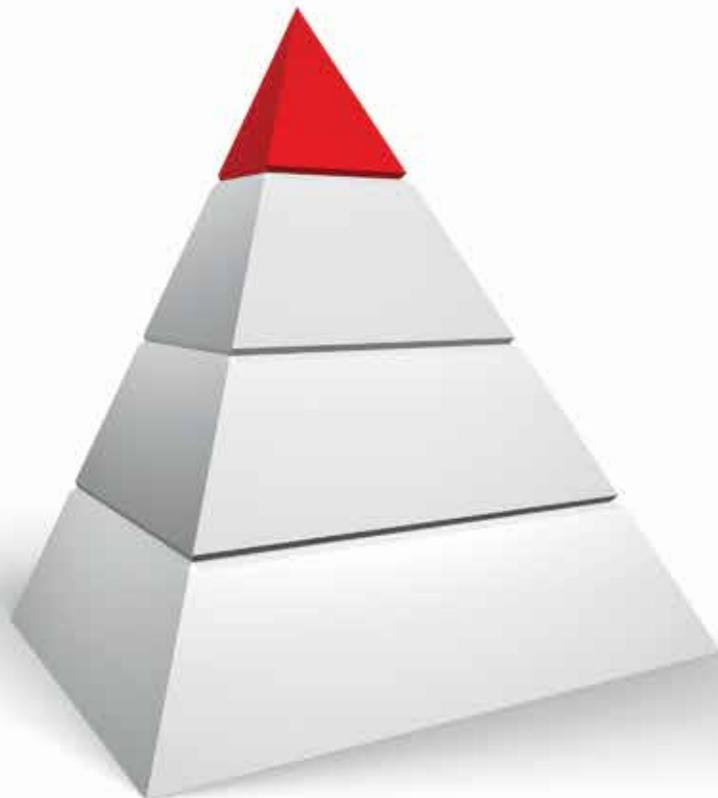


CIGI Papers No. 242 – May 2020

# Top-level Design for Supremacy

## Economic Policy Making in China under President Xi

Alex He





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# Table of Contents

vi	About the Author
vi	Acronyms and Abbreviations
1	Executive Summary
2	Introduction
3	Top-level Design for Full Control: Economic Policy Making under Xi
6	Institutional Changes for Top-level Design: The Strengthened Roles of Central Leading Groups
9	Building the Party's Solid Leadership over Everything Is the Key for Top-level Design
13	Top-level Design: Top Principle Is Stability, Main Goal Is Sustainable Economic Growth
16	The Problems with Xi's Top-level Design in Economic Policy Making
19	Case Study of Economic Policy Making under Xi: Supply-side Structural Reform
24	Conclusion: Impacts of Xi's Top-level Design on China's Economic Policy Making
28	Works Cited

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## About the Author

Xingqiang (Alex) He is a CIGI research fellow. His work focuses on China and global economic governance, the Group of Twenty, domestic politics in China and their role in China's foreign economic policy making and Canada-China economic relations.

Prior to joining CIGI in 2014, Alex was a senior fellow and associate professor at the Institute of American Studies at the Chinese Academy of Social Sciences (CASS) and a visiting scholar at the Paul H. Nitze School of Advanced International Studies, Johns Hopkins University in Washington, DC (2009-2010). Alex was also a guest research fellow at the Research Center for Development Strategies of Macau (2008-2009) and a visiting Ph.D. student at the Centre of American Studies at the University of Hong Kong (2004).

Alex is the author of *The Dragon's Footprints: China in the Global Economic Governance System under the G20 Framework* (2016) (in both English and Chinese) and co-author of *A History of China-U.S. Relations* (2009). He has published dozens of academic papers, book chapters and newspaper and magazine articles.

He has a Ph.D. in international politics from the Graduate School of CASS and previously taught at Yuxi Normal University in Yunnan Province, China. Alex is fluent in Chinese and English.

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## Acronyms and Abbreviations

<b>BRI</b>	Belt and Road Initiative
<b>CAC</b>	Central Auditing Commission
<b>CCAC</b>	Central Cyberspace Affairs Commission
<b>CCDI</b>	Central Commission for Discipline Inspection
<b>CCOLG</b>	Central Commission for Overall Law-based Governance
<b>CEWC</b>	Central Economic Work Conference
<b>CLGCDR</b>	Central Leading Group for Comprehensively Deepening Reform
<b>CLGFEA</b>	Central Leading Group for Financial and Economic Affairs
<b>CNSC</b>	Central National Supervisory Commission
<b>COPR</b>	Central Office of Policy Research
<b>CPC</b>	Communist Party of China
<b>MOHURD</b>	Ministry of Housing and Urban-Rural Development
<b>NDRC</b>	National Development and Reform Commission
<b>PBoC</b>	People's Bank of China
<b>PBSC</b>	Politburo Standing Committee
<b>RMB</b>	renminbi
<b>SARS</b>	severe acute respiratory syndrome
<b>SOEs</b>	state-owned enterprises

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## Executive Summary

Presenting China's reform as a holistic system consisting of economic, political, cultural, social and ecological subsystems, President Xi Jinping introduced a top-level design as the theoretical foundation for his overall control of the reform agenda and economic policy-making process. Xi greatly strengthened the roles of central leading groups in the reform and policy-making process; these strengthened central leading groups constitute the backbone of the institutional framework for his idea of top-level design. In a move that was different from his predecessors, Xi put an unprecedented emphasis on the Communist Party of China's (CPC's) control of economic policy, which is expected to be guaranteed through the greatly reinforced party control over the state bureaucracy and the private sector. Sticking to the party's tendency to be extremely risk averse, Xi's top-level design embraces stability as the top principle while seeking the primary goal of sustainable economic growth.

Supply-side structural reform constitutes Xi's first major economic and reform proposal to confront the most difficult and most important issue in China's economy, i.e., economic restructuring, and to deliver sustainable economic growth. In the four years after it was introduced at the end of 2015, supply-side structural reform achieved limited success and had negative impacts on China's economy. A heavy reliance on administrative orders, achievements in cutting low-end and ineffective supplies and improvements in the industrial structure in steel, coal and other sectors with serious overcapacity had negative consequences for the private sector; most of the state-owned enterprises (SOEs) in those sectors with overcapacity increased their profit and benefited significantly from the reform. The policy of inventory reduction in the real estate sector unexpectedly led to soaring real estate prices in 2016 and greatly intensified the existing asset bubble. The financial deleveraging policy was introduced with unprecedented strict supervision policies and led to a sharp liquidity shrinking and rise in interest rates in financial markets and to the default of many firms. Facing this mixed picture, supply-side structural reform began to shift its focus from 2017 and expanded from its original mandate of cutting overcapacity, deleveraging and reducing costs for enterprises

into an industrial upgrade moving up the global value chain and featuring innovation and cutting-edge technologies in advanced manufacturing.

Xi's style of leadership, featuring Xi-dominated party central's tightened control over policy making in every sector and field in China, had profound impacts on China's economic policy-making process. His unprecedented power and authority and the new approach of top-level design emboldened him to push forward the long overdue and difficult structural reform of China's economy. Policy making under Xi has followed a top-down approach; the trial-and error approach based on the bottom-up, incremental method has been followed less. Resorting to institutional power and unprecedented emphasis on party discipline and party loyalty, Xi put great efforts on the party's tight control of both policy making and policy implementation. The party's deeper involvement in economic policy making and economic management intensified China's model of government intervention in the economy and further complicated the relations between the state-owned sector and the private sector in the economy.

Xi's style of highly concentrated power and full control over policy making has achieved a mixed result. It may have pushed through some difficult economic reforms, but it created a variety of new problems and exacerbated the existing bureaucratic problems in China's political economy. These problems can have catastrophic consequences when facing an emergency situation, such as a public health crisis, as the novel coronavirus epidemic beginning in January 2020 demonstrated. The stability-obsessed ruling style under President Xi's top-level design and the unprecedented pressure it brought on state and local bureaucrats are, unexpectedly, unable to react swiftly when facing a crisis. Xi's style of an upgraded version of one-man control over major policy making on economic affairs and in other fields has the potential to last until his complete retirement, unless the ongoing economic downturn China is facing lasts and develops into a serious economic crisis.

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# Introduction

Each paramount leader since the founding of the People's Republic of China in 1949 has left his footprints on the legacy of the CPC's ruling in China. Chairman Mao and Deng Xiaoping are regarded as the leaders who enjoyed the highest authority and absolute power, respectively, over the party and the country in their eras. The subsequent leaders, Jiang Zemin and Hu Jintao, who did not belong to the generation of revolutionary leaders, are deemed more mediocre top leaders who lacked the charisma of Chairman Mao and Deng Xiaoping, and who tried hard to seize improved control of the party and the country during their terms but failed. Jiang Zemin's power likely reached its heyday at the end of his incumbency, but the governance on economic affairs was not in his control throughout most of his reign. Hu Jintao has been widely regarded as the weakest top leader since 1949 and he had to share power with the other eight members of the Politburo Standing Committee (PBSC) and could only grasp one-ninth of the power in his 10-year rule.

Xi Jinping, as a princeling who has the so-called red noble blood, seemingly holds the true ideals and convictions of the traditional values of the CPC, such as "serving the people" and "striving for the great rejuvenation of Chinese nation," claimed to be dedicated to reviving the glory of Communist China.<sup>1</sup> He began to consolidate his power with a surprisingly persistent, stern, even harsh anti-corruption campaign immediately after becoming China's president in 2013. After all, securing and fortifying the highest authority stands as the precondition for a top leader in China to proceed with his vision and reform goals during his reign.

Since democratic political reform disappeared from the agenda of the Chinese government after the 1989 Tiananmen event, the most important task for a paramount leader in China is to maintain sustainable economic growth and, subsequently, social and regime stability, which will conversely help the top leader reinforce his control over the party and the country. There has been consensus on achieving sustainable economic growth among China's elite and leaders for years. The goal relies

on further comprehensive and deepening reform to achieve the transition to an upgraded growth model that focuses on innovation and consumption instead of relying mainly on investment and export. The toughest part of this reform, however, has been the lack of uncompromising determination and capability for the top leaders to persist with the ongoing reform when facing economic downturn and the signs of political and social instability that typically followed the economic decline. It was the case in the Hu-Wen era prior to Xi. Furthermore, the lack of urgency and the 2008 global financial crisis helped to deter top leaders Hu Jintao and Wen Jiabao from pushing hard for the necessary economic transition.

China's economic policy-making process has shown some new features since 2013 — it seemed that President Xi was determined and equipped with a capacity to pursue the most difficult economic transition since the reform began at the end of the 1970s. Top-level design has emerged and developed into President Xi's signature approach to seeking full control over economic policy making. The idea of top-level design and the holistic way of thinking behind it had been raised by Xi and one of his close advisors even before Xi came to power in China.

This is the third and final paper in a three-part series exploring the decision-making process in China. Based on the previous two papers, which respectively reviewed the relevant literature, the theoretical framework and methodologies employed and scrutinized China's political structure and decision-making process, the paper examines the economic policy-making process featuring the top-level design for comprehensive control in China under President Xi. Supply-side structural reform is the significant economic policy initiative introduced since Xi assumed the presidency of China in March 2013. The paper further discusses the structural reform as a case study to demonstrate the new model of economic policy making. The paper concludes with a discussion of the impacts of President Xi's style of leadership on China's economic policy-making process.

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<sup>1</sup> Xi seems to reiterate and implement reviving the party's excellent tradition and working style to better serve the people more than any other previous top leader (Xinhua 2017a; Xi 2017).

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# Top-level Design for Full Control: Economic Policy Making under Xi

## The Rise and Development of the Top-level Design Approach

As a top leader who rose from the lower levels of the hierarchy in the CPC's and China's bureaucracy in the reform and opening-up era, President Xi was expected to have a good understanding of the priorities he had to focus on, as well as the challenges he faced. It appeared that he had developed his own views on how to proceed on the very difficult reforms to realize the goal of rejuvenation of the great China. He was prepared with a new idea that came to his mind as early as 2010 when he was promoted to the position of vice president of China, a sign of being chosen as the heir for the position of the supreme leader of the CPC and China.

