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# The Impact of the PRC's Economic Crisis Response on Regulatory Institutions: Preliminary Thoughts

**Margaret M. Pearson**

**Department of Government and Politics**
**University of Maryland, College Park, USA**

***China Analysis* is edited by**

**Sebastian Heilmann**
**Professor of Government / Political Economy of China**
**Trier University, 54286 Trier, Germany**

**E-mail: china_analysis@chinapolitik.de**

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## Table of Contents



* Professor Margaret M. Pearson, Department of Government and Politics, University of Maryland, College Park, USA. Contact: mpearson@umd.edu

## Introduction

Hu Shuli, one of China's most public voices on economic affairs, summarized the concern many economists have held about the PRC government's response to the global economic crisis of 2008-2009. Then the editor-in-chief of *Caijing* magazine, she opined about China's stimulus package in July 2009 that

> "A policy that encourages loose lending and investment is driving China's economic engine down an old, unsustainable path."[1]

Hu's comments underscore several core questions about China's economic and financial crisis responses: What does China's response to the global economic crisis reveal about the deep structures and preferences of PRC economic policy-making? Is China traveling down an "old" path that the more market-oriented voices have tried to permanently bury? Is the stimulus a temporary deviation, justifiable because of the crisis situation? Alternatively, has the crisis response provided an opportunity to see how shallow many of the reforms have been, revealing instead enduring – albeit sometimes latent – structures and fault lines of state-domination of the economy that continue despite substantial market reforms? Is the debate that surrounds the crisis response simply old wine in new bottles, or do they represent a fundamental movement of the economic preferences of the country?

This discussion article attempts to address some of these questions through the prism of regulatory politics. The regulatory system is in some ways an excellent lens through which to examine the question of whether China is traveling down an "old" path. Chinese reformers have made explicit efforts since the 1990s to establish new institutions to manage the market economy. Regulatory institutions – in many ways modeled on Western patterns of regulation – were an effort to break from the institutions of planning, and to build foundations of government oversight that would allow market mechanisms to work better. China's ongoing response to the economic crisis is a propitious moment to examine how deeply China's new regulatory system is rooted.

The article's primary conclusion is that the party-state's crisis response has drawn heavily on mechanisms – both institutional and policy – that are outside of the newer regulatory system. The most obvious sign of this is the reliance upon the "comprehensive agencies" of government, and especially the National Development and Reform Commission (NDRC), for policy formulation and implementation, and the sidelining of regulatory agencies – notably in financial services – that might be expected to have a role in expansion of credit. These patterns to some extent underline what we have already known: the new institutions have had difficulty become fully authoritative, and continue to be subordinated in important instances to the comprehensive agencies. There is some debate among outside observers as to whether the regulatory agencies have been marginalized against their will, or are active (if subordinate) collaborators in the crisis response. The proper interpretation of this latter issue remains unclear.

The article is organized as follows. The first section reviews briefly the literature on China's past responses to global economic crisis, particularly the Asian Financial Crisis, and makes a

[1] Hu Shuli, "Editorial: Reality Check for China's Monetary Policy," Caijing (English), 7-23-2009, online at http://english.caijing.com.cn/2009-07-23/110202368.html, accessed October 26, 2009.

brief comparison to the contemporary US government response to the crisis. The second section lays out the regulatory structure as created since the early 1990s, and discusses the ways in which it has interacted with older structures of the economic system. The third section discusses the available empirical information about the role of the regulatory institutions in the crisis response. The final section summarizes.

## 1. Reflections on the Asian Financial Crisis and the Current US Response

Although I admit to not having carried out an exhaustive survey, I have not found the existing political economy literature on the response of countries to economic crisis to be very helpful for understanding China in the current crisis. This is for a simple reason: the broader literature is primarily focused on democratic countries, and on the responses and constraints in democratic countries.[2] The primarily exception comes from within the literature on the Asian Financial Crisis (AFC) of 1997-1998. This crisis, which affected democratic and authoritarian regimes alike, was post-Mao China's first real experience with economic crisis. To the extent that the AFC was driven by rapid movements (and removals) of capital from Asian economies, the impact on China's economy was blunted by its vigorous capital controls. Indeed, by most accounts the fact that China did not devalue its currency to bolster exports was seen as a contribution by the PRC. While I am skeptical that the PRC failure to devalue was intended as a community good rather than a domestic-oriented response,[3] the main point is that China was isolated in this experience. Moreover, at the time of the AFC China had not yet established regulatory institutions. Thus China's reaction during the AFC provides few clues into the PRC's response to the current economic crisis.

