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Reform, corruption, and growth: Why corruption is more devastating in Russia than in China

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Abstract

This article explains why massive political corruption appears to be incompatible with economic growth in Russia but compatible with very rapid economic growth in China. The common assumption is that corruption is bad for economic performance. So how can we explain the puzzling contrast between Russia and China? Is Russia being more severely “punished” for its corruption than China? If so, why? This article demonstrates that three intervening factors—comparative advantage, the organization of corruption, and the nature of rents—determines the impact of corruption on economic performance, and that these factors can explain the divergent outcomes. The article thereby offers an alternative to statist explanations of the Russia-China paradox.

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Introduction

In recent decades, China has been vastly more successful than Russia in terms of economic growth. On average, Russian GDP fell by 1.8 percent annually between

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1990 and 2003, while China's output grew by 9.6 percent (World Bank, 2005).¹ Among the more recent converts to market reform, Russia's economic record is among the worst to be found, while China's economic performance is outstanding. Russia and China are extreme cases, at opposite ends of the scale.

While their economic trajectories have been wildly divergent, the two countries have one thing in common: both Russia and China have been plagued by systemic corruption during the marketization process. The common assumption, of course, is that corruption undermines economic performance. How, then, can we explain the contrast? Put simply, is Russia being "punished" more for its corruption? If so, why? The purpose of this paper is to provide answers to these two questions.²

My main argument can be summarized as follows. Contrasting China and Russia provides an opportunity to challenge current scholarly interpretations about the relationship between market reforms, corruption, and economic growth. I will show that state-centered explanations—which focus on the nature and character of the state (strong/weak, hard/soft, and so on)—for economic outcomes in the post-communist world do not necessarily help us understand why similar levels of corruption in Russia and China are associated with extremely divergent economic outcomes (Burawoy and Verdery, 1999; Popov, 2000a,b,c; Poznanski, 1998; Slider, 1997; Sun, 1999). I will offer an alternative interpretation by identifying three important reasons why we should expect corruption to have different effects on economic outcomes in the two countries. The first reason refers to differences in comparative advantage. The second relates to the political organization of corruption—the effective level of centralization, or fragmentation, of corrupt activities (Hutchcroft, 1997; Shleifer and Vishny, 1993). The third reason relates to the different types of rents that more or less corrupt political entrepreneurs have chosen to create in the two countries (Khan and Sundaram, 2000). Put simply, the impact of corruption on economic performance varies in response to the above intervening factors.

The paper is structured as follows. I first survey the literature on corruption and economic development. In doing so, I identify factors determining the economic

¹ China thereby extended an already impressive growth record. From 1980 to 1990, the first full decade of marketization, China's economy grew by 10.3 percent per year on average (World Bank, 2005).

² My definition of political corruption follows Philp. An act is considered to be corrupt when a public official, in violation of the trust placed in him by the public, and in a manner which harms the public interest, knowingly engages in conduct which exploits the office for clear personal and private gain in a way which runs contrary to the accepted rules and standards for the conduct of public office within the political culture, so as to benefit a third party by providing access to a good or service the third party would not otherwise obtain (Philp, 2002, p. 42). In addition, political corruption is understood to include institutional forms of political corruption, in which the main personal benefit to the public official is related to gains within the political process; such as the delivery of a block of votes in an electoral contest (Hutchcroft, 1997, p. 229; Philp, 2002, pp. 42–43). Political corruption thus encompasses a broad range of practices through which public officials pursue self-enrichment, including (but not limited to) bribe-taking, extortion, fraud, exploitation of conflicts-of-interest situations, and vote buying. The discussion does not extend to other common forms of "corruption," such as the abuse of the trust that owners and shareholders of privately owned firms place in appointed managers, since these only in exceptional circumstances have political resonance and public policy relevance.

impact of corruption. Second, I compare Russia and China in terms of the likely economic consequences of corruption, given differences in terms of national comparative advantage, the organization of corruption, and the type of rents created by rent-seeking state officials. In the concluding section, I make a few observations regarding the general discourse in which the fates of Russia and China in the era of market reform are compared.

Political corruption and economic growth

There is an extensive literature on the relationship between political corruption (and other forms of rent seeking) and economic growth, and on what role market reforms can play in either solving or aggravating the problem of corruption.³ Let me briefly outline the way in which thinking on these issues has evolved.

