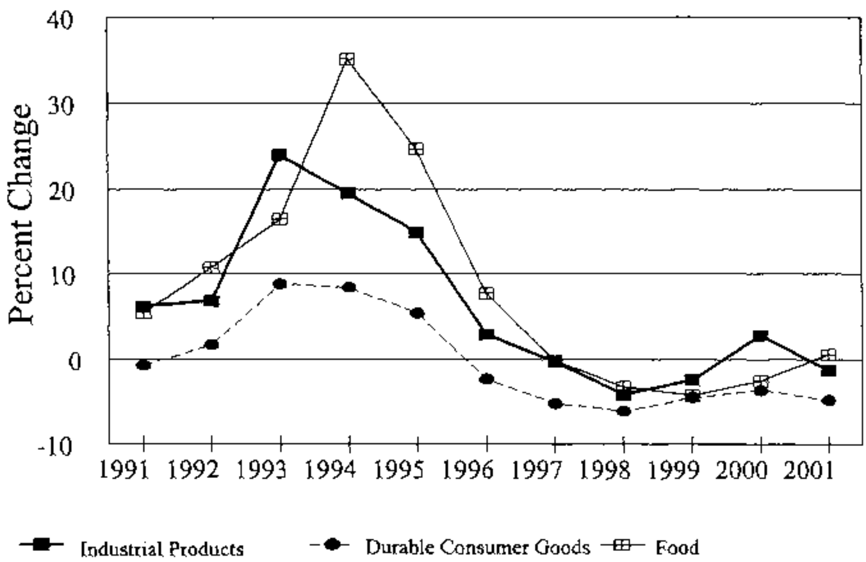
and 1992. However, as supply eventually overtook demand in 1996, prices stopped rising and began to fall (Figure 1) for both industrial and agricultural products (Figure 2).

Figure 1: Annual Change in Retail Prices in China



Source: *China Statistical Yearbook 2001; China Statistical Abstract 2002.*

Figure 2: Annual Price Change of Various Goods in China



Sources: *China Statistical Yearbook 1998, 2001; China Statistical Abstract 2002.*

The downward trend in prices could potentially be explained by political factors. Following a period of retrenchment to counter the previous round of inflation, the top leadership, led by Deng Xiaoping, gave the green light in 1992 to central industrial ministries, local governments and enterprises of all types to expand investment and production. State banks underwrote this investment by extending loans regardless of whether or not the ventures would be profitable.[29] Many industries produced record levels of output, and GNP soared. However, industries continued to expand production in 1995 and 1996, even though demand did not keep pace. When demand stagnated, firms lowered prices. But state-owned enterprises did not heed the signal of falling prices and slow down their production. By mid-1998, according to pricing authorities, 466 of 601 product categories, or 74.2 per cent, were in a state of oversupply.[30]

On the other hand, one could provide an alternative explanation for the deflation: that increased competition in various sectors, coupled with the freeing of prices, led what were monopoly prices to fall to levels more consistent with free market prices.[31] It is also notable that, in addition to domestic factors, the Asian financial crisis of 1997–98 led some of China's competitors to devalue their currencies, temporarily resulting in greater exports to and reduced imports from China. This increased the magnitude of the price drops in several sectors, including steel, electronics and food.

The two explanations conflict. The first argues that prices fell below normal free market levels because of over-investment funded by politically compliant banks, while the second holds that prices settled to market levels. In the late 1990s, China was at a policy crossroads: Should the government allow prices to remain low, knowing that some firms would fail, or should it intervene to prop up prices and stem firms' losses? Since the way in which the government acted would be critically important to companies, they had a clear incentive to influence the policy process.

The Changing Nature and Structure of Government–Business Relations

The general expectation among observers of Chinese politics is that firms would not—and could not—influence the policy process. Because of China's authoritarian political system and the apparent illegitimacy of interest groups, some Western observers have dismissed such participation as a possibility.[32] The

---

29 See Nicholas R. Lardy, *China's Unfinished Economic Revolution* (Washington, DC: Brookings Institution Press, 1998).

30 Liu Yu, "Dijia qingxiao zenme guan" (How to Regulate Low-Priced Dumping), *Fazhi ribao* (Legal Daily), 17 October 1998, p. 3.

31 Lardy, *Integrating China Into the Global Economy.*

32 Lieberthal writes: "Neither in theory nor in practice is individual advocacy or interest-group activity regarded as legitimate": Kenneth Lieberthal, *Governing China: From Revolution Through Reform* (New York: Norton, 1995), p. 181.

dominant view is that policy politics is dominated by policy debates and bargaining *within* the government.[33] But a look at the policy process in the latter half of the 1990s reveals a great deal of pro-active interest articulation within industry, both through intermediaries such as business associations and through direct lobbying by individual firms to influence regulators.

Previous research on Chinese associations has demonstrated their diversity, with some defending their members' interests, others working on behalf of both their members and the state, and still others solely taking directions from the state.[34] It should be noted that business associations in China can also be divided between those that *initially* recruited broadly among enterprises and those whose members are in one narrow line of industry. In the former category are the China Enterprise Management Association (CEMA), which originally only recruited among state-owned enterprises, and the All-China Federation of Industry and Commerce (ACFIC), which had only private companies as members until the late 1980s when it began to actively court state-owned enterprises as well. In the latter category are the approximately 500 national and several thousand local sector-specific trade associations, most of which have members of all ownership forms within a single industry and some of which even have foreign members (for example, in software, consumer electronics and textile associations).

China's system of associations has been described as corporatist. In fully developed state corporatist systems, associations lack autonomy, have compulsory membership, are hierarchically ordered and have jurisdictional monopolies.[35] The vast majority of China's associations, though, are voluntary, are not hierarchically ordered and do not maintain jurisdictional monopolies within their respective regions or sectors. By law, China's trans-sectoral associations do not have authority over each other and do not have authority over

---

33 See note 6, and Murray Scot Tanner, *The Politics of Lawmaking in China: Institutions, Processes, and Democratic Prospects* (Oxford: Clarendon Press, 1998).

