Chapter 3

Post-Socialist States and the Evolution of a New Development Model: Russia and China Compared

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Introduction

The onset of globalization in the 1980s–90s coincided with the shift in China and Russia from autarkic central planning to trade-driven market economies. The Chinese leadership consciously embraced globalization, and saw it as an opportunity rather than a threat. The reaction in Russia has been quite different, since during the 1990s Russia seemed to be suffering from the impact of globalization. Some observers even argue that globalization was itself one of the causes of the collapse of the Soviet state. However, the picture has changed over the past decade, as Russia has regained political stability and experienced rapid and sustained economic growth while continuing a policy of greater integration with the global economy.

Both Russia and China have emerged from the transition to global capitalism as stronger and more stable states. Yet neither of them has fully embraced the values and institutions of the "Washington Consensus" – the belief that the best economic policy is one of free trade, freely floating currencies, the lifting of government regulation, and the privatization of state-owned industries. Nor do they confirm the "Washington Hypothesis" – the idea that globalization promotes democratization (Rudra 2005). The Russian and Chinese development model combines an acceptance of market forces and global integration with a rejection of neoliberal economics and liberal democracy, and the reaffirmation of nationalism and sovereignty.

The first section of this article compares and contrasts the evolution of the Chinese and Russian economic systems over the past two decades. We find some many sharp differences and a few points of similarity. One important debate is the extent to which it was initial conditions or leadership policy choices which determined the outcome of the transition. A third factor – the external economic environment – must also be taken into account. The final section of the article summarizes the common features that have emerged as of 2008, and speculates as to whether this convergence amounts to the emergence of a new development model – one that could even contribute to the evolution of a new type of international economic order.

1. A Tale of Two Transitions

Russia and China are large autonomous countries with strong state traditions. They both turned their backs on the global capitalist system in the 20th century, and adopted communist systems. Prior to that, they had emerged historically as land empires in the center of Eurasia. This left them with a legacy of a strong central state with a distinct identity and legitimacy. Correspondingly they had weak traditions of civil society. The state acted as a gatekeeper for their interactions with the outside world, which was seen as hostile and threatening. Both had been subject to military defeats in the 19th–20th centuries and subsequent loss of territory, and had then emerged bloodied but victorious from World War Two. Both Russia and China have distinct cultures, tracing their roots and maintaining their identities *outside* of European culture. However, Russia's interactions with Europe were much more intense, so Russia is a hybrid with strong European elements, unlike China. Both countries' elites currently see themselves – and have long seen themselves – as economically backward compared to the West (since the early 19th century in the case of China, since the 16th century in the case of Russia). "Modernization" is a term that Chinese and Russian leaders still use when discussing their goals.

Under communist rule, their state-owned, centrally-planned economies had many common features and stood in stark contrast to the Western model of democratic capitalism. But in the 1990s, both countries abandoned many elements of their model. At first, they seemed to be headed in opposite directions: Russia towards Western integration and market democracy, while China strove to preserve its authoritarian rule alongside limited opening to foreign trade and investment. Russia experienced rapid political liberalization under General Secretary Mikhail Gorbachev, followed by *system collapse* and the break-up of the Soviet Union. China embarked on a *managed transition* that involved the step-by-step introduction of elements of capitalism while the Chinese Communist Party (CCP) retained a monopoly of political power. The Tiananmen Square crackdown in 1989 led some to believe that Communist China was experiencing the same profound contradictions that were sundering the Soviet system. However, the Chinese political system remains intact, and expectations that the introduction of capitalism must inevitably lead to the introduction of democracy have eroded (Nathan 2003).

Table 1. Development Indicators, 2006

	China	**Russia**
Life expectancy (years)	72	66
Fertility (births per woman)	1.8	1.3
Infant mortality (per 1000 births)	24	16
GNI per capita (Atlas, $)	2,010	5,800
GNI per capita (PPP, $)	4,700	12,810
Agriculture as % of GDP	12	5
Inflation (%)	3.3	15.7
Gross domestic capital formation as % of GNI	44	21
Phone subscribers (per 100 people)	63	137
Internet users (per 100 people)	10.4	18.0
High tech as % of manufacturing exports	30	9
Merchandise trade as % of GNI	66	47
Government revenue as % of GDP	9.6	28.7
Foreign direct investment (net inflow, $ bn)	78	12.5
Exports as % of GNI	40	34

Source: World Development Indicators, www.worldbank.org, accessed 20 October 2008