In the 1960s and early 1970s, it was often argued that political corruption could have considerable beneficial economic effects: it was a way of “greasing the wheels” and “cutting red tape” (Leff, 1970; Nye, 1967). Huntington (1968, p. 69) argued that, “In terms of economic growth, the only thing worse than a society with a rigid, overcentralized, dishonest bureaucracy is one with a rigid, overcentralized, honest bureaucracy.” By contrast, the contemporary understanding of corruption comes closer to the dissenting voice presented by Myrdal (1968, p. 932) who in *Asian drama* argued that, “corruption puts sand in the economic machinery; it is a force slowing down development.”

While the modernization school overall took a rather benign view of corruption, that cannot be said of the public choice-inspired, rent-seeking literature, where it is commonly argued that state regulations encourage socially wasteful activities such as lobbying and bribery, which then necessitate further waste of resources in the form of governmental anti-corruption efforts.⁴ The public choice school’s favored solution to the problem of rent seeking, including corruption, is straightforward: “the best and simplest way to avoid the rent-seeking problem is to avoid establishing the institutions that create rents, that is, the regulations and regulatory agencies that lead to rent seeking” (Alston et al., 1999, p. 245). This “solution”, however, does not address the issue of how existing rent-creating institutions can be dismantled. Given that interests are vested in their continued existence, and given the logic of collective action, public choice analysis does not provide a bright outlook for reform: war, the imminent threat of war, invasion and political upheaval are the

³ Rents are excess incomes or super-profits which would not exist in efficient markets (Khan, 2000b, p. 21). Rent seeking generally refers to competition over rents—opportunities for premium profits—that have been created by government restrictions of economic activity (Krueger, 1974). The means of competition can be legal (such as lobbying) or illegal (bribery, smuggling, black-market operations, etc.). However, this understanding of rents is unnecessarily restricted, in that it does not recognize innovation and entrepreneurship as sources of (temporary) rents that play a central role in processes of technological change and economic development (Khan, 2000b).

⁴ But note that Bhagwati (1982), echoing Huntington’s view, emphasises that “directly, unproductive, profit-seeking (DUP) activities,” even illegal ones such as bribery, may be beneficial to social welfare in situations where economic distortions already exist.

main avenues through which growth-retarding “distributional coalitions” can be dislodged, paving the way for an upsurge in economic growth (Olson, 1965, 1982, 2000; Herbst, 1990; Stubbs, 1999). Nevertheless, the market-oriented reforms of the past three decades—involving trade liberalization, financial liberalization, privatization and other measures aimed at enhancing competition—have clearly been influenced by, among other things, the public choice view of how the world works.

In practice, however, it has more recently become clear that marketization is no automatic cure for corruption or for other forms of economic mismanagement. *Harriss-White and White* (1996, p. 4) argue that what has emerged in the wake of market reform is an entirely “new” type of corruption, “rooted in the logic of economic and political liberalization, reflecting the activity of rapacious local elites”. *Schamis* (1999, p. 238) makes a related argument, portraying the constellation of political forces advancing market economic reforms in Latin America as distributional coalitions engaged in rent seeking “in order to reap the benefits of state withdrawal”. The purported dismantling of the rent-seeking society has, ironically, created new opportunities and incentives for rent seeking and thus for corruption.

While corruption may be pervasive throughout the world, there are good reasons to believe that the phenomenon has different economic implications depending on the context in which it occurs. Let me quickly introduce three salient factors:

- Comparative advantage. Economies inhabit different niches in the international division of labor, and these may require different sets of institutional capacities (*Hall and Soskice*, 2001). For example, corruption may be debilitating if a country is competing for trade and investment with countries where corruption is much less prevalent, but it may constitute less of a stumbling block if it is competing mainly with countries that are equally plagued by corruption.
- Political organization. *Shleifer and Vishny* (1993) argue that the organization of the “corruption network” has implications for both the level of corruption and the effect on economic activity. One of the distinctions they make is between a regime in which “the person paying the bribe is assured that he gets the government good that he is paying for,” and a regime in which “numerous bureaucrats need to be bribed to get a government permit, and bribing one does not guarantee that some other bureaucrat or even the first one does not demand another bribe” (*Shleifer and Vishny*, 1993, p. 600). According to *Shleifer and Vishny*, the former corruption regime characterized Russia under Communist rule, while the latter regime characterizes post-Communist Russia. In a similar vein, *Khan* (1996, p. 19) notes that, “the effects of corruption are ... specific to the particular distribution of power between the state and competing groups of potential clients. This makes it possible for apparently similar corrupt transactions to have very different effects in different countries.”
- Rent creation. The political context is not all that matters. Rents do not either. In general, corruption may be regarded as a particular kind of rent seeking. However, we should also recognize that corruption is both a response to situations where rents already exist—and an incentive for state officials to create new rents, so as to profit privately from the associated corruption “tax”. The latter point is