34 Gordon White, Jude Howell and Shang Xiaoyuan, *In Search of Civil Society: Market Reform and Social Change in Contemporary China* (Oxford: Clarendon Press, 1996). Also see Vivienne Shue, "State Power and Social Organization in China", in Joel S. Migdal, Atul Kohli and Vivienne Shue (eds), *State Power and Social Forces: Domination and Transformation in the Third World* (Cambridge: Cambridge University Press, 1994), pp. 65–88; David L. Wank, *Commodifying Communism: Business, Trust, and Politics in a Chinese City* (Cambridge: Cambridge University Press, 1999); Margaret Pearson, "The Janus Face of Business Associations in China: Socialist Corporatism in Foreign Enterprises", *The Australian Journal of Chinese Affairs*, No. 31 (January 1994), pp. 25–46; Jonathan Unger, "'Bridges': Private Business, the Chinese Government and the Rise of New Associations", *The China Quarterly*, No. 147 (September 1996), pp. 795–819; and Kenneth W. Foster, "Embedded within State Agencies: Business Associations in Yantai", *The China Journal*, No. 47 (January 2002), pp. 41–65.

35 The standard definition of corporatism is found in Philippe C. Schmitter, "Still the Century of Corporatism?" *The Review of Politics*, Vol. 36, No. 1 (January 1994), pp. 93–4. Lack of autonomy only applies to state, not societal, corporatism.

sectoral associations; and national associations do not have control over regional ones.[36] The strongest basis for claims of corporatism is the limited freedom of most business associations from government control.[37] However, there is significant variation in the associations' autonomy, which can be measured according to their origins, affiliation, staffing and financing. Almost all business associations are required to register and be affiliated with a government agency, and most, though not all, have been founded by some branch of the government. There is greater variance in staffing and financing. While most associations have retired officials in leadership positions, executives from member firms often hold influential positions. And pushed by the government's own budget shortfalls and pulled by the opportunity to increase their income, the financial umbilical cord that used to tie associations to the government has in many instances been severed.

The primary goal of the government when it set up associations was to have them assist in its regulation of the economy. To the extent that associations were conceived of as representing their members, these interests were seen as fundamentally consistent with those of the state. This official perception of the convergence between business and government interests legitimates the state's involvement in the associations.[38] But businesses' increasing sense of self-interest

---

36 The 1989 and 1998 "Regulations on the Registration and Regulation of Social Organizations" (*shehui tuanti dengji guanli tiaoli*) both discourage the formation of "identical" (*xiangtong*) associations in the same jurisdiction; however, this requirement is generally not followed in practice. The 1989 version, issued 25 October 1989, is contained in Wang Huaian et al. (eds), *Zhonghua renmin gongheguo falü quanshu 2, 1986–1989* (Collection of the Laws of the People's Republic of China, Vol. 2, 1986–1989) (Beijing: Jilin People's Publishing House, 1990), pp. 884–6. The 1998 version, issued 25 October 1998, is carried in *Fazhi ribao* (Legal Daily), 4 November, 1998, p. 3. In early 2001 tentative steps were taken to create a more hierarchical system when nine of the State Economic and Trade Commission's industrial bureaus were eliminated and replaced with associations; at the same time, some of these associations were given regulatory authority over more narrowly gauged trade associations. The genuine consequence of these changes for relations between associations is unknown. State Economic and Trade Commission, "SETC Distributes Idea on Entrusting Regulation of Industry Associations", 28 February, 2001, available on the SETC's web site (www.setc.gov.cn).

37 Margaret Pearson, "The Janus Face"; White, Howell and Shang, *In Search of Civil Society*; Ole Bruun, *Business and Bureaucracy in a Chinese City: An Ethnography of Private Business Households in Contemporary China* (Berkeley: Institute of East Asian Studies, 1993); Unger, "Bridges"; Jonathan Unger and Anita Chan, "Corporatism in China: A Developmental State in an East Asian Context", in Barrett L. McCormick and Jonathan Unger (eds), *China After Socialism: In the Footsteps of Eastern Europe or East Asia?* (Armonk: M. E. Sharpe, 1996), pp. 95–129.

38 Shi Zuoting, "Jiakuai fazhan wanshan guanli cujin zhengfu zhineng zhuanbian" (Speed Up Development, Perfect Regulation, Promote the Transformation of Government Functions), *Zhongguo jingmao daokan* (China Economy and Trade Reporter), 15 March 1999, pp. 14–15.

and rights distinct from and potentially in conflict with those of the state has led to a greater questioning of whether officials should have a role in associations. Many believe associations should only defend their members' rights, and to do so they need to be independent; otherwise, they inevitably become "second governments".[39]

This conflict in goals has meant that associations with little autonomy have great difficulty mobilizing their members, while those with more autonomy have more membership support and are more active. The more independent associations are able to exist in industries that are dominated by domestic and foreign private companies (for example, software), whereas industries heavily populated by state-owned enterprises (for example, steel) have far weaker and more quiescent associations.

Despite this variation, most business associations in China are generally still relatively weak and undeveloped. Because of restraints on associations' activities, companies, both state-owned and private, primarily try to influence government policy through direct contacts rather than through associations. Direct ties are also encouraged by the history of links between government agencies and state enterprises and by government agencies' worries about ceding their authority to associations. Large private and foreign companies have followed the state enterprises in establishing contacts with their regulators. Just as important has been the government's increasing willingness to obtain enterprises' inputs *prior* to policy decisions. Such exchanges of opinion are initiated by both sides and occur during the consideration of specific laws and regulations. They also take place as part of the regular process of regulatory oversight and sometimes prompt a new policy initiative. Many large companies have representative offices in Beijing, and those that do not can send delegations to the capital or communicate in writing or electronically.[40]

Through both associations and direct links, large companies have influenced policies in an array of sectors and issue areas, including intellectual property rights, advertising, securities, taxation, technical standards, international trade, and pricing. So, although associations have not uniformly matured and the state is

---

39 Zhang Delin, "Chongfen fahui hangye xiehui de zuoyong" (Fully Develop the Role of Industry Associations), *Qiye gaige yu guanli* (Enterprise Reform and Management), July 1996, pp. 21–4; Shen Li, "Si fangmian fuzhi zhongxiao qiye" (Four Ways to Foster Small and Medium Enterprises), *Zhongguo gongshang shibao* (China Business Times), 6 April 1999, p. 2; Lu Fengtai (ed.), *Shehui zhongjie zuzhi yanjiu* (Social Intermediary Organizations Research) (Shanghai: Xuelin Publishing House, 1998); and Yu Hui, *Hangye xiehui ji qi zai zhongguode fazhan* (Industry Associations and Their Development in China).

