

## 32: CONTEMPORARY CHINA AND TAIWAN<sup>1</sup>

*a. What were the main domestic political and economic reforms of the post-Mao years? What theoretical justification has been used for them? What Chinese historical precedents are there for them? What are the limitations of both the reforms and the theories justifying them? In what ways has Chinese foreign policy changed since Mao's death? What traditional precedents for these changes are there?*

*b. In what ways did Taiwan do better under Japan than under Qing? In what ways and when did it not do as well? What made the 1945 Chinese reoccupation of Taiwan so disastrous? How has the Kuomintang retrieved the situation since the mid-1950s? In what ways, political and economic, and why has Taiwan done better than the People's Republic since 1950? What do the historical precedents suggest may be the nature of the future relationship between the two? Why may the most apt precedents be misleading?*

### A. Post-Mao Economic Reforms

#### 1. The "contract system" and "beggars' capitalism"

The active phase of the Cultural Revolution ended by 1970. Its rhetoric and the sterile life it imposed on China continued until Mao's death and Jiang Qing's purge in the fall of 1976. It was another three years before the government was ready to do anything new, and before non-official Chinese regained the courage to participate in these new activities.

Until 1950 most farmers participated in what had long been a mature commercial and early industrial economy. Even since 1950 they had always been ready to return to the market. That had always been the path of least resistance for them.

The chief obstacle to doing so was the ruling class and the class interests of its urban Worker and Intellectual clients.

After 1976 the much beleaguered young apprentice meritocrats needed time to return from their rural exiles and regain their nerve. Only then could they serve as Deng's immediate constituency for drastic reforms in town. Cadremen at all levels had to be assured that the anti-Party and anti-meritocrat goals of the Great Leap and Cultural Revolution had truly been abandoned.

It also took time to work out ideas for economic reform, try them out regionally and then advertise them widely. As a consequence, the first post-Maoist decade did not really begin until some three years after Mao's death.

In 1978 the regime finally announced it would try out economic reforms in Sichuan. It quickly started applying them in rural areas beyond Sichuan during 1979-80, and gradually extended them into the urban areas during 1981-5. The reforms changed shape drastically when they reached the urban areas.

Sometimes called the "personal responsibility" or "household" system the new economic arrangement is most commonly called the "contract" system in English translation. It might more clearly have been labeled the "return to the market" system.

#### a. the "contract system"

Reform began in the countryside for several reasons:

1) Economic reform was more needed there. Rural income was only a fraction of urban income.

2) Rural reform was simpler than urban reform. It was only necessary for the government to stop doing some (but not all) of the foolish things it had been doing and cultivators would spontaneously begin doing economically rational things.

3) Since 80% of the population and half of national income came from the countryside, rural reform would stabilize a large portion of society and generate significant additional wealth for society's poorest sector.

4) Nobody important gave a damn about the countryside or lived there. Even the rural Communist Party cadre could never concentrate enough wealth in their hands to transform themselves from third-rate rural meritocrats to a rural Party aristocracy. The city-based Party aristocrats

running the government and the urban factories were content to let these poor hick peasants, living well below the salt at the meager Chinese table of plenty, be allowed to do more or less what they pleased (though still within established and not altogether rational guidelines).

Under the new "contract system," peasants could stop being wage workers on the state's plantations (a.k.a. communes) and instead sign contracts as sharecropping tenants. The agents of the state, the sub-commune cadre, began to behave like landlords. They were authorized to sign short term contracts, of one to five years at first, with individual peasant families under their jurisdiction.

Each family contracted, in exchange for this short term usufruct over the land, to deliver a set amount of grain or other specified crops to the state at fixed prices. But the family was free to privately market whatever else it could produce over and above that amount.

This was something more than a return to the minuscule private plots used in pre-Great Leap years and partly restored in fits and starts after the Great Leap had failed. Now these plots were raised in dignity, increased in size, and their use rapidly extended to cover much of the agricultural land of China.

Within a few years, what little non-agricultural economic authority remained at the local level also shifted from the commune down to township or village-sized collectives. Township and village authorities were soon carrying out most of the rural industrial activities.

The commune itself became a fifth wheel—a redundant layer of local government rather than an entity engaging in production. And so, without much fanfare, by the mid '80s the authorities began to abolish the communes. Before the end of the '80s, the last of them had disappeared. Only sentimental leftists inside (but mostly outside) China mourned their passing.

Agricultural production boomed almost immediately. As more of most crops went to market, the peasantry suddenly had enough income to at least repair their houses, and in ever more places they accumulated enough savings to begin to add to the rural housing stock for the first time in a generation.

The contract system worked so well because it restored access to markets to a large portion of China's actual producers.

<sup>1</sup> 1st draft, 12/87; 8th rev. 1/00, by Edward Kaplan.

Because only part of the production on these new privately contracted plots was to be delivered to the state, the rest could be sold in real markets at real market prices. At last the peasants had incentives to increase agricultural production.

This system had, however, several flaws as originally designed. One flaw was less inherent in the contract system itself than in the nature of the overall “social contract” that constitutes post-1949 Chinese society:

Could the state be trusted to honor these or any contracts, or at least to not insist on unilaterally forcing their renegotiation whenever it felt the need to? Since the late 1980s the answer seems to be that the state cannot be so trusted.

A year before the June 4, 1989 Tiananmen Massacre, the state began to *ex post facto* insist that contracts be rewritten in mid term to require that increased amounts of grain (as opposed to more profitable crops) be produced and then sold to the government at below market prices.

The economic price for such political arbitrariness was bound to be reduced grain production by suspicious farmers, and a slowing down of both agricultural growth and farm incomes. Both have occurred during the ‘90s. Urban investment by foreigners tapered off even before the post-1997 bust, but Overseas Chinese investors so far are still placing patriotism ahead of prudence. They are used to dealing with dishonest governments.

Another, more easily correctable flaw was that the lengths of the tenancy contracts were originally too short to encourage capital improvement of land, or even serious capital maintenance. This defect was more easily remedied. By 1983-84, as the first wave of contracts came up for renewal, new ones were negotiated running for a decade, fifteen, and in some areas even twenty-five years. By the late ‘80s, the question was being raised as to whether even that was long enough a contract to encourage proper maintenance of the capitalized aspects of the land.

### **b. return of the repressed**

Chinese precedents exist for still longer, even indefinite length tenancy contracts.

In many parts of southeast China, particularly Fukien Province during the Ming and early Qing, a land tenure system evolved called the “Two Lords of the

Field” system. Under this variant form of sharecropping, the landlord permanently owned only what was called the “subsoil,” while the tenant owned the “topsoil.”

“Subsoil” was not what we refer to as mineral extraction rights. It was metaphorical subsoil, something akin to what economists call “ground land”—land to stand on, land viewed separately from any improvements made upon it. The tenant owned the literal topsoil, that part of the land where plants actually set down their roots, and which could be improved or disimproved through human labor or neglect.

Ming and Qing Dynasty tenants in the southeast sometimes enjoyed permanent leases on topsoil, and usually got it on very favorable terms. This was because the areas where this system arose were deeply enmeshed in early industrial market exchange. As a consequence, competition was stiff among landlords to acquire tenants efficient enough to keep costs as far below market prices as possible. The lords of the subsoil lengthened contracts, reduced rents and increased their own obligations to dodge taxes, either altogether, or at least the most onerous of them, on behalf of such privileged tenants.

In many respects, this was the best of all possible worlds, even for the government, whether imperial or communist. Tax avoidance “bought” the government a much more thriving economy overall, and it could tax other aspects of this growing economy with levies other than the land tax.

Until late 1988, when it became evident that the state would insist on its power to unilaterally renegotiate contracts, even I thought that the People’s Republic’s contract system might be in the process of converging fully into something like the Ming-Qing Two Lords of the Field System, with the state’s localmost levels of government as the lords of the subsoil.

I ought to have known better. Even a weakening maximal socialist state is too powerful not to be tempted to use that power far too frequently for it to develop better habits. Punishment through reduced productivity sets in too slowly to inhibit reinforcement of the bad habit.

That is why production of grain flattened out during the late ‘80s. The government, having gotten itself in this hole through intervention, continued to inter-

mittently dig it still deeper.

Actually, even absent intervention, it paid better for north Chinese farmers to shift from wheat to other commercial crops and for China to buy its wheat from Eastern Washington, and Australia, paying for it with cheap industrial products. Of course the Chinese government would then have to be nice to the countries from which it buys grain, and it may not want to be that nice.

During the ‘90s, however, the government has tended to back off from the worst of the late ‘80s interventions, and farmers have had few difficulties evading or adjusting to those that remained.

Mid-‘80s extensions of the rural reforms allowed some contracting families to, in turn, sublease all of their contracted land to other families. This gave such families enough money let them move off the land altogether, perhaps to nearby towns or even from the deep interior to the coast to become migratory industrial workers. There are now over 100 million such migrants.

This is akin to a variant of the Two Lords of the Field System of late imperial times called the Three Lords of the Field System. The second lord (i.e. the tenant) would himself become landlord of the third lord, who alone remained on the land.

Such an arrangement was then and is now wholesome because it encourages creation of larger, more efficient units of cultivation. It also supplies labor for a gradual and orderly urban industrialization, an inevitable trend that had been artificially delayed during the Maoist era.

This incipient Three Lords of the Field system was, as you might imagine, causing ideological problems even before the onset of the great repression in June 1989. The social defect of the scheme is that it engenders a great deal of envy of the more successful tenant farmers by the less successful of those who give up their land. But since such people tend to move to town, they are usually not a problem for their home areas.

A greater local danger is posed by potentially envious rural lower (and hence more meritocratic than aristocratic) Party cadres. For a time some of them were bought off by giving them privileged access to public capital for establishing their own family-run rural enterprises. Such practices were, however, denounced as corrupt by student (i.e. apprentice merito-

crat) demonstrators in April-May 1989. Paradoxically, the repression of the students since 1989 has allowed more such buying off of local cadre.

While there is much justice to accusations that such buying off is corrupt, it is possible to argue that these practices partake more of the nature of side payments than bribes. As such, they are defensible, since by definition side payments win permission from the ruling class for everyone else to engage in a wider range of market exchanges than local officials would otherwise permit.

These obvious deviations from the old Maoist ideal of equality of status and talents were only partly papered over by the Party. One new slogan claimed that everyone was destined to grow rich in the rural and eventually also the urban areas, but that some would grow rich sooner than others.<sup>2</sup>

By hook and by crook, enormous numbers of small rural industrial enterprises established themselves under the shade of the surviving village and township collective organizations. Though really private, legal association with collectives allowed these firms to *call* themselves collectives too, and thereby retain respectability in a socialist cultural environment. Their numbers increased from 1.5 million firms in 1978 to 19 million firms in 1988. Their output constituted one-fourth of China's industrial product by that latter date, and they employed 100 million people, full or part time.

By the mid-1990s, buoyed by massive Overseas Chinese investments (chapter 25), these "village and township enterprises" were estimated to be contributing more than any other sector to the private wing of the economy's growth. Macroeconomists believe they now produce more than half of China's GNP.

### c. an urban "beggars' capitalism"

In the towns, the authorities very quickly permitted what Karl Wittfogel once called a "beggars' capitalism" to spring up. During the early '80s, an enormous congeries of small-scale, family-run mercantile and manufacturing operations

in light industry and consumer services sprang up like mushrooms almost overnight in the larger towns and cities. Labor for these was originally restricted to members of a single nuclear family, plus a strictly regulated (supposedly) handful of non-family employees.

The Chinese call such enterprises *getihu* 个体户—individualized households. Whether called by such euphemisms or more accurately characterized as representatives of "beggar's capitalism," they are not to be sneered at. They are very helpful in the manufacture of certain processed foods, the management of small restaurants, and even small (dare one say it) sweatshop operations in ready-to-wear clothing, as well as in the marketing of black market and gray market goods, particularly imported goods. All in all, this beggars' capitalism constitutes contemporary China's version of the transitional phase of the evolution of full industrialization that we have already seen in S. Korea and Japan and will see in Taiwan later in this chapter.

Unfortunately, "beggar capitalists" have proved even more vulnerable to state interventions than peasant contractors. Beginning in fall 1989 some of the larger ones on the manufacturing side, particularly those whose owners were associated with the agitation for political reform, were put out of business for supposed tax-dodging or profiteering.

During the '90s, however, the state's urban controls were overwhelmed by a tide of migrants into the cities from the still somewhat impoverished countryside. Shantytowns utterly outside the state's control sprouted on the outskirts of every major city. In such places beggars' capitalism resumed its previous growth, particularly in the booming southeast.