“Top-level design” is the new idea President Xi proposed. The term was written into one of the party's authoritative documents, “Central Committee of the Communist Party of China: Recommendations for the 12th Five-Year Plan for Economic and Social Development,” for the first time in October 2010: “It is necessary to comprehensively move reform forward in every sector, with greater determination and courage; pay even more attention to a top-level design and an overall plan for reform; and clarify the priorities and sequences for reform” (Xinhua 2010), following Xi's suggestion to bring it up in discussion (Naughton 2012; Kadozaki 2017). Liu He, who was regarded by a variety of sources as the top economic advisor to President Xi, even before the latter's ascent to the highest authority, is believed to have provided the origin of the expression based on his background of information science (Forsythe and Lawrence 2009).

Liu He is a veteran in China's economic policy making who participated in the development of the CPC's and China's most authoritative guiding documents, the Five-Year Plan, since the 8th Five-Year Plan in 1990 up to the latest 13th Five-Year Plan in 2015. He is also one of the major scriptwriters of the most important annual economic conference in China's policy making, the Central Economic Work Conference (CEWC), and has participated

in drafting the economic speeches for three top leaders since Jiang Zemin. Liu He had explained the meaning of the top-level design when it was first used in the party's suggestions for the 12th Five-Year Plan in October 2010. He described top-level design as a structure or model in which economic, social and political system reforms can be advanced in a coordinated and stable manner in order to adapt to the new economic situations and deal with the great challenges facing China after more than three decade of reform. The top-level design includes setting the main goals, priorities and sequences in the reform, which is very important and complicated and which requires specific arrangements to deal with each different situation (Hu, Zhu and Yang 2010).

Xi Jinping began to endorse and spread the idea of the top-level design right after his ascent to the highest power of the CPC at the 18th Party Congress in November 2012. In his speech at the symposium with non-CPC personages on November 30, Xi described the top-level design as a measure to achieve economic growth and a way to maintain the direction of socialist market economic reform (Xinhua 2012). During his first field investigation in Guangdong Province on December 7–11, 2012, after the 18th Party Congress, Xi himself defined the term for the first time by saying that “top-level design means holistic reform planning for economic structure, political institutions, cultural system, social management system and ecological system. Research and assessment on the correlation of reforms in different areas need to be enhanced, and try to match the overall and local reforming measures, combine palliatives and permanent solutions and make progressive reforms, and breakthroughs in the reform can be mutually reinforced” (Party Literature Research Center of the CPC Central Committee 2014, 32).

A major challenge to Xi's new route for further reform is how to maintain a delicate balance between his top-level design and “crossing the river by feeling the stones,” the basic methodology and philosophy of reform during the Deng Xiaoping era. Methodologically, the top-level design is the opposite of “crossing the river by feeling the stones,” and it implies the departure of Xi's method of reform from Deng's, which Xi was aware of. Deng has been widely accepted as the “general designer” of China's reform and opening-up policy, which began four decades of continuous economic growth and prosperity. With extremely

pragmatic philosophies such as “crossing the river by feeling the stones,” “it doesn’t matter if a cat is black or white, as long as it can catch mice” and “allowing some of the people to become rich first,” Deng’s reform brought China miraculous economic growth but caused severe unintended negative results, for instance, rampant corruption and growing inequality in Chinese society.

Xi understands the great potential negative ramifications if he blames Deng for the ongoing negative consequences caused by his reform. Deng’s historical achievement in the reform and opening-up policy cannot be defiled in China, and attacking it risks accusations of denying the direction of reform and opening-up and could encourage a conservative counterattack. As the top leader advocating further comprehensive reform, Xi is aware of this. A reasonable option for him is to propose a new approach to tackle these issues while not denying Deng’s legacy.

Xi eventually compromised on his idea of top-level design by combining it with Deng’s philosophy of crossing the river by feeling the stones in accordance with dialectics, the classical philosophy that ran through the CPC’s history. Xi mentioned the idea of top-level design frequently in his speeches in 2013 and began to put it together with Deng’s approach.<sup>2</sup> The combination of top-level design and crossing the river by feeling the stones as the fundamental methodology and philosophy for comprehensive reform was written into the guidance document, the “Decision of the CPC Central Committee on Some Major Issues Concerning Comprehensively Deepening the Reform” on November 12, 2013.

Judging from Xi’s policies that have been announced and carried out since the decision was approved in November 2013, top-level design has been practised frequently but crossing the river by feeling the stones, the trial-and-error approach that focused on grassroots-level experiences and wisdom, did not get the attention it deserved. Guided by his belief in inclusive, green and shared development, and including relentless anti-corruption measures and targeted

poverty alleviation, Xi began to practise his top-level design in his efforts to govern China.

## Top-level Design Aimed at Full Control in Policy Making

The work to explore the top-level design methodologically and philosophically ended when it was written into the decision in November 2013 and achieved the status of the fundamental methodology of the CPC’s work under Xi Jinping. In the years that followed, Xi developed and unfolded his top-level design in detail to achieve his vision for a great China. His vision includes comprehensively building a moderately prosperous society, comprehensively deepening reform, comprehensively advancing law-based governance of China and comprehensively strengthening party self-discipline. The first-stage goal of his plan is to finish building a moderately prosperous society by 2021; the final stage goal is comprehensively “turning China into a modern socialist country that is prosperous, strong, democratic, culturally advanced, and harmonious” by 2049.

The so-called “Four-pronged Comprehensive Strategy” constitutes the highest layer of Xi’s top-level design. The strategy was first raised by Xi in December 2014 when he did field investigation in Jiangsu Province and was upgraded to the new strategy for the governance of China at the sixth session of the CPC’s 18th Party Congress in November 2016. This new strategy was defined by Xi as the general plan in the new era of China’s socialist market-oriented economy.

Xi’s Four-pronged Comprehensive Strategy, however, is simply a repeat of past CPC policies. All of its components repeat what Xi’s predecessor, Hu Jintao, concluded in a report at the CPC’s 18th Party Congress in 2012. Hu (2012) outlined the goal of completing the building of a moderately prosperous society in all respects and deepening reform and opening-up in an all-around way by 2020. Hu and his predecessor Jiang Zemin also advocated the goal of promoting law-based governance of the country in an all-around way and the goal of strictly enforcing party discipline and willingly upholding centralized leadership of the party. The difference Xi made in the CPC’s platitudes is stressing the concept of holism in his plan.

The party’s history over nearly a century reveals that a cruel power struggle among party leaders and factions is the inconvenient truth behind

2 For example, Xi talked about this combination at the second collective study session of the 18th CPC’s Politburo on December 31, 2012 and at the 11th collective study session of the 18th CPC’s Politburo on December 3, 2013 (Party Literature Research Center of the CPC Central Committee 2014, 34-35, 48).

the moral high-ground catchphrases repeated by the propaganda machine. The real intentions are always cloaked in seemingly noble and standard communist slogans. Shrouded by the philosophic label, the so-called “holistic planning” serves well as a theoretical framework and ideological foundation to Xi’s ambition to control economic policy making and, furthermore, every other aspect in the party-state. Xi’s comprehensive strategy also embodied his belief in governing China in a better way: I can govern the great country well only if I can control every field and area within the state and the society.

Four key components of Xi’s top-level design provide the rationale, state priority and other policy goals, describe the main means to realize the goals, and outline actions to contribute to his full control of policy making in the economy and other sectors of Chinese society.

First, Xi gives and repeatedly underlines the rationale for his top-level design and overall planning, which is that, given the correlation and interaction among reforms in every area, comprehensive reform in all respects is greatly needed.

The decision in November 2013 emphasized “make holistic planning and promote development in a coordinated way” and suggested that more attention must be paid to “implementing systematic, integrated and coordinated reforms” (Xinhua 2013).<sup>3</sup> Xi underscored that the blueprint for reform must be comprehensive and it should include not only reform on economic and social systems but also reforms in other aspects (Party Literature Research Center of the CPC Central Committee 2014, 47-48), including promoting “reforms in the country’s economic, political, cultural, social and ecological systems, as well as in the system of Party building” (Xinhua 2013). The phrase that indicated the top-level design reform in the reports of the 18th Party Congress, “the overall approach to promote economic, political, cultural, social, and ecological progress” that underlines “the coordinated progress in all areas of endeavors” (Hu 2012), was also singled out and highlighted by Xi to emphasize the importance of a fundamental systemic design of the blueprint for reform.

Second, economic system reform is given as the top priority in Xi’s grand plan for deepening the reform comprehensively, which indicates his ambition to grab the highest authority for economic policy making in the following years. The decision emphasizes “the underlying issue is how to strike a balance between the role of the government and that of the market, and let the market play the decisive role in allocating resources and let the government play its functions better” (ibid.). Xi underscored economic system reform and the subsequent economic growth as the central tasks in his plan to comprehensively deepen reform (Party Literature Research Center of the CPC Central Committee 2014, 47-48). In the two years that followed, Xi declared that China’s economy had entered “the new normal” with a slower growth rate and outlined “the supply side structural reform” as his solution to the great challenges facing China’s economy in this new era.

Third, Xi set prominent goals in a variety of fields, which is in line with the rationale for the top-level design for comprehensive control over all sectors in the society. These goals include an innovation-driven economy, inclusive and sharing development, ecological civilization,<sup>4</sup> targeted poverty alleviation, preventing and controlling systematic financial risks, and playing a global leading role to advocate a community of shared future for mankind. The goal of comprehensively advancing the law-based governance of China to provide the people equality and justice is also included in Xi’s distinct efforts. For the first time, the CPC’s plenary session focused exclusively on the subject of law-based governance (Xinhua 2014a).

Fourth, Xi resorted to comprehensively enforcing strict party discipline as the means to guarantee the smooth implementation of his top-level design. The key party leaders and senior officials are the focal point of Xi’s endeavour to strengthen party self-discipline. Xi called them *yibaoshou*, i.e., the head of each department, ministry in the state’s bureaucracy and chief of each institution of the party system. Xi believed that the implementation of his efforts in comprehensively strengthening the party’s leadership in economic affairs and all other areas needed to be guaranteed through *yibaoshou*, or the “crucial minority.” The new idea

3 An English edition of the full text of the decision is available at: [www.china.org.cn/china/third\\_plenary\\_session/2014-01/16/content\\_31212602.htm](http://www.china.org.cn/china/third_plenary_session/2014-01/16/content_31212602.htm).

4 In the context of Chinese politics, ecological civilization refers to a new phase of modernization characterized by harmonious coexistence between humans and nature – between economic growth, social development and a beautiful ecological environment.

of the crucial minority indicates Xi's distinctive thoughts on cadre management. In particular, Xi has pushed to hold them directly accountable in policy making, coordination and supervision for policy implementation and has literally asked them personally to perform their duties in these key linkages of policy formation (Xinhua 2017b).

Corruption and notorious work styles are the two major concerns that have long existed in China's state and party bureaucracy and have been the major sources of people's growing discontent and negative comments on the Chinese government in recent decades. Xi has targeted these two problems to show his determination for stricter party discipline. Xi introduced the well-known Eight-point Regulation of the CPC Central Committee after he came to power and has vigorously pushed its enforcement throughout the whole party system to cut formalism, bureaucracy, hedonism and extravagance and other forms of unwelcome *modus operandi* to maintain close ties with the masses. Starting from the senior leaders and officials in the Politburo, Xi's top-down, aggressive campaign to battle against the CPC's abhorrent manner of working has lasted for years and seemingly improved the performance of the cadres as a whole. An enduring anti-corruption campaign constitutes another significant aspect of Xi's endeavour to strengthen party discipline and plays the role of "killing two birds with one stone." Xi's resolute and ruthless anti-corruption measures serve to clean up the party bureaucracy to ease the widespread resentment in Chinese society over the rampant corruption, as well as carrying out a great purge of Xi's main opponents to consolidate his power in the party.