The main lesson from the AFC literature for the scope of this paper comes out of the response of other Asian countries with relatively new regulatory systems – though the lesson is hardly unique to this context or this set of countries. At a time of crisis, when responses must be made quickly and large amounts of money are involved, the hallmarks of an independent regulator (described below) are often undermined. In large stimulus packages in particular, prudential and transparent lending standards are contravened by political pressure to distribute funds quickly, and often go out the window. In other words, moral hazard becomes even more of a problem, and the institutionalized weakness of new regulators is revealed.[4] Moreover, government regulators in an economic crisis typically must work under conditions of poor information. Capacity therefore also must be recognized as a major problem.[5]

While many aspects of the comparison between China's response and that of the US government may not be fruitful, one point of comparison helps frame the analysis of China's response. Actors in the US economy – those who promoted and then benefited from extensive deregulation of financial instruments in both the private and public sectors – bear a great deal

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2 Important works in this genre include Peter Gourevitch, *Politics in Hard Times: Comparative Responses to International Economic Crisis* (Ithaca, NY: Cornell University Press, 1986), and – within the literature on the Asian Financial Crisis - Andrew MacIntyre, "Institutions and Investors: The Politics of the Financial Crisis in Southeast Asia," *International Organization,* vol. 55, no. 1, 2001, pp. 81-122.

3 This echoes the reasoning in Thomas Moore and Dixia Yang, "Empowered and Restrained: Chinese Foreign Policy in the Age of Economic Interdependence," in David M. Lampton, ed., *The Making of Chinese Foreign and Security Policy in the Era of Reform, 1978-2000* (Stanford: Stanford University Press, 2001), 191-229.

4 On how the moral hazard problems were revealed in Asian government responses to the AFC, see Stephan Haggard, *The Political Economy of the Asian Financial Crisis* (Washington, DC: Institute for International Economics, 2000), pp. 24-32.

5 Ibid., pp. 32-33.

of responsibility for the crisis. But the US government under newly elected President Obama and his small cohort of financial advisors made policy responses that were quite *radical* for the US context. Decisions to bail out firms are of course not unknown in the history of the American political economy.[6] Yet the breadth and scope of the 2008-09 crisis intervention – especially direct government intervention to prop up financial (banks, investment houses, and insurance) and automobile firms – was, in context, massive. The point is not to assess whether the US response was good or bad (or adequate or inadequate), but to note that it moved the role of government intervention in the economy to a very different place than it had been for decades before. In contrast, China's economic response, though large in terms of the quantity of stimulus funds, appears – as Hu Shuli indicated – to be more in line with previous practice than a break from it. On the other hand, extant political forces in the US have prevented certain fundamental reforms of the American economy, especially as concerns streamlining and tightening of the financial regulatory system. Conservatism in this regard puts the US more on a par with what we shall find for China. In the grand scheme or things, then, we can say that – institutionally speaking - while the US response was an abrupt change in a long continuity of practice, China's was a more conservative effort, despite the size of funds committed, in the context of three decades of longer term reform.

## 2. China's Regulatory System Prior to the Economic Crisis

What did China's regulatory system look like before the economic crisis hit in late 2008? The process of creating a Chinese-style "regulatory state" did not follow the establishment of an *a priori* blueprint. Instead, the regulatory institutions that were established applied international models to existing interests and structures of party and state organizations. The organs of "economic regulation" were intended to apply primarily to China's "strategic" or "lifeline" industries – firms that are seen as central to economic and national security, and remain primarily state a place among the top global firms in their sectors.