Until the late '80s, these small private firms were not permitted to grow large enough to compete with the state factories and firms. Nor could they form large scale joint enterprises with foreigners. The latter still require a series of permissions from the state to operate, if only in order to ration expenditure of scarce foreign exchange so as to favor purchase factors of production abroad.

Supposedly to encourage efficient joint operations between bureaus and foreigners, but actually to keep the foreigners isolated from Chinese society, the authorities established a number of "special enterprise" or foreign trade zones (SEZs),

such as Shenzhen, a now city-sized neighborhood right next door to the ex-British colony of Hong Kong.

At first, unfortunately, SEZs served more as funnels for legal, semi-legal and sometimes wholly illegal import of foreign luxury goods for the Party ruling classes than as centers for adding value to foreign producers' goods and then re-exporting the resulting consumers' goods. As the state's power over the economy has receded, however, rational investments in SEZs have grown faster than these pseudo-investments.

State-linked firms in these SEZs still tend to charge foreign producers for high nominal wages. But state functionaries try to confiscate most of these nominal wages, legally or illegally, before they reach the workers. Hence the wages bills of the foreign firms remain very high, but the incomes of their Chinese workers stay relatively low. The result is high cost and hence loss-making sweatshops hurting both workers and foreign investors, and helping only officials on the take. Crack-downs on corruption and competition from other low-wage economies have recently limited such practices. Also, village and township enterprises have grown much faster than such exploitative SEZ firms. While their wages remain very low, the firms are only debited for these low wages and find it easier to undersell their Southeast Asian competitors.

### d. escape of the market

By the middle of the '80s, lagging foreign investment tempted the authorities to let the urban areas go beyond using beggars' capitalism and joint enterprises in two ways.

First, by 1985-86, they began to experiment with applying the contract method to the large, state-owned enterprises. The authorities contracted out management of some enterprises to (hopefully) skilled managers, who got to keep a percentage of any profits that they generated.

This, however, turned out to cause even more trouble and trouble sooner than similar inequality-generating reforms in the rural areas. What Chinese call the "red eye disease" (envy) showed up among the men of merit and lesser Party aristocrats holding fat jobs in the ministries and within the factories which were the line organizations of those ministries. Party aristocrats at the topmost levels of such

<sup>2</sup> George Orwell would have loved this slogan. It is like the sequence of slogans proclaimed by the evolving pig rulers in his *Animal Farm* from "four legs good, two legs bad" to, when the pigs started standing on their hind legs, the final "four legs good, two legs better." In fact, however, Deng's reformers borrowed this slogan from wartime Communism's "economism" phase.

enterprises and ministries displayed jealousy of their prerogatives.

Still worse, employees rendered redundant by such reforms, unlike their country cousins, found it easy to launch urban riots against them.

The authorities often quietly abandoned such schemes or incompetent but influential senior managers subverted them by pocketing (or sharing with employees) faked "profits" financed by loans from the state banks rather than genuine market income.

A second way around this bureaucratic hobbling was to permit some of those small family enterprises completely outside the ken of the officials to grow beyond the beggars' capitalism size. The authorities let the number of their employees grow, first into two-digit and by 1987-8 well into the three-digit level.

A corporate property law passed in June 1988 also guaranteed even absentee ownership rights in joint stock companies. In 1995, village and township enterprises were formally privatized under a corporate income tax law intended to be levied in place of all other local taxes and variable fees. Only time will tell how honestly the government will or can administer such taxation laws. Even the U.S. has not proved to be any sort of paragon in fair administration of its tax laws.

The proprietor of one such company was jailed on a tax dodging charge in August 1989, but such persecution has proved more the exception than the rule during the '90s.

Inflation was an ongoing concern from 1988 into the early '90s. Enormous and accelerating price increases, particularly of agricultural goods, could not be disguised. (From 1997, deflation has become the main problem involving prices.)

Shifting from commands to market signals from 1979 required ending the price controls which kept nominal prices of most agricultural goods below market levels. The only reliable way to induce farmers to produce more of X (on which a price maximum has been set) rather than Y (the price of which has not been controlled) is to take the price maximum off X.

Slight inflation was visible even by 1980 when prices were estimated as having increased 6%. In fits and starts, the government decontrolled additional prices from the mid-'80s, but only during 1988 did that process reach a critical point. To

buffer its urban pets from the price increases in the decontrolled sector, the state kept raising the money supply by ever greater amounts. It used the new money to increase the incomes of these favored urbanites through payments of subsidies disguised as loans to their work units.

This merely encouraged prices in the decontrolled sectors of the market to rise even faster. Inflation hit a 30% annual rate by the spring of 1989. Ominously, prices were apparently rising faster than the money supply. This was a sign that participants in the market sector had figured out what the government was up to. They were trying to raise their prices soon enough to compensate in advance for the next round of money supply increases.

The urban uprising of spring 1989 was preceded and likely partially caused by a sharp reduction in the rate of increase in the money supply. This caused a mild bust accompanied by a drastic fall in the real wages of hitherto privileged urban Workers and Intellectuals. No wonder they took to the streets.

By 1991 the central bank was increasing the money supply again, and by 1993-94 urban inflation rates were again pushing 25-30%. Showing it had learned the lesson of June 1989, the government once again cracked down hard on urban protest even as it prepared to cut back on the rate of increase of the money supply.

And yet growth in GNP of 11-12% (10%, with 6% inflation 1996) per annum was supposedly sustained through 1996. Fukien and Canton provinces were said to have sustained an incredible 25% regional annual growth rate 1991-95.<sup>3</sup> Though the Chinese post-socialist market has not been able to force a shift toward democracy or even much of a move toward the rule of law on the political side, it appeared to have escaped the control of the state as it hurtled toward full industrial maturation.

But as it must for all market economies suffering state intervention, in 1997, China's boom turned into a bust. Several years previously China had sharply depreciated its currency, rendering its goods cheaper expressed in dollars than the goods of its Southeast Asian competitors. By summer 1997 the central banks of the latter lost control of compensatory money devaluations and tumbled into the bust

phase of their business cycle.

Seeking to buy prestige and hence influence over its neighbors, China promised that it and its newly "liberated" acquisition, Hong Kong, would not engage in further monetary depreciation. However, during 1998, inventories of overpriced in dollars export goods piled up in Chinese warehouses. Hong Kong's economy also turned fragile, with a fifth by value of the shares in its stock market bought up by China's government. Central bankers of the world have been creating new money on a vast scale, in an attempt to force at least a simulacrum of a post-bust boom in Asia. In the mean time, the bust spread from East and Southeast Asia to Brazil and Russia. By December of 1998, it was by no means clear that a fairly steep if not necessarily prolonged world-wide bust had been avoided. By the end of 1999 China's situation was still unclear.

## 2. China's so-called "market socialism"

### a. rationales for minimal socialism

Chinese economists have found some theoretical justification for the post-Mao reforms in Central European revisionist Marxism, though they have not dared to go so far as the most radical of the pre-1989 revisionists of former Yugoslavia, Czechoslovakia, Hungary and Poland.

Milovan Djilas, for example, the Yugoslav politician and writer, in one of the century's most important books, *The New Class* (New York, 1957), was the first to identify what I call the upper meritocracy and Party aristocracy of the totalitarian socialist states. In 1957 he labeled these people the "new class," whose perversion of both state and economy had to be undone if socialism was to survive as a viable ordering principle for civilization.

In his preface to Michael Voslensky's *Nomenklatura* (New York, 1984), which illustrates the evolution of the Party aristocracy segment of this new class in Russia since it came into being under Stalin, Djilas concludes that such a system "has no important or promising powers of reform" (p. xvii). Needless to say, Djilas has had no official patronage in China.

Earlier, however, a number of Central European writers took courage from Djilas to try to work out the theory of how a society could both be socialist and operate

<sup>3</sup> Since the bust of 1997, foreign economists have grown suspicious of these rapid growth rates of the early '90s.

in a market. They hoped that the market could tame the ambitions and greed of this “new class.”

One such writer, whose work is easily available in English is, like Djilas, also a Yugoslav. Yaroslav Vanek writes about “worker-managed market socialist enterprises.” Vanek postulates enterprises run by and for their workers—worker managed enterprises—that compete with each other in an open market. Instead of trying to maximize “profit,” Vanek suggests, these worker-owned enterprises will try to maximize wages. Such a system is capable, Vanek believes, of heading off the worst abuses of Djilas’s new class, as well as the worker exploitation by the capitalism that socialism displaced.

Long before Vanek wrote in the 1970s, Oscar Lange, an interwar Polish Marxist economist, wrote similarly while teaching in the United States. When he went back to Poland after World War II, Lange applied the insights of the Neoclassical economic theory he learned from the academic consensus American economists to postulate a very similar version of “market socialism.” Lange would have the socialist planners play a kind of board game version of the market, adjusting prices where necessary to compensate for pre-equilibrium gluts and dearths in the socialist government’s warehouses.

Lange died in Poland in 1966. He did not get to see how badly the Polish economy turned out by following his advice.<sup>4</sup>

In China, Shanghai’s Fudan University was one of the pre-1949 Chinese centers of English Positivist economics—the economics of Adam Smith and David Ricardo and its Neoclassical offshoots. Fudan has taken up “market socialism” since the late ‘70s, but without adding anything significant to its Eastern European forms.

### b. failure of minimal socialist theory

Such theories are all suspect on empirical grounds since none of the market

socialisms based on them has worked. The Yugoslav economy was a mess and had been for more than a generation before the state imploded in 1991. The pre-1990 Polish economy was something worse than a mess and has improved dramatically after undergoing drastic privatization post-1989. The Hungarian market socialist economy was in deep trouble well before the upending of the Communists, also during the Revolution of 1989. Similar difficulties were clearly visible within the reformed Chinese economy of the ‘80s.

Vanek might argue that his system was never really tried. Like several other such writers, he had to write his book in English, publish it in America, and earn his living teaching at Cornell. He was run out of Yugoslavia during the time when Marshall Tito, the great patron of worker managed enterprises, was still alive.

The Fudan economists have not been run out of town, but have had to use language so Delphic in its indirectness in their published work when they allude to the superiority of fully private property, that they have sometimes confused themselves even more than the authorities.

Theories of market socialism also all fail in principle for the same *a priori* logical reasons.

First, like the moron joke about water pills,<sup>5</sup> all of them smuggle into their theories either an actual market or a board-game simulacrum of a market, as did Lange.

The board game is, unfortunately, always run by an upper Party aristocracy supervising the lower Party and non-Party meritocracy of a regime hostile to markets. Even if such market games evolve into actual markets, these Party people retain the power to intervene repeatedly and deeply in the market—i.e. to cheat in the game. It is even easier for the authorities to cheat if only a pseudo-market exists, a kind of big board game at Party headquarters using computers to simulate the bids and acceptances of a real market.

Powerful men can intervene in both real and board-game markets in the maximal socialist states because there is nothing to stop them from doing so. There are no institutional restraints on them. It is something like playing Monopoly with your bratty little sister, who steals your hotel on Marvin Gardens and then calls

for Mom to intervene when you pull her braids. It is something like that, only much nastier when Mom is the Party.

Second, Vanek’s book, like Lange’s essays and many of the Chinese works that imitate both, is also virtually a *reductio ad absurdum* of Ricardian Neoclassical economics. Given Ricardian assumptions about equilibrium, on paper it seems logically necessary that it work. And yet we know that it does not work at all in practice. Vanek’s simultaneous equations show that you must get market equilibrium if you try to maximize workers’ wages rather than entrepreneurs’ profits, which is normally what neoclassical economic theory tries to maximize.

What Vanek *et al* do not realize is that they are implicitly treating a scarce good (capital) as though it was so abundant as to be free. (If you ignore return to capital, that is tantamount to assuming that capital itself must literally be a free good—one you do not pay anything for.)

Since you are ignoring capital anyway, the easiest way to maximize wages in the short run is to consume capital, to not do preventive maintenance on your machines for making machines, and so let these machines rust away.

In the longer run, after running down your capital, you can only maintain wages at a higher than market clearing level by excluding junior workers from your market socialist economy. Instead, you make them go to work in some nearby proper market economy, at lower wages than they would have earned at home without market socialism. Such exclusion of workers consumes still more capital by cutting down on productivity. That, of course, is exactly what happened to the Yugoslav economy under Tito.

Some of the Fudan economists recognize this theoretical problem. They even write about it, but they can only very tentatively and furtively suggest that the only way out of this bind is to drastically curtail the intervention powers of state and Party, allow large-scale private property to appear, and allow the owners of this large scale private property to attempt to maximize the returns to that property.