In summary, Xi's top-level design emphasizes the nature of holism in his grand plan for promoting economic, political, cultural, social and ecological progress and implies his ambition for comprehensive control of every aspect of the state and the society. The core parts of the top-level design lie in comprehensively deepening reform and comprehensively strengthening party self-discipline. Economic system reform, with its central task of economic structural reform, is the priority of the comprehensive reform, while strengthening party self-discipline acts as the trusty resource he relies on heavily to guarantee the implementation of this strategy. The other goals are simply "new bottles that contain the old wine," which function as ornaments. For instance, the

goal of comprehensively advancing the law-based governance of China was criticized as being clichéd because of the inevitable conflict between law-based governance and the principle of the party's leading role in every aspect of Chinese society.

Following his idea of top-level design, it seemed that President Xi had resorted to both institutional changes in governance and an unparalleled emphasis on the party's discipline to try to obtain full authority in policy making and greater control over policy implementation. In the next three sections, the paper will discuss Xi's efforts to forge a model of ruling in which powerful central leading groups act as his trusted party agencies to make decisions and supervise the policy implementation, his endeavours to re-establish the party's solid leadership over everything, as well as his struggle to strike a balance between the goals of maintaining stability and seeking sustainable economic growth.

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## Institutional Changes for Top-level Design: The Strengthened Roles of Central Leading Groups

The strengthened roles of leading groups<sup>5</sup> constitutes one of the most distinguishing characteristics of Xi's style of governing China. Since the 1980s, the Politburo and its standing committee (the PBSC) have been the top decision-making bodies under China's party-state dual-governance structure. The State Council has been the highest administrative agency managing economic and other affairs on a daily basis, while a few leading groups coordinated between the party and the state on financial, economic and foreign affairs. But since 2013, Xi has notably strengthened the role of leading groups at the expense of both the PBSC and the State Council (He 2018), which indicated a significant institutional change that would reshuffle the policy-making and enforcement system in China.

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5 Xi did not initiate the model of leading groups ruling. Chairman Mao created leading groups to regain the authority over policy making in the 1950s and the 1960s. The Central Leading Group for Cultural Revolution in the 1960s once replaced the Politburo as the paramount policy-making organ.

By establishing, reshaping and upgrading leading groups in key sectors to the status of commissions, Xi has amassed a concentration of power unseen since Mao. He currently supervises nine newly established or revised leading groups, committees and commissions, which, accordingly, cover nine of the most important governance sectors: nationwide reform, financial and economic affairs, state security, foreign affairs, Taiwan affairs, military reform, cyber security, legislative issues and auditing. These commissions are under the direct control of Xi, which puts the State Council and the Politburo and its standing committee on the back burner. The leadership of party central commissions in determining national political and economic agendas is the most distinctive feature of Xi's governance (ibid.).

To better understand the position of the leading groups in China's governing structure, they can be analogized to White House committees such as the National Economic Council and the National Security Advisor, which play a crucial advisory role in policy making. Administratively, they are party agencies, not parts of the state bureaucracy. In terms of personnel, the members of these groups come from both the party and the state bureaucracy. The aim is to coordinate policy making from different government agencies in the state and departments in the party system. In this way, the authority in economic and non-economic policy making normally held by the State Council standing meeting in the state bureaucracy and the Politburo meeting in the party's bureaucracy have been undercut by these leading groups.

The Central Leading Group for Comprehensively Deepening Reform (CLGCDR), newly established by Xi in 2013, and the existing Central Leading Group for Financial and Economic Affairs (CLGFEA) play the most important roles in reform promoting and economic policy making. The rise of the CLGCDR and control of the CLGFEA greatly strengthened Xi's role in promoting reform and policy making in economic affairs at the expense of the premier of the State Council. As the highest decision-making advisory bodies, the control of the two crucial leading groups demonstrated Xi's top-level design in policy making on significant reform and economic and financial issues.

The founding of the CLGCDR became a game changer in Xi's endeavour to regain institutional control in China's reform. The establishment of the CLGCDR can be explained as an institutional

change under President Xi, who transferred the central role of managing the economy and other related fields from the government (State Council) to the party. From the time when it was announced in 2013 until it was formally established in 2014, the CLGCDR emerged as a powerful paramount cross-departmental agency, consisting of high-level officials from most of the key government and party departments, with President Xi and Premier Li as the director and deputy director, respectively.

At the party's third plenum of the 18th Congress in November 2013, the new institution was authorized as the highest body for the overall design, arrangement and coordination of reform and to push forward and supervise the implementation of the reform. Under the circumstances of Chinese political culture, however, the importance of any agency depends on the administrative ranking it has, particularly the authorities possessed by its top leader. Although it was expected that high-level personnel would fill the positions, the rarely seen high level of the eventual staff of the CLGCDR still shocked outside observers. The CLGCDR has four members of the PBSC as its leaders, including Xi himself as the director and premier Li Keqiang, head of the Central Secretariat Liu Yunshan and Vice Premier Zhang Gaoli as the deputy directors; its members include three other vice premiers and 10 ministers from the State Council.

What makes the newly established group unique is that it also contains senior officials from the Central Commission for Discipline Inspection, the party's highest anti-graft organ, and from the party's other departments, such as the Organization, Publicity, Policy Research, Political and Legal Committee, as well as representatives from the military, the National People's Congress and the Chinese People's Political Consultative Conference, and the heads of the Supreme People's Court, the Supreme People's Procuratorate and the Ministry of Public Security. The high and comprehensive level of its personnel makes the CLGCDR more like a committee that takes control of the overall situation than just a central leading group. The office of the CLGCDR was set up within the Central Office of Policy Research (COPR); its director Wang Huning<sup>6</sup> serves concurrently as the director for the office and two other senior officials from the

<sup>6</sup> Wang became one of the seven-member PBSC at the 19th Party Congress in October 2017 and made the CLGCDR even more powerful.

National Development and Reform Commission (NDRC) and the COPR serve as deputy directors.

Composed of such high-level personnel, the CLGCDR constituted the highest body to promote a comprehensive reform agenda that involves almost every arena in Chinese society, including political, economic, social, cultural, and ecological systems, and the military and party building.<sup>7</sup> The CLGCDR also supervises the implementation of these reform measures through its nationwide, top-down offices for reform at the provincial, regional and municipal level of local governments. By doing this, the CLGCDR created a vertical system on the sidelines of the state bureaucracy under the central government to promote the reforms. This is not a separate system, but one that combines the officials from both the state or local government and both the central and local party organizations. It penetrated the government and party systems and tried to improve the efficiency and effectiveness of policy making and policy implementation in terms of reform promotion. The CLGCDR is, to some extent, replacing the State Council to take measures for and supervise the reform.

The establishment of the CLGCDR was entrusted by President Xi and his senior advisors as the key institutional arrangement to solve obstructions in the reform. Along with the newly established CLGCDR, President Xi quietly and carefully put himself in the leading position in the CLGFEA, the most important existing coordinating group for financial and economic affairs.

The tradition of the premier assuming the role of director of the CLGFEA as the top policy maker for economic affairs began in the 1980s. Holding the post of director of the CLGFEA means legitimately and institutionally grasping the decision-making power in economic issues. In June 2014, the Xinhua News Agency, the most authoritative news agency in China, made an unusual announcement in a subtle way. It was announced for the first time that Xi, as the director of the group, hosted the sixth CLGFEA meeting, with Premier Li as just the deputy director (Xinhua 2014b).

The exceptional news report was closely followed by rebuttals from official media to the previously

long-existing narrative that, since the 1990s, the premier usually assumed the post of director of the CLGFEA. Official media claimed that the party had never announced who assumed the position of director of a leading group before while they confirmed that, since the 1980s, it was always the party general secretary instead of the premier who had been the director for the group. These self-contradictory arguments<sup>8</sup> demonstrated the official media's intention to claim Xi's legitimacy as the director of the CLGFEA, while Xi made the organizational structure of the group open to the public for the first time since its establishment in 1980.

This episode indicated Xi's determination to get involved and even take on the highest authority over important economic policy making above Premier Li. Before June 2014, information about the CLGFEA meetings had, for decades, never been announced or available to the public. The public reports on the CLGFEA meetings since June 2014 sent the important message that Xi has concentrated the decision-making authority over significant economic policies in the group, over which he conveniently takes full control. What the CEWC did was formally announce and explain in detail the policies made by the CLGFEA to the key senior officials in every sector of Chinese society.

Via these leading groups that oversee different fields, Xi can control the policy-making process in each important sector, such as economics, security and foreign policy, in a much more convenient way than in the Politburo. These developments showed that President Xi had been comprehensively reshaping the institutional structure in the governance of China and began to take control of policy making in both economic and non-economic affairs. The Politburo's status as the highest organ for policy formation and promotion since the founding of the CPC is being

7 Party building refers to a series of activities in the entire party system to improve the CPC's capacity in every aspect associated with its status as the ruling party in China, including organization, governance, ideology, work style, discipline, propaganda, connection with the masses and so on.

8 It is fair to say that Xi, as the party's general secretary, assuming the director of the CLGFEA has precedents, and who can assume the post and take the power in economic policy making depends, to some extent, on who has better political craftsmanship and economic expertise. In the early 1980s, Zhao Ziyang, as premier, assumed the role of director of the CLGFEA and shouldered the highest power in economic policy making due to his excellent reputation in managing the economy. After being promoted by the de facto paramount leader Deng as the party's general secretary, Zhao still held the post of the CLGFEA's director and managed economic and financial affairs because Deng did not trust premier Li Peng's capacity to run the economy. But in the following years, Li took advantage of a major policy failure in pricing reform in 1988 and gradually seized the power in economic decision making, even though he was only holding the post of premier, and not the director of the CLGFEA (Wu 2014).

eroded by the nine leading groups Xi heads. These leading groups are emerging and undermining the Politburo as the highest policy-making authority.

The significant institutional changes taken by Xi to establish new central leading groups and substantive control over key leading groups in the policy-making process is supposed to solve problems in the policy-making stage but not the ones in policy implementation. The central leading groups are basically key policy-making groups that exist at the central level, although some of them exist at local levels (for example, there are CLGFEA at the provincial level). Generally, they are groups for policy making, coordination and supervision and do not have the capacity for policy implementation. For example, the CLGCDR at the central and the local level are playing the roles of policy making, coordination and supervision but not policy execution, which is carried out by local government agencies.

Having full knowledge of the extreme importance of policy implementation, President Xi needed to make an extra effort to forge an effective mechanism to enforce policies. It is impossible to discard the entire bureaucratic system and rely on the party organization to fulfill the task. The State Council-headed national bureaucracy is still the fundamental force he must rely on for policy implementation. How to get better control of the state bureaucracy and improve policy enforcement is on Xi's agenda after all the institutional changes he made to establish the model of leading groups ruling. This means solving the difficult but crucial issues that blocked the reforms from being implemented. To do so, Xi turned to stricter party discipline and the party's overall control of the entire state bureaucracy and the whole of society.

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## Building the Party's Solid Leadership over Everything Is the Key for Top-level Design

The significant reshuffle of party and government institutions in March 2018 highlighted Xi's efforts to reinforce the party's leadership over

the state bureaucracy and strengthen the party's leadership in an all-inclusive way. The reshuffle was officially labelled the CPC's efforts to further boost the restructuring of the party and the state's institutions, but the core task of these reforms was aimed at establishing the party's full institutional control of the state bureaucracy to make it operate more effectively and smoothly. As for the private sector, Xi had already begun to strengthen the party's control over it before the reshuffle. During the reshuffle, Chairman Mao's 1970s slogan of "The Party exercises its leadership over all walks of life in every part of the country" was quoted in the newly revised Constitution of the CPC, a highly symbolic move that indicates the desire of the party to have central control over the state bureaucracy, the civil society and the private sector.

Chinese party-state government is, by nature, omnipotent and penetrates the whole society, with its huge network of bureaucracy consisting of departments, bureaus, divisions and sections in both the party and the state system at both the central level and the local level, as well as tens of millions of officials who fill up the bureaucracy. Xi's emphasis on the party's leadership over everything focuses on the party's tighter, closer and more direct control of the state bureaucratic system. Xi made it crystal clear in his explanatory notes for the reform of party and government institutions that giving the party's overall leadership full play in all areas and aspects is the most important principle and the priority goal of the reform (Xi 2018).

