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## Abstract

### Governance in China

by

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The performance of Chinese governance is widely rated as poor. Nevertheless, some authors evaluate the recent reforms as providing a chance to improve the governance within China. Although quantitative attempts to measure governance performance have been made, the results need more interpretation. To evaluate the performance of Chinese governance, this thesis begins with a review of different theoretical concepts of governance. The literature on the performance of the governance within China and quantitative approaches attests to China's moderately good performance in relation to effectiveness but sees a major problem in what we could define as 'good governance.' The interpretations of some particular reforms provide no clear answer as to whether they constitute a step towards improving the system or if the problem will worsen. Consequently, this thesis includes a case study on the galloping growth of coal-fired power plants within China which offers a different perspective and demonstrates that China's central government is incapable of implementing its energy policy at the local level. Illegal power plants and the disregard for environmental rules are an evident sign of a failure of governance. But I argue that China's governance problems and failures do not matter in the short term. It is the price that China has to pay for the central government's determination to achieve fast economic growth, and it is a bill that will to be paid in the future.

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## List of abbreviations

ADB	Asian Development Bank
Bcm	Billion cubic meter (1 E+9 m <sup>3</sup> )
CC	Control of Corruption
CCP	Communist Party of China
CGM	Central Government Owned Mines
CO <sub>2</sub>	Carbon dioxide
EPB	Environmental Protection Bureau
GDP	Gross Domestic Product
GE	Government Effectiveness
GW	Gigawatt
GWh	Gigawatt-hour
IEA	International Energy Agency
IGO	Intergovernmental Organization
IMF	International Monetary Fund
LGM	Local Government Owned Mines
LNG	Liquefied Natural Gas
MPC	Municipal People's Congress
MPPCC	Municipal People's Political Consultative Conference
Mt	Million tons
MW	Megawatt
NDRC	National Development and Reform Commission
NGO	Non-governmental organization
NO <sub>2</sub>	Nitrogen dioxide
OECD	Organisation for Economic Co-operation and Development
PM10	Particulate matter (PM) ≤10 μm
PRC	People's Republic of China
PV	Political Stability and Absence of Violence
RL	Rule of Law
RMB	Renminbi
RQ	Regulatory Quality
SARS	Severe acute respiratory syndrome
SASAC	State-owned Assets Supervision and Administration Commission
SEPA	State Environmental Protection Agency (SEPA)
SGI	Sustainable Governance Indicators
SO <sub>2</sub>	Sulfur dioxide
SOE	State Owned enterprise
TNC	Trans National Companies
TWh	Terawatt-hour
UN	United Nations
UNDP	United Nations Development Program
VA	Voice and Accountability
VTPM	Village, Town and Private-Owned Mines
WBI	World Bank Institute
WGI	Worldwide Governance Indicators
WHO	World Health Organization

## 1. Introduction

Views of China are segmented into many different groups. For one group, China is the authoritarian communist country that violates human rights, destroys the environment and supports internationally outlawed regimes. The recent riots in Tibet are seen as evidence that China is a “ticking time bomb.” The international protests during the Olympic torch relay in 2008 underscore their views that the Chinese government’s human rights record is far from where it should be. They closely correlate the two terms ‘China’ and ‘crisis.’ On the other hand, business people and certain political leaders see within China the promise of a bright future and a model of effective economic reforms. They see enormous opportunities in doing business in China, with the emergence of a huge consumer market. The seemingly everlasting annual 10% rise in GDP makes them confident that China is on the right path.

