FROM DENG TO DEMSETZ: SPECULATIONS ON THE IMPLICATIONS OF CHINESE GROWTH FOR PROPERTY THEORY

By
Frank K. Upham

No one needs to be told any more of China’s turn to market capitalism. China’s growth since 1978 when Deng Xiaoping instituted initial market reforms has been among the longest sustained periods of high growth in modern history. For those interested in the relationship between law and economic development, however, it is almost as if those thirty years of growth did not take place. Few would challenge the assertion that China has grown without an effective legal system, and yet relatively few scholars have addressed the implications of China’s economic success for the

---

"Acknowledgements: Eva Pins, Zhang Hong, Greenberg fund. Translations my own unless noted.


2 As Dam points out, pp 234-237, China is not always at the bottom of World Bank and other cross-national rankings of world legal systems, and at one point, he appears about to argue that the Chinese legal system may not be as bad as usually thought, but once he leaves the aggregate data and examines the Chinese legal system and particularly the judiciary and the enforcement of substantive rights more closely, he moves away from this view and appears to agree that Chinese growth has come without any effective legal system. See pp. 247-255. For reasons that I elaborate later in this article, I believe that excessive reliance on the quantitative methodology of cross-national studies of legal system effectiveness can explain a substantial amount of the mismatch between the performance of the Chinese economy and law and development theory."
theoretical bases of law and development. In much of the academic and popular literature on economic development the belief that the “rule of law” is a prerequisite to sustained growth remains remarkably strong. In 2004, for example, law and development scholar Kevin Davis was able to state without apparent fear of contradiction that “It is now widely accepted that markets are unlikely to function in the absence of bodies of contract law and systems of property rights.” He continued to assert that there exists a “consensus that the overall ‘quality’ of legal institutions is an important determinant of development” and that “the ‘rule of law’ is an essential pre-condition to development.” Davis, to be sure, immediately qualified this statement and went on to question the empirical basis for this “optimistic”

---


5 KED ROL Reforms, 142-143. Alvaro Santos phrased it similarly: “Law is at the center of development discourse and practice today. The idea that the legal system is crucial for economic growth now forms part of the conventional wisdom in development theory. This idea’s most common expression is the “rule of law”: a legal order consisting of predictable, enforceable and efficient rules required for a market economy to flourish.” Santos at 253. Kenneth Dam, despite an extensive discussion of the Chinese case, ended his 2006 book canvassing the relationship between law and development with “It is certainly too early to accept the notion that recent Chinese experience is a counterexample to the need for a focus on institutions in the developing world.” Dam at 277. Dam does recognize that the Chinese experience may indicate that some growth is possible without developed legal institutions. Ibid.
assumption, but that he was able to make such a statement after almost three decades of economic boom in a country without a well functioning legal system is deeply puzzling.

This article takes the opportunity presented by the passage of China’s Property Law in spring 2007 to address one aspect of this puzzle, the role of property rights in economic growth. I begin in Part I with a brief account of the controversies regarding the draft Property Law, including not only the unexpected opposition to the law itself but also the attention drawn to the law by a media-savvy couple who justified their refusal to vacate their house to make way for urban re-development in terms of private property rights. Both events demonstrate the symbolic importance and political meaning of property rights in contemporary China although from decidedly different ideological perspectives. Part II reviews the literature on the economic role of property law with an emphasis on the argument that development requires clearly defined and legally enforceable property rights. I begin with the conventional wisdom on the relationship between property rights and economic growth as exemplified by the World Bank’s technical assistance programs. I next place these beliefs in the theoretical context of neo-institutional economics created by scholars from Ronald Coase and Harold Demsetz to Douglass North. I close Part II with an examination of the
reaction to China’s growth in development theory and practice, again emphasizing World Bank literature and programs. Part III attempts to explain how China has grown without a robust rule of law, beginning with a brief description of the weaknesses in Chinese legal institutions and then describing the role of law in two different areas of the economy. I do not intend these descriptions to provide a full account of how Chinese markets have functioned, but they provide a flavor of the institutions that Chinese have relied on to provide economic stability in lieu of the rule of law. Part IV concludes with an attempt to explain why the Chinese experience has had so little impact on how we think about the interaction of markets and law.

Before proceeding, however, it is important to define the parameters of my claim that property rights are not necessary to economic growth. First, I define property rights as legal entitlements enforceable by courts. I recognize that economic actors require security in their investments and predictability in their exchanges, but I disagree with the current belief that formal legal institutions are necessary to provide these conditions in developing countries. Second, I do not deny that property rights are desirable and important. As we shall see, there is a strong demand for judicially enforceable property rights in contemporary China. China needs to improve social order by clarifying the relationships among people with
regard to valuable assets and to address increasing social injustice by giving average citizens – what the Chinese invariably refer to as “the old hundred names [老百姓]” – a politically legitimate means to resist an over-reaching state and its business allies. In other words, property rights are desirable and important for political reasons, not economic ones. Third, I use the terms “economic growth” and “economic development” advisedly to mean an increase in GDP/capita, what was the original metric for development before Amartya Sen and others broadened the concept to include freedom, human capabilities, and other non-economic aspects of social welfare. I do not deny that effective property rights over the past three decades might have allowed China to achieve higher levels of development in this wider sense. I do not believe, however, that they would have led to faster economic growth. Indeed, as I have argued elsewhere, strong property rights can often hinder growth, and strong protection of property rights for farmers and urban residents would likely have slowed China’s economic growth in the sense of GNP/capita. Nor do I see persuasive evidence that they are necessary at this time for growth to continue except in the attenuated sense that they may be necessary to avoid social conflict that might eventually affect growth itself.

\* Mythmaking