Given the traditional role of the State Council in handling the economic work, the decade-long priority in the CPC's ruling in China, the party's strengthened institutional control of the state bureaucracy indicates its intention to exercise a tightened control of economic work. The expected appointment of Liu He, Xi's trusted senior advisor in economic and financial affairs in the party system, as the vice premier to take charge of the financial and industrial sectors in the state bureaucratic system, represented the most prominent gesture of the reshuffle.

Specifically, President Xi built the party's solid control over the state bureaucracy through upgrading leading groups to permanent commissions and establishing offices within the institutions of government for these commissions, sharing offices between the party's organizations and the government agencies, as well as filling crucial positions in

government agencies with his protégés. The party also scaled up its intervention into the private sector and civic society under President Xi.

The restructuring and the upgrading of the party's leading groups to commissions was regarded as the most important component of the reform, which helped reinforce the party's control over the state bureaucracy regarding policy making in key areas, in particular economic-related fields. Xi also made this clear in the explanatory notes by saying the restructuring and upgrading of the party's leading groups to commissions were "to strengthen the party central's collective and unified leadership over important work and ensure a stronger leadership in which the party always control the overall situation and coordinate the efforts of all quarters" (ibid).

Four important central leading groups in the significant areas of reform promotion, financial

and economic affairs, national security, and cyber security were upgraded to permanent commissions. Two new commissions, the Central Commission for Overall Law-based Governance (CCOLG) and the Central Auditing Commission (CAC) were established (see Table 1). These central commissions cemented their control of the state bureaucracy by setting up their permanent offices at the ministries in the State Council for the first time. For example, the office for the CCOLG is set up at the Ministry of Justice and the office for the CAC is established at the Agency of Audit; the Central Cyberspace Affairs Commission's (CCAC's) office is set up at the Cyberspace Administration of China. Previously, the leading groups only had their offices and staff in the party system, never in the state bureaucratic system.

The substantiation of these commissions and leading groups and the establishment of their

**Table 1: List of Nine Central Leading Groups (Commissions) President Xi Jinping Heads**

Original Name	Name after Being Upgraded	Original Acronym	Acronym after Being Upgraded	Responsibility	Year Founded
Central Leading Group for Comprehensively Deepening Reforms	Central Comprehensively Deepening Reforms Commission	CLGCDR	CCDRC	Nationwide reform promotion in all areas	2013, upgraded in 2018
Central Leading Group for Finance and Economic Affairs	Central Financial and Economic Affairs Commission	CLGFEA	CFEAC	Major finance and economic affairs	1958, upgraded in 2018
Central Leading Group for Foreign Affairs	Central Foreign Affairs Commission	CLGFA	CCFA	Foreign affairs	1958, upgraded in 2018
Central Leading Group for National Security	Central National Security Commission	CLGNS	CNSC	National security	CLGNS: 2000 CNSC: 2013
Central Leading Group for Internet Security and Informatization	Central Cyberspace Affairs Commission	CLGSI	CCAC	Cyber security	2014, upgraded in 2018
Central Leading Group for Taiwan Affairs		CLGTA		Taiwan affairs	1954
Central Leading Group for Military Reform		CLGMR		Military reform	2014
	Central Commission for Overall Law-based Governance		CCALG	Promoting law-based governance	2018
	Central Auditing Commission		CAC	Auditing	2018

Source: Author.

offices in the ministries in the state bureaucracy demonstrated that the party further corroded the de facto decision-making power enjoyed by the State Council. Xi's direction that "the party's leadership should be implemented and materialized at every links and aspects in the duties of the party and government's agencies" (Xi 2018) is intended to institutionalize the position and the role the party plays as the highest level of leadership. Before the commissions' offices were established in their counterpart ministries in the State Council, party committees and party groups that have long existed in all ministries at the State Council were the organizations the party relied on to materialize its control of the state bureaucracy. But that is not enough in the eyes of President Xi. With these new commissions, the party's control of policy making in certain important aspects has been reinforced.

In addition to the office setting of the leading groups and commissions in the State Council, another key reform measure taken by Xi to strengthen the party's control over the government is "sharing offices by the similar agencies of the party and government or mergence of these agencies" (ibid.) to coordinate the restructuring of party and government institutions. The one that attracted the most attention is office sharing by the newly established Central National Supervisory Commission (CNSC) and the CPC's Central Commission for Discipline Inspection (CCDI). Xi clarified in his explanatory notes for the reform that the purpose of sharing offices by the CNSC and the CCDI is to strengthen the party's unified leadership over its anti-corruption campaign and to supervise all public officers that exercise public power. This plainly indicated that the party's supervisory power has extended to all public officers, including non-CPC members in the state bureaucracy.

Other significant sharing of offices and merging of agencies occurred in the fields of human resources, ideology, and religious and ethnic affairs. The CPC's Organization Department will take care of all human resource issues and the Bureau of Public Officers in the State Council was incorporated into the Organization Department, but the name of the bureau was kept for the purpose of external exchanges. The Publicity Department of the CPC Central Committee has completely taken over press and publication supervision, including film, television and radio, which was previously overseen by the State Administration of Press, Publication, Radio, Film and Television.

This indicated that the Publicity Department has greatly expanded its authority and taken over direct control of press, publication, television, radio and film. The Publicity Department has developed into the base camp for the CPC's tight and direct grasp of the ideology and propaganda work. The United Front Work Department of the CPC Central Committee has also expanded its jurisdiction by incorporating three state agencies previously supervised by the State Council — religious affairs, overseas Chinese affairs and ethnic affairs.

Xi also mentioned office-sharing arrangements at the provincial and lower levels at the 19th CPC National Congress. Although sharing offices or merging similar agencies of the party and government is not something new, all of these unprecedented significant arrangements in the reshuffling of party and government institutions in 2018 displayed Xi's determination to underpin and facilitate the party's control over significant issues in anti-corruption, human resources, ideology and religious and ethnic affairs.

At this point, it is fair to say that the relations between the party and the government under President Xi were being restructured in a way that contrasted with his predecessors. Zhao Ziyang's advocacy of the separation of the party and the government in the 1980s stalled following the 1989 Tiananmen event, and the reform toward separation of the party and the government remained on paper only during the eras of Jiang and Hu. The reform has been entirely denied under Xi's reign (Wang 2017; Zhang 2017). In the name of comprehensively strengthening the party's role, the reforms in Xi's era have focused on the division of labour between the party and the government instead of separation of the party and the government. This means that authority over decision making has been further transferred to the party's central commissions and leading groups, and the State Council acts more like executive agencies. The role of the premier of the State Council in policy making has been further enfeebled, and the party central exerts control over the ministries more easily and quickly to enforce policy.

Politically, the significant reshuffling of party and government institutions in 2018 indicated that the government has further become a mere appendage of the party. The very weak separation of party and state that previously existed in some fields and sectors is gone, and a full integration of the party

and the state has materialized. Observers have used terms such as “unified party and state,” or “the party is the state” to describe the relationship between the two under President Xi (Deng 2019). Behind the unification or integration of the party and the state, an obvious fact is that the party is above the state and has grasped total control of the state bureaucratic system. From the perspective of policy making and implementation, the significant reshuffle of party and government institutions in 2018 indicated that the party’s leading role over the government was institutionalized and could be more easily materialized, and the roles played by the party and the government were further fused to ensure the smoothness of decision making and policy implementation.

The restructuring of the NDRC is a typical case that demonstrates the transition of policy-making power from the state bureaucracy to the party’s institutions. Since the inception of the CLGCDR in 2013, the NDRC has been concerned that its status as the leading agency in macroeconomic planning could be affected. Defined as a super committee that stands apart from vested interests in the government, the CLGCDR was designed to comprehensively push forward reforms and break the obstructions from all types of interest groups. With its extensive authority over investment and project approvals, as well as pricing power over key resources and services, the NDRC was targeted as the top agency in need of reform, given its role in creating vested interests and breeding corruption. The reform to the NDRC itself must be done by a detached body, which partly explains why the CLGCDR was set up for party central’s design for the comprehensive reform and the NDRC was downgraded to the executive agency for the reform (Xie 2013; *21st Century Business Herald* 2014).

Personnel adjustments in crucial positions in the party and government institutions were believed to have contributed to the party’s tighter control over the state and created smoother links between policy making and policy implementation. Xi took a two-pronged approach in this regard. On the one hand, since coming to power in 2013 he has quietly promoted his protégés to key positions in the party and government as the main way to fulfill his vision and plans. For instance, Xi’s former subordinate and long-time ally He Lifeng was appointed as the head of the NDRC in 2017, the crucial ministry in specific policy making and enforcement in economic affairs, which will help Xi’s efforts to consolidate its control

over the regulatory bodies in China’s economic management.<sup>9</sup> On the other hand, a consistent campaign to comprehensively strengthen party self-discipline, or emphasize the “purity” of the party, has been employed to ensure policy enforcement.

Liu He’s promotion to vice premier indicated that he had become a significant supervisor on policy implementation with substantive authority over the state bureaucracy, in addition to his existing role as Xi’s top economic advisor and the senior policy maker in China’s economic and financial policy. Liu’s dual senior positions in both the party and state bureaucracy and in both policy making circles and policy implementation would help further smooth the interlinkages between policy making and policy execution. Seen from this perspective, Liu He has emerged as the new economic czar, as Premier Zhu did in the late 1990s.

The private sector had already developed into a vital component of China’s economy following the reform and opening up that began at the end of the 1970s, accounting for 50 percent of tax revenue, 60 percent of GDP, 70 percent of technological innovation, 80 percent of urban employment and 90 percent of the total number of enterprises in China by 2018 (Xinhua 2019). The party under Xi’s rule has tried to exert direct influence over both domestic private enterprises and foreign companies but maintained the policy of encouraging the development of the private sector and further opening up to foreign capitals and investment in China in recent years.

Before Xi, the party clearly required that the party organizations “cover” all the private enterprises in May 2012 (People’s Daily 2012). Xi strengthened the party’s control over non-government organizations in the field of business, culture and social groups by renewing the party’s work regulations on the “party group” in 2015 (Xinhua 2015b). President Xi pushed more aggressively for the party’s total “cover” over all the private business groups and non-government social groups. The establishment of party committees in some newly emerged domestic private companies, such as Xiaomi, Meituan and Kuaishou, and foreign companies, such as Samsung, in recent years sent strong messages in this regard. The percentage of private enterprises that have established party organizations in all private

<sup>9</sup> A large number of senior officials elevated to key party and governmental positions were Xi’s former subordinates, classmates or colleagues. They are supposed to be loyal to him and are trusted to fulfill his policies.

enterprises soared over a period of a few years, up from 54.3 percent in 2012 to 73.1 percent by 2017. The number of private enterprises that have established party organizations increased from 1.627 million in 2013 to 1.877 million in 2017 (Xinhua 2014c, 2018).

The way the party organizations (party branches and party groups) operate in the private sector demonstrated the party's total control of the whole society but not a direct interference with private enterprises' business operation. It appears that the party wanted to stay informed about the status quo and trend of development in the private enterprises but did not try to take them over and push them out of the economy.

Other moves undertaken by the party in recent years, however, demonstrated that the party is gradually intruding in the private sector. The CPC is advocating for the party committees to play a greater role in the management of private enterprises, even foreign companies or joint ventures. It also pushes for democratic management of private enterprises, meaning owners and employees jointly running the business, as shown by Qiu Xiaoping, vice minister of human resources and social security in 2018 (Ministry of Human Resources and Social Security of China 2018).

The worst-case scenario could be the private sector being pushed out of China's economy or being nationalized after "accomplishing its historic mission of achieving growth and should leave the market gradually," as a widely circulated blog post (Wu 2018) claimed in September 2018. Under these circumstances, President Xi came out and mollified private entrepreneurs by announcing high-profile government support for the private sector following extensive concerns and dissatisfaction in the circle of private enterprises in the second half of 2018.

Through these institutional arrangements and discipline control, the power of the top-level design has been finally realized and discerned in the state bureaucracy. The private sector has also been aware of the increasingly tightened control from the party under President Xi. It has become evident that, as demonstrated by the top-level design, Xi's efforts targeted not only the persistent problem in policy implementation, but also substantial and efficient control of the whole state and the society for stable governance in China.