one of the keys to understanding the economic impact of corruption. Many rents exist largely because of the opportunities for corruption they create. However, different types of rents have different implications for economic efficiency and growth. Khan and Sundaram (2000) thus make a distinction between growth-reducing rents (monopoly rent), generally growth-enhancing rents (natural resource rent, Schumpeterian rent⁵), and rents that have indeterminate effects on economic growth, depending, once again, on the institutional context (rent-like transfer, rent for learning, rent for monitoring).

In essence, these more context-sensitive formulations about the relationship between corruption and economic development bridge the rather simplistic pro and con views characterizing much of the earlier work on corruption. Thus, even if we assume that rent creation by state officials is an entirely self-serving activity, motivated by the desire to reap benefits from corruption, we would nevertheless expect different economic outcomes depending on the institutional context and on what types of rents they chose to create.

The political economy of corruption in Russia and China

In this section, I compare Russia and China in terms of the likely impact of corruption given differences in comparative advantage, organization of corruption, and the rents created by state officials.

Comparative advantage

There is reason to believe that corruption in Russia would be more damaging than corruption in China due to differences in comparative advantage. When China launched economic reforms, its comparative advantage lay in low-tech, labor-intensive production. In this segment, China competed for investment and export markets with other low-wage economies, many of which were also highly corrupt. When Russia launched economic reforms, it had two comparative advantages: natural resource extraction being one, and capital- and knowledge-intensive production being another. In the former area, a strong state is not a requirement for international competitiveness, as Nigeria and many other Third World natural-resource exporters amply demonstrate. In the latter area, however, Russia would have to compete for venture capital with institutionally very well endowed capitalist economies. The relatively large gap between comparative advantage and institutional development in the case of Russia, and the high degree of “fit” between these attributes in the case of China can help explain why Russia has been less successful than China in attracting foreign direct investment (FDI). In the 1990s, FDI destined for Russia equaled only some 7.6 percent of that destined for China (see Fig. 1). Even when we

⁵ Schumpeterian rent refers to an entrepreneurial rent which rewards innovation.

account for the size of the host economy, Russia stands out as an underperformer (see the Inward FDI Performance Index in UNCTAD, 2002).⁶

Yet, there is reason to believe that China, given lower levels of corruption, would have attracted even higher levels of FDI, due to the size and rapid growth of the market, and its proximity to major source countries. “Contrary to a cursory reading of the news, China is an underachiever as a host of foreign direct investment” (Wei and Sievers, 2000, p. 96). A balanced conclusion would be that corruption in China has not been as paralyzing as in Russia, but it has not been cost free either.⁷

Organization of corruption

Analysts often make the mistake of equating formal structures with organizational capacity. It is, however, important to recognize that, “it is possible for states with formally centralized institutional structures to behave in a fragmented way if ... powerful but dispersed interest groups can prevent co-ordination by state agencies” (Khan, 2000a, p. 133). Conversely, states and society that are formally fragmented may nevertheless have the capacity to coordinate corrupt activities.

Thus, I would challenge the argument that Russia “lost control” over corruption when the communist party lost power, and that this disorganization of corruption explains the country’s poor economic performance; whereas the Chinese communist party retained its ability to control corruption, thus paving the way for strong economic growth (Blanchard and Shleifer, 2000; Shleifer and Vishny, 1993). On the contrary, Soviet-era state institutions and social networks and practices did not disappear with the Soviet Union (Hsu, 2005; Kneen, 2000). Important elements of these remain in place and continue to play a pivotal role in the coordination of economic and political transactions throughout the Russian economy, as can most obviously be illustrated by the rise of inefficient barter trade (Woodruff, 1999). That such coordination produces sub-optimal results as regards economic growth is another matter.