40 The predominance of direct lobbying also conflicts with descriptions of China's government–business relations as corporatist. In corporatist systems of Europe and Latin America, although direct contact between firms and government occurs, associations are the primary vehicles for industry influence and government regulation. That is the case in very few industries in China.

still formally authoritarian, there have been clear signs of growing business influence.

That does not mean that either the government or industry is satisfied with the status quo. To the contrary, the central government's concern with promoting associations has grown significantly. In the past decade, associations have been the subject of research groups and national conferences, and senior leaders have mentioned the issue with increasing specificity and frequency.[41] A clearer recognition of the need for action emerged as a result of the central government's March 1998 restructuring that eliminated some industrial ministries while turning others into less powerful and smaller bureaus of the State Economic and Trade Commission (SETC). The commission's range of authority grew, but the resources available to it (and to ministries) to closely regulate industry did not expand but, in contrast, dropped. Thus, many in the central leadership, the SETC and the ministries wanted to encourage associations to take up the slack to avoid the creation of a regulatory vacuum.

Given their focus on direct lobbying, enterprises had shown that they were not content with the state of associations either. For their interest in associations to grow, the associations would have to be permitted to have broader authority on the array of issues that affected their industries. Thus, by coincidence, two issues were conjoined in 1998. While price deflation intensified, government restructuring reduced its capacity to regulate firms. Thus, to the above question of whether or not to respond to the price deflation was added another: how? Up until 1998 the pricing authorities, headed by the State Development and Planning Commission, had administratively intervened directly. Perhaps it was time for a change.

Self-Discipline Prices

Association-led cartels became the dominant vehicle for attempting simultaneously to solve the problems both of deflation and of an emerging regulatory vacuum. In so doing, the policy of cartels met the interests of associations, many companies and certain government agencies. Interviews have revealed the depth of large companies' influence on policy, how this magnified the fragmented nature of the policy process and the deep-seated conflict over norms of competition and cooperation.

Pre-1998 Attempts at Cartels

Cartels were not new to China in 1998, but previous efforts to set up cartels were primarily local and did not affect the national economy. They were largely

---

[41] Ou Xinqian and Du Jinling (eds), *Zhongguo hangye xiehui: gaige yu tansuo* (Chinese Industry Associations: Reform and Exploration) (Beijing: China Commercial Publishing House, April 1999); Lu Fengtai, "1996 hangye guanli luntan kaimu" (1996 Forum on Industry Regulations Opens), *Renmin ribao* (People's Daily), 19 November, 1996, p. 2.

initiated by enterprises and on occasion were justified by reference to foreign examples. In Wenzhou, Zhejiang, home to one of the largest concentrations of private firms in the country, the local Price Bureau gave local associations authority to set "industry negotiated prices" in the early 1990s. It is not known how many of these successfully formed cartels, but it appears that at least some of Wenzhou's many industry associations made the attempt.[42] Officials from the State Economic and Trade Commission visited the city in 1996 and 1997 to study Wenzhou's experience. Brick and tile makers elsewhere in Zhejiang in 1992 and 1993 attempted to institute cartels, what they called "mini-OPECs".[43] Another publicized case was the creation in Sichuan in 1997 of a cartel for steel strips and pipes. Organized at the initiative of both private companies and state enterprises, the cartel required members to submit deposits, which they forfeited if they were found to have sold steel below the agreed price floors. Coupled to long-term sourcing arrangements with larger steel producers, the cartel apparently worked, and attracted national attention.[44]

The most significant early nationwide attempt to establish price cartels occurred in the video compact disk player industry. Faced with an influx of large numbers of small producers and falling prices, the China Electronics Chamber of Commerce's magazine, *Shijie dianzi kuaixun* (World Electronics Express), organized an industry "roundtable" in Guangdong in mid-1997. The twenty-two participants drafted and signed a "China VCD Enterprise Competition Self-Discipline United Manifesto (*Zhongguo VCD qiye jingzheng zilu lianhe xuanyan*) that called not only for floor prices but also for ethical advertising and other elements of fair competition. It gave the *Shijie dianzi kuaixun* and a board of signatories to the cartel the right to monitor and report on firms' behaviour and to "castigate" (*bianda*) violators. The companies voluntarily signed the manifesto, but, in a pattern to be repeated in other industries, violations occurred soon after.[45]

Pressure for and Initiation of the Self-Discipline Price Policy

As the impact of deflation in China deepened in late 1997 and early 1998, pressure on the government to take action intensified. A key source of pressure was the makers of farming vehicles, whose losses skyrocketed in 1997. They and a subsidiary of the Farm Machinery Industry Association pressed the idea of a

---

42 On the development of associations in Wenzhou, see Ou and Du, *Zhongguo hangye xiehui*, pp. 182–223.

43 White, Howell and Shang, *In Search of Civil Society*, pp.149–50.

44 Zhong Guizhao, "Hangye zilü gongmou fazhan" (Industry Self-Discipline Collectively Planned and Developed), *Zhongguo jingmao daokan* (China Economy and Trade Reporter), 15 January 1999, pp. 29–30.

45 "1997 nian VCD shi da xinwen" (1997 VCD Top Ten News), *Zhongguo dianzi bao* (China Electronics News), 2 January 1998, p. 12. The text of the manifesto is available from the author.

cartel on the State Bureau of Machinery Industry, which in turn received approval from some members of China's political elite.[46] In June 1998, the association announced a deal among the industry's top nineteen producers to adopt price floors for three-wheeled farming vehicles and to require those who sold vehicles below the floors to pay penalties as decided by the association.[47]

Around the same time, China's industrial elite began to exert pressure. The head of one of the country's largest steel makers met with and convinced a senior SETC official that their losses were mounting as a result of dumping by smaller steel mills and cheap imports and that some sort of cartel arrangement would be necessary to restore order to the market.[48] The most dramatic lobbying occurred in late July 1998 when thirteen enterprises from a variety of industries submitted a joint appeal on their own initiative to the SETC calling on it to help stem deflation and "standardize market order" by encouraging associations to organize price cartels. They characterized the low prices as signs of "dumping", "vicious competition" (*exing jingzheng*) and "disorderly competition" (*wuxu jingzheng*).[49] Supplementing the voices of large businesses, many association leaders also proactively pushed for association-organized cartels, in part because they saw such a step as a way to augment their association's previously meagre powers.