China's transition away from state socialism is generally considered a success, while Russia's is generally considered a failure. China has doubled its GDP every decade, and has lifted 400 million people out of absolute poverty – perhaps the largest single increase in human welfare in world history. In key development indicators such as phone lines, internet usage, life expectancy, and high-tech exports, it has closed the gap with Russia (Table One). These economic achievements have translated into a substantial rise in China's global status, a process symbolized by the success of the 2008 Olympic Games. In contrast the Soviet state lost half its territory and population, and the Russian Federation has struggled to maintain its status as a great power. Although the implosion of the Soviet Union was shocking enough to Chinese leaders, equally disturbing was the collapse of Russian society that occurred *after* 1991 – economic recession, an upsurge in crime and lawlessness, a falling birth rate rise and rising death rate, and the war in Chechnya. The Chinese leadership tried to learn from Moscow's mistakes. They scrutinized developments in the Soviet Union very closely, and adjusted their policies accordingly (Marsh 2005). They concluded not only that they must be willing to use repression, but also that reforms were needed to increase the state's capacity to rule, and to bolster the regime's legitimacy in the eyes of the people. In contrast, there is little evidence that Russian leaders have made any serious effort to draw lessons from China's success.

1-1. Initial Conditions

The initial conditions at the onset of transition in Russia and China were very different. Moreover, the political leadership of the two countries pursued radically different transition strategies. Despite starting in different places and heading in different directions, the two countries are now converging on a similar model of state-led development in the face of common global challenges and opportunities.

By the late 1980s Russia was a mature industrial economy with an educated, urban labor force. It was a military superpower equal to the United States that still saw itself as a world leader in science and technology. At the onset of its transition in the late 1970s China was still overwhelmingly agricultural (80% peasants, compared to 15% in Russia), with a small and uncompetitive industrial base and minimal scientific capacity. China struggled with the problem of excess population relative to the available land, but at least this meant it had a pool of cheap labor. Russia faced a declining population and chronic labor shortage, but was resource rich, while China was relatively resource poor.

Not only were the economic conditions quite different, but the political evolution of the two countries prior to 1980 was also very distinct – although both Chinese and Russian elites saw the need for reform. The Chinese Communist Party was rebuilding in the wake of the Cultural Revolution (1966–76) which had seriously damaged its organized coherence, governing capacity, and popular legitimacy. The Soviet Union had experienced 20 years of stability under General Secretary Leonid Brezhnev – but this period had produced rising corruption, bureaucratic ossification, economic stagnation, and a number of costly foreign policy adventures (notably, the invasion of Afghanistan, and a renewed arms race with the US).

An obvious difference is that while China is ethnically homogenous (90% Han), the Soviet Union was ethnically diverse. Ethnic Russians made up only 53% of the Soviet population, and 80% of the Russian Federation. It might be argued that this ethnic homogeneity should have made it easier for Beijing to introduce democracy. But Chinese leaders had other reasons to fear democratic contestation – there are strong regional differences in their vast country, and there is a huge pool of desperately poor peasants.

Figure One Contrasting Reform Paths

	Sequence	Pace	Initiative	Spirit	Western advice
Russia	Politics First	Rapid	Top-down	Shock therapy	Strong influence
China	Economy first	Gradual	Middle-up	Controlled transition	No influence

1-2. Different Paths

Not only were the initial conditions different in the two countries, but the respective national leaderships chose divergent development strategies. It is often said that the key difference between Russia and China was the *sequencing* of reform. The argument goes that Gorbachev's big mistake was to opt for political liberalization first and economic reform second. Clearly, the Chinese leadership cannot be accused of committing that error. In Gorbachev's defense, however, it can be argued that economic reform without political reform had been tried by a succession of Soviet leaders since the 1950s – and was attempted again by Gorbachev in 1985–87. It was the failure of these earlier economic reforms in the face of bureaucratic intransigence that forced Gorbachev to embrace political reform.

Western scholars had predicted that political liberalization would cause problems for economic reform in the socialist bloc. Subsequent events proved them right – but they got the political mechanism wrong. In an influential 1991 book Adam Przeworksi argued that democratization in Eastern Europe would empower the workers, who would mobilize to protect their state-guaranteed jobs (Przeworksi 1991). Thus political reform would enable the interest groups created by the socialist economy to block radical economic reform.