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## Top-level Design: Top Principle Is Stability, Main Goal Is Sustainable Economic Growth

The top priority of maintaining stability has featured in China's decision-making model in its decades-long effort to push reform for sustained economic growth since Deng Xiaoping, who began to emphasize stability as the priority for the CPC's ruling in China after the 1989 Tiananmen event. Since then, the party's top leaders have become increasingly obsessed with stability and made it the core value and top priority in governing China (Yu 2008, 2012). Stability maintenance, that is, ensuring the party's perpetual rule in China as the overriding principle, has led top leaders to develop a widespread and deep-rooted attribute in policy making: a tendency to be extremely risk-averse.

President Xi, unsurprisingly, embraces this core value to promote his top-level design for governing China. While carrying out the institutional changes in China's decision-making and policy implementation mechanisms, Xi has been seeking sustained economic growth and fulfillment of the blueprint for comprehensively deepening reform. He must walk a tightrope to keep Chinese society stable while promoting his top-level idea for comprehensive reform in economic and other areas.

At the same time, sustained economic growth via market-oriented reform has evolved into the fundamental source of legitimacy for the CPC's rule in China since 1989, as democratic political reform, freedom of the press, pluralism and other universal values have not been appreciated in Chinese society under the CPC rule. Chinese official media and scholars have called this "the symptom of high growth reliance," which means high economic growth has evolved into the main solution to ease social conflicts and maintain social stability; the slowdown of economic growth would otherwise precipitate instabilities in the society (Chen and Yao 2012; Jing 2013; Chen 2014; Yang 2016). Since 1989, the core task of governing China for the CPC has become a fine balance between the top leaders' extreme risk-averse tendency and seeking sustained economic growth via deepening market-oriented reform.

President Xi faced even more pressure to maintain this delicate balance when China's economy entered the so-called "new normal" and growth slowed down from 2015 on. Under these circumstances, the two goals of maintaining stability and seeking economic growth are in constant conflict, and the leaders are always under pressure to make choices between maintaining short-term growth to contribute to social stability (but with key reform measures suspended) and pursuing the long-term reform goals (but with decreased economic growth).

Achieving this balance is particularly evident on key reform issues such as the SOE reforms, market-oriented exchange rate reform, interest rate liberalization reform and economic restructuring. Reform comes with risks, and key reforms entail potentially huge risks, while, if successful, they could bring significant progress and benefits. Chinese top leaders typically show some indecisiveness and wavering attitudes on these tough reforms. For example, the practice for SOE reform has been carried out for decades, since China began its economic reform at the end of the 1970s, and did not achieve much substantive progress in terms of marketization, even though market-based reform has already evolved into a new orthodox idea and the party leaders always advocate market-oriented reform in almost every economic sector. When it comes to the SOE reform, however, the long-established concept that the SOEs constitute the most important economic foundation of the CPC's rule in China prevails and has substantially obstructed the reform. Any market-oriented reforms that would endanger the status of SOEs as dominant, privileged economic entities would be rejected, mostly likely in a subtle way.

As a result of this compromise, the SOE reform under President Xi has been stuck between the efforts to promote market-oriented reform and the guarantee of SOEs' dominant status in some key economic sectors. The latest guiding opinion for the SOE reform was released on September 13, 2015, with emphasis on improving state-asset supervision through transitioning from managing enterprise to managing capital, as well as the mixed-ownership reform (Xinhua 2015c). These two priorities in the guiding opinion demonstrated the willingness of the top leaders to usher the market forces into the SOEs. However, the mixed-ownership reform was regarded as a way to capture

wealth from private enterprises to save the heavily indebted SOEs, and caused wide suspicion from prominent private owners. Strengthening the party's control of the SOEs in the guiding opinion marked a big step backward in the market-oriented SOE reform and was disheartening for proponents of the market-oriented SOE reform. This did send a clear message on the top leaders' consistency on the direction of the SOE reform: keep the SOEs as the economic and political foundation for the party's ruling in China. This could partly explain why the process of mixed-ownership reform went slowly after it was formally introduced in 2015.

The economic restructuring process in the past decade also demonstrated this balance between the risk-averse tendency and deepening market-oriented reform. The 2008 global financial crisis had a huge impact on China's investment and export-driven growth model. The drop in external demand and the accumulated structural problems in the economy since the reform and opening-up at the end of the 1970s (Yang 2014) have also pushed Chinese policy makers to proceed with economic restructuring. From 2008 to 2011, the annual CEWC prioritized the promotion of transforming the growth model and economic restructuring and expanding domestic consumption. However, the enormity of the structural problems and the vested interests that developed and were perpetuated in Chinese society during the reform signified that the task of economic restructuring is exceedingly difficult.

Furthermore, economic restructuring is supposed to go hand in hand with a short-term growth slowdown. The consequences of "the symptom of high growth reliance" posed serious obstacles to the transformation of economic growth patterns and economic restructuring. Whenever the growth rate was going down, measures such as expanding investment and easing credit would be resumed to hold the economic growth; measures to restrict investment and tighten credit would be introduced while inflation was looming. The stability-obsessed Chinese leaders have struggled to maintain the fine balance between economic restructuring and maintaining stable growth since 2008.

President Xi's efforts to solve the overcapacity issue via industrial restructuring began following the CEWC in 2012. To adjust to the new normal, a period featuring a slower economic growth rate declared by Xi in 2014, policy makers' attention shifted to seeking economic restructuring and

high-quality growth instead of the GDP growth rate. However, once the economy suffers a quick and serious slowdown, it is difficult for President Xi to hold and resist the impulse to resort to short-term stimulus policies and measures.

For instance, China's economic growth suffered a substantial drop beginning in the first three months of 2015, with the GDP growth rate going down to seven percent, reaching a record low since 2009 (Wildau, Mitchell and Anderlini 2015). A series of contingent policies to "stabilize the growth" were adopted to bolster the economic growth following the so-called worst-case-scenarios thinking President Xi advocated. The PBoC lowered the deposit reserve ratio twice, in February and April, and cut the interest rate in March to release liquidity (Su and Gou 2015; Yicai 2015). The Ministry of Finance, Ministry of Housing and Urban-Rural Development (MOHURD) and other departments also took measures to stimulate the economy in the first quarter of 2015 (Li 2015). The dull performance of the economy lasted into the second half of the year, and more ministries joined the chorus on the need to stabilize growth in September to boost investment and export, including the PBoC, the NDRC, the Ministry of Finance, the Ministry of Commerce, MOHURD, the Ministry of Transport, the General Administration for Customs and the Ministry of Industry and Information Technology (*Shanghai Securities News* 2015).

These measures indicated that whenever the economic downturn endangers social stability, policy makers would take whatever steps necessary to stabilize growth. Policies, including economic restructuring, the monetary policy goals of the PBoC or policy goals from other departments, usually need to be set aside or modified for the time being to guarantee the de facto top priority of maintaining stability. For example, the PBoC's target of formation of a market-oriented exchange rate mechanism had yielded to the more important goal of stabilizing growth. The August 11 exchange rate reform in 2015 toward a free floating exchange rate mechanism was suspended three days after it was launched out of worries over depreciation and further overshooting of the value of the renminbi (RMB) that would cause widespread

market jitters and jeopardize the stability of the financial market and thus the whole economy.<sup>10</sup>

It is fair to say that there is a general tendency among Chinese top leaders since Deng Xiaoping to prioritize stable economic growth and social stability and try to strike a balance between economic and social stability and seeking reform and growth. The trend has not started with President Xi, but he has made even more of an effort at both ends of the balance, equipped with strengthened party control over each sector of China's political economy. Whether on SOE reform, economic restructuring or exchange rate reform, the top leader pushed harder, promoting reforms and restructuring with greater government intervention while keeping the focus even more closely on maintaining social stability. With a more intense sense of urgency at both ends of the balance, Xi pushed harder in both economic reform and growth and maintaining social stability. Certainly, after noticing the great potential risks, Xi would push policies to go back to guaranteeing the top priority of maintaining stability.

## Summary

The top-level design laid the theoretical foundation for Xi's overall control of the reform agenda and economic policy-making process. He claims that China's reform is a holistic system consisting of economic, political, cultural, social and ecological subsystems. The model of renewed central leading groups' control established the institutional framework for Xi's top-level design to promote the reform and dominate the policy-making process. The top-level idea emphasizes building the party's full control of economic work and everything else, which is expected to be guaranteed through tightened party control over the state bureaucracy, private sector and civil society. The top-level idea follows even greater efforts to keep the balance between the extreme risk-averse tendency and seeking economic growth. This represents Xi's greater caution in handling the economy. After all, delivering sustainable economic growth constitutes the most important foundation of the party's legitimacy in governing China.

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10 Some scholars, such as Yu Yongding, insisted, in retrospect, that the August 11 reform could be the critical point to finish China's journey of moving to a free-floating exchange rate system if the PBoC could hold the line and did not jump hastily into the market to intervene (Yu 2017).

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## The Problems with Xi's Top-level Design in Economic Policy Making

With the central leading groups' institutional control, unprecedented emphasis on the party's leadership in economic work and everything else, and special efforts on keeping a fine balance between growth and stability, Xi's top-level idea achieved tightened control over China's policy-making process. However, the long-standing problems in China's policy-making process, in particular, how to effectively enforce decisions, have haunted President Xi and his top policy experts. These problems include old bureaucratic problems in China's policy-making and implementation process, categorized by Xi as the "first kilometre, middle obstruction, and last kilometre" barriers (Xinhua 2015a). There are different bureaucratic problems as well that emerged or were exacerbated in the policy process under President Xi's top-level design.

First, there are serious problems that exist in China's decision-making mechanism that constitute major obstacles for Xi Jinping. Xi used the metaphor of the "first kilometre," referring to the first stage of policy implementation that usually causes problems in his remarks at the tenth meeting of the CLGCDR in 2015 (Xinhua 2015a). Specifically, the first kilometre means the initiative of reform design, in which many of the decisions are vague, confused, or even in conflict with each other and unfeasible. Obstruction for the reform thus formed at the beginning. China's decision making at the highest level typically only gives instruction and indicates the direction for the important issues in vague language, instead of giving explicit policies, which renders the bureaucrats more room to interpret the top leaders' design and get involved in the decision-making process at an earlier stage than in other countries (Chen and Naughton 2016).

In the context of China's decision-making system, this is called the second-time decision making, which refers to confirmation and elaboration, as well as optimization and evaluation of the feasibility of the decisions made by top leaders. It is a stage that combines both policy making and implementation, and it happens at the ministerial

and local levels. This indicates the great importance of the bureaucracy at the ministerial level for policy formation and at the local level for policy execution.

The second-time decision-making is an ordeal as it always involves turf wars among multiple ministries and usually ends up with no substantive policy being made. As a result of this, many vaguely worded decisions by the top leaders are stalled in the stage of the first kilometre, reflecting the fact that the real consensus on reform and important policy issues is still missing. This is typical when it comes to tough decision making, such as SOE reforms. Although the party central and the State Council already made decisions in 2015 to promote the SOE mixed-ownership reform, the process has not been substantively advanced. This is due, in part, to the lack of real consensus on the reform, and the reform proposals on key issues in the SOEs have been compromised. The key government agencies such as the NDRC and the State-owned Assets Supervision and Administration Commission of the State Council still hold crucial power over management and personnel in the SOEs. Xi's comprehensive reform plans have not been carried out at a level deep enough to touch the long-existing difficulties in China's policy implementation process.

Second, interest groups "kidnap" or hinder decisions to be implemented in a variety of ways. This is what Xi called the "middle obstruction" and happens mostly in the process of reform promotion. These groups could be ministries or local governments. Ministries, as the leading agencies that make specific second-time decisions and execute the reforms, are usually the targets of the reform, or at least beneficiaries of the existing policy. This drawback, which is a result of China's government structure and decision-making mechanism, can, to a large extent, prevent any essential reform measures from being made. To make it worse, these key ministries simultaneously enjoy the powers of decision making, implementation and supervision. Under these circumstances, reform can easily turn out to be an excuse and opportunity for these ministries to expand their jurisdiction and interests, or selectively enforce the policies that benefit them.