According to several interview sources, the various appeals had a significant effect on the SETC leadership's thinking in mid-1998. The SETC was open to

---

46 Early in 1998 Wu Bangguo, a Standing Politburo member and the senior leader responsible for industrial affairs, supported strengthening associations in speeches and endorsed price cartels. Little is known of Zhu Rongji's position, but one well-placed source said he believes Zhu did not support the policy.

47 "Zilü xiaoshou jiage" (Self-Discipline Sales Price), *Jingji ribao* (Economic Daily), 27 July1998, p. 2; Ai Jun, "Jiage zhan che kaichu migong"; Xu Qionglin and Chen Hexin, "Xiehui gao zilüjia jiwei yiwei butuo" (SDPC Believes Association Making Self-Discipline Prices Inappropriate), *Zhonghua gongshang shibao* (China Business Times), 6 November 1998, p. 1.

48 One association to which this enterprise belonged advocated forming an independent "sales alliance" among the largest producers without involving the government, but no agreement could be reached as to how the alliance would run and what products would be included.

49 The group was led by E'erduosi Wool Group, which drafted its own separate appeal and coordinated the writing and submission of the joint letter. The other signatories were Sichuan Changhong Electronics Group, Chunlan Group, Guizhou Maotai Brewery, Tsingtao Beer Group, Idall Electronics, Tianjin Auto Industrial Group, Monkey King Group, Guangxi Yucai Machinery Co., Shanghai No. 1 Department Store, Beijing Wangfujing Department Store, Shenyang Zhongxing Commercial Building Co., and Dalian Department Store. See Yang Boxian, "Guifan shichang zhixu zhizhi wuxu jingzheng" (Standardize Market Order, Stop Disorderly Competition), *Zhongguo jingmao daokan* (China Economy and Trade Reporter), 30 September 1998, p. 22; Lu Zheng (ed.), *Zhongguo gongye fazhan baogao 1999: gaobie duanque jingjide zhongguo gongye* (China Industry Development Report 1999: Good-bye to Chinese Industry's Shortage Economy) (Beijing: Economic Management Publishing House, 1999), pp. 132–3.

such suggestions for its own reasons. Government restructuring had increased its authority over industrial policy, but in the past industrial policy did not include adjusting prices, which fell under the jurisdiction of the State Development and Planning Commission (SDPC). In fact, in late June 1998 the SDPC issued a regulation jointly with the State Building Materials Bureau prohibiting the dumping of flat glass, which stressed the authority of the SDPC and local pricing bureaus in regulating prices.[50] The SETC, by promoting association-led price cartels, would now have a chance not only to redraw the boundaries of industrial policy but also to enhance its own power. The SETC was also motivated by the mounting losses of state enterprises, which meant a decline in tax revenues and, if unemployment rose, greater labour unrest. Finally, according to interviewees, some in the SETC saw the policy as a way to "enliven" associations, many of which had yet to become either important avenues of state control or business representation.

Responding to the outside pressure and acting in its own interests, SETC director Sheng Huaren told provincial and city officials in early August to encourage a small number of associations to set "enterprise self-discipline prices" for their own products.[51] Two weeks later, the SETC issued its "Idea on Instituting Industry Self-Discipline Prices for Some Industrial Products". This document called on industrial bureaus and industry associations to help coordinate the prices of twenty-one products, using the industries' average costs as the basis for the price floors.[52] Critically, it used the Price Law's permission for associations to encourage price self-discipline to provide its policy with a stronger legal foundation. The SETC circulated the document to ministries over which it had no direct control, encouraging them to apply the proposal to other products. As a review of cartel efforts from the early 1990s to the early summer of 1998 shows, the SETC directive of August 1998 came after some industries had already initiated attempts to set price floors; however, it lent further legitimacy to these attempts and led others to follow suit. As Table 2 shows, nine

---

50 "Jinzhi pingban boli dijia qingxiao exing jingzheng" (Prohibit Low-Priced Dumping and Vicious Competition of Flat Glass), *Jingji ribao* (Economic Daily), 27 June 1998, p. 1.

51 Sheng placed his instructions in the context of the SDPC–State Building Materials Bureau joint regulation of late June 1998, but, in a critical twist, he stressed the role of associations, not government pricing authorities. Ai Jun, "Jiancai jiage zhan ting huo" (Building Materials Price War Flame Extinguished), *Zhongguo jingying bao* (China Business), 18 August 1998, p. 4.

52 The list of products was based on suggestions from enterprises, associations, and government agencies. For the list of products, see Yang Xiaoping, "Dijia qingxiao kewang jiesu" (Low-Price Dumping End in Sight), *Zhonghua gongshang shibao* (China Business Times), 10 September, 1998, p. 2. Also see Chen Bangzhu, "Jiaqiang hangye jiage zilü guifan shichang jingzheng zhixu" (Strengthen Industry Price Self-Discipline, Standardize Market Competition Order), *Zhongguo jingmao daokan* (China Economy and Trade Reporter), 15 October 1998, pp. 4–5.

of the fifteen documented cartels in which associations became involved in 1998 emerged after the SETC's statement was issued. In some cases the associations were quite proactive (for example, those related to farm vehicles and polyester strips), while in others cases associations were involved but took a back seat to ministries and pricing authorities (for example those related to colour televisions). Although some local associations attempted to form cartels during this period on their own accord, most cartels in 1998 were initiated by national associations. This made sense for two reasons: national association members comprised the industries' most important firms; and many industries simply did not have local associations. Nevertheless, in every instance, pro-price-control enterprises were deeply involved in advocating and forming the cartels.[53]

Table 2: Attempted Price Cartels Involving Associations in 1998

Date Initiated	Product	Association Involved	Government Agency Involved	Information Source
Early 1998	Colour televisions	China Video Association	Ministry of Electronics Industry	Interview
May 1998	Specialty steel	China Specialty Steel Enterprise Association	State Bureau of Metallurgy Industry	Interview
28 Jun. 1998	Farm vehicles	Farm Machinery Industry Association Farm Transport Vehicle Sub-Association	State Bureau of Machinery Industry	*Jingji ribao*, 27 Jul. 1998
25 Jul. 1998	Beer	Fujian Beer Association	Provincial Economic and Trade Commission	*Zhongguo jingmao daokan*, 30 Nov. 1998, pp. 28–9.