The same debate exists in the academic world. One group considers China’s recent achievements as very promising. They interpret the reform outcome as positive and see China as being on the right road, while the other group draws the contrary conclusion. The studies by Dali Yang<sup>1</sup> and Minxin Pei<sup>2</sup> are a case in point. Even though both authors have written about the same topic and in parts have used the same primary sources, they have reached mutually contradictory conclusions. For instance, Yang<sup>3</sup> praises the introduction of job-rotations among cadres in the center’s nomenclature and county magistrates as positive. He suggests that their working performance was enhanced and the likelihood for bribery and corruption, lowered. Yang underlines the end-of-term audits for such officials which “have become a crucial link in the enhancement of the cadre disciplinary regime.”<sup>4</sup> The same institutional reform can be seen from a completely different perspective. Pei describes the rotations of cadres as new exit options that dramatically reduce the time horizon for responsibilities. Self-interest and rent seeking became more salient. Pei’s radically

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<sup>1</sup> Dali L. Yang, *Remaking the Chinese Leviathan: Market Transition and the Politics of Governance in China* (Stanford: Stanford University Press, 2004), 181.

<sup>2</sup> Minxin Pei, *China's trapped transition the limits of developmental autocracy* (Cambridge, Mass.: Harvard University Press, 2006), 153.

<sup>3</sup> Yang, "Remaking the Chinese Leviathan: Market Transition and the Politics of Governance in China", 181.

<sup>4</sup> *Ibid.*, 182.



different view leads him to conclude that “the unintended effect of this institutional practice is to turn these officials, literally, into roving bandits.”<sup>5</sup> The problem of different interpretations can even be found within the statistics used. Pei sees the problem of overstaffing as a risk to a steadily growing Chinese state carrying an immense cost and constituting the root cause for China becoming a predatory state. Pei stresses that the problem became worse during the 1990s. In particular, district and township governments significantly raised their staff levels above those officially authorized. Underreporting and the lack of a standard classification of employees made matters even worse in Pei’s opinion. He compares the growth rate of state employees between 1953 and 1978, 1.8%, and between 1979 and 1990, 6.7%, and concludes that the official figures for 2002 suggest a doubling of employees compared with 1978.<sup>6</sup> The same statistics can be read and interpreted very differently. According to Yang,<sup>7</sup> the Chinese state at the local level was recently massively downsized. The plan, at the time of writing his book, to reduce 20% of its staff would first affect the unauthorized employees and act as an effective tool to make a slimmer state.

This was a relevant discussion. Very different aspects of China’s political, social and economic life are affected by this debate. Will corruption take over and become a major threat? Will the growing social inequality lead to social unrest? How will this affect the authoritarian one-party-state and the political stability in China?

It is an unresolved discussion; scholars are divided on this topic. There is no common theory or consensus about key questions. Will market forces reform the political system? Will the Communist Party survive? Or will the environmental problems become a major issue affecting China’s stability?

It is far-reaching discussion; China’s relations with other countries will be affected more and more. The world economy has much greater dependence on China and the expression ‘China threat’ has become a popular issue. The salience of these questions makes them, in my view, worthy of focus. In this thesis, a theoretical approach is

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<sup>5</sup> Pei, "China's trapped transition the limits of developmental autocracy", 153.

<sup>6</sup> Ibid., 136.

<sup>7</sup> Yang, "Remaking the Chinese Leviathan: Market Transition and the Politics of Governance in China", 47.

sought to contribute a different viewpoint to the discussion. To look at the practical aspect, a salient topic of governance will follow the theoretical part.

### 1.1. Research question and design

The thesis uses the governance approach to find an answer to the ongoing discussion on China's recent achievements. I suggest that under the angle of governance, the interpretation of the manifold problem areas is more meaningful than the use of one specific theory. Economic theories for instance help to interpret some particular effects in the economic development but obscure major changes in society and in politics.

If China's challenges are analyzed from a governance perspective, it should be possible to include various effects on China's rapid changes. The focus on governance within China will help to find an answer to the question 'where are we?' in the discussion mainly because the governance perspective is more suitable to give an inclusive picture of development.

In the first step, a literature review is undertaken focusing on the different concepts and definitions of governance. A second step will narrow the discussion on governance within China. I will begin with the debate on positive and negative outlooks on China's achievements in relation to reforming the state under a governance perspective. Furthermore, governance theories on measuring China's performance are applied to selected topics. The theoretical discussion will be followed by a case study discussing the governance of energy policies in China.