Ministries and local governments as institutional agencies have their own vested interests and worry that their interests would be hurt in the reform; therefore, they tend to decline or at least show reluctance to promote real reform measures, and

would obstruct policy implementation by using all the bureaucratic means to hold off policy execution, selectively implement, water down or change policies to protect their own interests. Under pressure from the top to push reform, a variety of superficial reform measures, such as issuing policy documents, convening conferences and introducing proposals, were taken but no specific policies were implemented. Reform, therefore, exists only on paper without any real concrete actions being delivered. “Issuance of documents is reform itself” best illustrates the feature of formalism in the reform: officials pretend they are promoting reform by issuing policy statements but take no actions. Even if specific ministries or agencies show resolve to advance reform, they would find that difficulties in coordination between different departments and between different *tiao* and *kuai*<sup>11</sup> would kill their willingness for reform.

Third, there are the “last kilometre” problems that exist in the final enforcement stage of specific policies at the grassroots level. Who “pays the piper” for the reform is a major issue that essentially always obstructs the final implementation of specific policies. Basically, the reform measures could only be finally materialized if the concern of who pays the bill for the reform was addressed. The issue of who pays the piper for the reform relates to a key issue that local governments pay the most attention to, i.e., defining the respective powers and a better expenditure structure (spending responsibilities) of the central and local governments. In addition, many grassroots-level officials face the dilemma that the reform would hurt their own interests, and promotion of the reform would not benefit them. As a result, they usually chose to deal perfunctorily with the reform requirement from their superiors.

Xi’s top-level design, featuring more consolidated power and control at party central over policy making and execution, as well as an unprecedented obsession with stability, has worsened some of the existing bureaucratic problems in China’s daily economic management and brought devastating repercussions in its crisis response.

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11 In the context of China’s politics, *tiao* refers to the vertical leadership system over various sectors (for example, agriculture, transportation) reaching down from the ministries of the central government to departments, bureaus and offices at the lower provincial, municipal and township levels; *kuai* refers to the horizontal level of authority within a provincial or lower-level territorial government. Conflicts between *tiao* and *kuai* is a well-known bureaucratic problem in China’s officialdom.

First, Xi’s determined anti-corruption campaign and strengthening of party discipline, combined with China’s ongoing economic transformation, created negative consequences in policy implementation that he probably did not fully expect.

A large number of officials showed indolence in performing their duties. Avoiding the suspicion of corruption or violation of party discipline is the primary reason for the large scale of officials’ unwillingness and failure to perform their duties. Bureaucrats at all levels of the Chinese government play the role of policy enforcement and push for local economic development. As a result of a great deal of dereliction of duty in the bureaucracy, China’s government intervention-driven economic growth model is losing a significant part of its momentum.

Under the overwhelming pressure brought by Xi’s ruthless fight against corruption, the previously normal activities practised by officials, such as connecting with businesspeople and investors to promote economic growth, now could be regarded as a type of corruption. The likelihood of officials being investigated on graft charges is much higher simply because of the decisions they made to promote reform. The more you work, the more mistakes you could make. It is not worth taking risks to make decisions, and the best strategy for officials is to do nothing. Plus, with their superiors and colleagues under ongoing corruption investigation, many local cadres feel insecure and have no desire to perform their duties.

Another reason for the phenomenon of sloppiness in performing duties lies in the changes in how officials work to promote economic growth. The party central has been advocating economic restructuring and encouraged measures such as more restrictions on the untamed growth of the real estate market and improving the real living standard instead of increasing GDP. The old model of economic growth, which typically includes doing whatever it takes to attract investment, such as tax breaks and preferential land policy, is being transformed and discarded, leaving many officials bewildered when it comes to performing their duties. The simple, direct old ways of selling land, preferential investment promotion and loans from state-owned banks to expand investment are ending. Structural reform to get away from debt-addicted growth and move toward an environmentally friendly model of economic development is much more

challenging and requires officials to meet a higher calibre to achieve the policy goals.

Researchers at the NDRC analyzed a wide variety of practices used by China's bureaucrats at the local level and examined how these bureaucratic nightmares prevent policies from being effectively enforced (Zhang, Sun et al. 2017). Typically, officials would water down or expand the original policy from central or other higher-level authorities or replace it with their own local policy in the name of enforcing the policy, depending on which way would benefit them most. They would also simply selectively execute the policy that would benefit them. For a policy that could harm their own interests, they would promise to promote it but actually resist implementation, carry it out superficially and frivolously, or push it rigidly without any flexibilities. They would also explain and enforce a policy completely out of their own deliberate or accidental misunderstanding of it, or pretend to be implementing policy but actually be holding a wait-and-see attitude, and so on.

The widespread idleness among officials has drawn attention from the top. President Xi pushed officials to be more diligent in policy implementation and they faced new pressure to avoid suspicion of indolence in performing duties. Officials typically demonstrated two types of actions at this point: they were either still reluctant to take initiatives to implement policies but have to show they are busy performing their duties to avoid being suspected of inaction, or they were becoming inflexible and over-eager in enforcing policies. As a result, policy implementation is either halted by officials in many innovative and delicate ways to give the impression they are working hard, or executed in a rigid but ardent way. One recent example of the latter was the barbarous mass demolition of neighbourhoods in Beijing where many migrant workers lived in winter 2017 under the leadership of the newly appointed mayor, Cai Qi (Mai 2017).

Second, the stability-obsessed ruling style and unprecedented pressure on state and local bureaucrats to maintain economic and social stability intensified the existing notorious bureaucratic problems, including tight control of the flow of information, only reporting

and releasing good news<sup>12</sup> and evading taking responsibilities by waiting for orders from superiors before taking any essential actions. These problems could have catastrophic consequences in times of crisis, such as an epidemic outbreak.

All of these ramifications, if they happened in the daily management of economic and other areas, are gradual and the damage would not be immediate. But when prompt reactions are needed when facing a crisis, these worsened bureaucratic problems under Xi's top-level tightened control can have disastrous results, as shown in China's initial handling of the COVID-19 pandemic when it first broke out in Wuhan, Hubei Province, China, in December 2019.

Here are some observations on China's local and central government's initial response to the coronavirus outbreak in Wuhan based on public information available.<sup>13</sup>

First, China's response and initial handling of the coronavirus up to January 7, 2020, seemed hesitant as it was a novel virus at that point and the disease it caused was still called "pneumonia with unknown cause."

An early assessment of the novel virus by the national health authorities concluded that the virus is a brand-new coronavirus homologous to severe acute respiratory syndrome (SARS) and supposed to be transmitted through the respiratory tract (Caixin 2020a<sup>14</sup>). With the wisdom of hindsight, it is obvious that the top leaders did not give enough attention to the coronavirus crisis in its early stage. It is safe to say that outbreak prevention was not the priority agenda item at the PBSC meeting on January 7 and Xi gave only general and vague instructions on responding to the virus, according to public information available (Xi 2020; Xinhua 2020b). However, the top leaders' early response seems conceivable, especially when compared to

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12 A late Chinese writer, Wang Xiaobo, had hinted at this bureaucratic vice in China by telling a fictitious story about messengers of the Khwarezmian dynasty in the approximate period of the eleventh to thirteenth century, where the emperor rewards the messenger who brought good news and kills the one who came with bad news.

13 Please refer to Caixin (2020a), Caixin (2020b), Caijing (2020), *Bingdian Weekly* (2020), Gupta (2020), *The Wall Street Journal* (2020) and Xinhua (2020a) for China's local and central government's initial response to the coronavirus outbreak in Wuhan.

14 The original article has been removed. A copy of the original article can be seen at: [www.jenniferzengblog.com/home/2020/2/26/tracking-the-source-of-novel-coronavirus-gene-sequencing-when-thealarm-goes-off](http://www.jenniferzengblog.com/home/2020/2/26/tracking-the-source-of-novel-coronavirus-gene-sequencing-when-thealarm-goes-off).

the initial slow response of the United States and some EU countries as the coronavirus spread in late February and early March 2020, when they were supposed to be well informed about the novel virus and to have had enough time to prepare for it.

Second, as a country that had learned costly lessons in dealing with the similar SARS epidemic in 2003, China could have been more proactive in handling the novel coronavirus. However, there exists a pattern of concealing bad news among local officials of hospitals, health authorities, and government in Wuhan and Hubei Province. As a result, critical information about the coronavirus was covered up, which contributed to the outbreak becoming uncontrollable.

Following SARS, China set up a direct online reporting system for infectious disease, which is supposed to empower doctors in hospitals to directly report suspected cases of illness to local and national health authorities simultaneously. The system, however, failed in practice to capture full direct online reporting for suspected cases of coronavirus. The reporting system was tightly controlled by Wuhan local authorities during most of January 2020 (Caixin 2020b) out of a concern to be cautious and to avoid creating widespread panic that could destabilize the social order. Key information about human-to-human transmission and medical staff infection was concealed from the three on-site investigation expert groups sent by China's National Health Commission between December 31, 2019, and January 20, 2020 (Caijing 2020, Caixin 2020b, *Bingdian Weekly* 2020). The missing information contributed to Chinese top leaders' failure to realize earlier on the seriousness of the coronavirus as a highly contagious epidemic.

Third, it is, in essence, the obsession with stability and the unprecedented emphasis on the party central's control and authority in policy making behind President Xi's top-level design that led to the escalated trend of local officials withholding bad news from their superiors and eventually contributed to the coronavirus outbreak in January 2020.

It is unsurprising that under the current highly centralized top-level policy-making system, without clear instructions to make the handling of the unknown virus the top priority, the national health authorities and local health authorities at different levels in Wuhan and Hubei Province tended to maintain the status quo and tried their

best not to cause widespread panic because of the virus. This explains why local leaders withheld information about the coronavirus and tried to control the crisis and resolve the problem within Wuhan and Hubei Province. Reporting bad news would not only upset and embarrass top leaders but would also mean local officials would be held accountable before they are able to attempt to deal with the coronavirus within their jurisdictions.

Xi, as a veteran who has immersed himself in the party and the state bureaucratic system for decades, is supposed to understand the extreme importance of and the huge challenges facing policy execution in China. Before rising to the position of the highest leader, he had listed many types of problems that led to policy failing to be implemented at one of his speeches in 2011 at the Central Party School (Xi 2011). He was aware of the danger of failure for his top-level design due to the lack of implementation in the process of reform and has repeatedly emphasized the significance of policy enforcement in some of his keynote speeches. However, these deep-rooted bureaucratic nightmares are not easily eradicated and can be seen at the implementation stage of many major policy initiatives by President Xi.

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## Case Study of Economic Policy Making under Xi: Supply-side Structural Reform

Supply-side structural reform is President Xi's first major effort to manage the micro-economic policy with the aim of restructuring the economy and guaranteeing sustainable growth in the long run. It is also a major proposal initiated by Xi to refresh the stalled reform process since the CLGCDR, the new institutional arrangement to design and push the reform, was established in 2013.

## What Is Supply-side Structural Reform?

Theoretically different from the emphasis on the demand-side troika of investment, consumption and export, supply-side structural reform focuses on the supply-side elements — the supply and effective utilization of production factors. It is not identical to the traditional economics of supply side, which focuses on the management of supply, such as tax cuts and deregulation from excessive government intervention. Xi's supply-side structural reform focuses on the structural changes in the supply side. Specifically, it aimed to solve three major structural issues: the imbalance between the overcapacity and oversupply of low-end, low-quality goods and the high-level, high-quality and diversified demands in China's real economy; the unproportionally high percentage of the monetary sector in the economy, which shadowed the shrinking manufacturing sector and posed high financial risks; and the overheated real estate sector attracting unproportionally large capital and increasing the cost of the real economy.

China's economists explained the need for and advantages of supply-side structural reform. Basically, they argued that there are problems in both the demand and supply sides in China's economy, but the major issue was that the supply did not match with the changed demands. Key problems in the demand side were usually rooted on the side of supply, and supply-side structural reform cannot only solve the structural problems in the supply side but also address issues in the demand side. Many aspects of goods demand in consumption, export and investment in China could not be met as they could not be matched well by the massive quantity of products provided by the supply side, and a lot of services for which there was demand were not supplied (Ma 2016; Jia 2015; Xu 2016). For example, the steel sector in China has accumulated serious problems of overcapacity since the beginning of the twenty-first century, but the demand for high-value-added steel products such as high-end tool steel and special steel could not be met and still relied heavily on imports. Steel overcapacity exists mainly in low-value-added crude steel.