[53] In the case of standard steel products, the relevant association at the time, the China Metallurgy Enterprise Management Association, was viewed as so irrelevant by its members that price control advocates bypassed it in favour of directly lobbying the SETC and the State Bureau of Metallurgy Industry. Four large supporters who complained loudly about the unfair low prices of competitors selected the three products (wire rod, rebar and hot-rolled coils) for which price floors were set in September 1998. See "Guojia jiwei, guojia yejiju lianhe fabu zhizhi dijia qingxiao gangcai zhanxing guiding" (SDPC and SBMI Issue Joint Temporary Regulation on Stopping Low-Priced Dumping of Steel Products), *Zhongguo yejin bao* (China Metallurgy News), 27 September 1998, p. 1.

28 Jul. 1998	Detergent	China Wash Products Industry Association	None	*Zhongguo jingmao daokan*, 30 Nov. 1998, p. 25
Mid-1998	Soda ash	China Soda Ash Industry Association	State Bureau of Petrochemical Industry	*Zhongguo jingmao daokan*, 30 Nov. 1998, p. 25
18 August 1998: SETC "Idea" Issued				
1 Sep. 1998	Shipping service	Unnamed Qingdao shipping association	n/a	*Zhongguo shibao*, 1 Sep. 1998, p. 2
Sep. 1998	Sugar	China Sugar Association	n/a	*Zhongguo shibao*, 23 Sep. 1998, p. 1
1 Oct. 1998	Small cars	China Automobile Industry Association	State Bureau of Machinery Industry	*Asian Wall Street Journal*, 1 Dec. 1998, p. 11
Oct. 1998	Colour televisions	China Electronic Video Industry Association	Ministry of Information Industry	Interview
Oct. 1998	Stainless steel billet	China Specialty Steel Enterprise Association	State Bureau of Metallurgy Industry	*Zhongguo yejin bao*, 20 Oct. 1998 p. 1.
Autumn 1998	Ostriches	China Ostrich Association	n/a	*Asian Wall Street Journal*, 1 Dec. 1998, p. 11
Autumn 1998	Paging service	Unnamed Shanghai paging association	n/a	*Zhongguo jingying bao*, 13 Nov. 1998, p. 18
25 November 1998: Joint SETC– SDPC "Regulation" Issued				
Dec. 1998	Stainless steel	Ouhai (Wenzhou) Stainless Steel Chamber of Commerce	Municipal administration of industry and commerce	Interview
Late 1998	Polyester strips	China Chemical Fibre Association	State Bureau of Textile Industry	Interview

Note: This list is necessarily partial. A more systematic review of the media and further interviews would probably reveal other cases. The most precise date is given for when cartels were initially attempted. In most cases, firms met on more than one occasion. "N/a" is given when it could not be determined which government agency was the primary regulator involved or if one was involved at all. Most of the cases listed here were identified from multiple sources, but only one source is listed for brevity's sake.

Conflict and Reversal

Almost as soon as the policy was unveiled, opponents quickly surfaced among enterprises, within the government and from within academia. In particular, the more efficient state-owned and private firms in a variety of industries baulked at price floors since they were capable of selling goods at a profit below the floor; price floors only benefitted their more inefficient competitors.

The farm vehicle industry served as a test case and ignited national debate. One of the original supporters of the price floors, the Shifeng Group, broke the June 1998 agreement, after which the association fined it several hundred thousand yuan. In what one former industry official says was an increasingly common strategy, the Shifeng group played on internal government rivalries by lodging complaints with the local and provincial pricing authorities. The latter determined that the price floors violated "normal competition" and in September 1998 asked the SDPC to investigate.[54] The SDPC quickly sent an investigation team to Shifeng's factory in Shandong and over the next two months attended meetings on the self-discipline price policy with firms, experts and the SETC. The Farm Transport Vehicle Sub-Association's chief defended its actions, saying Shifeng had strongly supported the price floors at prior meetings and that the association had received SETC approval before it fined Shifeng for its violations. Shifeng countered that the price floors were set above its own costs and that it had to lower its prices to clear inventory. Playing on the SDPC's interest in maintaining authority over the regulation of prices, Shifeng charged that the fines were against the law because they were not invoked by government pricing authorities as specified in the Price Law.[55]

The Shifeng case touched off a national debate. On one side stood controlled-market forces made up of large enterprises that were either inefficient or bent on gaining a greater market share through cartels, industry associations,

---

[54] Liu Jian and Zhang Shenjin, "'Zilüjia' chushile" ("Self-Discipline Prices" Have Accident), *Zhongguo gongshang shibao* (China Business Times), 17 September 1998, p. 1.

[55] Xu Qionglin and Zhang Shenjin, "Sanlun nongyongche 'zilüjia': lisizhang you shuofa" (Three-Wheeled Farm Vehicle "Self-Discipline Price": President Has Explanation), *Zhongguo gongshang shibao* (China Business Times), 21 September 1998; Yang Boxian, "Sanlun nongyongche jiage zilü shijian 80 tian" (Three-Wheeled Farm Vehicle Price Discipline Carried Out 80 Days), *Zhongguo jingmao daokan* (China Economy and Trade Reporter), 15 November 1998, pp. 30–1.

and the SETC. On the free-market side stood the more efficient state-owned and private companies, some associations, economists and the SDPC.

The first issue was how to characterize the price trends. As noted, those who were in support of price controls saw the price drops as dumping below reasonable costs, which had been made possible by state banks and by state enterprises' soft budget constraints. The other side held that price competition had only eliminated the monopoly rents that had existed for so long and argued that prices were not too low; rather, due to inefficiency, the cost structures of most state enterprises were too high.

They also disagreed about the benefits and costs of competition and cooperation. Price-control advocates characterized the deflationary price competition as "blind" and "irrational" and as "fratricidal fights".[56] Ideally, competition should lead to the elimination of inefficient firms, but, since state enterprises are not responsible for their losses, "'prices that leap off buildings' [quickly falling prices] have not caused men [state enterprises] to leap off buildings" and go out of business. Such competition only led to greater enterprise losses and declining tax revenues.[57] Thus, price-cartel advocates argued that cooperation between firms was needed and that companies also needed to compete more on quality and less on price.[58]

By contrast, the free-market advocates praised price wars as beneficial for pushing forward industrial restructuring and improving efficiency, something cartels would only make more difficult by enabling inefficient companies to remain in the market.[59] As one association leader who opposed cartels wryly remarked to me, with price controls "those that should die won't; those that should live don't live well". They accused pro-cartel firms of just trying to protect their profits at the expense of consumers; they accused associations and their government patrons of being motivated more by a chance to assert their

---

56 "Too Many Price Cuts Hurt Market", *China Daily*, 12 September 1998, p. 4; Lu Jingxian, "Firms' 'Price War' Should be Regulated", *China Daily*, 14 September 1998, p. 4.