As it turned out, this did not happen. It was nationalism, not worker unrest, that sealed the fate of the Communist states in Europe. In Poland, the workers were swept up in the nationalist project of getting out from under Soviet influence by joining the West – which meant embracing capitalism. In Russia, the political turmoil that the country experienced in 1989–93 was so severe that the workers were politically neutralized and were unable to prevent President Boris Yeltsin's embrace of liberal market reforms. What happened next was equally unexpected: the emergence as if from nowhere of a small group of powerful oligarchs, who helped to keep Yeltsin in power, while blocking the second wave of reforms that liberals had hoped for.

Second, there is the contrast in *pace* of reform. The conventional wisdom is that China followed a gradual path while Russia embraced shock therapy in 1992. The Chinese were burned by a century of failed efforts at radical change and were thus philosophically committed to incrementalism (Fewsmith 2001: 80–83). In contrast Moscow had grown tired of decades of incremental change, and the crisis conditions of early 1992 seemed to leave Yeltsin with no option but to embrace radical reform (Gaidar 1999). It also reflected his advisors' conviction that the only way to break with central planning was to enforce hard budget constraints and market-clearing prices as part of an integrated package. The reformers also made a Przeworksi-type argument about a political window of opportunity: that Yeltsin had to capitalize on his power in early 1992 before anti-reform forces rallied and used the democratic process to unseat him. Freed from the threat of a democratic turnover of power to reactionaries, the CCP leadership could afford to take a more gradual reform path.

2-1. The Politics of Transition

In retrospect, it was neither the sequencing nor the pace of reform that was the crux of the problem. The key question is more basic – the need to maintain political power and state capacity. Putting economic reform first allowed the Chinese state to maintain the political capacity to manage the process, correcting for mistakes and imbalances as they arose. In a more negative light, Minxin Pei argues that it gave the political elite the resources they needed to maintain their repressive system of rule (Pei 2006b: 19). In contrast, Gorbachev threw out the very tools with which he hoped to promote economic reform. Gorbachev's reforms disrupted the organization cohesion of the Communist Party apparatus and directly undermined its ideological legitimacy (Hua 2006). His reforms destroyed the party and then the Soviet state itself. In their struggle to hold onto power, both Gorbachev and Yeltsin used divide-and-rule strategies that split the elite and fragmented political institutions.

Chinese leaders seem to have managed to avoid such divisions, despite – or perhaps because of – the fact that the CCP leadership was historically much more ridden by factionalism than its Soviet counterpart. The Chinese learned their lesson from the Cultural Revolution – and from the Soviet break-up. Despite deep disagreements over policy (such as over Tiananmen) they have managed to preserve a united front in the public arena (Zhang, Nathan and Link 2001). They have also undergone two relatively smooth transitions in the top leader position (from Deng Xiaoping to Jiang Zemin in 1997, and then to Hu Jintao in 2002) without experiencing a political crisis (Nathan 2003). This is something Russia has not managed. Yeltsin's nomination of Putin as his successor in December 1999 was a fairly smooth transition, though it was accompanied by the second war in Chechnya. The transition from Putin to Dmitry Medvedev is not yet a clean break.

Looking back, one sees a surprising pattern. In both Russia and China, the highest level of democratic debate occurred in the late 1980s, during the early experimental period when various reform paths were being debated by the national leadership. Over time, as the economic reforms eventually took over, the scope for political dissent actually shrank. This is the opposite of what one would expect from modernization theory, which expects socio-economic development to produce new constituencies (workers, the middle class and businessmen) that demand a say in decision-making (Pei 2006a).

In the wake of the Tiananmen crackdown, in China oppositionists were jailed or driven from the country; reformists were purged from the CCP leadership; and intellectuals lost their faith in the possibility of the "fifth modernization" – democracy. Nevertheless, Deng Xiaoping in his 1992 tour of the south made the historic decision to accelerate economic reform – in a bid to build a new basis for CCP legitimacy, and thereby prevent a repeat of 1989. This danger was magnified by the dramatic implosion of the Soviet state at the end of 1991. The failure of the August 1991 coup attempt by Soviet hardliners was a blow to CCP leftists who thought that repression was a sufficient basis for rule. Subsequent political reforms in China have been limited to the spread of electoral competition at village level, introduced in 1988; a strengthening of the oversight role of national and local legislatures; and steps to bolster the rule of law and fight corruption (Pei 2006b: ch. 2; Fewsmith 2001).[1] None of these measures have been allowed to infringe on the authority of the CCP. The CCP has undergone some organizational reforms to maintain its effectiveness post-Mao – most notably, the 2002 decision to allow private entrepreneurs to become CCP members.[2]

1 Even so, the Standing Committee of the National People's Congress only rejected government-proposed bills three times in 28 years. A more positive statistic is that 21% of lawsuits filed against government officials succeeded in 2002 (Pei 2006b: 60, 67).