Beyond that, supply-side structural reform is expected to bring attention to the institutional issues that have helped create the problems existing in the demand side in the first place,

including the mismatched supply of labour forces, non-competitive financial market and long overdue restructuring in the manufacturing and services industries. In short, economic structural problems could not be solved simply by stimulating the domestic demand, and they need to be addressed by improving the structure on the supply side and creating new effective demands.

Supply-side structural reform is a revision of China's long-standing growth model driven by export and investment, which has created and exacerbated many problems associated with overcapacity. It requires profound restructuring in manufacturing, financial services, the labour market and so on. Initially, supply-side structural reform mainly targeted the overcapacity in many sectors, such as coal, steel, cement and others, in which they produced more industrial products than the market demands. In particular, supply-side structural reform focused on dealing with the so-called zombie enterprises. The main way to meet the goal was to shut down or scale down these enterprises and control the credit and subsidies that feed them.

Officially, the five major tasks of supply-side structural reform are: addressing overcapacity, reducing inventory, deleveraging, lowering costs and bolstering areas of weakness. Supply-side structural reform started with production reduction, with the emphasis on cutting overcapacity effectively, optimizing and restructuring industries, cutting costs for enterprises, accelerating the development of emerging strategic industries and modern service industries, and providing more public goods and services, to improve the adaptability and flexibility of the supply-side structure to the changes in the demand side (Xi 2016). In order to realize the goals of supply-side restructuring, Xi also reinforced the need to enhance and expand the effective supply and reduce ineffective supply, while improving total factor productivity (Xinhua 2016a).

Centred on these five major tasks, five policy pillars were introduced to sustain the general idea of supply-side reform, including macro-level policy to maintain economic stability, industrial policy to target specific sectors, micro-level policy to inject dynamism into the economy, reform policy to deliver specific results, and social policy to meet basic living needs. Xi tried to connect his new idea of supply-side structural reform with the concepts declared in the party's other authoritative documents. Most importantly, he furnished

supply-side structural reform with the principle of promoting innovative, coordinated, green, open and shared development, which was first proposed at the CPC Central Committee Suggestions for the 13th Five-Year Plan for Economic and Social Development in November 2015 (Xinhua 2015d).

## How and Why It Started

The idea of supply-side structural reform can be traced back to 2013, when the party central made an assessment of the entire economic situation and concluded that the Chinese economy had entered a critical period in which it was necessary to simultaneously deal with a slowdown in economic growth, make difficult structural adjustments and absorb the effects of previous economic stimulus policies. In the year that followed, this judgment was further explained as the so-called new normal of economic development, the term President Xi used to describe China's economy in 2014. Under the conditions of the new normal, Xi outlined three characteristics of the economy in detail in his speech at the Asia Pacific Economic Cooperation CEO summit in 2014: the growth rate was shifting gear to medium-to-high speed from the previous high speed, the economic structure was optimizing and upgrading, and the engines of growth were diverting from investment and being factor-driven to being innovation-driven (Xi 2014).

Facing these three major problems under the new normal, Xi picked up the most fundamental one in 2015, economic restructuring, and renamed it supply-side structural reform to try to adapt and lead the economic development in a sustainable way. This is a reasonable development after Xi defined that China was entering the new-normal economic stage. With the all-embracing reform measures introduced by the Third Plenary of the 18th Congress in 2013 going nowhere, President Xi was determined to proceed with the difficult but indispensable economic restructuring to transform China's economy. In November 2015, Xi raised the idea of supply-side structural reform for the first time at the CLGFEA meeting, focusing on improving the quality and efficiency of the supply system to reinforce the driving forces for economic growth (Xinhua 2015e). One month later, in December 2015, Xi finished the comprehensive elaboration for the idea of supply-side structural reform at the CEWC, detailing the framework of top-level design, policy measures, principles and the key tasks for the ambitious restructure reform.

Supply-side structural reform refers to fundamental changes to the existing economic structure that are required in order for China's economy to transform and upgrade. It was described as a significant innovation to deal with the new normal and an active choice for China to compete with other economic powers in the post global financial crisis era, during which major economies realized the necessity of pushing for restructuring to maintain sustainable economic growth. China, with its 4-trillion-RMB (US\$586 billion) stimulus package that has intensified the long-standing problems in the economic structure over the years since the global financial crisis, witnessed the evolution and aggravation of issues such as overcapacity in steel, coal and many other sectors. Another casualty of China's huge stimulus package in 2008 is the rapidly surging real estate bubble since then. Bolstered by high leverage in the financial market, soaring house prices led to a large accumulation of excessive stocks in the real estate market over just seven to eight years.

## How Has It Performed?

After one year of efforts in supply-side structural reform, progress was made in addressing excess capacity in the steel and coal industries, although the other tasks of reducing the stockpile in real estate and other sectors, deleveraging and lowering costs for enterprises did not produce much in the way of positive results. That being said, problems that arose in the process of cutting overcapacity underlined the complexity of the issue and the indispensability of the government's role. Cutting overcapacity turned out to be an extremely tough job, in particular when it came to the SOEs, which have most of the overcapacity in these sectors. The governments at all levels had to use administrative powers to do the job in practice, although top leaders have repeatedly said that market-based measures should be the choice for overcapacity reduction. The reason behind it is simple. Market-oriented measures mean market selection for capacity reduction, and the process of market selection takes time. It would take years to see the results, but top decision makers wanted to see the policy results for each year. The toughest issue is how to handle the workers that are laid off as a result of capacity reduction. SOEs involved in the process argued that a larger number of unemployed workers caused by cutting overcapacity would lead to social unrest, and they could not help resettle these workers properly without government aid.

The advancement of supply-side structural reform, in particular cutting overcapacity in steel, coal and other sectors, fully demonstrated the deep involvement of the Chinese government in China's economy, which, conversely, explained why the central and local governments had, inevitably, intervened deeply in the process of capacity reduction. Market-based measures are simply not a practical option for cutting overcapacity under the circumstances of China's heavy government intervention in managing the economy. Largely relying on the administrative orders to cut overcapacity of both SOEs and private enterprises and provide subsidies to resettle the laid-off workers, cutting overcapacity could not have been done without the government's deep involvement. In practice, each province was assigned a quota of overcapacity-cutting in the steel sector, and the tasks of each province are further assigned downward to each municipality and county.

Under these circumstances, it is not surprising that the goal of reducing overcapacity in the steel sector in 2016 was reached. Three factors contributed to the result. First, nationwide, 70 percent of capacity that was cut was in the so-called ineffective capacity or zombie capacity that was already idle before the reform began. In other words, most of the steel capacity being removed was idle capacity. Second, most capacity cutting happened in private steel companies, with a high percentage of effective capacity being cut. In other words, SOE steel companies only contributed a small part of the capacity reduction, and more than 80 percent of the reduction was ineffective capacity. Capacity cutting in private steel companies accounted for about 70 percent of total capacity, with 61.4 percent in iron manufacturing and 76.3 percent in steel production; 54.8 percent of the effective capacity of iron production and 31.5 percent of steel manufacturing in private companies were cut (Greenpeace and custeel.com 2017, 33). In Hebei Province, the top region in China's steel production, capacity cutting by private steel companies accounted for 97 percent of total capacity reduction (Phoenix International Think-Tank 2016). Third, the great number of government subsidies to resettle the laid-off workers played a key role in guaranteeing the delivery of the goals. The State Council appropriated a "pork barrel" fund of 100 billion RMB to subsidize the steel capacity reduction in February 2016. In total, 38.4 billion RMB of the fund was used in 2016 (Greenpeace and custeel.com 2017, 43). Generally,

each laid-off employee could receive about 30,000 RMB from the fund (Phoenix Finance 2017).

Following the same model, the goals of capacity reduction set out in the 13th Five-Year Plan were achieved by 2018, two years ahead of the deadline given in the plan. One hundred and fifty million tons of capacity in crude steel production was cut, 810 million tons of coal production capacity was removed, and 20 million kilowatt capacity in coal-fuelled plants was eliminated (NDRC 2019).

In summary, supply-side structural reform achieved some positive results by cutting low-end and ineffective supplies and improved the industrial structure in steel, coal and other sectors with serious overcapacity. Industrial enterprises, in particular the middle and large ones, improved their profit margin notably. These achievements, however, came with a remarkable cost and had quite negative impacts on China's economy. Relying heavily on administrative orders, such as restrictions on working days and setting limits on capacity for a steel factory, the efforts for overcapacity cutting twisted market supply and demand and further distorted the price and profit distribution among middle and upstream and downstream enterprises. Most SOEs are middle and upstream enterprises that enjoy monopoly status in steel, coal and other sectors with overcapacity. They basically improved their profit notably and benefited a lot from supply-side structural reform because of capacity reduction driven mainly by the administrative orders while private enterprises suffered and were squeezed out of the market in many sectors.

The policy of inventory reduction in the real estate sector unexpectedly caused housing prices to soar in 2016 and greatly intensified the existing asset bubble. The policy, matched with other measures taken by the central government to stimulate house sales and reduce house inventory in small cities, led to a frenzy of house purchases in the first-tier cities and drove up the overall price of houses while failing to solve the overstock in the housing market in small cities. The financial deleveraging policy was introduced with unprecedented strict supervision policies and led to a sharp liquidity shrinking and interest rate rise in financial markets. A great number of companies defaulted and, to a large degree, the peer-to-peer lending market collapsed.

Facing the mixed picture of limited successes and the highly negative impacts it brought to

China's economy, the main attention of supply-side structural reform turned to its fifth task, bolstering areas of weakness. Starting from 2017, supply-side structural reform expanded into almost the entire scope of industries (Naughton 2018) and incorporated many areas of advanced manufacturing, such as robotics, semiconductors, next generation information technology, aviation and new materials. Many of these have been proposed in China's aggressive blueprint for the development of advanced industries, Made in China 2025. President Xi's speech at the 38th Study Session of Politburo on January 22, 2017, provided a clue for this transition. Xi explained further at the study session that, to bolster areas of weakness, China needs to rely on technological innovation and industrial upgrade and improve its economic competitiveness (Xinhua 2017c). Of course, the areas of weakness also include targeted poverty alleviation and building ecological civilization and modern infrastructures, but without a doubt, supply-side structural reform expanded into China's new industrial revolution and focused more on technological innovation, advanced manufacturing and industrial upgrades, and moving up the global value chain. President Xi's report at the 19th CPC National Congress in November 2017 endorsed and confirmed this shift of focus (Xinhua 2017d).

In short, supply-side structural reform has expanded from its original intent of cutting overcapacity, deleveraging and reducing costs for enterprises into an industrial upgrade moving up the global value chain featuring innovation and cutting-edge technologies in advanced manufacturing.

## Supply-side Structural Reform Epitomizes Xi's New Model of Economic Policy Making

Supply-side structural reform constitutes Xi's major economic and reform proposal to confront the most difficult and most important issue, economic restructuring to guarantee sustainable economic growth and the accompanying social and political development. It fully demonstrates two of the characteristics of economic policy making under President Xi.

First, it left deep footprints of Xi's philosophy in policy making, i.e., the top-level design for the overall strategy for economic development and reform. Supply-side structural reform is a result

of Xi's top-level design and the top-down style of policy making in key economic reforms.

Supply-side structural reform was raised to address the long overdue economic restructuring, attempt to cut the overcapacity in the steel, coal, chemical and real estate sector and upgrade China's industries with innovation in the advanced manufacturing and high-tech fields. It shows the consensus Chinese elite and leaders reached that the reform had entered "uncharted waters" and that the reform needed to be designed instead of being initiated from the grassroots level or pushed spontaneously by market forces. Although Xi advocated "allowing the market to play a decisive role in allocating resources," his statement included another part, "improving the government's role" in the decision passed at the Third Plenary Session of the 18th CPC Central Congress (Xinhua 2013).