As regards China, the large variation in the patterns of corruption at provincial as well as local levels suggest that Chinese state and party agencies have in fact not been able to effectively control or coordinate corruption and other forms of rent-seeking. Pei has argued that, “Rampant corruption [in post-Mao China] arose because the

⁶ In fact, Russia’s record in terms of attracting FDI is dismal not only when compared with China, but also when compared with many other developing countries. For example, Peru attracted larger FDI inflows than Russia for much of the 1990s. This argument also holds for the postsocialist context. Note, for example, the fact that Hungary, a country one-fifteenth the size of Russia, has attracted far more FDI.

⁷ Higher/lower levels of corruption refers to the overall prevalence of corruption, and not to the locus of corruption (high state officials versus lower-level bureaucrats). While direct measures of corruption are unavailable, an indirect, quantitative measure of the prevalence of corruption, frequently used in quantitative studies of the causes and consequences of corruption, has been developed by Transparency International (<http://www.transparency.org/>). The so-called Corruption Perceptions Index ranges from 0 (highly corrupt) to 10 (highly clean). In 2005, the “cleanest” country was Iceland with a score of 9.7, and Chad and Bangladesh, scoring 1.7, were the countries with the highest level of corruption of the countries surveyed. Also in 2005, Russia received the score 2.4 while China scored 3.2—indicating a fairly high level of corruption in both countries (Transparency International, 2006).

Year	Russia	China
1990-1995 (annual average)	1167	19360
1996	2579	40180
1997	4865	44237
1998	2761	43751
1999	3309	40319
2000	2714	40772

Source: UNCTAD (2002)

Fig. 1. FDI inflows, 1990–2000 (millions of dollars).

decentralization of power, a virtue, was accompanied by low levels of accountability and a lack of civic participation” (Pei, 2001). The continued power of the communist party certainly suggests that China may have been in a better position to impose some semblance of order on corruption. However, the political turmoil unleashed by rampant corruption in the form of the anti-corruption, pro-democracy demonstrations of 1989, indicates that the Chinese Communist party was unwilling or unable to restrain the predatory behavior of cadres, in spite of a decade of vigorous anti-corruption campaigns. In the market reform era, organized crime has expanded on a massive scale under the political patronage of local officialdom (Chen, 2005, pp. 104–106).⁸ As the reform process progressed, corruption in China underwent qualitative changes. Corruption intensified in the sense that it increasingly involved “high-level, big-stakes corruption” rather than “ordinary” forms of official malfeasance (Wedeman, 2004, p. 895).

Thus, continued political control and repression does not necessarily mean that corrupt behavior is disciplined effectively. There is much evidence to suggest that the central government has been spectacularly unsuccessful in its efforts to root out corruption, as officials also freely admit (British Broadcasting Corporation, 2001; Pan, 2001; Radio Australia, 2001).⁹ The lack of success is partly related to the weakness of the judicial system, where “corrupt prosecutors, incompetent judges and biased courts” hold sway (Kynge, 2001b). The lack of success is also related to the party’s

⁸ Organized crime is not equated with corruption. However, in instances where organized crime receives protection from public officials one can speak of a nexus of corruption between organized crime and public officials.

⁹ In addition, if uncertainty constitutes the important difference between corruption in Russia and in China, then the dissolution of the Soviet Union looms larger as contributory factor to uncertainty than whatever corruption happened to occur in the process of dissolving and then recreating the state.

emphasis on co-opting new elites—technocrats and entrepreneurs—which has left the party “less able to mobilize and control society and its own members at a time of increasing political, economic, and social change” (Dickson, 2000, p. 539). The proliferation of criminal “secret societies”—an instructive parallel to the rise of the Russian “mafia”—also speaks to the weakness of the Chinese state (Chen, 2005).

In short, the considerable coordinating capacity of the networks (lodged partly in the state, partly outside the state) that Russia inherited from the Soviet era, has been used to exclude new entrants to markets, maintain monopoly rents, and reproduce soft budget constraints. Political corruption has played an important role in this process.