2 20% of entrepreneurs are members, but the CCP has branches in less than 1% of the 1.5 million private enterprises (Dickson 2003b).

Ironically, the quality of Russian democracy arguably peaked in 1990–91, the last year of the Soviet Union. In 1992–96 politics settled down into an ugly standoff between a reformist president and an opposition-dominated parliament, and after 1996 the level of competition steadily eroded from election to election.

The most well-known democracy index is that compiled by Freedom House, grading the level of political rights (PR) and civil liberties (CL) on a 1–7 scale, with 1–2 being “free” and 6–7 “unfree.” Freedom House regarded the new Russian Republic as “partly free,” ranking it 3 for PR and 4 for CL from 1993 through 1997. Russia’s grade slipped to 4/5 in 1999 and 5/5 in 2000–2003. In 2004 Russia was relegated to the category “unfree,” with a 6 for PR and 5 for CL, which has stayed its rating through 2008.[3]

There has been much less variation in the political climate in China, especially since 1989. Freedom House scored China a 7/7 from 1972 through 1977, when it jumped to 6/6. In 1989 it slipped back into 7/7 and stayed there until 1998, when it rose to 6 for civil liberties and 7 for political rights. Freedom House has kept that score for China through 2008.

In both countries, the traditions of one-party rule have created a culture inimical to pluralism, in which politics is seen as a “winner takes all” game. The key liberal argument for pluralism is that you cannot always be sure of being a winner, so it is better to share power and grant rights to all political actors. But in neither country has the political elite accepted this idea. Both countries have preserved one-party systems based on clientilistic networks in which particularism rather than pluralism is the structuring principle of political life.

2-2. The Economics of Transition

There are many differences between the Russian and Chinese economic reform strategies. Russia’s government unleashed a hastily-assembled package of radical reforms in 1992. Beijing’s reforms were middle-up rather than top down – the center encouraged and tolerated initiative from below, and local entrepreneurs and politicians respond-

3 Orttung (2005) puts Russia’s political system *below* that of Afghanistan, Bahrain or Burkina Faso.

ed to the challenge. The operative metaphor in China was "feeling the stones as you cross the river (Fewsmith 2001: 83)," while in Russia one of the reformers' favorite sayings was that "you cannot cross a chasm in two jumps (Taber 1992)."[4] Crucially, the CCP preserved the capacity to monitor the implementation of the reforms, and adjust them when necessary. While the Chinese talked about "growing out of the plan," Russia was effectively "falling" out of the plan (Naughton 1995).

Russia launched "shock therapy" in 1992, but the government was unable to control monetary and fiscal deficits, which meant that high inflation and macroeconomic instability prevailed until stabilization was finally achieved in 1999. The privatization program was hijacked by a small group of well-connected insiders, leaving the Russian public feeling cheated and the state treasury empty. Foreign investors were largely shut out from the "crown jewels" of the economy – oil, gas and metals. Although the basic structures of a market economy had emerged by 1999, free entry was still limited, oligopolistic rents were high, and the incentives to efficiency and investment were low. By 2001, the country's 23 largest firms accounted for 30% of Russia's GDP, and these firms were effectively controlled by a mere 37 individuals (World Bank 2004). In addition to the national oligarchs, many regional markets were controlled by local monopolists.

After Putin was elected president in March 2000 he started an energetic campaign to strip the oligarchs of their political influence. Putin both consolidated and rolled back the market reforms. On one hand he created a more robust legal infrastructure, increased taxation, and oversaw eight years of economic growth averaging 6% a year. On the other hand he strengthened state control over key industries, and a new system of state corporatism took shape. The post-Soviet state bureaucracy, spearheaded by a team of ex-KGB officials, had asserted its dominance over the newly-minted capitalist oligarchs.