Most of China's strategic industries have been made subject to new "independent" regulators. These are based explicitly on a model of arms-length distancing of firms from their regulators, and of regulators from undue political influence. Whereas in Western models the concern is to avoid undue political influence by legislatures, in the Chinese case concern is for excessive influence from ministries and other relevant actors in the formerly planned economy. Also crucial to the model is prevention of regulatory "capture" by industry and prevention of monopoly (i.e., regulation is "pro-competition").[7] Pursuant to this model, the PRC government set up regulatory commissions governing strategic infrastructure sectors (electric power, telecommunications, and civil aviation) and financial services (securities, insurance, and banking). Most of these regulators were carved out of previous ministerial level agencies. For example, the three financial service regulators were created out of bureaus formally part of the Bank of China, while the telecommunications regulator, the Ministry of Industry and Information Technology (MIIT), was reorganized to become an "independent regulator" in the context of China's WTO succession. The establishment of new regulators was supported by passing corporate governance laws. The major regulators are listed in Table A.

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[6] Op cit, Gourevitch (1986).

[7] Margaret M. Pearson, "Governing the Chinese Economy: Regulatory and Administrative Reform in the Service of the State," *Public Administration Review* Vol. 67, Issue 4 (2007).

**Table A: China's Strategic Sectors Regulatory Bodies**[8]

| Regulatory Body | Industry scope | Year established | Organization formerly in control |
|---|---|---|---|
| **China Securities Regulatory Commission (CSRC)** | Financial services: securities | 1992 | People's Bank of China |
| **Ministry of Industry & Information Technology (MIIT)** | Telecommunications, information | 1997 | Ministry of Post & Telecommunications, Ministry of Electronics |
| **China Insurance Regulatory Commission (CIRC)** | Financial services: Insurance | 1998 | People's Bank of China |
| **General Administration of Civil Aviation (CAAC)** | Aviation | 2002 | Old CAAC |
| **State Electricity Regulatory Commission (SERC)** | Electric Power | 2003 | Ministry of Electric Power |
| **China Banking Regulatory Commission (CBRC)** | Financial services: Banking | 2003 | People's Bank of China |

In addition to being carved out of old institutions of the planned economy, these new regulators were overlain onto an existing set of bureaucratic and institutional features. Together they create a unique regulatory system that departs from the independent regulator model. Existing literature highlights three major trends in the emergence of the Chinese regulatory structure. Each of these trends will be commented on in examining the impact of the economic crisis on Chinese patterns of regulation. First, and most crucial for the purpose of this paper, is that the authority of regulators remains relatively weak vis-à-vis other party-state institutions. Indeed, "independent" regulators must compete with powerful supra-regulatory bodies. The state-owned assets of non-financial services companies in the top tier have been placed under the control of the State-owned Assets Supervision and Administration Commission (SASAC). SASAC, formed in 2003, presently holds supervisory power over 156 large holding companies, and maintains substantial authority over assets, including the privatization, sales and purchases of businesses. It also appoints top managers to about two-thirds of these firms (the other top managers are appointed directly by the Party Organization Department). SASAC itself has had some difficulty exerting influence over the top managers of these firms, most of whom are independently important in the party-state system, and some of whom are of high enough party rank to sit on the Central Committee.[9]

Most of the top tier firms, including both those which are and are not on SASAC's list of strategic companies, are subject to the authority of the even more powerful National Development and Reform Commission (NDRC).[10] The NDRC remains the source of industrial policy,

[8] From Margaret M. Pearson, "The Business of Governing Business in China: Institutions and Norms of the Emerging Regulatory State," *World Politics*, Vol. 57, No. 2 (2005), pp. 296-322.
[9] Barry Naughton , "SASAC and Rising Corporate Power in China," *China Leadership Monitor* 24 (Spring, 2008), online at http://media.hoover.org/documents/CLM24BN.pdf, accessed September 14, 2009.
[10] To clarify, those industries not under the authority of SASAC but under purview of NDRC (as well as under new regulators) include the financial services companies.

and in addition must approve major investments and industry decisions. Atop the NDRC, the Party, through its Organization Department – but also at key times including in the crisis response through the Politburo Standing Committee – remains keenly interested in the health of China's "strategic" firms. It has long been general practice of the CCP to use its personnel function as a lever of control, and this tool remains a powerful force for Party control. It appoints top management to 53 of the firms – the core non-financial enterprises – formally under the supervision of SASAC. In the same year SASAC was established (2003), the party also reasserted its *nomenklatura* control over top executives in the financial system (i.e., that are not under SASAC). As a result, the Party Central Committee has power of appointment for all of the financial regulators (PBOC, CBRC, CSRC, and CIRC) as well as over the top ten state-owned financial companies.[11]