Governments can play an important role in economic restructuring. Under the conditions of China's current political economy structure, it is also a necessity for the government to take the initiative to push for supply-side structural reform because there is not a fully competitive market in China and economic restructuring would not happen automatically. There are a variety of problems that exist in China's economic development, such as strong regional and trade protection, an underdeveloped market economy with strong government intervention and SOE monopoly. These problems prevent the market from playing its role in the allocation of resources. The chaotic, underdeveloped and segmented market is unable to run itself smoothly. Intervention from the government is necessary in China's economic restructuring.

Supply-side structural reform has been designed based on a quite high consensus that economic restructuring, focusing on cutting overcapacity in many manufacturing sectors, is essential. The official narrative emphasized that the government should withdraw from its strong intervention in the supply-side structural reform once the "invisible hand" was capable of running itself smoothly and functioning well. However, the government continued to be involved in the whole process of resource allocation and intervened in the micro-level economic development. In practice, too many administrative measures and orders have been used for cutting overcapacity in steel, coal and other industries.

In short, supply-side structural reform demonstrates more government intervention in economic activities, which is identical to the nature of Xi's top-level design in the policy-making process.

Second, the central leading groups (the CLGFEA and the CLGCDR) take charge of economic policy making. They designed and introduced supply-side structural reform as Xi's signature measure to restructure the economy. The CLGFEA has initiated almost every significant economic policy since Xi Jinping was announced publicly for the first time as the director of the CLGFEA in an elaborately planned media pronouncement on June 13, 2014. The CLGFEA, as the key decision-making body, discussed and made key decisions on national energy strategy, innovation-driven growth, the Belt and Road Initiative (BRI), the creation of the Asian Investment Infrastructure Bank and the Silk Road Fund, the RMB joining the Special Drawing Right currency basket, poverty alleviation and the healthy development of the stock market, and so on (Chen et al. 2018).

As the top priority of Xi's measures for economic restructuring and deepening reform, supply-side structural reform was first initiated at the eleventh CLGFEA meeting on November 10, 2015. The idea of supply-side structural reform set the tone for the CEWC that was convened during December 18–21, 2015. The fact that the CLGFEA generated the original idea of and made the decision on introducing supply-side structural reform illustrated that the group had openly stepped onto the front stage on drafting major economic decisions. Following the main task of supply-side structural reform, the CLGFEA continued to focus on refining the guiding principles, designing the road map and setting priority areas for the reform at the twelfth and thirteenth meetings on January 26, 2016, and May 16, 2016, respectively. More specific measures for further promoting supply-side structural reform were worked out at the fifteenth meeting on February 28, 2017, aiming to solve some particular issues, including how to tackle the zombie enterprises, preventing and controlling financial risks and establishing a permanent mechanism to promote a healthy housing market (Xinhua 2017e).

In addition, Xi tried to use the authority and institutional resources at the CLGCDR to help promote supply-side structural reform. At the twenty-third meeting of the CLGCDR that was held on April 18, 2016, four months after the idea

of supply-side structural reform was formally introduced at the CLGFEA and the CEWC, Xi tried to connect supply-side structural reform with institutional reforms in other sectors under the umbrella of the CLGCDR. Specifically, Xi asked at the CLGCDR meeting to accelerate the institutional reforms in the SOE, finance and monetary sectors and deepen opening-up so as to lay a solid foundation for supply-side structural reform (Xinhua 2016b). Xi highlighted supply-side structural reform as the touchstone of the resolution for reform and called for all the ministries and local governments to combine the promotion of supply-side structural reform with implementing the measures on the agenda for comprehensively deepening reform at the twenty-fourth meeting of the CLGCDR on May 20, 2016 (Xinhua 2016c).

In short, the CLGFEA and the CLGCDR, the party's two leading groups with a dominant role in promoting supply-side structural reform, fully demonstrated the idea of Xi's top-level design in the reform. Xi pushed further in this regard. Supply-side structural reform was added to the party's constitution at its 19th National Congress in October 2017, constituting a component of Xi and the party's leadership over everything. This move unprecedentedly demonstrated Xi's idea of the party's absolute leadership over significant economic policies and reform measures.

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## Conclusion: Impacts of Xi's Top-level Design on China's Economic Policy Making

In a nutshell, Xi's style of leadership is a modern version of Mao's rule in the era of the digital economy, featuring the Xi-dominated party central's absolute control over policy making in every sector and field in China. It is a total counter-reaction of the political reform toward a more open, pluralized, democratic and collective decision-making process since Deng Xiaoping in the 1980s. Compared with Xi, it is fair to say that in the eras of Jiang and Hu, political reform stalled and the democratization

of the policy-making process achieved only very limited progress. However, Jiang and Hu's ways of governing China never went back to a Mao style of one-man control. Under Xi's leadership, the political reform and democratization of the policy-making process quickly reversed to the level in Mao's era.

Xi built up the roles played by the central leading groups and established new ones, and he headed most of them as a measure to cement control of policy making in almost every sector at the central level. He strengthened the party's control over the government at every level and in every sector. Contrary to the separation between the party and the government, he proposed merging party and government in the same area or sharing offices between those party and government agencies that have similar duties. He also shored up the party's tight control over the press, congress, the military, rank and file government officials and the SOEs by reiterating the party's leadership over everything and relying on the party chief in every government department, party organizations and government-affiliated social groups, and SOEs.

This modern version of one-man control over the political process under President Xi in the digital age has had, and will continue to have, far-reaching impacts on China's economic policy-making process.

First, Xi, with his unprecedented power and authority and the new approach of top-level design, is determined to start the long overdue structural reform in China's economy, which is a positive thing. As history has shown, tough reform needs a tough leader to advance it. The great difficulties and predictable economic slowdown and subsequent negative political repercussions facing the economic restructuring kept the top leaders from pushing the real economic structural reform during the Hu-Wen era, prior to Xi coming to power. China's economic transformation toward being driven more by consumption, innovation and technology and less driven by export and investment was talked about and prioritized for years during the Hu-Wen era, but no substantial policies and actions have been taken since then.

Xi's determination to push forward the real economic structural reform is probably derived, in part, from his understanding that China's economic slowdown was unstoppable, as well as his realization of the exigency for immediate and essential structural reform, judging by his major policy statement on the definition of the

new-normal stage in China's economy. To promote economic restructuring, it is necessary to grasp the power in economic policy making and the effective means and ways for policy implementation as the Chinese premier normally holds the authority in economic policy making and China's bureaucratic system has a reputation of weak capacity for policy execution. What Xi did to seize the authority in economic policy making reflected the logic and philosophy of top-level design, which says that, as a holistic reform, the top policy makers' grip on comprehensive power over every sector of the Chinese political economy is absolutely necessary. Certainly, Xi's determination and measures he took for the economic structural reform could also be explained as a means to concentrate power in his hands, in particular, he must grasp the most crucial power in economic reform and growth. In any case, it is safe to say that Xi has concentrated unprecedented power in economic policy making and took substantial measures to promote the long-standing, thorny structural reform.

Second, policy making has followed a top-down approach under the theoretical framework of top-level design, and the trial-and-error method that is based on the bottom-up, incremental approach and appreciates the wisdom and practice gained from the grassroots level in the policy-making process has been less and less applied. The top-level design, a more top-down policy-making approach, increased the chances of introducing unwise or impractical policy making. Xi's major economic policies, such as supply-side structural reform, preventing systemic financial risks and the BRI, were based on the judgment on the situation and wisdom by his close allies of senior leaders and his small circle of close senior advisers. Certainly, Xi's policy making was usually based on many rounds of field investigations and broad consultations and recommendations from both within and outside of the government and party systems, as shown in the decision-making model developed in China over the past decades. It is hard to say, however, if the decision can truly be based on an understanding of the real situation. The fact that, in practice, measures to promote supply-side structural reform and prevent systemic risks caused many new problems in the economy demonstrated that the theoretical design of economic policy needed to be constantly complemented by the ongoing grassroots-level practice in managing the economy.

Third, using institutional power and unprecedented emphasis on the party's discipline and party loyalty, Xi put great efforts into the control of both policy making and policy implementation and achieved a mixed result. He headed as many as nine leading groups, indicating his ambition to advance direct control of policy making through his leadership in existing leading groups and newly established ones. Xi used central leading groups as his tool for policy-making control and appointed the officials and personnel he trusts in key government positions. By doing so, he can have confidence in making his vision and plans. Xi's deep worry is how to implement his grand plan to rejuvenate the nation, given policy enforcement has been the lingering, obstinate problem facing China's government system. Comprehensively strengthening the party's self-discipline, or emphasizing the "purity" of the party, is his last resort to guarantee policy implementation. Relying on the "crucial minority," the key officials in key government and party positions, indicated his thinking and solutions to strictly push and supervise the policy implementation at all levels, from the highest and middle levels to the grassroots level.

It turned out that Xi's control of policy implementation concerning reform measures made some progress through the CLGCDR system at all levels, which formed a new vertical system that supervises and inspects policy enforcement from time to time at all local levels, including provincial and county levels. When it comes to the complicated economic and financial issues, however, the rigid and one-size-fits-all approach caused many problems. Deleveraging under the major policy of preventing systemic financial risks compounded the difficult problems of financing facing private enterprises, in particular the mid-sized to small companies, and contributed to the slowdown of the economy since 2017. Structural reform in many sectors, such as steel and coal, played a part in the mounting pressure of economic downturn. Cutting inventory policy that was targeted to bring down the home prices in small cities unexpectedly triggered soaring prices in the housing market in major cities in 2016. Cutting overcapacity in the steel and coal sectors as one of the major policies concerning supply-side structural reform relied mainly on administrative power to enforce, and achieved noticeable success at the expense of the private companies in these sectors.

Fourth, under President Xi's ruling, the party's deeper involvement in economic policy making and economic management intensified China's model of government intervention in the economy and further complicated the relations between the state-owned sector and the private sector. Mixed ownership reform in SOEs, with the goals of both making state-owned assets stronger, better and bigger, and encouraging private companies to participate in the SOEs as shareholders, further sent unclear messages about the party's viewpoint on the private sector in China.

Private enterprises in the steel and coal sectors undertook the cost of the supply-side structural reform and shouldered most of the capacity reduction in the two sectors. Large SOEs have squeezed out private businesses in many sectors since Xi came to power in late 2012, resuming the trend of "state march on, private retreats" of the early 2000s. This trend intensified and aroused wide media attention in 2018; Xi himself along with other top leaders had to clarify their support for the private sector.

It is safe to say that the ending of the private sector in the Chinese economy represents the extreme left-wing voice and is not likely to happen any time soon in today's China. However, despite the assurance by the top leaders and the constant introduction of policies from the government, in particular from the central bank, to support the development of the private sector, the party-state's gradual encroachment on private sector businesses is still quite noticeable.

Finally, Xi's style of highly concentrated power and absolute control over policy making has intensified existing old bureaucratic problems and brought a variety of new problems to China's political economy. His heavy-handed approach to ruling in the party-state under the idea of top-level design has created a highly intense mutually suspicious atmosphere among officials, which, ironically, led to many new forms of maladies of bureaucracy in China's politics, contrary to Xi's expectation. The atmosphere of mutual suspicion among officials created bureaucratic methods such as "slow-walking" orders or keeping information from superiors, in order to avoid performing their duties. The party's more direct involvement in the economy, in particular in the management of private companies, created a tense and suspicious sentiment among business

circles and beyond about China's future in further market-oriented reform and opening up.

China's initial reaction to the COVID-19 pandemic demonstrated that when facing a crisis, such as a public health crisis, the stability-obsessed ruling style and unprecedented pressure on state and local bureaucrats under President Xi's top-level design is unable to react in a timely and swift manner, with potentially catastrophic consequences. The existing notorious bureaucratic problems, including a tightly controlled flow of information, and local officials' inclination of not reporting and releasing bad news and dodging responsibilities by only taking actions following a superior's orders, have been amplified under President Xi's top-level governance style and eventually played a large part in the coronavirus outbreak in January 2020.

Looking to the future, Xi's style of an upgraded version of one-man control over major policy making on economic affairs and in other fields could be weakened if the ongoing economic downturn China is facing lasts and develops into a serious economic crisis. Otherwise, Xi's ruling in China has the potential to continue until his complete retirement.

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