The final concluding chapter will provide answers to several questions:

- How can governance theories help in the interpretation of governance indicators?
- How can governance theories explain changes in China's performance in governance indexes?
- How can we explain China's governance problems?
- What are the limits of governance reforms?

Finally, are governance theories helpful in the debate as to whether China's future should be seen in a more positive or negative perspective?

## 2. Governance theories

This chapter presents a brief overview on different governance approaches. Although the term governance is widely used and most of us have a general idea of what governance means, the definitions and use of the term governance are manifold. Governance is used in different disciplines. For instance, in business administration the conception of corporate governance is used to explain the sets and arrangements that determine the leadership of a corporation and how accountability of the individuals who lead it can be ensured.

To discuss the different approaches of governance, the term governance itself is addressed first. Based on the general definition, references to specific fields follow. Good governance, corporate governance, public governance and global governance all have their roots in the general concept of governance.

### 2.1. Governance as theory

Governance plays a prominent and critically important role in international development strategies.<sup>8</sup> This can easily be seen in international agencies which are in charge of developing and implementing such strategies. For instance, the OECD, World Bank, IMF, Asian Development Bank and several UN agencies, all assign an important role to the idea of governance. The specific use and definition of governance in these institutions is discussed further in chapter 2.1.6.

Although governance is frequently used to describe current problems and challenges in terms of how governments can govern in order to guarantee the effectiveness of their actions, governance as theory embraces a broader concept. According to J.P.

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<sup>8</sup> Arthur A. Goldsmith, "Is Governance Reform a Catalyst for Development?," *Governance*, Vol. 20, (2007), 165.

Burns' definition, governance is confined neither to governments nor to the state.<sup>9</sup> Kahler and Lake<sup>10</sup> make the same point poignantly: "governance is not government." Governance used as theory correlates with other terms which "denote changes in the way public policies are managed."<sup>11</sup> In many ways governance, networks and partnerships express this general concept.

Governance used as theory involves virtually any duty of a government. According to Cheung and Schott,<sup>12</sup> governance is often used as a synonym for government: "the manner in which power is exercised in the management of a country's economic and social resources for development." Although governance and government are related, the discussion of governance as theory expands its focus. Governance theory "implies thinking about government, its role and mode of functioning in relation to non-government actors."<sup>13</sup> Burns dissected and described it in a general sense as "the manner in which power is exercised in the management of a country's economic and social resources for development."<sup>14</sup> Rhodes saw it as the changed rules and conditions "by which the society is governed;"<sup>15</sup> the state becomes less important.

In the following chapters, different governance theories are discussed, starting with the general concept of governance followed by more specific topics and hot spots where governance is applied (chapters 2.1.2– 2.1.5). These theories involve state-society, corporation-state and NGO-state relations, and much more. Chapter 2.1.6 presents a discussion of the governance concepts of international organizations. It is followed by a critique on the use of governance in chapter 2.1.7.

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<sup>9</sup> John P. Burns, "Governance and public sector reform in the People's Republic of China," *Governance and Public Sector Reform in Asia - Paradigm shifts or business as usual?* (eds.) Cheung and Schott, (New York: RoutledgeCurzon, 2003), 68.

<sup>10</sup> Miles Kahler and David A. Lake, "Globalization and Governance," *Governance in a global economy: political authority in transition* (eds.) Kahler and Lake, (Princeton, New Jersey: Princeton University Press, 2003), 8.

<sup>11</sup> Sonja Wälti, Daniel Kübler and Yannis Papadopoulos, "How Democratic Is "Governance"? Lessons from Swiss Drug Policy," *Governance*, Vol. 17, No. 1 (2004), 83.