In banking, the center of state monetary and fiscal policy, party control is direct. As Shih shows, the party and the State Council both have held sway since the major reorganization of 2002 (which also created the China Banking Regulatory Commission, CBRC).[12] The joint party-state Leading Group on State Banking Reform in particular, has high-power heads in a Vice-Premier and Bank of China Governor Zhou Xiaochuan, and maintains appointment power and sets the major policy direction for the four state-owned banks. As Shih states, "the Party's tight grip over the financial sector did not relax even after the latest round [2002] of restructuring."

These supra-regulatory institutions can easily justify their involvement in regulatory activities, for they retain ultimate responsibility for overall economic performance of the economy and its most strategic sectors. Moreover, they are the source of policy goals that must be implemented by regulators – a function that in Western economies is often served by national legislatures.[13] The bottom line for the so-called "independent" regulators is that their independence is limited.

There is also a central-local dimension to the question of regulators' authority. The main office of regulators is at the central level. At the local level (province and municipality), there may be branches of the central regulatory, but these are primarily under the authority of the local government.[14] Thus, both the capacity and authority of regulators are weak below the center.

Second, and consistent with the previous discussion, authority over Chinese state firms is highly fragmented. A major result of fragmentation is that many (often many, many) players from within the government have a seat at the bargaining table. In telecommunications regulation, for example, the formal regulator – the Ministry of Industry and Information Technology (MIIT) – must routinely negotiate with the People's Liberation Army (responsible for information security concerns), the Ministry of Finance (oversees accounting) and, on the regulation of internet, the State Administration of Radio, Film, and TV, the State Secrets Bureau, the Ministry of Public Security, the Ministry of Commerce, and State Administration for Industry and Commerce.

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[11] Hon S. Chan (2009), "Politics Over Markets: Integrating State-Owned Enterprises into Chinese Socialist Market," *Public Administration and Development* 29, pp. 43-54.

[12] Victor Shih, *Factions and Finance in China: Elite Conflict and Inflation* (New York: Cambridge University Press, 2008), pp. 39-44. On the role of the CCP in financial regulation, see also Sebastian Heilmann, "Regulatory Innovation by Leninist Means: Communist Party Supervision in China's Financial Industry," *The China Quarterly* No. 181 (March 2005), pp 1-21.

[13] The Party Organization Department also plays a major role in governing major state-owned institutions.

[14] Yukyung Yeo and Margaret Pearson, "Regulating Decentralized State Industries: China's Auto Industry," *China Review*, Vol. 8, No. 2 (Fall 2008), pp. 231–259.

The need to deal with these actors is in addition to the leading small group in telecommunications, and the aforementioned NRDC, SASAC, and the party. Similar situations exist across the board for China's regulated industries.[15]

Finally, although the regulatory model adopted in China has as one policy preference the breakup of state monopolies and promotion of competition, the ultimate revealed preference is for oligopolistic structure, limited competition, and the strengthening of the state-owned sector. Indeed, while at an international level the independent regulator model has been more associated with a private economy, the PRC government, for those industries considered strategic, has paired the model with a plan to strengthen the state sector so it can meet international competitive norms. This contravenes a core element of the independent regulator model: independence from state intervention. Stated differently, and consistent with the structural features discussed above, the regulatory system in China leaves much scope (and retains clear channels) for the party-state to shape industrial structure. This goal, in the purview of the NDRC, has been actively exercised, for example, in the ongoing consolidation of steel, auto, and other industries in which there is judged to be substantial overcapacity.[16]

Each of these three features of the Chinese regulatory system – weak authority relative to comprehensive state institution, fragmentation, and efforts to strengthen the governance capacity of state ownership – continue to be revealed in the government's response to the economic crisis. We will see that, while the regulatory institutions have not been abolished, they are not at the center of crisis resolution and, in the case of prudential lending by banks, the norms to which they are supposed to adhere have been compromised.