That in fact is what has been happening in fits and starts in China since 1979. The trouble is, no one in China dares say this out loud.<sup>6</sup>

<sup>4</sup> In one of his interwar American works, Lange thanked Ludwig von Mises for raising the socialist calculation problem (chapter 30.A.3), which Lange believed socialist economists like himself had then solved. In gratitude, Lange wrote, tongue planted firmly in cheek, the future socialist states ought to erect a statue of Mises. In 1990, the year after the collapse of Communism in Central and Eastern Europe, the American Mises Institute placed a bust of the great Austrian economist in the hallway of the Economics Department of Warsaw University, facing the door of what had been Lange’s office.

<sup>5</sup> All you have to do is add water to the pills, and wham, you have water!

<sup>6</sup> Judging from recent essays in the M.E. Sharpe journal of translations from the Chinese economic literature, *Studies in Chinese Economics*, the Chi-

### 3. Reaction against reform

By the end of 1988, the surviving Maoists in China (somewhat confusingly called “conservatives” by *The New York Times* and the academic consensus) were already accusing the reformers of proposing to do what I suggested in the previous paragraph they were afraid to recommend. The Maoists were even beginning to hint that the reformers were merely new-fangled capitalist roaders of the sort Mao used to denounce. This is what the Marxian economist Chen Yun was saying during the ‘80s.

Chen, until his death before the end of the ‘80s, was the octogenarian critic of both Deng Xiaoping in recent years, and of Mao Zedong during the late ‘50s and ‘60s. This was when Mao deviated to the left of an orthodox, supposedly sane Stalinist economic policy.

Deng was, from Chen’s perspective, essentially a right deviationist. Chen considered himself a moderate, middle-of-the-roader. From my perspective he was a Stalinist who would prefer to do without a Stalin, lest the privileges of the Party aristocracy and its meritocratic subordinates and urban worker clients be infringed upon by a Stalin’s (or a Mao’s) crazy excesses.

Beginning in January 1987 the economic reformers began to lose out at the political level. The leading member of Deng’s Sichuan faction, Party Secretary Hu Yaobang, was forced from office. However, Hu’s ally, the Premier, Zhao Ziyang, held on, taking over the Secretaryship for a time.

Six months later Chen Yun was also eased into near retirement. Unfortunately, the new (as of fall 1987) Premier, Li Peng, with a Leninist heavy electrical equipment engineering education received in Russia, seemed even then to be, in terms of his background and previous public statements, a chip off the same old sane Stalinist block as Chen. Li survived long enough to retire peaceably in 1998. Though he was careful not to say much, he mostly agreed with Chen Yun’s anti-reform policies.

nese economists are not yet taking many chances along these lines.



Hu Yaobang. (Hsü.)



Zhao Ziyang. (Hsü.)



Li Peng. (Hsü.)



Jiang Zemin. (Hsü.)

Jiang Zemin, a one-time mayor of Shanghai and a supposedly less “conservative” figure in terms of his economic policy, took over from the disgraced Zhao Ziyang as Party Secretary after the Tiananmen Massacre in June 1989. Jiang has since become President.

At the Chen Yun faction’s insistence, removal of price controls from key agricultural commodities was postponed for at least two years in 1987. The reformers, in desperation, began to sharply increase the money supply so as to keep up subsidies to state firms. In many ways, therefore, not only was economic reform undermined but the chief actors in the bloody acts of political reaction after June 4, 1989 were set in place during the preceding two years.

During the latter part of 1989, political repression allowed the state to risk constricting growth of the money supply. This cut the inflation rate from c. 30% to under 10%. By October a sharp recession began. Coastal regions, particularly Canton (closely linked to Hong Kong’s economy) mostly avoided negative growth (according to government figures). However, unemployment grew sharply among the 100 million employees of private and nominally collective firms in rural areas and small towns.

By the spring and summer of 1990 signs of recovery appeared and soon hints were published in the official newspapers that a return to the limited economic reforms of the early ‘80s might be possible so long as these did not engender renewed calls for political reform. In 1992, a feeble Deng Xiaoping made a symbolic visit to Shenzhen to indicate his continued support for special economic zones and economic growth, but Deng thereafter faded out of active political life and died in February 1997.

Fitful political repression has not, after all, been the direct cause of perverse economic effects during the ‘90s. While monetary manipulation postponed the bust and for a time kept most influential people prosperous, renewed inflation during 1993-5, led to growing unease which seemed to require driving down the value of the currency. Inflation eased during 1996, but the seeds were sown for the post-1996 Southeast Asian bust to affect China as well as Japan and S. Korea.

During the transition from Deng’s rule, Jiang Zemin gave Li Peng’s admini-

stration its head in enforcing political repression, but in exchange won the dubious right to keep money flowing into the state sector so that it would acquiesce in continued growth of the private sector. But of course that Western-style empiricist intervention is what brought on the bust. Sometimes empiricism is just not practical!

## B. Post-Mao Political Reforms

### 1. Pragmatism

The economic reforms could only be carried out after the half-generational change in the political leadership finally came about in the late '70s, essentially a half generation—i.e. a little over a decade—late. Deng Xiaoping became the preeminent leader when he was already in his late seventies, rather than in his mid-sixties, as Zhou Enlai had originally intended.

At the political level, economic reforms have had to be justified essentially on so-called pragmatic grounds as a way to dodge theoretical arguments which would have tended to undermine the legitimacy of the Chinese “new class.”

Deng called himself a pragmatist. He no doubt remembered from his days in the '20s as a student-worker in France the old French adage that at night all cats look gray. In the late '70s he transposed the adage from its French quasi-sexual context to the more wholesome traditional Chinese statement of the pragmatic ideal. His motto became: “it does not matter whether a cat is black or white, so long as it catches mice.”

Deng finally managed to rise back to the top of the political hierarchy only through a pragmatic alliance with the unknown nominal successor to Mao, Hua Guofeng. Deng and Hua clung to each other not just until the Gang of Four was jailed (1976) but until after all four of them had been tried and found guilty (fall 1980).

By then, Deng's own protégés, Hu Yaobang and Zhao Ziyang, a half generation younger than himself and so a full generation younger than Mao, too young to have been on the Long March, were raised into important positions. Hua was eased back into the obscurity of an unimportant vice premiership from which rank

he had originally come. Hu Yaobang became Party Secretary, and Zhao Ziyang became the Premier.

Deng retained for himself merely a vice premiership but also the headship of the state military hierarchy. This let him keep control of the organs of force.

Hu and Zhao first rose to prominence during the late '70s by conducting experiments in the use of the rural contract system and urban beggars' capitalism in Deng's home province of Sichuan.

During the early '80s, Sichuan became the geographic base of a new faction. A Sichuan “Mafia” replaced the old Hunanese “Mafia” of Mao and his eventual enemy, Liu Shaoqi and their junior fellow-provincials. The post-Mao political shift was from a Hunan-Hubei geographic factional coalition to a Sichuan one.

Deng also benefited from the fact that, like the First Emperor of Qin, Mao had let no giants grow up in his shadow. Once Mao had purged Liu Shaoqi, no Hunanese “don” was left to replace the old boss, Mao. The only alternative to Deng's crowd was the “dowager empress's” faction—the Gang of Four under Jiang Qing—the Shanghai Mafia, if you will.

But once even the epigonic remnants of Mao's Hunanese Mafia, led by Hua Guofeng, saw what the alternatives were, they preferred a coalition with the Sichuan crowd, even if that required becoming junior partners, to continuing to be bullied (or worse) by the Shanghai mob. And so, almost by default, Deng's crowd became dominant.

Deng's people could even buy off the younger Maoists—the fortyish new men who had been thirtyish when they crowded onto the ladder of merit prematurely at the beginning of the Cultural Revolution. These hotheads were finally growing up or at least beginning to suffer from tired blood by the late '70s.<sup>7</sup>

In any culture, such men are easily bought with the same sorts of toys; 25” Sony color TVs work well for both American and Chinese Maoists. I personally know several once bloody-minded Chinese Maoists who by 1983 were content to show off their new 25” Sonys acquired in the gray or black market in one of the SEZs through political connec-

tions.<sup>8</sup>

Unfortunately, after a few years of making such side payments to its ruling class, the government ran short of foreign exchange to pay for them, and could not continue such genteel bribery at the former scale. Still more unfortunate is the fact that most of these Maoists are dishonest politicians in New York terms: even when once bought with a 25” Sony, they tend not to stay bought. Most of them eagerly joined the reaction against reform in June 1989.

### 2. Has socialist society been indefinitely postponed?

Sensing the inadequacy of pragmatism, by the mid-'80s, Deng's crowd began to feel the need for a new and more theoretical defense of their position. Having shifted from a white socialist cat to a black market economy cat, and with problems of mouse distribution piling up, Deng was going to have to justify using black cats in other than empirical terms.

Unfortunately, Deng's house ideologues could come up with nothing better than a mirror image of Mao's late '50s thesis that China could make a quick jump from Capitalist Society to Socialist Society and then to Communist Society by means of his Great Leap Forward.

Deng's mouthpieces now said that Mao had actually been more wrong than everyone had thought. He was even wrong at the historical level. We are still, they argued, even after all of the anguish of the Great Leap and the Cultural Revolution, only at the early stages of the transition from Capitalism to Socialism. It would be absurd to talk about beginning the transition from Socialism to Communism for perhaps as long as another century or more.<sup>9</sup>

In other words, Deng's men were arguing that China was still in what I earlier characterized as the consolidation stage of the revolution of the early to mid 1950s, when the Party still tolerated a large

<sup>8</sup> When one of them in 1983 showed such a toy off to a genuinely reactionary American colleague (me) who then owned no better than a 1976 model 19” Sony bought on time at the K-Mart, the result was low comedy of the most satisfying sort. An American Maoist of my acquaintance had a somewhat higher price. He married money and was last seen tooling around town in a snazzy little red Miata.

<sup>9</sup> Liang Qichao call your office! You said as much in 1907, and have been denounced as a mere Social Democrat ever since by Marxist-Nativists! Now this!

<sup>7</sup> Such people were still common in all the American universities by the '80s—fifty year old hippie professors who no longer fit into their blue jeans.

chunk of market activity, and even the existence of a “national bourgeoisie” to run these market activities. Deng’s theorists could also point to Lenin’s New Economic Policy of the 1920s as the main precedent for what they were doing.

As early as 1987 I doubted that the Chen Yun faction would accept this idea and the series of Party advertising slogans it implies after they had been run up the flagpoles of China. In fact this formulation has not been mentioned in the Party press since the spring of 1989. The Party, we can now recognize, had simply been making one more of its periodic oscillations between what it earlier called “commandism” and “economism,” i.e. between varying degrees of interventionism.

For a time during 1988-89 and again during 1993-4, the reformers toyed with an idea that they borrowed from Gorbachev’s crowd in Russia called “the new authoritarianism.” It might be necessary, they argued, for the marketizing reformers to rule autocratically for a time so as to retain the power to continue the reform.

Few of the reformers’ constituents accepted this notion. But after the June 4, 1989 massacre some of the anti-reformers took it over, adding the pseudo-traditionalist argument that authoritarian rule was more congruent with China’s political traditions. Some anti-reformers even began to celebrate the Confucian political tradition precisely for the authoritarian qualities of its “hard” wing. This represented a complete reversal of the hostility toward Confucianism which dominated Party ideological formulations as recently as the anti-Lin, anti-Confucius campaign of the early 1970s.

By the fall of 1990, therefore, the reformers were bereft of usable justifications for political reform, and the conservatives seemed to finally be justifying the label bestowed on them by the Western press. The death watch over Deng Xiaoping since 1993 inhibited any revival of serious discussion of how to handle the reform (or abolition) of socialism.

After Deng finally died in February 1997, the immediate transition was uneventful, though some observers mistakenly predicted the beginnings of instability might accompany the Party Congress in October. Over the long run, Deng’s pragmatism represented tacit abandonment of the Marxist-Maoist vision of Heaven and is bound to undermine any post-Deng Party regime.

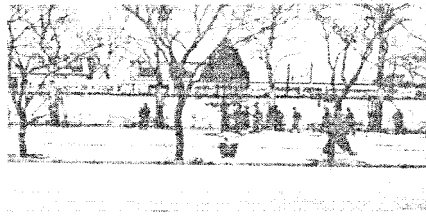
### 3. Illusion of democratization

#### a. “democracy wall”

It was evident even when I wrote the original draft of this chapter in 1987 that neither Deng’s nor his opponents’ faction had or have any tolerance for what both call “bourgeois democracy.” The events of the last decade has only confirmed that not so original insight.

For the first time since 1957 and 1987, a substantial number of students in Beijing attempted to assert their civil liberties at the end of 1978 and the beginning of 1979 to explicitly call for democratization. This coincided with the opening of full diplomatic relations with the U. S.