57 Han Zhenjun, "Jiaqiang hangye zilü zhizhi exing jingzheng" (Strengthen Industry Self-Discipline, Stop Vicious Competition), *Zhongguo gongshang shibao* (China Business Times), 21 September 1998, p. 2. The SETC reported that profits for industrial SOEs in the first eight months of 1998 dropped RMB 32.1 billion, and blamed the decline entirely on price wars. See Chen Bangzhu, "Jiqiang hangye jiage zilü guifan shichang jingzhang zhixu".

58 A manager of one of China's largest department stores appeared overly caught up in the moment when he reportedly said, "We never consider price cuts as an effective way to attract more customers". Wang Chuandong, "Retailers to Impose Market Order", *China Daily Business Weekly*, 18–24 October 1998, p. 6.

59 Liu Jian, "Ruhe kandai 'zilüjia'?" (How Should "Self-Discipline Prices" Be Seen?), *Zhongguo gongshang shibao* (China Business Times), 20 October 1998, p. 2; Lin Yifu, "Jiage zilü: yi you fu lie bu yi xing" (Price Self-Discipline: Repress the Excellent Support the Inferior Difficult to Implement), *Zhongguo gaige* (China Reform), January 1999, pp. 13–14.

authority and improve their own income (through fines) than by genuine concern for the economic well-being of the country.[60] The free-market advocates also dismissed the benefits of foreign cartels, saying few, if any, have succeeded in halting price slides.[61]

In late October 1998, the SDPC sided with the Shifeng corporation, concluding that the dumping charge was invalid. It found that the association had violated the rights of firms to set their own prices and had bypassed the authority of pricing authorities and the SDPC to regulate and punish those engaged in unfair market activities.[62] Amazingly, despite its well-deserved reputation as a supporter of planning and government intervention, the SDPC in this case took the posture of a free-market advocate by opposing a cartel.

The mounting opposition to association-led price controls helped to resolve the conflict with the SETC over jurisdictional boundaries in the SDPC's favour. In late November 1998, the two organs jointly issued a "Regulation on Stopping Unfair Price Activity on Low-Priced Dumping of Industrial Goods", marking the end of *formally* sanctioned price cartels. The new regulation retreated from the August 1998 SETC policy in two ways. First, it scaled back the authority of the SETC, industrial ministries and associations on pricing matters. Henceforth, they could only monitor price trends and offer suggestions to pricing authorities, who would have the right to regulate prices, determine if dumping had occurred and punish violators. And second, it restored the Price Law's very high standard of proof of dumping. It also stressed that a company could not be charged with dumping if its prices were below an industry's average costs but higher than its own production costs.[63]

---

60 Wang Lei, "Zilü weishenme" (Why Self-Discipline), *Zhongguo gongshang shibao* (China Business Times), 27 October 1998, p. 7; Shi Yan, "Hangye 'zilü jiage' ji qi beihou" (Industry "Self-Discipline Prices" and Their Background), *Gaige* (Reform), January 1999, pp. 6–8.

61 Li Jianlin, "New Rule Expected to Ease Price War", *China Daily*, 28 December, 1998, p. 4. Advocates and opponents of cartels squared off at a conference hosted by the SETC in late November 1998. Participants included officials from the SETC and SDPC, several academics and leaders of some associations, and one pro-cartel state-owned enterprise, Changhong Electronics. Excerpts of statements from the conference are contained in "Quanmian renshi jiage zilü" (Fully Understand Price Self-Discipline), *Zhongguo jingmao daokan* (China Economy and Trade Reporter), 15 December 1998, pp. 18–22.

62 Xu Zionglin and Chen He Xin, "Xiehui gao zilüjia jiwei yiwei butuo".

63 The text of the regulation and an SDPC spokesperson's explanation is carried in *Zhongguo gongshang shibao* (China Business Times), 8 December 1998, p. 2. The SDPC independently issued another anti-dumping regulation in August 1999 that demonstrated more clearly its leading role in regulating pricing activity. The text is carried in *Jingji ribao* (Economic Daily), 5 August 1999.

The vanquishing of the self-discipline price policy initially seemed a complete victory for the free-market forces. However, it soon became clear that this reversal meant primarily a change of form and not of substance. The SDPC, which had sided with efficient firms and attacked cartels on free-market principles, soon proceeded to expand its intervention in the prices of various sectors as it had done in the flat glass and steel sectors. In mid-December, following a further fall in farm vehicle prices, seven producers lobbied the Machinery Bureau to re-intervene. So, in early January 1999, over a dozen farm vehicle makers, their association, the Machinery Bureau, the SETC, the SDPC and pricing authorities all met in Beijing to set price floors.[64] In addition to continuing to periodically coordinate the prices of some steel products with the State Bureau of Metallurgy Industry, the SDPC became involved in 1999 in setting floor prices for colour televisions and other products.[65] The SDPC had not opposed *what* the ministries and associations had done; it opposed *how* they had done it. It appears the SDPC just wanted a piece of the action.

Economic and Political Consequences

While some prices halted their slide after the self-discipline price policy went into affect, the success of the controls was momentary. In most of the sectors in which price cartels were attempted, prices continued to fall during 1998 and 1999. Even in sectors dominated by state-owned enterprises, such as the steel industry which set price floors for several products including wire rod in late September 1998, prices rose only briefly before continuing their decline (Figure 3). The SDPC's own attempts to institute price floors in 1999, in the wake of the self-discipline battle, fared no better. In the most amazing case, the agency set price floors for colour televisions that were lower than the current prices in stores. Companies followed the unintentional signal and dropped their prices, even below the SDPC's figure, leading one company executive to shake his head at the SDPC's "loss of face".[66]