In China, on the other hand, *de facto* social and political disorganization has allowed new players to enter markets and thereby destroy monopoly rents.¹⁰ Political corruption has helped drive and/or facilitate this process, too. It remains to be seen whether the “collective corruption”—involving collusion between party members, state officials, and third parties—which has become a “conspicuous pattern and even a trend in the commission of corruption” in more recent years (Gong, 2002, p. 101) will transform Chinese corruption into a system of corruption with Russian characteristics, in which well-coordinated networks of corruption stifle economic growth.

The roots of these divergent functions of corruption are to be found in the decades before the initiation of economic reforms. Much of the discussion regarding the role of the state in economic development in Russia and China tends to proceed in a decidedly ahistorical manner. Particularly striking is the manner in which the political events and economic developments leading up to the launching of market reform are downplayed. For example, China’s Cultural Revolution is virtually ignored in most accounts analyzing and contrasting the economic reform process in Russia and China. This is highly unfortunate, since the abandonment of central planning in China did not start in 1978. In fact, Mao Zedong abandoned the centrally planned economy in 1966 under the rallying cry “Bombard the Headquarters.” The Cultural Revolution constituted a violent attack on the state and party apparatus administering the centrally planned economy. It also weakened the party-state as such: “For much of the Cultural Revolution, the Party was an empty shell. In practice, the Party consisted of a set of warring factions” (MacFarquhar, 1992, p. 442). The violence unleashed during the Cultural Revolution resulted in the death of an estimated half a million people, which further weakened both the party and its moral authority.

From a political economy perspective, one of the important effects of the Cultural Revolution was that job security for cadres in China never developed to the extent that it did in the Soviet-style economies of Europe (Bunce, 1999, p. 33).¹¹ Thus, unlike the Soviet/Russian reforms of the 1980s and 1990s, the Chinese reformers led by Deng Xiaoping did not face much resistance from an elite lodged in the organs of the

¹⁰ To what extent budget constraints have hardened in China is less clear: the much publicized high ratio of non-performing loans in the Chinese banking system, as well as stock market manipulation (Kynge, 2001a), suggests that many Chinese state-owned enterprises continue to face soft budget constraints.

¹¹ Furthermore, “it is important to note that the rapid and radical changes in Russia have occurred with the majority of state officials keeping their posts” (Levin and Satarov, 2000, p. 117).

state. The violence of the preceding decade, the death of Mao, and the imprisonment of the radical leftists in the Gang of Four had considerably weakened the ability (and desire) of vested interests to return to the status quo ante. “Deng could do what Gorbachev and the other European communist reforms could not do: win out over the countless cliques engaged in covert collective action and other insider lobbies” aiming to undermine reform measures (Olson, 2000, p. 167). The Cultural Revolution explains why China was able to avoid, at least in part, the destructive dynamic described by Winiecki (1990), by which economic reforms in Soviet-style economies stall or are reduced to quasi-reforms because of the “counterreformation” launched by lower-level party *apparatchiks* and bureaucrats.

Another important consequence of the radical brand of late Maoism was that it gave rise to an economic structure that was much less complex and embedded than that of the Soviet Union. At the end of the Cultural Revolution, China’s socialist economy was made up of autarkic economic *units*, whereas central planning had created complex webs of interdependence between firms in the autarkic Soviet economy. These webs were not limited to the plan, but also took the form of an extensive “underground” or “second” economy dominated by barter and bribery.

Shue (1988, p. 130) has argued that the Chinese polity under Mao came to display a cell-like, honeycomb pattern, characterized by a high degree of localism and segmentation. By the end of the Cultural Revolution, “local officials ... had acquired such considerable leverage and skill at evading and distorting central policy, that top leaders from whatever faction were greatly handicapped in getting *any* policy—even one that was generally beneficial—implemented widely *as it was intended to be implemented.*” The objective of Deng and his comrades was to smash the cells and build a more open polity, centered around market-based exchanges, that was more amenable to central party and government control and direction (Shue, 1988, pp. 131–132). This would, in effect, strengthen the influence and authority of the party and provide new career opportunities for its representatives. Thus, to correctly situate China’s economic reform program in a historical and political context, it is important to understand that market reforms there went hand in hand with the project of party-state (re)construction. In this way, their function was regime- and state-building—a purpose that helps explain as well the centrality of nationalism in the Chinese reform project.