## 3. The Regulatory Structure and China's Response to the Economic Crisis: Mutual Impact

The basic outlines of the PRC government's response to the economic crisis have been well described elsewhere, and need not be discussed extensively here.[17] Suffice it to say that the package has consisted of three components:

- A large investment package estimated to amount to RMB four trillion (US$586 billion), or 13% of China's 2008 GDP. These funds were to supplement the state's existing investment plan, and in some cases (as with earthquake relief) were already part of the state investment plan. This investment was to be funded only at about 30% by the center, and only about RMB 1.7 was new investment (nine billion has been included in the 11th FYP, and 1.4 billion in other recent initiatives).
- A plan for moving investment funds to the target projects. A complex mix of central funds and "matching" local funds were rapidly to be committed and flushed into the system, and were to be channeled primarily through the state banking system. This has led Bottelier to see the stimulus to be more of a monetary stimulus than a fiscal stimulus package, and to focus our attention on the banking system.[18]

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15 Pearson (2007).

16 In the steel industry, for example, consolidations have been continuing through the same period as the economic crisis. See, e.g., "China Approves Hebei Steel Merger Plans," Xinhuanet.com, online at http://news.xinhuanet.com/english/2009-09/22/content_12095341.htm (accessed October 15, 2009).

17 This description is based primarily on: Naughton (2009); and Pieter Bottelier, "China and the International Financial Crisis," in Ashley Tellis, Andrew Marble, and Travis Tanner (eds.), *Strategic Asia 2009-10* (Seattle, WA: National Bureau of Asian Research, 2009), pp. 71-102.

18 Bottelier (2009) argues that the ratio of monetary-to-fiscal portions of the stimulus has been about 85/15.

- An industrial policy-related set of restructuring and investment initiatives, part of which were a new framing of longer held objectives. 10 industries were targeted (e.g., steel, non-ferrous metals, automobiles, chemicals, cement and textiles). The 10 industries produced over 40% of China's 2008 GDP.

Before turning to discussion of how the PRC response to the economic crisis has involved and affected the emerging regulatory structure, several caveats are in order. First, not all aspects of the regulatory system are relevant to this inquiry; the financial services regulators are most involved, since the monetary expansion of the Chinese response relates to their core regulatory objectives. Other sectors that are overseen by regulators, such as insurance, civil aviation, and telecommunications are less involved (except to the extent that they may receive government funds).[19] Second, as regulators are not generally blamed for or central to China's vulnerability (in contrast to the US), they are secondary actors. Third, and most important, analysis is limited at this stage of inquiry by the fact that the story is still being played out and many sources of empirical description lump central institutions together. It is therefore hard to parse the various roles of, in particular, comprehensive agencies (such as NDRC) and regulators (such as CBRC). While we have signals to lead us to believe that the analysis below is accurate, in truth further field inquiries need to be made.

With these caveats in mind, what are the main findings? The most prominent finding of this investigation is that the new regulatory institutions are not front-and-center in the current environment; some of them – notably the financial sector's CBRC and CSRC – are present, but not the dominant institutions. While this is perhaps to be expected, for reasons just given, the clear impression is that they have been somewhat marginalized by the comprehensive agencies, notably the NDRC, itself directed by the party. Just below this surface level, though, there are indications that the place of regulatory institutions is secure – there is no question they will not be "players" in the bureaucratic regime. Although they are secondary actors and have been somewhat marginalized, their involvement as institutional actors is expected. Most intriguing, perhaps, are rumors that regulators in financial services do not always agree with the dominant direction of the economic rescue, and on some important tasks (especially the CBRC's duties to prudential lending) they may feel their missions are compromised. Nevertheless, in terms of public positions they appear to be quite consistently supportive of the dominant line; party-state discipline is upheld. The evidence for these broad comments is laid out below.