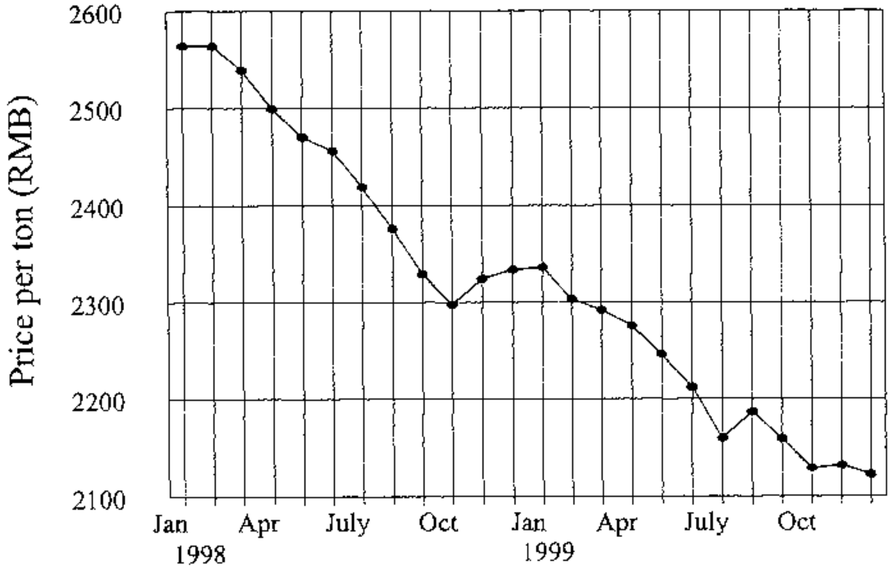
---

64 Liu Run, "Zilü shaobujin chunfeng chui you sheng" (Self-Discipline Can't Be Burned Out, Spring Wind Blows It Back to Life), *Zhongguo gongshang shibao* (China Business Times), 20 January 1999, p. 2.

65 "Guojia yejinju fabu xiancai, luowengang, rezha juanban hangye pingjun shengchan chengben" (SBMI Issues Industry Average Production Cost for Wire Rod, Rebar, and Hot-Rolled Coils), *Zhongguo yejin bao* (China Metallurgy News), 15 April 1999, p. 1; "Daji dijia qingxiao xian na caidian kaidao" (Strike Low-Priced Dumping First Operate on Colour TVs), *Zhongguo gongshang shibao* (China Business Times), 9 April 1999, p. 2.

66 The SDPC investigated the TV firms but never issued a verdict or penalized them. "Caidianye xin yilun jiage dazhan baofa" (Colour TV Industry: A New Round of Price Wars Breaks Out), *Zhongguo jingying bao* (China Business), 27 April 1999, p. 1.

Figure 3: Wire Rod Average Price in China



Source: Japan Iron and Steel Federation, "Collection of Materials and Statistics on China's Iron and Steel Industry and Iron and Steel Policy", October 2002, pp. 29–30.

Most Chinese commentators blame the failure of self-discipline prices on the limited powers of Chinese associations. Interviewees repeatedly bemoaned the associations' lack of "restraining power" (*yuesuli*) over their members and contrasted their predicament with the strength of associations in Japan, Europe and elsewhere. They also contrasted the success of price coordination efforts by what they perceived to be more autonomous local associations, such as those in Wenzhou, with the failed attempts of less independent national associations. As one central government source said, "a reform of associations did not arrive on time". The SDPC's equally poor record was blamed on its own declining powers vis-à-vis other bureaucracies and companies, and on its limited ability to keep abreast of market trends and enforce penalties, which had been made harder by the recent rise in the standard needed to prove dumping.

A more compelling explanation for the widespread failure of Chinese price cartels is the extremely low concentration of production in Chinese industries. For example, in 1997 China's top four steel enterprises combined only produced

29 per cent of the country's finished steel, down from 33 per cent in 1990.[67] These concentration levels in the steel industry are low by international standards, and this is true, too, for many other industries in China.[68] In his study of Japanese cartels, Mark Tilton credits high concentration rates, supplemented by a "high-tech hook" and downstream cartels or import protection, with the relative success of cartels in Japan's basic materials industries.[69] High concentration means that the behaviour of only a few producers needs to be monitored. As the number of producers increases, the chances of cheating rise. Interviewees in large Chinese companies and in some associations charged that small township and village enterprises bore responsibility for falling prices and the collapse of cartels, whereas in reality firms of all stripes—small and large, state-owned and private—were not immune from the impulse to cheat and sell at prices set below those of their competitors. Even some of the strongest advocates for cartels, caught in a game of prisoner's dilemma, dropped prices soon after pledging to abide by price floors. And some advocated price floors in order to gain a temporary advantage over competitors by being the first to drop prices.[70]

Cartels were only successful in sectors that were regionally concentrated or in which a small number of large firms controlled the national market. Wenzhou's cigarette lighter association has successfully set floor prices, not because of the association's autonomy and its high proportion of private members, but because Wenzhou accounts for almost all of China's production of lighters. The China Chemical Fibre Association, closely connected to the former Ministry of Light Industry, reportedly achieved a rare success in instituting a cartel for polyester strips and later for viscose filaments, because both products

---

67 *Zhongguo gangtie gongye nianjian 1998* (Yearbook of the Iron and Steel Industry of China 1998) (Beijing: State Bureau of Metallurgy Industry, 1998), pp. 72, 113–14.

68 A list of 4-firm and 8-firm concentration levels for a cross-section of industries in 1990 and 1996 is contained in Chen, Jiagui (ed.), *Zhongguo gongye fazhan baogao 1998: zhidu chuangxin, zuzhi bianqian yu zhengce tiaozheng* (China Industry Development Report 1998: Institutional Innovation, Organizational Changes and Policy Adjustments) (Beijing: Economic Management Publishing House, 1998), pp. 391–3. For a comparison of concentration levels between China, Japan and the United States in several machinery products, see Lu Zheng (ed.), *Zhongguo gongye fazhan baogao 2002: WTO guize xiade qiye he zhengfu xingwei* (China Industry Development Report 2002: Enterprise and Government Behavior under WTO Rules) (Beijing: Economic Management Publishing House, 2002), p. 157.

69 Tilton, *Restrained Trade*, pp. 190–211. Schaede agrees, arguing that cartels in Japan have been successful in industries "dominated by a few large firms, with high barriers to entry and low imports": Schaede, *Cooperative Capitalism*, pp. 21–2.