In Russia, in contrast, economic reforms went hand in hand with an increasingly localist political agenda (Woodruff, 1999). President Boris Yeltsin “bombarded the headquarters” in his own fashion, in an alliance of regional power brokers. The attack on the center was highly successful, so successful that it resulted in the dissolution of the Soviet Union. Micro-nationalism, but no “macro-nationalism,” accompanied this process and both state and regime unraveled.

Thus, China started market-oriented reforms in 1978 with a weak, fragile and, in many respects excessively decentralized and under-institutionalized state apparatus. Russia’s starting point a decade later was the direct opposite: an excessively strong, unlimited and centralized political and economic order. While Russia has since developed into a somewhat more cell-like and “feudal” society (Verdery, 1996), local self-sufficiency has yet to reach a level comparable of that of the late-Mao China.

Rent creation

The divergent political—and economic—contexts outlined above provide clues as to what type of rents have been favored by political entrepreneurs in Russia and China, respectively. Rent-creation was, however, also shaped by natural and ideological opportunities and constraints. The abundance of natural resources and the breakdown of the political taboo against privatization thus provided Russian power brokers with the opportunity to: 1) create growth-retarding monopoly rents—control over natural resources (Sachs and Warner, 1995; Gylfason, 2000) and heavy industry; and 2) engage in rent-like transfers of a highly inefficient kind. *Nomenklatura* privatization is a prominent example of the latter kind of rents.

In addition, one may regard the high rates of inflation in Russia during the early 1990s as a highly inefficient form of rent transfer (this section draws heavily on Treisman, 1998). The government's inflationary monetary policies transferred central bank credits and household and enterprise savings to favored commercial banks and to selected enterprises and sectors of the economy (particularly agriculture, fuel and energy, and defense industries). Apart from the negative effect of transferring capital to firms with little ability to make productive use of it, a high and unpredictable rate of inflation in itself has a more general, dampening effect on a country's investment climate.

As inflation was brought under control towards the mid 1990s, the inflation rent was replaced by new rents. Commercial banks were given the opportunity to reap enormous profits—tax free—from investments in short-term state securities (*Gosudarstvennoe Kratkosrochnoe Obyazatelstvo*, or GKO). Troubled state enterprises were indirectly subsidized: companies did not have to pay their bills to energy suppliers, and energy suppliers were in turn compensated by the state, which allowed the energy sector to run up tax arrears as long as politically important, but delinquent customers continued to receive energy supplies.

None of these rents—inflation tax, GKOs, debt delinquency and tax arrears—served to gear the Russian enterprises, new or old, towards making investments that enhanced market competition. On the contrary, the combined effect was to concentrate financial and industrial resources in the hands of a select few. State socialism was thus transformed into an oligarchic form of capitalism. However, the problem is not oligarchy per se, but rather that capital accumulation in this oligarchic setting became oriented towards the creation and seeking of rents—based on natural resources, transfers and monopolies—which were economically inefficient. They reduced the incentive and compulsion for owners of capital to enhance the productivity of firms under their control.

One effect of these rents was to crowd out private enterprise. While the “second generation” of rents may have been inefficient, one could argue that they were slightly less so because of the more limited macroeconomic damage. It is true the Russian government was forced to default on its GKO debt in 1998, thus precipitating an immediate financial crisis. However, the longer-term effect of the financial crisis was to eliminate the GKO rent, thus contributing to a sounder incentive structure.

As China is less rich in natural resources, and since the ideological taboo against large-scale privatization has remained in force, Chinese officials have, in contrast, had to create rents more compatible with efficiency and long-term growth—whether they wished to or not. In particular, Chinese policy makers have been inclined to engage in (or accept) rent-like transfers of a growth-enhancing nature. These transfers—ranging from the decollectivization of farm land to the semi-private, entrepreneurial use of state assets—have encouraged new entrants to markets and intensified competition. In many respects, these transfers have been “spontaneous”—they were initiated from below rather than from above. The effect of these rent-like transfers has been to promote new entrants into high-rent markets. That is why they would enhance growth.

While the beneficial effects of the transfer of effective ownership of farm land from the state to individual peasants is a well-known aspect of the early days of market reform in China, it is instructive to consider the effects of spontaneous privatization of state assets at the local level.