China started in 1978 by freeing peasant farmers from plan controls through the household responsibility system. This boosted output and also started released labor for factory work. Then local state authori-

4 Taber (1992) writes that the well-known advisor Jeffrey Sachs "frequently cites the old Russian maxim that you cannot cross a chasm in two jumps."

ties were allowed to set up profit-seeking town and village enterprises (TVEs). State owned enterprises (SOEs) were likewise freed to become more entrepreneurial. The seventh five year plan that began in 1986 encouraged coastal regions to engage in manufacturing assembly for foreign markets. Between 1978 and 2003, China recorded an annual growth rate of 9.4%, while per capita income rose from $150 in 1978 to $1,700 in 2005. China maintained the state industry sector with its social guarantees, initially through budget subsidies and then through soft credits via the four state-controlled banks. The rapid growth of the private sector meant that the state sector's share of the industrial labor force fell from 80% to 29% 1978–2000 (Pei 2006b: 3).[5] Small and medium SOEs began to be privatized in 1994 – though the government avoided using that term, instead talking of restructuring and asset transfers. In 1997 a major program of restructuring SOEs was launched, leading to wage arrears and layoffs. The government softened the blow by introducing severance pay at 60% of the previous wage for three years. Overall, the state planners showed caution and flexibility in introducing these reforms. For example, price controls on grain were lifted in 1993, but restored in 1995 after the move triggered shortages and price gouging. In 2001 controls were once again eased in grain consuming regions (Pei 2006b: 97–102).

While agriculture was the initial driver of the Chinese, in Russia the organization of farm production was largely untouched by the reforms. There was a divergence in the pace of change in the opposition direction in the case of banking. The Chinese state kept firm control over the banking system, while in Russia the lifting of controls led to the sprouting of 1,500 private banks, many of which collapsed in the August 1998 financial crisis. Russia's mass privatization program converted state firms into legally independent corporations, in line with Western theory stressing the importance of creating clear property rights in a rule of law system. China pursued a very different path: no mass privatization, but the evolution of a hybrid model of SOEs and TVEs behaving as profit-seeking entities with unclear property rights. These Chinese enterprises were also deeply embedded in strong local and even family

5 SOE share of industrial output fell from 78% to 41%.

networks (Ma 2000). One important step was the 1998 decision ordering the CCP and army to divest themselves of businesses. In practice, the Russian approach failed to generate the transparent and secure property rights that the reformers claimed as their goal. There were hundreds of cases of organized crime groups seizing control of enterprises by force, and dozens of cases of state officials seizing firms through manipulation of tax arrears and other instruments. Putin's expropriation of the leading private oil company Yukos in 2003–5 and Shell's forced sale of its majority stake in Sakhalin II in December 2006 are two striking examples of the political contingency of property rights.

So at the end of the day the weakness of property rights is something that unites rather than divides the Russian and Chinese cases. And in neither Russia nor China has the state given up control over key strategic sectors such as telecommunications or power generation (Pearson 2005). Small steps have been taken in both countries to promote competition in these sectors and create a modern regulatory framework, but in practice political dirigisme is still decisive. Another similarity is that in both countries the tax-gathering capacity of the central state shrank and then recovered in the course of the reforms. In China central government revenues fell from 31% of GDP in 1978 to 10.7% in 1995, rebounding to 17.1% in 2001 (Yang 2003). Similarly, Russian federal revenues fell to 9.2% of GDP in 1998, recovering to 17.1% in 2001 (OECD 2004). But after 2001, the two countries drew apart, with China's state revenues shrinking to 10% while Russia's grew to 28%, thanks to the oil boom.

Regional and social inequalities sharply increased in both countries as a result of the reforms. In Russia the Gini coefficient rose from 0.29 in 1992 to 0.40 in 1997, where it stayed through 2008, while in China it went from 0.28 to around 0.45 1978–2000 (Rosstat www.gks.ru; Pei 2006b). In Russia there was a more extreme concentration of wealth in the hands of the new oligarchs than in China. This was a result of the more uncontrolled nature of the privatization; the weakness of law enforcement agencies; and the resource-based character of the economy. By 2006 *Forbes* magazine was reporting 33 dollar billionaires in Russia, but "only" eight in China.[6] Their ranks had risen to 87 by 2008, putting

6 India was listed with 23 billionaires (*Forbes*, April 2006, at http://www.forbes.com/billionaires/).

Russia in second place after the US. In contrast to the Russian oligarchs, who were in effective control of the political system between 1993 and 2000, Chinese tycoons stayed in the political shadows, colluding with regional political bosses but avoiding anything like a direct challenge to the national state.[7]

Corruption is a debilitating problem for both countries; a drag on efficiency and a turn-off for foreign investors.[8] Its practice is so commonplace at both high and low levels that bribery and clientilism seem to be the glue holding the political system together (Pei 2006b: ch. 4; Sun 2004). The character of corruption in China shifted after 1992 as marketization took root and the role of "connections" (*guanxi*) diminished.[9] Leaders in both Moscow and Beijing claim that battling corruption is a top priority, but their actions have barely made a dent in the problem. China has seen the arrest of thousands of top officials, even including a Beijing mayor and two governors.[10] Russia has been less decisive: Putin's anti-corruption campaigns have taken down a few top private businessmen and some police generals, but it was not until 2006 that a sitting governor was arrested.