What came to be called the “Democracy Wall” on Chang’an Street in downtown Peking began to sprout “big character” and “little character” political posters proclaiming this or that claimed new civil right. In April 1979, the authorities took down the posters and told the American press that a new wall was being made available in the “suburbs.”<sup>10</sup>



Democracy Wall in early 1979. (Hsü.)

The young civil rights advocates were all arrested in the spring of 1979 and sent off, as Lincoln’s Secretary of War, Edwin Stanton, liked to put it in his threats against Copperheads, “where they would not hear the birds sing.” A few of them are still there (or have been returned there) nearly two decades later. Though Wei Jingxian, their no longer so young leader was released to what amounts to house arrest early in 1994, he was soon rearrested and in 1996 was returned to prison.

To its credit, Amnesty International, which once tended to avoid dealing with the maximal socialist world, has repeatedly found China guilty of having a perfectly lousy civil rights record. China has

<sup>10</sup> They did not specify how far away that suburb was. Certainly nobody ever found it anywhere in China. For a long time I dined out on the joke that Deng had actually moved it way out to the far far eastern suburbs, and that the wall was now located on the second floor of the Humanities Building, in Bellingham, between the two staircases, and had been renamed the Center for East Asian Studies Bulletin Board.

an even higher rate of executions than South Africa did in *apartheid* days. In 1983, the Party launched a brief but intense campaign against “spiritual pollution” by the West, and enforced it with some 6,000 executions, most of them supposedly of non-political criminals.

In 1996 the renewed spiritual pollution campaign emphasized not spitting in public and killing harmful insects, a weird merging of the anti-spitting aspect of the KMT’s New Life Movement of the ‘30s with Mao’s consciousness-raising anti-bug campaign of the ‘50s.

#### b. the road to Tiananmen

Student riots occurred again in January 1987 to demand democratization and protest against ongoing civil rights violations. But these led only to Hu Yaobang’s fall from power after he failed to move vigorously enough against these demonstrators.<sup>11</sup>

The Thirteenth Party Congress met during the autumn of 1987. It confirmed the status quo: a rough stalemate between Deng, whose faction had had a bad year, and the “conservatives,” who despised marketization of the economy, but feared to give up the economic benefits of reform altogether.

Though Hu lost his job, he kept his seat in the Party Politburo. Zhao Ziyang not only survived, for a time after Hu’s demotion he held both the premiership and Party Secretaryship. Later, though he had to yield the premiership to Li Peng, a sane Stalinist, he remained as Party chief.

The indecisiveness of the Thirteenth Congress’s turn toward reaction gave some hope that reform could continue. The old fellows—the men of the Long March years a half-generation younger than Mao—were all chivvied into retirement. Deng himself also retired, except that for a time he retained his substantive post as head of the Military Commission, the key to retaining his power.

At the end of the ‘70s, Deng persuaded the army to trade heavily increased modernization expenditures for a reduction in its force level from 4 to 3 million men. In 1979 the Army had been humbled by its lack of success against the Viet-

<sup>11</sup> My loss was not as great. I merely had to give up my joke about doing all of my lectures in “costume,” wearing a business suit, just like Hu, who made a big splash in China during the ‘80s by becoming the first high leader to dump his Mao jacket for a business suit.

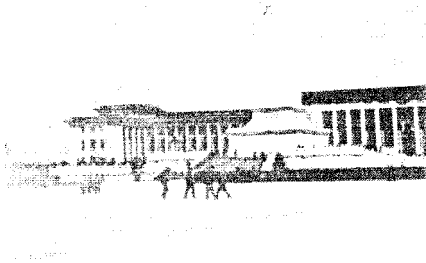
name (see below), and so it felt obliged to cut a deal with the Sichuan crowd.

Optimists hoped the army would continue to have only a limited role in the state—one much more limited than during the Cultural Revolution, when it virtually ran the Party and state. In exchange for freedom to modernize, no one would ask it to do terribly much along military lines to achieve great power status for China.

During the '80s, there seemed to be a realistic reason to expect such prudence. China seemed not to have any immediate prospects for becoming a great power anyway.

By 1995-7, however, that assumption became questionable. The army was always expected to protect socialism at home. After some hesitation during late May of 1989, by the beginning of June the military rallied to the regime and put down with great ferocity the students occupying Tiananmen Square.

The square is the world's largest urban open space. It is located right in front of the old Forbidden City, part of which serves as the residences of the highest Chinese leaders.



Tiananmen Square, looking toward the Tomb of the Unknown Soldier. (Hsü.)

The occasion for these student demonstrations was Hu Yaobang's death from a heart attack in mid April of 1989. After honoring Hu, the students kept extending their occupation of the Square, first to commemorate the 70th anniversary of the May 4, 1919 demonstrations against Japan's takeover of Germany's imperial prerogatives in China, and then to take advantage of Russian President Gorbachev's visit later in May. Gorbachev was coming to officially restore relations between the two Communist Parties. The Party was much embarrassed by the students' continuation of the occupation of the square.

Then the demonstrators insisted on remaining in the square even after Gorbachev left. Neither Party Secretary Zhao, who appeared sympathetic, nor Premier Li, who looked nervous, could move them. For a few days late in May it

seemed as though the regime was losing its nerve. Rumors spread that the army was refusing to move.

Then, after all, the army moved, or at least that part of it run by one of Deng's contemporaries did. The President, General Yang Shangkun, had his son-in-law move units from the north into Beijing.

Before dawn on June 4, 1989, the army killed hundreds, perhaps thousands of student and Worker demonstrators on the square and along its approaches. (The Chinese official account denies that any demonstrators died.) Policemen and soldiers arrested thousands more. Courts executed dozens during the next few weeks, all of them workers, rather than students. Some of those executed had tried to spread the demonstrations to workers in other cities.

The post-Mao political reforms had never really amounted to more than informal tolerance, some of the time, of a much wider range of speech and behavior than would have been put up with before the mid-'80s. During July and August, 1989, all of these informal political reforms were either rolled back or hints were issued that they soon would be. The last illusions of achieving democratization by evolution or by demonstrations disappeared.<sup>12</sup>

Most leaders of the student demonstrators escaped to Paris and Washington and Chicago where they (like Sun Yat-sen before them) proclaimed a new revolutionary movement. The PRC, which was the ultimate beneficiary of the May 4 Movement that launched the new meritocracy on its path to power in 1919, now faced a June 4 Movement directed against itself. Would it take another thirty years for this new movement to succeed? During the last decade the June 4 movement has made little visible progress with its revolution.

<sup>12</sup> China's emergence from isolation (see part C below) had allowed several dozen thousand students to study abroad, mostly in America, since 1979. Enough of them had returned by 1989 for them to teach the lessons of college radicalism they had learned in America to the Chinese students who had remained at home. A number of American college graduates, themselves mostly student radicals, had been serving as English teachers on Chinese campuses since the early '80s. Some of them also taught or exemplified student activism, but no doubt these Americans were often carrying coals to Newcastle. The May 4 tradition had never been lost, just stifled.

## C. Post-Mao Foreign Policy

### 1. China's full emergence from isolationism

It was a fiction of the World War II years of the early '40s that China had become one of the "great powers." Franklin Delano Roosevelt concocted this polite lie to help keep the Kuomintang active in the war against Japan. The KMT and the Soviet Union between them tied down half the Japanese army and over half of the Japanese merchant fleet allowing America to finish off Germany first.

China's own understanding of its political heritage, of course, is that it was not to be a great power, but to be *the only* great power, the only fully sovereign Under Heaven. If it cannot be the only great power, it tries to collapse into isolation from any non-East Asian state that might prevent it from at least making such a claim within East Asia.

During the Communist regime's first decade, China did not have much of a foreign policy except for its relations with Russia and via its rhetorical exchanges with the so-called "third world" nations. Still too busy "building socialism" at home, it made a few gestures toward foreign policy activism during the early '60s, but reverted to extreme isolationism during the first few years of the Cultural Revolution after 1966. It even closed down most of its embassies.

It never missed them during the Cultural Revolution. Even that extreme an isolation both fit China's traditional self-image as a self-sufficient civilization and Mao's variant form of that self-image of China as being unique because it was becoming the first Pure Communist Society. Isolation also allowed Mao to concentrate on the Cultural Revolution.

However, the Soviet Union soon became a danger that could not be ignored. The Chinese realized, once Zhou Enlai got a grip on policy again during the late '60s, that it had been a mistake for China to simultaneously have both America and Russia as foreign enemies. It was ideologically impossible to risk going back to an alliance with Russia. Therefore, the only prudent alternative was to make some sort of connection with America.

So at the beginning of the '70s, when Henry Kissinger was preparing to play

America's "China card" against Russia, Zhou Enlai was prepared to play the "America card," also against Russia.

Because America and China were so distant from each other, and because both were inherently isolationist, they had no occasion for any fundamental quarrel with each other. Under the circumstances, there was nothing to keep them from becoming at least tentative and temporary allies. The American connection gave Zhou a lever not only to move China out into the world again, but also to neutralize the extreme Maoists back home. It helped him to get rid of Lin Biao, for example.

Even before Kissinger arrived in Beijing during July 1971 (see ch. 31, p. 12), China had exchanged a few coy flirtations with America. That spring the two nations engaged in "Ping-Pong diplomacy," when Americans and Chinese played each other in China at the world table tennis championships (and China, as usual in table tennis, won). China started reopening diplomatic relations with other states earlier, in 1970 with Belgium and Canada.

In the fall of 1971, with the U.S.'s acquiescence, Peking replaced Taiwan in the "China seat" at the UN. Though the Chinese accepted and sometimes used the veto that went with permanent membership on the Security Council along with the four other "great powers," they did not try to play a great power's role.

China continued to identify itself with the so-called "Third World"—the poor countries not formally linked to either the industrialized Western "First World" or the supposedly maturing industrial socialist nations of the "Second World." Nevertheless, everyone knew it was meaningless to lump big and somewhat (though peculiarly) developed China in with these little and even less developed African, Asian and Latin American states.

## 2. Brezhnev's counterattacks

The American defeat in Vietnam in 1975 threw America and China more tightly into each other's arms. Both feared Vietnam would upset the Southeast Asian balance of power. Emboldened by winning full diplomatic relations with the U.S. after December '78, During his tour of America Deng also took on the fellows whom people were beginning to fear as "Brezhnev's Gurkhas"—the Vietnamese—in the spring of 1979. But he was surprised and rather alarmed when the

Vietnamese fought him off and won that armed exchange.

He should not have been surprised. There was ample precedent for Vietnam's success. The Vietnamese had been periodically giving China bloody noses ever since they had broken away from the Song Dynasty in the 10th century.

This Chinese defeat threw the Americans and Chinese even closer together. The Chinese kept hugging the American connection even when the superficially unsympathetic Reagan replaced the superficially sympathetic Carter after 1980. But though Reagan hated to do so, he embraced China for the same reason that China embraced him. America and China were the two big losers to Brezhnev's Russia in the East Asian and world balance of power competitions. They needed each other's support, at least for a time.

Brezhnev's foreign policy seemed to go from strength to strength during the '70s. His African clones took over the ex-Portuguese colonies and Ethiopia in Africa, grasped Nicaragua and much of El Salvador in Central America, and finally moved against Afghanistan in Southwest Asia. The "Third World" seemed to be falling into Russia's hands.

Iran was already wracked by revolution by the time the invasion of Afghanistan had begun. Brezhnev seemed likely to be able to use his new Afghan colony as a stepping stone to control the oil of Iran and even of the whole Persian Gulf.

America and China embraced each other still more tightly at this prospect of Russia finally winning the "Great Game" of 19th century power politics in Southwestern Asia.

## 3. Gorbachev's new *détente* and the fall of the Evil Empire

Stalemate in Afghanistan and El Salvador, and the end of the Brezhnev era in the mid-'80s quickly changed this situation. After two no-starters, Comrade Drop-off (i.e. Andropov) and his even more moribund successor, Chernenko, the Russians finally picked a live wire—Gorbachev. "Gorby" began trying to provide Russia with a new version of Stalinism without a Stalin while showing a humane face abroad. For a time he also seemed to be dragging his aristocratic Party establishment toward the same sort of market

socialism that China had partly implemented.

However, despite suffering an economic collapse climaxing in 1991 almost as severe as the one China underwent in the aftermath of the Great Leap, the Russians did not go as far as China did with its rural reforms and urban beggars' capitalism. Gorbachev did not even start a rural contract system. Though that and various supposedly radical market-based reforms had been promised since June 1988, Gorbachev implemented none of them by the time of his fall at the end of 1991.