<sup>12</sup> Anthony B. L. Cheung and Ian Schott, "Governance and public sector reforms in Asia: paradigms, paradoxes and dilemmas," *Governance and Public Sector Reform in Asia - Paradigm shifts or business as usual?* (eds.) Cheung and Schott, (New York: RoutledgeCurzon, 2003), 4.

<sup>13</sup> OECD, *China in the Global Economy: Governance in China* OECD, 2005), 39.

<sup>14</sup> Burns, "Governance and public sector reform in the People's Republic of China", 68.

<sup>15</sup> Rod A. W. Rhodes, "The New Governance: Governing without Government," *Political Studies*, Vol. 44, No. 4 (1996), 653.

### 2.1.1. Governance

The easiest way to begin to define governance is to look at what scholars agree that it is not. Most scholars agree that “under either conception [...] governance is not government.”<sup>16</sup> Howell made a second general remark about the nature of governance<sup>17</sup> that governance is, in principle, not different from other political science concepts.

A **first attempt** to define what governance is can be made with the distinction between a broad or narrow conception<sup>18</sup>; such conceptions are either to describe and explain a process between society and state or as a set of authority relationships.

Beside the scope of the theory, governance can also, **as a second attempt**, be classified on the basis of its activities. Keohane and Nye<sup>19</sup> suggest three levels and three actors which are involved in governance activities:

**Table 1: Activities of governance**<sup>20</sup>

	Private	Governmental	Third Sector
Supranational	TNCs	IGOs	NGOs
National	Firms	Central	Nonprofits
Subnational	Local	Local	Local

This classification proposes governance activities in the private sector, in the government and a third sector, society. Governance is not limited to the national state but also coexists on supranational and subnational levels.

<sup>16</sup> Kahler and Lake, "Globalization and Governance", 8, Oran R. Young, *Governance in World Affairs* (New York: Cornell University Press, 1999).

<sup>17</sup> Jude Howell, "Governance Matters: Key Challenges and Emerging Tendencies", *Governance in China* (ed.), Howell, (Oxford: Rowman & Littlefield, 2004a), 1.

<sup>18</sup> Kahler and Lake, "Globalization and Governance", 7.

<sup>19</sup> Robert. O. Keohane and Joseph S. Nye, "Introduction", *Governance in a Globalizing World* (eds.) Nye and Donahue, Brookings Institution Press, 2000), 13.

<sup>20</sup> *Ibid.*, 13.

A **third attempt** is to consider the usage of governance. Mayntz<sup>21</sup> writes that governance was originally related to political guidance or steering. The root of the modern theory of political governance (also known under the ‘Steuerungstheorie’) “emerged after World War II, at a time when governments aspired explicitly to steer their nations’ social and economic development.”<sup>22</sup> The first theories were based on a paradigm with policy development and implementation from a legislator’s or top-down perspective.<sup>23</sup> The paradigm shift reflects a continuous development of the first theories. However, the first theories could not explain a number of phenomena in the context of European policy developments. The theories went through five changes: the bottom-up perspective, including public/private networks, analyzing the effects of European policy, the European level of policy making and political input processes.<sup>24</sup> Besides this change, Mayntz observes another occasion where governance theories changed. Different actors believed that the emergence of new forms of self-government meant a loss of steering capacity: “The state appeared weak [and] ‘semi-sovereign’.”<sup>25</sup> But the results of empirical political science research suggested that it “is not so much a loss of state control as a change in its form.”<sup>26</sup> Recently, Mayntz has observed a paradigm change and the emergence of two new uses of governance since the late 1980s. Mayntz sees on the one side that governance is used to describe a new mode of governing. The new element was “the hierarchical control model, a more co-operative mode where state and non-state actors participate in mixed public/private networks.”<sup>27</sup> On the other side governance has, in her opinion, another new meaning from a different, and much more general, viewpoint. “Here governance means the different modes of coordinating individual action, or basic forms of social orders.”<sup>28</sup> Contandriopoulos et al.<sup>29</sup> have proposed a composite schema that integrates the new paradigm under three problematic facets:

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<sup>21</sup> Renate Mayntz, "New challenges to governance theory", *Governance as Social and Political Communication* (ed.), Bang, Manchester University Press, 2003), 27.