### 3.1 Resurgent Dominance of Comprehensive Institutions

The NDRC is clearly the dominant publicly identified player in China's crisis response. As noted in the caveat, this makes sense, as its *raison d'être* is largely to direct public investment – a key essence of the response strategy. The State Council clearly directed the NDRC to launch a stimulus as a result of its emergency meetings in early November, 2008. NDRC, with offices at the central and local levels, has the mechanisms to launch a timely emergency program, and within the Chinese system appears to be the highest economic planning and implementing authority, as well as the designer of industrial policy. This remains true despite the fact that other regulatory bodies (and their heads) hold ministerial rank. In fact, the NDRC has been key to drafting and implementing all aspects of the stimulus programs, a role not held by any of the regulators (except, in some cases, MIIT). The potential for the NDRC to

[19] As mentioned previously, the various social regulators are also not directly involved.

provide consistency, coordination, and oversight in a crisis context is probably a positive force for policy stability.

It was noted above that many elements of the stimulus package were continuations of existing initiatives – initiatives that the NDRC was responsible for in their original form. An important example is the effort, under the guise of "consolidation" to close surplus and heavily polluting export-oriented factories in southern China beginning in early 2007.[20] The stimulus mechanisms thus make heavy use of China's well-refined planning and policy-lending mechanisms, and employ non-market-based mechanisms that were already in play before the economic crisis.

The role of the Party is important as well. Naughton makes clear that the party was active in defining the scope of the stimulus package behind the scenes simultaneous with the more public State Council activity. This too makes sense, as the Party has the legitimate role for setting overall direction and policy. Once the Party's line has been set, subordinates must publicly align. More important, perhaps, the Party possesses the tools for rapid informational response that were important for the stimulus. Its system of intra-party circulars were perhaps the most effective means for communicating to local leaders the parameters of the stimulus plan.[21]

In this environment, there was no obvious major role for China's new regulators. At the same time, the picture is variegated. In the bond and corporate paper markets in particular reforms begun in the middle part of the decade, and driven largely by the People's Bank of China and the CSRC and outside the purview of NDRC, have continued to flourish. While the effort to push funding into the system is consistent with the central government's stimulus package, the fact that other regulators have maintained supervision of this niche is significant.[22] Moreover, the "independent regulator" MIIT appears to have had a high-level role in directing industry-specific policy.[23] Yet to some degree this exception proves the rule: MIIT is not a typical "regulator" for China. It retained more of its ministry ties when it was formulated, and indeed gained the name "independent regulator" more as a result of a deal with the ITU than any major transformation of its role.[24] It is more of a superministry involved in broad policy formulation, and does not even pretend to be an arms-length market regulator.

### 3.2 Role of "Independent" Regulators: The Case of the CBRC

One regulatory organization that has been directly involved in the Chinese crisis response is the Chinese Banking Regulatory Commission (CBRC). Although (or perhaps because) it is China's youngest regulator – established in 2003 – it is widely considered outside of China to be the most effective and market-oriented of the "independent" regulators. It is perceived as having some of the best trained staff, with many of them trained and employed overseas. It oversees an industry with perhaps the most internationally-competitive financial services in-

[20] Albert Keidel, "China in the Global Cr5isis: Recovery and Continued Reform?" Paper presented at the XXI National Forum, Rio de Janeiro, Brazil (May 2009).
[21] On party documents and distribution of party circulars directing the stimulus, see Naughton (2009), p. 2.
[22] On the institutional evolution of bond and corporate paper market regulators, see Scott Kennedy, "China's Emerging Credit Rating Industry: The Official Foundations of Private Authority," *The China Quarterly*, No. 193 (March, 2008), pp. 65-83.
[23] MIIT was involved in auto stimulus implementation. Communication from David Michael, BCG, June 1, 2009.
[24] The ITU requires members to have "independent regulators," so when China joined it had to have one body designed as China's "independent regulator." A behind-the-scenes deal apparently led to the designation of MIIT (at the time MII) to be this body. Pearson (2005).

dustry – the ICBC; it therefore may feel less pressure to manufacture a national champion. These characteristics make it an interesting case to examine as to the impact of the economic crisis on PRC regulatory bodies.