2-3. External Integration

Both countries relied on external integration as a key driver of their economic transition. But here, again, their experiences diverged. Chi-

7 For example they are absent from the national legislature, in contrast to the Russian case (Pearson 1997: 111; Dickson 2003a).

8 Transparency International's Corruption Perceptions Index, based on surveys of international businessmen, rates Russia 126th out of 159 countries surveyed in 2005, with a score of 2.4 out of 10, while China is seen as less corrupt, ranked 78th with 3.2. The situation is unchanged since 1998, when Russia ranked 52nd (out of 85) with 2.4, and China 76th with 3.5 (www.transparency.org)

9 Sun's data suggest that the number of cases did not substantially increase in the 1990s, although the author herself does not highlight this point. Table 1.2 shows the number of economic crimes fell from 65,000 in 1992 to 35,000 in 1999, and Table 1.8 shows the number officials investigated rose from 150,000 1992 to 175,000 2001 (Sun 2004).

10 Yan Sun provides a list of 21 such officials 1986–2004 (Sun 2004: 49).

na's trade tripled in every decade, raising its share in world trade from 0.8% in 1978 to 7.7% in 2005. Because of the 1990s slump and the breakdown of the Comecon trading bloc, Russia's share of world trade fell from 3.4% in 1990 to 1.5% in 2000, recovering slightly to 1.8% in 2005 (Wolf 2006b; Navaretti 2004; WTO 2006). China's economic regeneration was led by an explosion of manufacturing assembly plants in coastal locations, importing components and raw materials and exporting manufactured goods to foreign markets, and tapping into its seemingly limitless supply of cheap labor (Wei 2002; Nolan 2004; Lardy 2001).[11] Russia had neither the labor reserves; nor the ports close to global shipping routes; nor the entrepreneurial spirit; nor the political will to embrace this kind of export manufacturing-led growth path.

Unlike Russia, the Chinese relied on an influx of foreign direct investment (FDI), while keeping portfolio investors at arm's length. China attracted an annual average of $12 billion FDI 1985–95, rising to $78 billion in 2006 (UNCTAD 2005). Russia averaged only $1.3 billion FDI per year 1985–95 and $12.5 billion in 2006, while experiencing an annual outflow of capital far in excess of those figures. By 2006 China had accumulated a net stock of $207 billion FDI (15% of all capital), while Russia had only $17 billion (Huang 2003). To facilitate this inflow of capital China created Special Economic Zones with favorable tax and regulatory conditions. This process was greatly facilitated by the existence of Chinese capitalist exclaves in Hong Kong and Taiwan, part of the 50 million-strong Chinese diaspora (McKinley 2005). Though foreign investors were encouraged, they were typically forced into joint ventures with their own stake capped at 50%.

China preserved tight controls on capital flows. The renminbi is convertible on current account but not on capital account, and was pegged to the dollar after 1995, at a rate equal to about 25% of purchasing power parity (PPP).[12] Thanks to these controls, China has maintained its cheap labor advantage, and has prevented the speculative capital inflows and outflows that have devastated other developing economies. They rode out the 1997 Asian financial crisis largely unscathed.

11 By 2007 wage costs were rising, providing a constraint on growth in the coastal region.

12 In July 2005 the peg was switched to a basket of currencies.

In contrast Russian reformers largely followed Western advice to pursue external liberalization – in part because IMF credits were conditional on such policies (Stone 2004). Russia lifted many capital controls in 1992–94 and dollars flooded in, forming a parallel currency for most of the 1990s. $40 billion of speculative capital entered the country – mainly to cover the government's yawning fiscal deficit. This reckless borrowing led to the August 1998 financial crash, which was triggered by the slump in the price of oil following the 1997 Asian crisis. August 1998 saw a 75% devaluation of the ruble, a default on foreign loans, and the destruction of the assets of most of the financial oligarchs. The crisis ironically cleared the decks for an economic recovery by making Russian food and manufactures more competitive with imports. More importantly, it enabled a renaissance of state power by fatally weakening the oligarchs, financially and politically.

3. Future Prospects: Stability or Instability?

According to conventional Western assumptions about the congruence of political and economic liberalism, the current situation in Russia and China is unsustainable. In both countries, the economic system is significantly more market-driven and hence pluralist than the political system. "The market's irresistible force is meeting the party's immovable object. At some point, one of them must surely give" (Wolf 2006a). Liberals assume that a breakthrough to democracy is still possible and necessary in both countries. Pessimists expect the state to take more steps to rein in the market – jailing businessmen, nationalizing private companies, erecting protectionist barriers.