In China, bureaucratic resources have increasingly been put to uses that enhance rather than restrict competition. Local state governments account for a substantial portion of all the entrepreneurial activity in China. Duckett (2001, p. 30) argues that these activities—which may be illegal, and generally are regarded as “corrupt”—tend to be productive rather than profiteering, since the local entrepreneurial state is “far removed from the centralized administrative control of the command economy and operates in an increasingly competitive market environment.” These economic activities are thus characterized by neither monopoly nor monopsony, and they may, furthermore, promote the growth of competitive markets: “In the early stages of marketization there may be limited knowledge of producers and markets, and state entrepreneurialism may fill gaps in certain markets” (Duckett, 2001, p. 32).

Other rents created at various levels of the Chinese state have also tended to channel resources in productive directions. He (2000) argues that corruption in reform-era China has taken two main forms. First, corruption has served as a means for non-state actors to develop alongside the planned economy, dominated by large state-owned actors. Second, corruption became a means by which local governments competed for favors from the central government. These favors took the form of both preferential financial treatment and special “flexibility” of the kind initially accorded only to special economic zones. Political corruption has thus contributed to the establishment and spread of competitive and growth-enhancing markets and institutions.¹²

In contrast with the Russian case, many corrupt activities in China have been associated with the creation and exploitation of rents that tend to reduce the importance of growth-retarding monopoly rents in the overall economy. In China, this

¹² That is not to deny the fact that local governments also engage in predatory activities—such as illegal taxation (Wedeman, 2004)—that would tend to have negative implications for economic growth.

positive outcome was *not* the result of the intentional design of a “strong” state—but rather the lucky side effect of a state and party gone “soft.”¹³

One can argue, therefore, that both Russia and China are “soft” states. The beneficial consequences of a soft state in China—and the negative consequences in Russia—are to some extent the result of an interaction effect with the country’s level of technological development (an aspect of its competitive rather than comparative advantage). In low-tech China, the failure of the state to create the growth-enhancing rents envisaged in the classic liberal literature (private property rights, intellectual property protection) was not debilitating. Neither was the failure to create the growth-enhancing rents envisaged in the more “statist” development literature (rents for learning). These failures did not inhibit decentralized, small-scale, low-tech production in what was, at the outset of reform, an agrarian economy.

Russia, in contrast, paid a higher price for the same failures. Russia inherited an urbanized society, well-educated workforce, and an industrialized economy from the Soviet Union. Given this point of departure, the Russian state would have had to be able to create the rents supporting and promoting large-scale, high-technology production in a modern market economy (private property rights, Schumpeterian rents, rents for learning, rents for monitoring).

The Russian state obviously failed to provide these necessary conditions for sustained economic growth in a structurally mature economy. The task facing the Chinese state was in this respect much simpler. However, as the Chinese economy develops, growth momentum can be maintained only if the state proves able to create the rents underpinning sophisticated market economies. That China will manage this “transition” is not a forgone conclusion.

Conclusion

A paired country comparison between Russia and China reveals that the level of corruption seems to have limited explanatory power. This has important theoretical implications.

One implication which needs to be mentioned, if only in passing, has to do with the limits of ahistorical approaches to understanding market reform dynamics. As this article has demonstrated, market reforms and their consequences cannot be understood without due reference to what came before it. The legacies of the Mao and Brezhnev eras have had a profound influence on the nature and economic consequences of political corruption in the two countries.

A second implication has to do with the emphasis in much of the recent literature on states and economic development on the importance of institutions and good governance. My argument does not refute this position, but does raise questions about the emphasis that should be placed on these factors. The fact is that weak institutions and “bad” governance may in some contexts be compatible with rapid,

¹³ China is not alone. The “soft” state of Thailand is also associated with strong economic growth, and parallels between the two cases have been made (Doner and Ramsay, 2000).

sustained economic and social development. I argue that China over the past two decades may very well be such a case.

Why, then, is it that the Chinese state is often described as so “strong,” even if it is by no means obvious that it is, and that this “strength” is considered in such positive light? I suspect that the answer lies in the more general conclusion made in the literature on the quality of governance, that “good economic institutions, particularly those in the public sector, are instrumental to economic growth” (La Porta et al., 1999, p. 222). This may have led some analysts to jump to conclusions regarding the case of China and perhaps also regarding some of its neighbors. Lacking reliable instrumental measures of “good government” and state “strength,” a track record of rapid economic growth is simply taken as evidence of “good government” and “high stateness.” The argument thus becomes circular and functionalist: the effect explains the cause.