The Chinese stimulus package, as noted previously, dictates that a large quantity of government funds be fed to end-users in a short period of time. To the practically giddy delight of local governments (Naughton, 2009), local governments immediately sprang to action, haggling with the central government (NDRC) over which expensive projects should be funded and how much the central and local contributions would be.[25] After the center gave permission to invest, banks then were to be a major channel through which central funds would be distributed. As the regulator responsible for overseeing standards of prudential lending, and appropriate channels for lending, CBRC would appropriately have a major role in the day-to-day distribution of funds to localities.[26] Moreover, local governments often have to borrow money to fund their portion of the projects, and the center has permitted issuance of corporate bonds, issued treasury bonds specifically earmarked for local government use, and facilitated long-term concessionary loans. Through these three sources – concessionary loans from policy banks, bond issuances, and commercial bank borrowing – local governments can finance some projects completely through debt(!). Bank regulators are not openly questioning this underlying use of funds, but rather "are only asking banks to shore up their bad-debt provisions in anticipation of the inevitable rise in nonperforming loans."[27]

In the Chinese planning context, when local governments moved to negotiate with the center over investment monies, they frequently pressured anyone who would get in their way to cede ground. Similarly, in the AFC in other Asian economies, bank regulators often were pressured to ignore shoddy standards.[28] So the expectation that local CBRC regulators, already relatively weak, would be unable to stop the outflow of monies to projects that did not merit them or were very risky. There was central pressure to distribute massive amounts of funds quickly, and local government pressure to do the same. In this sense, the role of the regulators would almost certainly be undermined by the implementation of the crisis response.

It is also interesting to note that incentives for local governments to be more fiscally prudent appear to be not at all influential. This may be a Chinese-style version of "regulatory capture"; rather than capture of regulators by firms, the local political economy is characterized by capture of regulators by local governments.

Did the CBRC collaborate in this distribution of funds, thereby following the lead of policymakers who focused on rapidly getting funds into the system, even at the expense of prudence? Or did CBRC officials object to the compromising of the regulatory culture, including independence from political pressure, they had been cultivating? Or might CBRC officials, knowing they cannot influence this process, retrenching until conditions are better to continue a regulatory mission? There has been some reportage that CBRC officials have been unhappy with the stimulus plan, and have complained in private debates. However, it is clear that in public they support the lending. This position is presumably made more palatable insofar as

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[25] The majority of central funds went to local governments (73% in 1Q09), as opposed to central government ministries. (Naughton, 2009, p. 4.)

[26] NDRC has a more substantial role in this implementation than CBRC, as already suggested. According to Naughton (2009, p. 3), "The NDRC checks the proposed [local] projects to make sure they fit with the priorities and restrictions imposed by policy; and to see whether preparatory work has been completed and the projects are 'shovel-ready.'"

[27] Victor Shih, "Comparing China's Stimulus Programs," *Asian Wall Street Journal* (July 22, 2009), reprinted at http://chinesepolitics.blogspot.com/ (accessed November 1, 2009).

[28] Haggard (2000, p. 33).

the government has guaranteed many loans, and the impetus for loan expansion is clearly not from the banking sector, allowing plausible deniability of responsibility in the future. What is more important for the current analysis, however, is that the standards for lending that the CBRC has worked to cultivate are being ignored. This scenario suggests that bank regulators are taking their cues from the Party and NDRC, at the expense of their independence.

## Conclusion

It is clear that the Chinese government's response to the economic crisis of 2008-09 has *not strengthened* the impulse toward arms-length market regulation, and probably weakened the role of independent regulators vis a vis the comprehensive agencies. The policy preferences that have played out rely extensively upon strong state intervention in the economy, including mechanisms of state-led consolidation of the state sector and massive government spending.

This article does not intend to argue that these mechanisms are inappropriate. Rather, they may have been necessary, just as US policy-makers argued similar and in many ways more radical reorientation of a crisis response to state intervention was necessary. The point, however, is that these responses hearken back to a prior status quo position where comprehensive agencies and the CCP were the strongest voice in the government's economic management. In all this, the new regulators – never having terribly strong authority in the first place – have been elbowed aside. They have been elbowed aside as an institutional force and in terms of a policy force. This may be appropriate, institutionally, and we would not expect the regulators to be the major policy voice. However, the response has seemed to force financial system regulators into the position of having to look the other way in terms of enforcing prudential standards they had been seeming to try to enforce in the years since their establishment. Once again, they were weak and so it was not hard for them to be sidelined. It does seem, however, that the crisis response has set back the position of the new regulators in the post-Mao economy.