Moves by the CCP to broaden the political elite to include businessmen have exposed the contradictions within a regime that embraces capitalism while maintaining Marxism-Leninism as its official creed. The dismantling of the Maoist-era social safety nets, and the never-ending battles with corruption, also raise doubts about the long-term viability of the Chinese model. The country is highly vulnerable to cyclical and exogenous shocks – the bursting of the property bubble; the collapse of the pyramid of bad loans to loss-making SOEs; a slump in demand for China's manufacturing exports; health crises and ecological disasters

(Change 2001). This all leads Pei to conclude that without democratic reform, economic growth will stagnate and regime will be faced a series of mounting internal challenges (Pei 2006b), though his pessimism is not shared by all China watchers (Nathan 2006). The international climate that was so favorable for China's export-led growth cannot continue indefinitely: the 2008 global financial crisis may well mean the end of growth driven by US consumers with money borrowed from China, Japan and the petro-states.

But in a world replete with failed and failing states, the Chinese state still looks fairly effective. It is still able to identity problems and deal with them, to complete massive projects such as the Three River Gorges dam or the building of pipelines from Kazakhstan. Even their ability to create a system to effectively censor the Internet is something of a technological and political achievement (Pei 2006b: 84–88). On the other hand, the dismal failure of regulatory agencies to prevent the tainted milk scandal in 2008, and the thousands of protests each year surrounding illicit land seizures, are persisting challenges to state capacity.

There are also plausible crisis scenarios in Russia's near future. Russia gained little from its political and economic opening in the 1990s. Not until the commodities boom that saw the oil price rise from $12 a barrel in 1997 to $60 in 2005, did Russia enjoy a clear benefit from global integration. During the years 2000–08, oil and gas alone were accounting for 60% of export earnings and one third of government revenues. The bursting of the financial bubble and global economic slowdown inn 2008 caused the world oil price to fall from a peak of $147 in July to below $80 in October, which bodes ill for Russia's future growth prospects.

4. The "Regulated Market" Consensus

The differing trajectories of Russia and China underline the point that the impact of globalization on individual states is unpredictable. Despite the common pressures brought by global economic competition, leadership choices and the contingencies of historical evolution still matter. Both China and Russia present a common lesson for theorists of globalization: that the world is not "flat," and that strong states can find a niche role in the new global economic order.

Both countries now seem to be converging on a regulated market model in which elements of market pluralism are embedded in post-communist, authoritarian institutions and practices.[13] This is sometimes called the "Beijing consensus."[14] What are the elements of this new "regulated market" model?

1) The leaders are committed to preserving the integrity of **state sovereignty and national identity**. This means preventing foreign leaders and institutions from forcing political or economic decisions on the government of Russia or China. Participation in international economic integration must not require a trade-off of national sovereignty. Critics argue that this insistence on sovereignty is merely a façade to justify the leaders' grip on power. Defenders would say it is a principled stance, based on a concern for the welfare of their people, whose histories have shown the dire consequences of allowing foreigners to infringe on the country's territory.

Nationalism is part of the leaders' rhetoric, but they do not want to allow it to get out of control, lest it ignite a destabilizing mass movement, and/or threaten relations with important trading partners (Gries 2004). Still, it seems clear that nationalism has been strengthened in both Russia and China as they opened up to international market forces, contrary to the argument that globalization necessarily produces "the continuing fragmentation of identities and institutions (Cerny 1999: 20)."

2) The leaders are focused on **economic growth** as a major goal – something that is good for national security and good for boosting the popular legitimacy of the regime – at a time when other ideological justifications are eroding. Growth also expands the opportunities for personal

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13 See Zhang (2006) and the debate between Wu Shuqing and Cheng Enfu (Shuqing and Enfu 2005). Harley Balzer uses a more neutral term, "managed pluralism," to describe the Russian-Chinese convergence (Balzer 2004).

14 The term "Beijing consensus" was coined by Goldman Sachs advisor Joshua Cooper Ramo, in his article (Ramo 2004). Ramo focuses on China's embrace of the neo-liberal paradigm, and he arguably overlooks the distinctive political features of China's policies which are outlined in this section.

enrichment by political cadres – while regrettably taking their attention away from human development issues.