At first alarmed by Gorbachev's rhetoric about the changes he anticipated making, the Chinese eventually were willing to separate foreign policy from approval of Russian domestic policy. Gorbachev proved similarly flexible. Gorbachev was in a sense already playing his China card against the United States by the end of 1988. His May 1989 visit to Beijing constituted the placing of that card on the table. But it did him no good.

The Revolutions of October-December 1989 in Eastern Europe may have been the unintended result of attempts by Gorbachev to place clones of himself in charge of the satellites. But the result was rapid and complete disintegration of Russia's Central European empire. Two years later the Soviet Union itself fell to pieces. This rendered all earlier balance of power calculations irrelevant. Fearing the spread of these revolutions to it, but fearing isolation even more, China has retained both its Russian and American connections since 1992, helped by the Clinton administration's knee jerk sinophilia.

Both Russia and China backed the Americans in their confrontation with Iraq during August and early September 1990, but both were disconcerted at the ease of America's victory during the "Desert Storm" campaign in early 1991.

In an increasingly novel and vaguely threatening international context, and with a new domestic "deathwatch" (this time for the 93 year old Deng Xiaoping) under way during the '90s, the first impulse of China's leaders must have been to once more withdraw from the world. And yet China needs foreign trade if it is to resume the amazing (and perhaps exaggerated) growth of the late '80s and early '90s. It has to retain relations with both Russia and America if it is to short-circuit any tendency of either to combine with the other in some way that might threaten

China's interests.

That means staying out in the traffic as part of the world balance of power. Since the risk of a domestic explosion during the crisis of the first full generation succession remains, the team of Li Peng and Jiang Zemin tried to rally the military behind it by encouraging missile sales from the Chinese military's factories to the Middle East and Pakistan, and by throwing China's naval weight around in the South China Sea. China also bought substantial amounts of weapons from Russia, including (perhaps) the services of otherwise unemployed Russian missile scientists and engineers.

The 1997 meeting of the national legislative body nominally retired Li Peng as Prime Minister. He had already served the two terms specified in the Chinese constitution. His replacement was Zhu Rongji, a former mayor of Shanghai, and more recently head of the central bank, and hence subject to nomination as scapegoat if the 1997-99 bust gets out of hand.

If the Americans do not let themselves be bluffed by China's renewal of its Russian connection, Jiang and/or Zhu might lose out in to some general who might well replace one or both of them. This hypothetical military strongman might not have to go back to Li and Jiang's aggressive policy. The rest of the military, in alliance with the new plutocracy of the village and township enterprises and the private partners of the stronger state enterprises, might be content with participating, to be sure somewhat corruptly, in the maturation of China's full industrial economy during the next couple of decades.

Who this Chinese version of South Korea's General Park Chung-yi might turn out to be is not yet clear. To fit the South Korean pattern he ought to be somehow linked to the Hong Kong-Canton-Overseas Chinese incipient plutocracy, but not to Hong Kong's social democrat men of merit nor to those central economic authorities who will be blamed for the overdo cyclical downturn.

The April 21, 1997 *Barron's*, p. 42, reported an alarming general rise in inventories in China, in the private as well as state sectors. By August 1998, however, anonymous Chinese sources were claiming that increased sales at home and abroad were beginning to work down inventories. By December, it was still not clear that an economic upturn was under

way, and these doubts increased during 1999.

(China's foreign trade balance dropped by 37 percent during 1999. Economic growth fell from 9.6 percent in 1996 to 8.8 percent in 1997, to 7.8 percent in 1998, and to an estimated 7 percent for 1999. China won the gratitude of its Southeast Asian neighbors by not devaluing the *yuan* as they did in 1995, but got a similar effect by increasing export rebates by 24.2 percent.

(During 1998, state owned firms used 70 percent of resources but produced only 30 percent of output. During 1999 the state was unable to make up its mind whether to encourage or ban foreign investment in communications and internet firms. There is no consensus on the level of unemployment, but a late 1999 UN guestimate set urban unemployment at 8 percent during 1998. The beginnings of state firm reform may have turned loose 15 percent of urban workers.

(In July 1998 President Jiang ordered the military to divest itself of control of its 15,000 business enterprises, which yield annual revenues of \$25 billion, three times the size of the defense budget. So far the civilians are maintaining control of the military, but control of these businesses may be falling into the hands of hoards of brothers-in-law and cousins of generals and colonels.)<sup>13</sup>

## D. Taiwan Under Japan

When we left the story of Taiwan in chapter 26, the Manchus had just taken over the island in 1683. I briefly alluded to the subsequent history of the island in chapter 25, as part of the story of Overseas China and in chapter 20 as part of Japan's empire. We can now draw these several historical threads together.

Taiwan remains now the only substantial population of Overseas Chinese with a claim to sovereignty. This seriously challenges the sovereign prerogatives of the People's Republic. Taiwan's history may, therefore, contain some hints for the future of the People's Republic.

### 1. Taiwan's sinification

Taiwan was not a part of China or even of the Chinese sphere of cultural influence before Zheng Chenggong's (Kox-

inga the Pirate's) invasion of the 1650s and the subsequent migration to Taiwan of thousands of Fukienese refugees fleeing the Manchu conquerors. Taiwan was the last part of Zone C that Chinese civilization swallowed during its twenty century-long expansion into zone C from zone B. There were reasons for the delay.

Taiwan was not a very attractive site for extensive Chinese settlement. It is a medium sized island, shaped like a ragged teardrop, and hardly bigger than Vancouver Island. The only extensive flat parts are on its western edges, and these comprise less than a third of its area. The rest of the island is very hilly, and the east coast is alarmingly vertical. The east coast is an above surface edge of an old continental plate. Hence much of eastern Taiwan just stops at an elevation of about 2,000 feet and drops straight down to the Pacific Ocean, leaving the east without much of a coastal plain or many ports.

Early Chinese settlers founded several Taiwanese cities: Taipei in the north (*pei*, *bei* 北 in the new transliteration, meaning "north" in Chinese), Taichung in the northcentral part of the west coast (*chung/zhong* 中 meaning "center"), Tainan toward the south (*nan* 南 meaning "south"), and Kaohsiung (*Gaoxiung*) near the southern end of the island, now a very important commercial and industrial city. (The little black and white TV in your grandfather's shop a generation ago and your computer's VGA computer monitor and mother board were probably manufactured there.) Notice that all these places are on the west coast.

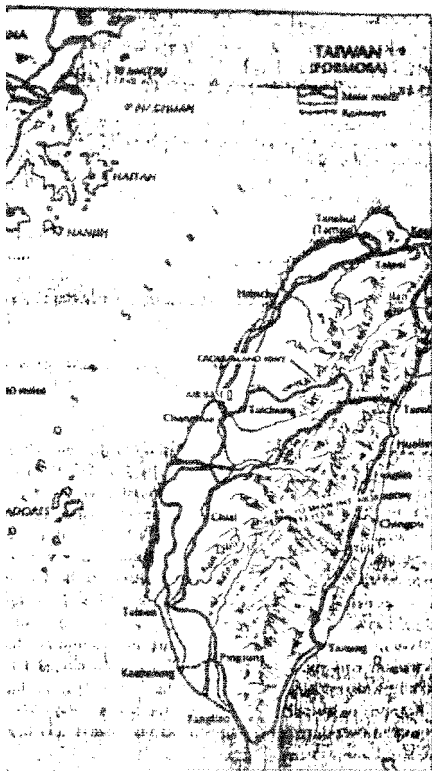
The Portuguese discovered the island in the 16th century. They gave Taiwan 臺灣 (literally meaning "Platform Bay") its Portuguese alternative name—Formosa—short for *Ilha Formosa*—"beautiful island." After the Dutch muscled the Portuguese aside as the major Western power on the China coast during the second quarter of the 17th century, they put up a fort near what later became the city of Tainan.

The Dutch set up shop on Taiwan because the Portuguese had already been allowed by China's Ming Dynasty to take over the choicest location on the China coast, Macao, near Canton. The Ming refused similar privileges to Holland, and so the Dutch took over the nearest place not under Chinese jurisdiction. Tainan was also out at the margin of Dutch power, and so could not put up any real resistance

<sup>13</sup> Summarized from Stratfor.com, 12/21/99.

to Koxinga's invaders.

Most of the refugees accompanying Koxinga hailed from Fukien (Fujian), just across the straits from Taiwan. Their migration, though they did not have to come as far, resembled that of those marginal Englishmen who moved to the east coast of North America during that same generation. Coastal Fukien was beginning to get crowded enough so that settlers would likely soon have begun to move from there to Taiwan anyway.



Taiwan.

A century before, other Chinese merchants from Fukien had gone much further to begin to trade and settle heavily in what became Manila. Chinese had also begun to move into Thailand, Burma and Vietnam. As early as the Song Dynasty, Chinese overseas settlement stretched as far west as the Straits of Malacca and as far east as the north coast of Borneo.

Why did it take the Chinese so long to settle a place so much closer to home? You must remember that these earlier migrants were mostly merchants. They moved first into the commercially most interesting areas regardless of their distance from Fukien or Canton, from where most of them came.

What, after all, could they sell to a bunch of primitive headhunters on Taiwan? What did these Taiwanese have to exchange that was not more conveniently available back home in Fukien? Taiwan

was just a place to sail past on the way to someplace commercially more interesting. For a century after the discovery of the New World, New England was similarly uninteresting to Europeans, even though it lacked headhunters.

Taiwan first became interesting to Fukienese in the middle of the 17th century as a refuge from Manchu invaders, and thereafter as a source of land for crowded Fukien landlords and their tenants. A bit earlier, New England became interesting as a refuge for Puritans from and unsympathetic English government.

At this point, the analogy between Taiwan and the New World gradually breaks down due to the shorter distances between the old and new worlds of China. After they took over the island, the Manchus treated Taiwan as little more than a mirror-image extension of Fukien province. Both had hilly back country above a narrow, commercially well-developed coastal plain. However, the western plains of Taiwan were economically almost as remote, as much out of the main lanes of traffic, as was the inland hill country of mainland Fukien, where tea was the only crop of commercial interest.

The best people from Fukien were still not interested in Taiwan. For those whose class status was below the level of the best people, however, it did represent a chance to acquire scarce flat land. Once interest in the island was kindled by Koxinga and his fellow refugees, immigration continued.

Koxinga died at age 39, soon after conquering the island, just as he was planning to strengthen his base for an eventual return to the mainland by putting together an Overseas Chinese empire. The first link to his new Taiwan base was to have been the Chinese settlement of Manila.

He intended to save the Manila Chinese from their Spanish persecutors. (The Spanish did not have any Jews there to persecute, so they had to make do with pogroms against Chinese pariah entrepreneurs instead.) Koxinga still had his father's big commercial fleet, and would probably have wiped up the floor with the already overextended and declining Spanish as handily as he had done with the Dutch.

Once he died, however, this project was given up for all time. Overseas China was apparently destined to remain a rope of sand, a congeries of atomized, uncon-

nected Chinese local states and Chinese communities subordinate to local peoples.

Koxinga's death also aborted the best chance before the 19th century to develop a powerful plutocratic sector at the national levels of the Chinese ruling class, first in Overseas China, then in China proper.

In the 1680s the Kangxi Emperor took over Taiwan from Koxinga's descendants. This reopened the island to the mainland and to the land hunger of both would-be meritocrat landlords and eager tenants. All during the 17th, 18th and first part of the 19th centuries, settlers slowly drifted into the western third of Taiwan, mostly from Fukien, and most of them seeking agricultural land.

The settlers tamed some of the aborigines and, especially in the south, where the natives were more numerous and more devoted to agriculture, intermarried with them, but elsewhere pushed them aside into the hilly eastern two-thirds of the island, just as Chinese had done earlier with other non-Chinese peoples when settling the mainland parts of subzones C2 and C3.

The Qing Dynasty soon lapsed into a policy of chronic neglect of this out of the way part of Fukien Province. Taiwan was not even detached as a separate province until late in the 19th century, just before China lost it to the Japanese.

Only then, when it was too late, did the Manchus realize that Japan was after the island, and that they had better stop neglecting it. They also had to put some serious military resources into the island after the middle of the century to repress several local uprisings. But all this was too little and too late, the usual story for the late Qing Dynasty's reforms in general. Taiwan was ripe for the plucking, and the Japanese finally plucked it after the 1894-95 Sino-Japanese War.

## 2. The early colonial period

The Japanese had been casting covetous eyes upon Taiwan since the early 1870s, when they developed a modern strategic sense. They categorized it, along with the Ryukyu Islands and the Bonin Islands to its north, as simple extensions of their own home islands, which in some geological sense, I suppose, is true.

