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THE WALL STREET JOURNAL

WSJ.com

OPINION ASIA | May 10, 2012, 12:35 p.m. ET

Beijing Can't Outgrow Corruption

Trying to get graft out of the Chinese system is like trying to take the sugar out of an already baked cake.

By **SCOTT KENNEDY**

The made-for-movie saga of disgraced Politburo member Bo Xilai and his family is mesmerizing because it lifts the veil on the relationship between power and money in today's China's. Images of rich "princelings" in Ferraris have replaced perceptions of China as a technocratic wonderland or as the factory floor of the world where entrepreneurs and laborers toil day and night. Beijing is in full damage-control mode, promising it will work harder to clean up corruption. But what if corruption is too much a part of the system to take out?

The Chinese system is like a cake. Its ingredients, once stirred together, can't be separated. First, there's a regulatory layer that benefits certain companies, industries and localities over others, and allows officials to dispense perks or inflict pain on a whim. Add to this a leadership *raison d'être* that places achieving rapid growth above everything else, with health, safety and the environment relegated to secondary concern. And the final ingredient is that these officials (and the party) are their own watchmen. The media, minority shareholders, credit rating companies and voters are kept on a short leash.

This recipe has been baked into a masterpiece both tasty and unhealthy. With trillions at their disposal, bureaucrats from Beijing to Bengbu (in Anhui province) dole out tax holidays, land, information, cash and contracts to achieve their official growth targets. If such policies also help them and their friends, why not? Tools to manage conflicts of interest aren't in the recipe.

No wonder China has witnessed both stunning economic growth and a shadow boom in official corruption. While the country has gone from bicycles to high-speed trains in a generation, a railway official was reported to have received more than \$2 billion in bribes in exchange for contracts. The Chinese are becoming world leaders in telecom, nanotechnology and other areas of science. But academic fraud and worthless patents are commonplace.

Regional experimental zones often generate great innovations and tremendous waste. Does the government really need to fund dozens of cloud computing projects? Some of the estimated \$150 billion China plans to spend on cloud computing in the next few years will foster genuine innovation, while the remainder is likely to fuel distinctly non-innovative real-estate development and benefit individuals up and down the regulatory hierarchy.



Reuters

Former Politburo member Bo Xilai.

The Communist Party has certainly tried to tackle corruption. Since 1987, 125 ministerial-level officials have been removed from office, and since 2000, over 130,000 corruption cases have gone through the courts. But eliminating corruption is like trying to extract sugar from the already mixed cake batter.

This is particularly true for local leaders. Control over local resources and distance from Beijing's prying eyes create severe monitoring problems. Mr. Bo's family likely benefited more from his running Dalian, Liaoning and Chongqing than being minister of commerce.

Fully rooting out corruption is impossible with the incentive structure currently in place for officials and those dependent on them. During a drunken moment of frankness, a local official from Henan province recently admitted to a visitor that anyone who worked in the system who was truly clean could not survive for long because he would be seen as a threat to everyone else.

Although this cake's main ingredients are homespun, multinational businesses and the global economy are increasingly part of the mix. Some foreign companies have also been caught up in this web. But more importantly, privileged Chinese use no-name foreign bank accounts, tax havens, expedited paths to overseas citizenship for wealthy investors and schools that accept students from anywhere and cash tuition checks without asking questions. Each serves a legitimate purpose, but they also are the arteries that facilitate the globalization of corruption.

The mixture of money and politics is not easily undone. The real danger is not the amount of funding bureaucrats and their kin skim off the top. Rather it is special interests who benefit from the status quo and grow stronger: state-owned enterprises with easy access to resources and protected markets, exporters who enjoy an undervalued yuan, banks that have profited from depressed interest rates for deposits and their benefactors in officialdom. It's an open question whether China's leadership has the political will to break these ties.

This has worked so far, but if the Chinese cake is to continue to expand, there needs to be a new recipe. With shrinking profit margins in manufacturing, substantial debt levels and growing demands to improve welfare and reduce environmental degradation, greater efficiency in allocation of resources will be paramount in the next stage of development. This will require containing regulatory intervention, nurturing entrepreneurship and creativity and facilitating additional sources of oversight to ensure everyone plays by the rules. If China continues with a system in which the well-connected try to bake their cake and eat it, too, there eventually won't be much of anything left except a few crumbs.

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