3) The **market mechanism** is the most effective tool for economic growth, both domestically and internationally. International trade is a win-win situation for all participants (Information Office of China's State Council 2005). The country must find the most appropriate place in the international division of labor, by accepting the logic of comparative advantage. In China, that means exploiting the country's pool of cheap labor, through export-oriented manufacturing. In Russia, it means selling off the country's mineral resources. But in each case, the leaders want to move up the food chain by developing more capital and technology-intensive industries. China has outpaced Russia in accepting the logic of globalization. Beijing is even more committed to lowering trade barriers than the old US ally Japan (Overholt 2005).

4) The **market has its limits**, which must be policed by the state (see point #1). Market forces that erode state legitimacy and capacity, that unleash uncontrollable social protests, must be corrected. The state must step in to provide public goods, from investment in infrastructure to compensation for the reform losers, to the creation of a regulatory framework. The political elite is uncomfortable with the idea of economic actors beyond their control. So the political economy that emerges is one characterized by the hybridity of political and economic power. This may be less efficient than a separation of politics from economics, but it has the advantage (for the leaders) of ensuring the indispensability of the political class.

5) **Liberal democracy is inappropriate** or unnecessary, and open public contestation between rival members of the ruling political elite is to be kept to a minimum. The Chinese leadership unequivocally rejects the liberal-democratic paradigm: as Andrew Nathan puts it, "The argument that democratization, freedom, and human rights would lead to a truer kind of stability – as convincing as it may be to the democrats of the world – holds no appeal for these men" (Nathan 2003: 16). They even have the audacity to issue a report critical of human rights in

the US in response to the State Department's report on China's human rights record (State Council of the People's Republic of China 2005). The Russian position is more nuanced: the leadership officially embraces democratic values, and they are enshrined in the 1993 Constitution. But Russian practice diverges markedly from democratic theory. In partial recognition of this, Kremlin ideologists have floated notions of "managed democracy" and "sovereign democracy" to try to bridge the gap between Russian practice and Western ideas (Surkov 2006).

6) The **new middle class** that the economic boom has produced serves as a social basis for the regulated market regimes. This is contrary to the expectations of Western liberals, who traditionally saw the middle class as the trusted standard bearers for democracy. Fewsmith writes that the basis of the post-1989 social contract in China is "economic prosperity in exchange for political quiescence" (Fewsmith 2001: 103). Ed Freidman argues that "The new middle class in urban China tends to imagine democracy as a system that would empower the majority who are the rural poor" (Friedman 2006). The Chinese middle class were also frightened by the chaos that followed the Soviet collapse and were thus more willing to support a technocratic authoritarian leadership (Xiao 2003: 60–65).

In Russia, professionals were traumatized by the economic shocks of the 1990s and welcomed the stability brought by Putin's firm hand, as is evidenced by opinion surveys and election results. In both countries the middle classes have embraced consumerism and "bourgeois individualism" with a vengeance, fusing it with politics in what Wang Hui has called "consumer nationalism" (Hui 2006).

Conclusions

Does this "regulated market" approach really amount to a coherent paradigm, intellectually and practically? Or is it a contradictory mixture of ideas and policies, a temporary coincidence of diverse trends that will pull apart within a few years?

The previous wave of authoritarian developmentalism of the 1960s–80s, from Brazil to East Asia, fell apart in the 1990s. The context of that previous wave was quite different. There was a real anti-capitalist threat, both internationally (global communism) and domestically (powerful labor unions). So the state needed to defend the market from its adversaries. When those adversaries were weakened by the end of the Cold War, the rationale for authoritarianism dissolved. But the regulated market model is rooted in a different world order, that of globalization, which is not likely to vanish any time soon. The state's role is seen as providing the political stability for market forces to do their work, and the regulatory interventions needed to ensure that international trade and investment benefits the host countries and not just foreign partners. The regulated market seems to represent a viable organizational response to the exigencies of life in the post-Cold War world for these two large, ex-socialist powers.

This phenomenon opens the door to a new phase of global development in which the rules of the game may not be dictated by the established Western powers. Russia and China want to be rule-makers and not just rule-takers on the international stage. But is the development path of the two respective countries sustainable? And if so, will they be able to forge a consensus with the other leading powers on a new set of values, different from those currently in force, which will shape the global political and economic institutions of the next decade? Countries such as Brazil, India, South Africa, Mexico, and Indonesia are also experiencing rapid growth having embraced international integration – but unlike Russia and China they are robust democracies. So, the globalized world is not "flat": there is a broad and diverse range of viable models that have emerged in response to its challenges.

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