The Sino-Japanese War of 1894-95 gave the Japanese their chance. The French-Russian-German intervention in

the aftermath of that war let Japan keep Taiwan as a consolation prize after forcing Japan out of Korea and Manchuria.

The Japanese took over possession of the island in 1895, and from then through the early to mid 1920s, their period of “liberal imperialism,” they did a rather decent job as reforming imperialists.

On Taiwan, if not in Korea, the Japanese proved to be at least as admirable a set of liberal imperialists as the Americans in the Philippines and Puerto Rico during the same period. Even on Taiwan, however, they were a little closer in behavior to the rather nasty tone the Americans took toward their sphere of imperial influence in Cuba. Overall, though, they were on all fours with the Americans as transmitters of modern economic and social institutions to their colonies.

Town walls quickly came down all over the island, half a century sooner than in China proper. The Japanese have never favored city walls, even in Japan. Many of the ordinary, every day manners of the Taiwanese became odd yet rather pleasant combinations of Chinese and Japanese manners. The Japanese even brought in baseball almost as soon as they acquired a taste for it themselves from the Americans.<sup>14</sup>

All in all, people on Taiwan were at first intrigued by the novelty of Japanese rule more than they resented it. After all, the Qing Dynasty’s tenure had been no treat for them. By the 1890s, patriotic Taiwanese were also coming to think of the Manchus as an alien conquering race. At least the Japanese were liberal, modern-minded imperialists, rather than archaic imperialists like the Manchus.

The Japanese behaved much more benevolently toward the Taiwanese than they did toward the Koreans, whose country also became a Japanese colony by 1910. This may have been partly because the Japanese respected Chinese culture more than they did Korean. Korea’s culture was so parallel to Japan’s that the similarity might have bred contempt for it in Japanese eyes. Partly it may have been because there were fewer Taiwanese than

Koreans, and the Taiwanese had not developed much in the way of *Taiwanese* nationalistic sentiments. *Chinese* nationalism of the modern sort hardly existed even on the mainland in the 1890s. The Koreans, however, had been nationalistic for centuries. Japanese good behavior on the island during the first decades of Japanese colonization tended to evoke a cooperative Taiwanese response. This in turn reinforced Japanese inclinations toward benevolence.

Within a few years, Japan provided the Taiwanese with wide access to modern public schools. This was sooner than Chinese mainland governments provided wide access to modern schools. To be sure these were segregated public schools, but this was Plessy vs. Ferguson style segregation—separate, but sort of equal. That the Taiwanese were at this stage kept separate from the Japanese school kids may have been something of an advantage. The Japanese settlers had all the political and social advantages of being the bosses or the bosses’ relatives. By segregating the Japanese out of the new Taiwanese public schools, the Japanese, however inadvertently, made sure that the Taiwanese did not have to compete with the Japanese settlers under unfair circumstances.

Also, certain jobs in these new primary, secondary and tertiary schools as well as such other public jobs as policemen and other local functionaries were open to Taiwanese who had modern educations.

By the end of World War I, Japan’s liberal imperialists had built up a fairly decent political and social infrastructure on Taiwan.

In addition to schools, Japanese public capital provided roads and other modern public institutions. By the late 1920s the Japanese colonial administration began to add industrial infrastructure. This included dams, electric generators and power lines leading from the dams all over the island, improved harbors and railroad lines. It was almost impossible at first to do much for the rugged eastern two thirds of the island.

### 3. The later colonial period

It is the later colonial period, beginning after World War I, that raises ambiguities, moral as well as material, for judging the Japanese version of imperial-

ism. The Japanese added still more industry during this period. They even integrated the schools. But this educational integration probably made life tougher for the Taiwanese. The lower bureaucracy in the schools was heavily infiltrated by the now more numerous Japanese *colons* (settlers), just as in Korea. These Japanese had an unfair advantage in competing for public sector jobs with Taiwanese since they were the members of the “master race.”

The flip side of this disadvantage was that since the Taiwanese business class now had fewer chances to gain jobs in the public or quasi-public sector, they were obliged to concentrate on business. They thereby both helped develop the market sector of the Taiwanese economy and increased their own wealth. They even got on pretty well with the Japanese in the market. More or less voluntarily, most of them learned to speak Japanese, and most middle class Taiwanese over age 60 still speak tolerably good Japanese.

The Japanese *colons* took over a very large role as landlords during this period, very much as they were doing in Korea, but with a slight time lag. The *colons* did not show up in large numbers in Taiwan until the ‘20s, when they ran out of available land to engross in Korea.

Tenancy was already quite common in Taiwan before 1895, just as it was in Fுகien. Settlers carried over to Taiwan variants of the Two Lords of the Field system even before the Japanese arrived. Also as on the mainland, in fairly well-commercialized areas, such as the northwestern part of the island, tenancy terms fairly favorable to the tenants (the scarce skilled and diligent labor factor) were common.

These conditions still more or less continued to hold under the Japanese. So Japanese landlords tended to have to offer favorable terms to their tenants as well. But we must add the quibble that Japanese *colon* landlords could and often did more easily take unfair advantage of Chinese tenants than native Taiwanese Chinese landlords could get away with earlier.

The result of all these changes was increased social tension between Taiwanese and Japanese settlers and administrators during the last half of Japan’s colonial tenure. This was particularly the case in relations between the Japanese and the increasing numbers of Taiwanese secondary and tertiary school graduates. Taiwanese students, like contemporary mainland

<sup>14</sup> That is why during the 1970s and ‘80s and again in 1995 Taiwanese kids regularly wiped up the floor with American Little Leaguers in the World Little League championship series. For some reason, though, Taiwanese champions seem to burn themselves out by the time they grow up. Taiwanese players have so far only been able to break into the Japanese big leagues. The Japanese Babe Ruth is a Taiwanese.

China students, raised increasing amounts of increasingly pan-Chinese (as opposed to localistic Taiwanese) nationalistic hell during the '30s. The Japanese escalated their repression accordingly, though Taiwanese student violence never got as bad as nationalistic violence did in Korea.

Christian missionaries were present, but there were not as many of them as in Korea. Nor did they have the same kind of self-identification with Taiwan as their brethren in China and Korea had with China proper or with Korea. This was partly an accident of the history of Christian missions in the east. Because Taiwan was still thought of by missionary organizations as just one small part of greater China, their Taiwan mission branches did not have visibility as separate entities.

So Christian missions did not play the same conspicuous role as nurturers of either Chinese or local nationalism in Taiwan as they did for Korean nationalism in Korea. Still, they bulked larger in Taiwan than in China, and almost as large as in Korea.

As a consequence, they influenced the development of the middle classes more than in China, though less intensively than in Korea. Protestantism (as compared to Catholicism) was more important in Taiwan than in Korea. As in Korea, Protestantism took pietistic forms that encouraged the budding off of new sects under an independent native clergy. This further limited missionary influence and further depoliticized Christianity's role.

## E. Taiwan Under KMT Control

### 1. Return of KMT China

#### a. "Formosa betrayed"

In 1945, when the Japanese empire collapsed, no heroic measures were required for China to take back control over Taiwan. The KMT occupation force could make do with inefficient, cruel and corrupt officers and thuggish soldiers, who anyway were all that could be spared from the civil war.

The locals had fitfully rioted against Japanese rule during the '30s. They now expected the KMT to grant Taiwan a large measure of self-government. They began to protest when they did not get it. In February 1947, wide scale riots broke out.

These quickly evoked savage reprisals, worse than anything the Japanese had done. Perhaps several tens of thousands were killed, many more injured, and all the rest had their hearts broken.<sup>15</sup>

In a sense the KMT military government merely replaced the Japanese as colonial overlords from 1945 to 1949. Hence it was natural for the KMT functionaries and the carpetbaggers who accompanied them to assume some of the same privileges as colonial occupiers that the Japanese had enjoyed. Few of the KMT mainland officers were even from Fukien. They had little in common with the Taiwanese, and probably found them as culturally alien as the Japanese.

Taiwan had lived half a century under Japan. In several key ways it was no longer fully Chinese, but rather a hybrid between China and Japan in both the details and overall style of its culture. The KMT functionaries sensed this, and intuitively resented the Taiwanese almost as much as if the natives had been fully Japanese. Beyond this, they were infuriated by the implication that the Taiwanese might even be a step up in development from China proper, just because of their former Japanese connection. As a consequence, they persecuted the Taiwanese all the more nastily.

The best you can probably say about the first four years of KMT rule is that it at least got rid of the Japanese *colons*, who were all shipped home almost overnight before the end of 1945.

Once the atrocities of February 1947 had calmed things down, the KMT governance of Taiwan reverted to a policy of unbenign neglect, resembling the governance of the Qing Dynasty previously.

#### b. the KMT diaspora arrives

And then the KMT-Taiwan relationship suddenly got much worse. In 1949, the defeated KMT national government fled the mainland. Two million refugees flooded into a little island already containing ten million people. That was an enormous proportion. How would the five million people of the state of Washington react to one million people from British Columbia fleeing a New Democrat provincial government into the fertile but narrow region west of the Cascades?

Half of these KMT refugees were sol-

diers, who were (until demobilized) mostly economically idle and useless—just mouths attached to hands that performed no economically useful work. This further increased what was already an enormous burden for this poor little island to bear.

Still, Taiwan perhaps was better able to handle the two million mainlanders because it was already undergoing a population explosion under the Japanese. Its population had more than doubled to ten million in the course of the fifty years of Japanese rule, thanks to public health measures and the growing economy. For both of these the Japanese can take much credit.

As is normally the case when development is occurring, while the death rate drifted down modestly under the Japanese, the Taiwanese birth rate initially remained high. As nearly as we can tell, however, the standard of living still managed to drift upwards under Japanese rule.

Still, to support even ten million people was something of an exploit for a small island with less than a third of its area flat enough to support very many people to the acre. A sudden increase to twelve million made people fear that life would become impossible.

Of course such things are relative. The population is now double that (the 20 millionth Taiwanese was born in July 1989), and the 21st million arrived by 1994. But now Taiwan's economy has become a mature full industrial one. A visitor hardly feels more crowded in Taipei than in any other fully industrial big city. (Holland is more densely populated than Taiwan.)

Over the short run of the early 1950s, however, wealth per capita temporarily declined while the refugees were being assimilated. Given this demographic-industrial factor and the associated cultural stress, it was grotesque for right wing Americans of the China Lobby during 1949-50 to have howled about the necessity to "unleash" Chiang Kai-shek and the KMT armies so they could reconquer the mainland. The KMT army could not have received much support for such a campaign from the overburdened Taiwanese economy.

Right after the war in Korea broke out in June 1950, President Truman put the 7th Fleet in the Straits of Taiwan. But this was to protect an enfeebled Taiwan from a barely existing Communist invasion fleet that was forming on the Fukien coast

<sup>15</sup> This nasty episode is extensively chronicled in George Kerr's accurate, though somewhat excessively anti-KMT tract *Formosa Betrayed*.

then, and to give Chiang an excuse *not* to try to execute some hopeless invasion.

The 7th Fleet was never intended to serve as the escort for such an invasion of the mainland. President Truman stated quite clearly that the Fleet was to prevent invasions from *either* direction. Nothing said at the time nor in the documents from the archives opened since then to indicate that such an escort service back to the mainland was any part of the intent of President Truman or his Joint Chiefs of Staff.

The coming of these two million refugees was enormously alienating culturally for the Taiwanese. The Mainlanders came from all over China. The most influential of them, however, were sharpies from Shanghai and nearby parts of Chekiang and Kiangsu Provinces in the lower Yangzi valley, as well as snooty northern intellectuals. Ethnically and linguistically, all these people were somewhat different from the locals, who were mainly settlers from nearby Fukien Province. The Taiwanese spoke an entirely different Chinese language from most of the Mainlanders. They were as different from these interlopers linguistically and culturally as are the English from the Dutch, Germans, French and Spanish taken together.

## 2. Land reform & industrialization

If you compare old photos of and anecdotal evidence about the '50s with similar evidence from the '30s, early '50s Taiwan looks like a much poorer country than the '30s Japanese colony. Still, KMT Taiwan had some assets, most of them, to be sure, inherited from the Japanese occupation, and resembling the assets South and (to some degree) North Korea inherited from Japan.

As in North Korea, Japan built lots of hydroelectric dams in the rugged eastern two-thirds of the island. Like South Korea, Taiwan had lots of land formerly held by the Japanese government and Japanese settlers, but which was now held by the KMT government. In both places such land could be sold cheaply to tenants as a large part of a land reform program. As in South Korea earlier, such a land reform was in fact carried out by the KMT on Taiwan by the mid '50s.

The native Taiwanese bourgeoisie had been engaging in some urban industrial activity for a generation. The KMT inher-

ited from Japan a fairly large quasi-public and public industrial infrastructure—bus lines, for example.