70 Sichuan Changhong Electronics is perhaps the most egregious case, alternating between undercutting fellow colour television makers at one moment and demanding price floors and penalties for violators the next. See Xu Guangjian and Li Huihua, *Zhongguo jingjide kunhuo yu chulu* (Black Hole of Finances: The Chinese Economy's Puzzle and Way Out) (Guangdong: Zhuhai Publishing House, 1998), pp. 5–17; and "Quanmian renshi jiage zilü".

are dominated by a handful of firms. In short, the responsibility given in 1998 to Chinese associations would, in less concentrated industries, very likely be beyond the capabilities of most industrial associations anywhere else in the world.

Despite the inaccuracy of the charge, laying the blame for the cartels' failures at the feet of the associations tarnished the already fragile image of China's associations. Some interviewees recognized the irony: a policy geared to revitalize associations had had the opposite effect. Whether or not a government official or business leader supported cartels, the sentiment that associations "are not of much use" was reinforced by the fiasco of the self-discipline price policy.

Critically, people differed over what the lessons were for competition policy. Because of the cartels' failures, some companies became even more convinced of the inappropriateness of government intervention or inter-firm coordination over prices. One official at a large state-owned steel maker was adamant that "prices are set by firms", which was consistent with one of his private counterpart's declaration that "we set our own prices". Such sentiments were expressed repeatedly by many other interviewees. On the other hand, not all in government and industry agreed. The SETC's very public endorsement of cartels and the SDPC's continued intervention lent official legitimacy to inter-firm cooperation in setting prices. For those considering doing this, the lesson was that China's associations need to be given greater authority and greater support by their members in order to effectively coordinate prices, not that cartels are inherently wrong or unworkable. Thus, in the wake of 1998, some enterprises have taken it upon themselves to informally cooperate with their industry colleagues, while some associations have redoubled their efforts at shaping cartels. Most of these attempts have similarly collapsed for the same reason, low industry concentration. Nevertheless, there have been some occasional successes that renew some observers' faith in the utility of such behaviour.[71]

---

71 The most important case involved a production cartel established in mid-June 1999 among eight television picture-tube makers. The members, which included one foreign company (Matsushita), halted production for almost a month, momentarily sending tube prices up. See Zhu Yanyan, "Ba da caiguanchang tingchan" (8 Large Picture Tube Factories Stop Production), *Zhongguo gongshang shibao* (China Business Times), 29 June 1999, p. 1; Zhu Yanyan, "Ba da caiguan chang huifu shengchan" (8 Large Colour Tube Factories Resume Production), *Zhongguo gongshang shibao* (China Business Times), 16 July 1999, p. 1. (It should be noted that production stoppages are easier to monitor than either adjustments to production amounts or prices.) The following year several steel makers, some in coordination with the State Bureau of Metallurgy and the new China Iron & Steel Association (CISA), set floor prices for some steel goods. But rather than rise to the planned levels, prices shot up much further, though they later fell to earlier levels. According to steel industry interview sources, CISA, which replaced the Bureau in 2001, has continued these efforts largely at the initiative of several large members. Also see China News Service, "Zhongguo shangtiao bufen gangcai jiage" (China Raises Some Steel Products Prices), 4 April 2000; "Quanguo daxing gangcai shengchan xiaoshou xietiaowang chengli" (National Large Steel Products Production and Sales Coordination Network Established), Sinometal.com, 11 April 2000; "Dazhongxing gangtie qiye gangcai jiage zuotanhui

Conclusion

China's political economy is in a state of flux. The policy process is no longer limited to government participants. Companies, Chinese and foreign, have taken the initiative to become more involved in identifying problems and shaping solutions that fit their interests. In the self-discipline price debate, businesses engaged in a game of tug of war, first pulling the government in one direction to direct the associations to prevent prices from collapsing, then pulling the government back in the other direction to have it revamp its approach. To achieve their goals, firms energized bureaucratic allies within the SETC and SDPC, who acted with both the interests of the companies and their own bureaus in mind. The growth of business influence on policy has occurred despite the continued weakness of associations in most industries. The fight over cartels soured the attitude of many firms toward the existing associations, but it also produced no consensus on how associations should be reformed. Regardless of the associations' development, businesses' greater political activism has turned the policy process from what one scholar aptly described as "organized chaos" into an even more fractious and dynamic affair.[72]

In addition to changes in the policy process, there is also no consensus on the norms of economic competition either. In late 2001, the Chinese government announced that it had scrapped 124 price regulations in order to comply with its commitments to the World Trade Organization.[73] Despite these changes, the self-discipline prices story reveals a high level of ambivalence regarding whether inter-firm coordination of prices and production is legitimate and, if so, under what circumstances.[74] The persistence of such views and a legal framework that permits cooperation under certain circumstances and does not prohibit monopolies shows that China's march away from a planned economy does not lead inevitably in a free-market direction. Elements of both free-market and controlled-market principles are still competing with one another. This situation exists not because China is a "transition economy". Rather, the debate in China

---

qingkuang jieshao" (Introduction to Situation of Large- and Medium-Steel Enterprises Steel Products Price Meeting), Sinometal.com, 9 May 2000; and "Quanguo gangcai jiage 6 nian lai shoudu shangzhang" (National Steel Product Prices Rise for First Time in 6 Years), *Shanghai qingnian bao* (Shanghai Youth News), 9 May 2000.

72 Tanner, *The Politics of Lawmaking in China*, pp. 31–5.

73 "PRC Scraps 100-Plus Price Regulations for WTO", Xinhua News Agency, 23 November, 2001, in FBIS-CHI-2001-1123.

74 Writing in early 1998, Dali Yang posited that the failure of cartels to that point demonstrated that in China "producers have come to accept the reality of competition". The expansion of cartels later that year and the variety of lessons learned from their failure suggest that a commitment to free markets is not universally shared in China, most importantly not by businesses. See Dali Yang, "Survival of the Fittest".

reflects the variation in competition standards that exist across the capitalist world.[75]

The existence of rival norms and interests in China and different levels of influence over public policy ensures the continuation of a complex struggle to define China's economic system. The real price of competition is that the rules of political and economic behaviour are, in fact, subject to influence and shaping beyond ready-made moulds. Chinese business people are not simply competing over prices, but over how to define their present and their future.

---

75 Because of conflicting positions, WTO members have still not agreed on whether to include competition policy under the WTO umbrella, and if so, to what extent rules should be harmonized across member countries. See Sam Laird, "A Round By Any Other Name: The WTO Agenda After Doha", *Development Policy Review*, Vol. 20, No. 1 (March 2002), pp. 41–62.