A future reversal in economic fortune for China would almost certainly lead to a shift in theoretical perspective—highlighting bad government and state weakness—as has already been the case for Japan and many of the East and Southeast Asian “tigers.” China’s economy may have developed rapidly in the past two and a half decades, yet, as Rose-Ackerman has argued, “it is too soon to tell whether the trend is toward virtuous circles that will produce a competitive market economy or toward vicious circles where the treachery and corruption of some breeds more of the same in others” (Rose-Ackerman, 1999, p. 108).

As for Russia, media campaigns about the corrupt and “criminal” Russian state have contributed to a similar feedback process. There may be some truth to this characterization, and I do not want to deny that corruption and crime is a serious problem in Russia. But that is true also in some very dynamic societies. It is also interesting to note that Russia has now come full circle. Under socialism, ideological and political concerns dictated that corruption and other forms of crime could not exist, except as very rare cases of deviancy.¹⁴ Under post-socialism, in contrast, ideological and political concerns dictate that virtually every economic transaction is corrupt and criminal. “One must consider why the government’s response to similar crime rates has swung from complete denial to hysteria over crime” (Sanford, 1999). Verdery (1996, p. 219) similarly stresses the importance of making a distinction “between ‘real mafia’ and ‘conceptual mafia,’ or mafia-as-symbol.”¹⁵

The corruption/criminality discourse centered on the Russian “mafia” may be less driven by objective evidence than by political pressures and conveniences related to the transformation of the Russian polity. Sanford highlights a few such political motives: the need for the former Soviet security agencies to find a new reason for being;

¹⁴ “Corruption like inflation, suicide, military expenditures, and others, is among the subjects forbidden to be discussed in the official Soviet literature if they concern the USSR” (Katsenelinboigem, 1983, p. 221). Here, it is critical to note, if only in passing, the earlier point about a historical understandings of reform dynamics. The corruption started already under Stalin (Gregory and Harrison, 2005).

¹⁵ Verdery (1996, p. 219) writes, “Talk of mafia is one way of saying that exchange and enterprise are still suspect, if not in fact condemned, as they were under socialism—that they bring unmerited riches and rely on questionable practices. Talk of mafia, then, may reveal people’s ambivalence about the effects of the deepening marketization of their countries.” The same may be true of talk of “corruption,” both in Russia and in China.

the threat posed by Chechen separatists to the integrity of the Russian Federation again made it convenient to label that ethnic group as “criminal”; and the usefulness of “law and order” as electoral campaign themes, and “corruption” allegations as a method of tarring political opponents.¹⁶

The various campaigns concerning “corruption” and “criminality” might be likened to “talk of witchcraft,” which is one way of putting blame for difficulties of all possible kinds on invisible, evil forces (Verdery, 1996, p. 220). Given the frequent use of terms such as mafia, corruption and criminality in a symbolic rather than objective and descriptive manner, it is unfortunate that this largely uncritical discourse has come to dominate not only media reporting, but also much scholarly writing on post-Soviet affairs.

Similar “talk of witchcraft” is evident also in China and in the discourse on Chinese economic development. In its propaganda, the Chinese party-state uses “corruption” as one way to put the blame on all kinds of bad phenomena that plague contemporary society. Bad policy or, more generally, bad politics are certainly not to blame for rampant corruption. Ironically, this is reminiscent of the last decades of the Soviet Union, where the problem was defined as deviant individuals, not a fundamentally flawed system. At the same time, a central political factor—institutional stability, evidenced by the longevity of the communist party’s monopoly on political power—is claimed to explain the Chinese economy’s giant leaps. In this way, political success versus political failure—or regime and state capacity—are anointed with considerable explanatory power.

This type of argument has a distinct rhetorical and political appeal. The messages fit so nicely into seductive morality tales—in which economic and social woes can be blamed on gangs of evildoers, while the credit for all things good goes to the guardians of the strong state.

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¹⁶ The political and organizational incentives are not limited to the former Soviet Union. Russian organized crime is replacing the “evil empire” as a focus for national security agencies and security analysts in the post-Cold War era as well (see Webster et al., 2000 for an illustration of this phenomenon).

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