The KMT could easily give away shares in these government or partly government-owned urban enterprises to Taiwanese landlords in exchange for the land taken away from them as part of the land reform. This quickly transformed a rural landlord class into an urban capitalist class, and encouraged it to thereafter continue to save so as to invest in and further develop urban industry. As in South Korea, land reform did not undermine the market by confiscating large amounts of private property without real compensation in capital goods and capitalized land elsewhere in the economy.

The KMT also used its large army for labor-intensive public works, particularly building roads in the mountainous eastern two-thirds of the island to open this region to the automotive age. In the course of the 1950s, such projects turned what had been the disadvantage of an economically useless army into at least a modest asset. The KMT government probably could not have afforded to hire so many civilians for such tasks, if only because the marginal return from the tasks' completion would not have equaled the cost of hiring these men on the market.

Once the KMT signed the American-sponsored peace treaty with Japan in 1951, large-scale trade with Japan quickly resumed. Japan soon thereafter matured its industrial economy. This let Taiwanese industries get hold of ever more Japanese capital and licenses to use its technology on easy commercial terms. Access to the Japanese market allowed Taiwan to pay for this capital with agricultural and eventually crude industrial products. For some time, virtually all the bananas sold in Japan were from Taiwan.<sup>16</sup>

Taiwan reconnected up with Japan sooner than did South Korea, which was distracted by the Korean War, and then by its people's much more intense hatred of the Japanese. The Taiwanese remained at peace after 1945, had never been that resentful of Japan, and had long since transferred most of their resentment from the Japanese colonialists to the KMT semi-colonialists. Hence Taiwan had its Japanese connection pretty well reestablished during the '50s. Only during the early

'60s did South Korea link up again with Japan.

Most of the middle class Taiwanese, as opposed to the mainlander refugees, still spoke pretty decent Japanese, which they had learned for business purposes in the course of the preceding half century. Taiwanese could easily restore and further develop their business connections with Japanese firms. Doing so put the Taiwanese one up on their mainlander rulers, fewer of whom could speak Japanese.

Of course, despite this lag, and the effects of the Korean War, South Korea is more developed in some ways than is Taiwan. The main reason for this is simply that with a population of 44 million (as opposed to Taiwan's 21 million) South Korea enjoys certain economies of scale.

There are some things you just cannot afford to do with less than thirty or forty million people. You cannot, for example, afford a big integrated steel industry. Taiwan has an inefficiently small state-owned integrated steel complex, its small size dictated by the small size of the Taiwanese domestic market and the limited resources of the government. But that has rendered the plant incapable of realizing some crucial economies of large scale. As a consequence, it has always lost money, and always will do so. South Korea can afford a large and efficient steel industry.

But aside from such inefficiency-causing differences in scale, Taiwan is very well developed even in ferrous metals. Recently, its private sector actually began producing specialty steels profitably in several modern "mini-mills." It can easily afford to buy from foreigners those goods it cannot produce. So access to large external markets more than compensates for Taiwan's own small size. As expected, the economic laws of absolute and comparative economic advantage protect small states too.

## 3. The American connection

The American connection in general and American foreign aid in particular are often said to have played a crucial role in Taiwan's rapid development.

Over the long run, access to the large American market undoubtedly helped Taiwan both to complete its takeoff and move rapidly toward industrial maturation by compensating for the small size of the Taiwanese domestic market.

Over the short run, American military

<sup>16</sup> This shows that even a "banana republic" can industrialize, if the conditions, though not the bananas, are ripe.

protection unquestionably shielded Taiwan during its time of greatest vulnerability during the 1950s.

It is also, however, conventional among academic consensus economic historians to give a lot of credit to the Americans for their *economic* foreign aid, particularly for their help with the land reform of the '50s. Much American economic aid was, however, short-term relief delivered in grain, which as in South Korea, depressed domestic grain prices, and long-term military aid, which (though highly useful for defense) had little direct effect on economic development.

In the land reform, the U.S. just advised the Taiwanese to do what was the only thing for them to do anyway. It was really all the freely available land previously confiscated from the Japanese that made a market-nurturing land reform possible. A similar reform worked in South Korea for the same reasons. Japan already had a maturing industrial economy at the time of its land reform, and its landlords had been discredited by loss of the war. Hence no serious harm to the prestige of the market resulted from fleecing them.<sup>17</sup>

The University of London economist, Lord Peter Bauer, has for nearly half a century put forth arguments demonstrating the perversity of all government to government foreign aid. Such aid necessarily undermines markets by placing resources in the hands of recipient country bureaucrats who are either enemies of the market or enjoy corrupt relationships with privileged players in the market. Lord Bauer's arguments hold for Taiwan too.

Fortunately, most of the American aid to Taiwan was military rather than economic. It is significant that most of the big growth came *after* American aid, mostly the limited economic aid, petered out at the end of the 1950s.

Some people say that at least the UN population control programs (also mostly

funded by the Americans) enjoyed significant success. But even with these programs, by the late '80s Taiwan had coasted up from 12 million to 20 million people. With 21 million people in 1994 and half a million more by 1998, Taiwan has the world's second highest population density, coming just after Holland. If you leave out the virtually uninhabited eastern two-thirds of the island, the population density is even higher than Holland's. Notice that both Holland and Taiwan are nevertheless very rich countries.

The UN's birth control programs were not only unsuccessful in their own terms, they were also redundant. Statistics verified by the UN itself show that the Taiwanese birth rate started to drop eighteen months *before* the first UN population control aid started.<sup>18</sup>

What apparently happened in Taiwan, as elsewhere before and since, was that during the industrial takeoff of the late '50s, women noticed that fewer infants were being lost to disease, and so they figured that to have seven children survive they did not any longer have to undergo a dozen pregnancies.

Women also participated in urbanization, along with their husbands. When ambitious young women moved into a maturing urban industrial society, they soon delayed marriage (or practiced divorce more, or both) and after marriage maximized the amount of investment they devoted per kid, particularly investment in education. So they quickly decided to not even have seven kids, but three, and these days barely more than or even less than two.

Whether in Taiwan, Japan or South Korea, each of these kids is educated to within an inch of its life, formally in public schools and in Japanese-style private cram schools, and informally, through the constant nagging of "education mamas."

If a contemporary Taiwanese woman overshoots her self-determined quota of children, it is usually only because she has had the bad luck to give birth to a run of girls. In some families she keeps trying until she produces a boy, which is what you would expect in a Chinese context. Even so, at current birth rates, Taiwan's

population will actually start declining in 2025. There is also no need even for mainland China to force abortions, especially of girls, to also eventually reach ZPG.

So I would argue that there is no credit at all to be given to the UN/U.S. population control aid. Taiwan industrialized, and then the population problem took care of itself, just as happened earlier in Europe, North America, and Japan.

## F. Contemporary Taiwan

### 1. The "pariah" states

Since the '70s, Taiwan has seemed to be vulnerable, at least in its external political relations. Economically and militarily, it has, at least until recently, gone from strength to strength.

Once it was thrown off the "China seat" in the UN to make room for Red China in 1971, Taiwan became one of the world's leading "pariah" states, along with Israel, White settler-controlled Southern Rhodesia and South Africa. These pariah states were the Rodney Dangerfields of contemporary international politics: well-off and interesting, but they "didn't get no respect."

Southern Rhodesia has been rebaptized as the Black-run state of Zimbabwe and is no longer a pariah, even though its government still does nasty things to both blacks and whites, and it is no longer well off. South Africa has been redeemed by its rejection of *apartheid* and election of Nelson Mandela as its president. Even Israel is almost respectable now that it has a tentative deal with its Palestinian opponents if not all its Arab nation enemies. Only the addition of Iran to the pariah list in 1979 and Iraq in 1991 kept Taiwan from being the sole surviving member in the original pariah nations' club.

Everyone who is anyone broke diplomatic relations with Taiwan during the '70s. Like the other pariah states, Taiwan was treated as ritually unclean by the sorts of people who in this country belong to United Nations Association chapters and spend most of their evenings going to political meetings.

It turned out, however, that being a pariah state, like being Rodney Dangerfield, was not such a bad deal, at least for Taiwan, as long as the pariah did not mess up its economy. Israel did nearly ruin its

<sup>17</sup> Professor Roy Prosterman of UW (who is not a historian) for a generation studied and attempted to duplicate these three land reforms elsewhere. Prosterman advised American foreign aid officials and governments in the Philippines, South Vietnam and El Salvador, but had no success at all in reproducing the Taiwanese, South Korean and Japanese land reforms in these countries, even though the American government threw much more money into these than it did into the South Korean or Taiwanese successes. None of these other governments could acquire enough land for redistribution without confiscating it from native landholders, thereby undermining their domestic markets and the stability of their ruling classes.

<sup>18</sup> There are similar statistics for many other places. The city of Tianjin on the mainland, for example, got its first family planning bureau in 1963, but its natural increase rate (crude birth rate minus crude death rate) started falling in 1957. As of 1998, demographers estimate that world population will likely peak at 7-8 billion in 2040.

economy, but the Israelis have somewhat cleaned up their act recently. South Africa permitted *apartheid* to undermine the rationality of its markets, and paid the political price for that error with the loss of white rule. Iran and Iraq are economic basket cases, but survive anyway via black markets.

Taiwan has kept its interventionist state more or less in check, cutting the state sector share of GNP from c. 50% to well under 20% through fast private growth. The growth of the world market provides so many outlets for any nation intelligent and energetic enough to supply that market, that it can poop along very nicely even though all the best people sneer at it and do not invite it to their political conferences.

Some of the pariahs of the '70s even informally joined in what amounted to a secret society adjunct to their pariahs' club to support each other's arms industries. Rumors long spread of joint nuclear weapons projects amongst Israel, Taiwan and South Africa, and it now appears that these rumors were true. South Africa, for example, probably did help Israel test a hydrogen bomb over the South Atlantic and stockpiled as many as a half-dozen A-bombs. Even now Taiwan may have dibs on Israel's much larger nuclear stockpile.

Of course diplomatic isolation is not an unmitigated blessing. It provides a government with a degree of illegitimacy which may encourage it to support key "infant industries," so long as they can be linked to defense, even indirectly. Since such subsidy does, however inefficiently, give a still quicker, hothouse-like stimulus to the growth of the industrial side of the economy, proponents of such intervention may seem to be justified in the short run, even though such subsidies inevitably distort and weaken the economy over the long run.

Still, if you are going to be denied access to armaments, you had better at least start your own domestic armaments industry, even if it is not efficient to do so. Zimbabwe, the ex-Southern Rhodesia, though no longer a pariah, is still living off some of the benefits of such hothouse economic growth under Ian Smith's Southern Rhodesian pariah government.

Taiwan started losing the diplomatic game in the early '70s, when Zhou Enlai brought the People's Republic back out into the world again. Taiwan lost the recognition of Canada in 1970 and of Japan

in 1972. It lost its UN seat in 1971, and a whole series of Afro-Asian and European recognitions before the end of 1978, when it lost formal diplomatic recognition by the U.S.

Some of these countries would have been willing to recognize Taiwan as Taiwan, or even as a "Chinese Republic of Taiwan," but neither Taiwan (which still calls itself "Republic of China") nor the People's Republic would then or could now accept such a formula. The KMT would have difficulty maintaining its legitimacy even as Taiwan's ruling party without claiming title to the rest of China. The mainland government threatens military action against any Taiwanese government that so much as claims independence lest its legitimacy be doubted.

Loss of widespread diplomatic recognition certainly made no difference economically for Taiwan. Political backing for trade was left unaffected, even with the major powers. When the Americans and Japanese formally broke off relations, they set up in Taipei Alice in Wonderland-like un-embassies under retired diplomats and businessmen.

Aside from the aura of whimsy that surrounds them, such un-embassies are actually rather wholesome institutions. They are not tempted to do as much intervention in a host country as official diplomats might think they could get away with. If you are visiting in Taipei, and you need something about your passport adjusted, you can visit the American Un-embassy, and talk to the un-ambassador or his Un-Foreign Service minions in residence there, and get as much satisfaction as you can from any formally constituted American diplomatic establishment elsewhere (i.e. not much).

Taiwan has even begun to attend international meetings again, especially ones where money talks, under its own flag and more or less under its own name, including an Asian Development Bank meeting in Peking just before the June 4, 1989 massacres. It is currently (January 2000) pressing for joint membership in the new WTO version of GATT along with the mainland. Both Chinas belong to APEC.

The U.S. and Japan have also quietly upgraded their un-embassies recently. They are beginning to staff them with non-retired foreign service personnel. The U.S. even let the President of Taiwan, Li Teng-hui, attend the graduation ceremo-

nies of his alma mater, Cornell, where he received an honorary doctorate to go along with his earned doctorate from Cornell in agricultural economics. China was furious, but apparently more because of the clumsy way the Americans handled the incident than because of what actually happened.

## 2. Industrial maturation

By the late '80s, after nearly three decades of high single and more than occasional double digit compound annual growth rates, Taiwan virtually hit industrial maturation. The comfort level, even for a tolerably poor American student living in one of its cities is comparable to that of Miami (except to substitute what at first strikes you as a whopping big China Town for a massive Little Havana).

Taiwan's first post-maturation decade, the '90s, has produced an increasingly self-conscious rich society.

Industrial maturation has, however, brought some problems. Taiwan has at a surprisingly early stage of maturation developed a chronic trade surplus. Since the late '80s the surplus has remained (despite losses caused by depreciation of the dollar) more than US\$74 billion. It is mostly in dollar denominated assets held abroad, mainly in American banks. What this really means is that Taiwan is exporting capital, and perhaps doing so too soon in its maturity.

This is the fault of the American economy's inability to produce enough attractive goods to sell to Taiwan, and partly because of tariff and non-tariff barriers in Taiwan itself. It is also partly a result of the prolonged immaturity of the Taiwanese financial and banking system, which until recently could not efficiently recycle foreign earnings back into Taiwanese industry. Many Taiwanese also want to export their capital to foreign refuges in case they have to flee a Red Chinese takeover.

Problems in creating a private banking system no doubt contributed to a dramatic fall in the Taiwan stock market (from 12,000 to 3,000) during the first half of 1990, and to what appeared to be the beginnings of a serious industrial recession. But the recession of the early '90s proved mild and short, and the economy was again growing at a 5-7% rate by 1994. Another slight downturn hit in 1996 and (as one would expect a decade or so into

post-maturation) the growth rate has had trouble getting much above 5% ever since. So far (early January 2000), however, Taiwan has dodged the main symptoms of the bust plaguing its neighbors.

Labor costs have grown, tempting movement of Taiwanese capital to Thailand, Indonesia and increasingly to the nearby Fukien province on the mainland. What military threats from the mainland could not accomplish is apparently being brought about by the logic of the market. Nearby parts of the mainland are becoming economic satellites of Taiwan, heavily dependent on Taiwan for capital and expertise. Of course Taiwanese capital is dependent on continued good behavior by the mainland political authorities. Both Taiwan and the nearby parts of the mainland can also transmit bust symptoms from their Southeast Asian trading partners and rivals. That the Taiwan government is nervous about the economy is demonstrated by the government's formation of a "capital fund" of U.S.\$8.6 billion in November 1998 to stabilize the Taiwanese stockmarket whenever it falls below 7000. (Beijing does the same for the Hong Kong stock market.)

### 3. Social and political change

#### a. a Taiwanese plutocracy and a Mainlander refugee meritocracy

Within the Taiwan ruling class, a Taiwanese plutocracy has grown out of the Taiwanese middle class that the Japanese had inadvertently nurtured through not discouraging economic development and a relatively benign form of social segregation. This social discrimination forced Taiwanese to rely almost exclusively on the market. Taiwanese middle class people were ready to produce a plutocracy as their uppermost element by the time the Japanese departed.

The Mainlander refugees of 1949 were mostly meritocrats, civilian and military. Top plutocrats mostly went to Hong Kong and North America. The KMT had only abortively aristocratized its upper levels. Through intermarriage with the Taiwanese since the '60s, some KMT meritocrats have plutocratized themselves and invited a Taiwanese plutocracy to form and join them in the government.

That is, they have done what the Ming meritocrats refused to do during the 17th century. Taiwan's pariah status has encouraged the KMT to intensify this trend,

but it was already under way in the '60s, before diplomatic isolation began. To be sure, the integration of the meritocracy and plutocracy only became visible during the '70s.

In the '50s and '60s, the Taiwanese middle class could still justly complain of social discrimination at the hands of the Mainlanders. In 1971, however, the first harbinger of change could be discerned. The first Taiwanese Miss Taiwan was elected! All of her predecessors had been mainlanders.

By the '80s and '90s, intermarriage between the two groups became so commonplace that people no longer made much of it. There is a convention on the TV soap operas for the "rich bitch" type of character—the beautiful but sneaky and sometimes downright nasty girl who studies in America and leaves a trail of broken hearts behind her in Taipei—to speak with a native Taiwanese accent. The genteel but poor scholar who upholds the standards of civilization and is regularly treated as the wimp he is by the rich bitch, usually speaks with a pure Peking (i.e. Mainlander) accent.

This shows who has the money, but also who still has the prestige. Mainlander meritocrat and Taiwanese plutocrat each need the other, even on TV. In real life, however, the teenager you see in her Jordache jeans hanging out at the McDonald's in downtown Taipei, is as likely to be from a mainlander as a Taiwanese family. Fortunately for the future of Taiwan, she is likely to be grinding away on her high school calculus homework as she sips her Coke and nibbles at her Big Mac.

So rich and variously developed had Taiwan become by the '80s that even its many overseas detained students finally began returning at a much higher rate than before. Detained student Berkeley and Stanford electronic engineers no longer had to stay in Silicon Valley to get fat jobs. They migrated back to suburban Taipei's version of Silicon Valley. There they could get almost equally fat jobs and enjoy better Chinese cooking than in the Bay Area.

That this is not yet as much the case for detained students in the West from the People's Republic is a measure of the economic gap that still exists between the two Chinas.

The renewed attractiveness of Taiwan for returned students and other meritocrats may be one reason why two things I

feared might happen in the 1980 taped lecture version of this chapter have not come about. I feared then that some mainland-origin meritocrats might undermine their legitimacy by their readiness to run off to the West, and some detained students who returned to Taiwan might identify with their fellow meritocrats on the mainland and agitate for reunification on the mainland's terms.

Except for their financial capital, which now wanders the planet like most people's, there now seems little danger of the plutocratic sector of the Taiwan ruling class contemplating exile. Nor have returning members of the private wing of the meritocracy shown signs of turning traitor, perhaps partly because the new knowledge industries have in a sense plutocratized them. Partly too it may be because maximal socialism has recently lost much of its attractiveness, even to the public branch of the meritocracy.

#### b. political democratization

Chiang Kai-shek died peacefully of old age in 1975. His eldest son, Chiang Ching-kuo, the one-time "butcher of Nanking," was elected to succeed him in 1978. Much to everyone's surprise, the younger Chiang led Taiwan from authoritarianism to a genuine multi-party democratic state during the next decade. When he died in 1988 he was mourned sincerely and soon replaced by a native Taiwanese intellectual, a returned student with a Ph.D. in agricultural economics from Cornell, Li Teng-hui, who in 1996 became the first Chinese ever elected president in a direct presidential election.

While the mainland lay bleeding under the repression of the June 4 Movement during the summer of 1989, Taiwan was holding its first genuine multiparty primary election. Voters selected candidates not just for the KMT but for the DPP (Democratic Progressive Party), the formally recognized successor to the *Dang-wai* (non-KMT) informal political movement of the '70s.

The DPP got over a fourth of the popular vote in the fall 1989 parliamentary elections. KMT-DPP negotiations have proceeded fitfully since, punctuated by street riots much milder than South Korea's and a parliamentary style even more exuberantly disorderly than South Korea's. The DPP has not, however, managed to greatly increase its share of the vote in the several island-wide and local

elections held during the '90s, but it has not lost ground either. Polls suggest that at least 40% of the electorate favors in the abstract independence from China.

The DPP won the Taipei mayoralty race in December 1994, but lost the governorship race to the KMT. A third party appeared during that election, the New Party, a breakaway KMT group whose members feared the KMT might make a deal to allow the mainland to take over Taiwan in exchange for allowing the meritocratic wing of the KMT to continue to govern the island.

The KMT feared that the New Party might split its vote enough to allow the DPP to slip in with a plurality. However, thanks to the threatening military maneuvers by the mainland navy during the presidential campaign in spring 1996, Li Teng-hui was reelected by a majority of the vote. Saber rattling by the Li-Jiang government of the mainland as it moved into a possible crisis of the succession from the first generation of rulers apparently proved counterproductive, at least in the short run. It is possible, though not likely that the DPP will win the presidency election scheduled for March 2000, if only because of a further split in the KMT ranks.

In any event, it is clear that Taiwan has become one of the normal parliamentary market societies in the course of the '90s. That places it on a plateau of respectability it never enjoyed as one of the authoritarian pariah states.

The smart political money for a time in the early '90s speculated about the prospects for a South Korean-style alliance between the KMT and the DPP's right wing, the initial aim of which would be to freeze out the New Party. This might eventually also allow the KMT to back off from its insistence that it is entitled to rule all China and render it content to retain a measure of power in what might eventually become a Republic of Taiwan. However, neither Taiwan nor S. Korea has stuck to this route. Indeed, the election of the maverick Catholic Kim Dae-chong as president of S. Korea lends some credibility to the DPP sticking to its independent political position.

Any deal involving de jure independence for Taiwan will probably have to wait until the second generation of leaders currently ruling disappears from the scene in China, and either a stable third generation of rulers is in position there or a post-

Communist government takes over. It is hard to imagine Premier Zhu Rongji, linked as he is to President Jiang Zemin, making a deal for Taiwanese independence, even as part of a Chinese Commonwealth of Nations. But Zhu Rongji or even some thoughtful authoritarian general, might be imagined as making such a deal after Jiang's retirement.

When saddled with the tar baby of the central bank by his rivals a few years before being selected as premier, Zhu survived without tripping off inflation, but might well lose out if blamed for the central bank-induced bust that ended the inflation.

The KMT in October 1994 leaked a report that a plan existed within the mainland government to launch an invasion of Taiwan should the DPP win the 1996 Taiwan presidential election.

At the time it was plausible to surmise that this leak was almost certainly directed by the KMT more against the DPP than the mainland. The naval maneuvers the Chinese navy held off Taiwan during the campaign justify a more ominous face-value interpretation as does the placing of various missiles on Beijing's side of the strait.

### c. comparison with Hong Kong

At least, however, the Taiwanese have a much better chance of retaining control of their own destiny than did Hong Kong, which was inevitably swallowed up by the mainland in the June 1997.

The mainland authorities insist they will keep Hong Kong's "capitalist system" intact for at least another fifty years. They even promise to keep tax rates no higher than they are now. The Hong Kong plutocracy has, therefore, always been tempted to go along with what was inevitable anyway.

Opposition to annexation by China mostly came from the Hong Kong meritocracy, public (led by the faculty of the Chinese University of Hong Kong) and private (mostly lawyers). This faction generally wins the elections (including the last election for the limited power legislative body to be held before 1997, held on September 16, 1995). Once in power, the meritocrats would surely be both more democratic and greater spendthrifts compared to the plutocracy that ruled the crown colony using the British civil servants as their tools, and perhaps even compared to the local rulers mostly drawn

from that plutocracy that the Communists have appointed.

The above quandary is almost certainly a moot question. Hong Kong is likely already becoming just another Shanghai, unless China itself once and for all breaks away formally from the maximal socialist pattern.

This break from Communism would have to be so thorough in practice that the power of the Communist Party withers away or shatters. The state would likely also have to fall into the hands of a post-Communist military meritocrat who, like General Park in South Korea, allies himself with native and returned Overseas Chinese plutocrats and keeps *all* the meritocrats under his thumb, including the ex-aristocratic high rank Party members.

The above scenario may in the end prove more likely than a modest proposal I made in ending the 1987 version of this text to have the Whatcom County Council offer Hong Kong a 99 year lease on Cherry Point and its deep water harbor to replace Hong Kong's current site.

By 1988, some Hong Kong political speculators were looking at a site similar to Cherry Point near Darwin, Australia. That deal fell through, probably because northern Australia is too far from both Hong Kong's Asian roots and its North American customers. But Cherry Point is on the Great Circle route to East Asia, and it is within commuting distance of the rest of North America.

A deal to lease Cherry Point to Hong Kong would, if China itself refused to turn into an oversize Hong Kong, finally solve Whatcom county's problem of how to best develop Cherry Point. It would also enrich the WWU East Asian Studies faculty beyond the dreams of avarice, by enabling us to train hordes of students to serve as *comprador* intermediaries between our increasingly hypoindustrial fellow-countrymen and the more up-to-date traders, bankers and manufacturers of the new Hong Kong East. (At last report the Whatcom County Council signed a deal for some Canadian entrepreneurs to modestly develop the Cherry Point harbor, but a final agreement was being blocked by the state Environmental Department, so perhaps circumstances have borrowed more time for Hong Kong to get its act together.)