<sup>22</sup> *Ibid.*, 28.

<sup>23</sup> *Ibid.*, 29.

<sup>24</sup> *Ibid.*, 30.

<sup>25</sup> *Ibid.*, 32.

<sup>26</sup> *Ibid.*, 32.

<sup>27</sup> *Ibid.*, 27.

<sup>28</sup> *Ibid.*, 28.

<sup>29</sup> Damien Contandriopoulos, Jean-Louis Denis, Ann Langley and Annick Valette, "Governance Structures and Political Processes in a Public System: Lessons from Quebec," *Public Administration*, Vol. 82, No. 3 (2004), 628.

*(1) securing agreement on a program of action among a diversity of actors and organizations; (2) redistributing the capacity of actors and organizations to interpret decisions according to their own values; and (3) gaining acceptance among the collective that resultant actions are legitimate.*<sup>30</sup>

The shift away from the original top-down approach resulted in a more diversified conceptualization of governance. Policy outcomes were no longer the sole achievement of a central government. “The center may pass a law but subsequently it interacts with local government, health authorities, the voluntary sector, the private sector and, in turn, they interact with one another.”<sup>31</sup> This signifies a shift to a theory of policy development and implementation under a network angle. Most prominent, this idea resulted in the term ‘new governance’ which is defined as self-organizing networks.<sup>32</sup>

In a second step, the focus switches to concepts of governance which describe, in a broader sense, the functional position of governance. It includes some particular definitions, which several scholars have used as theory. As an example of a narrow definition, Kahler and Lake<sup>33</sup> mentioned: “Governance can [...] be understood more narrowly as that subset of restraints that rests on authority, where authority itself is a social relationship in which A (a person or occupant of an office) wills B to follow A and B voluntarily complies.” Narrow in its conception, governance defined in this way is not very useful for further use. It only refers to two actors where one of them obeys a decision of the other. Other scholars focused more on processes and the order of power distribution. Howell<sup>34</sup> defined governance as “the totality of processes and arrangements, both formal and informal, by which power and public authority are distributed and regulated.” This definition is more general and does not specify the direction of power. It studies places where governance is relevant, including: political institutions, the military, judiciary, and informal processes. “It embraces not only the study of states but also the arrangements and processes within political and civil

<sup>30</sup> Tim Freeman and Edward Peck, "Performing Governance: a Partnership Board Dramaturgy," *ibid.* Vol. 85, No. 4 (2007), 908.

<sup>31</sup> Rhodes, "The New Governance: Governing without Government," 657.

<sup>32</sup> Sonja Wälti and Daniel Kubler, "'New Governance' and Associative Pluralism: The Case of Drug Policy in Swiss Cities," *Policy Studies Journal*, Vol. 31, No. 4 (2003), 500.

<sup>33</sup> Kahler and Lake, "Globalization and Governance", 7.

<sup>34</sup> Howell, "Governance Matters: Key Challenges and Emerging Tendencies", 2.

society, the relations between these, and in turn their linkages with the state.”<sup>35</sup> A similar concept of governance follows Keohane and Nye,<sup>36</sup> who proposed governance as “the processes and institutions, both formal and informal, that guide and restrain the collective activities of a group.” The authors underline that besides government, several other players in distinct areas are involved, namely: private firms, associations of firms, nongovernmental organizations (NGOs), and associations of NGOs. International organizations act as organizations to which the governments delegate authority. Another possibility of how scholars see governance can be found in the discussion on European governance. In this context, governance is a political program with an intent “to introduce territorially unbounded public and private actors, acting outside of their formal jurisdiction, into political institutions’ decision-making processes.”<sup>37</sup> Governance is faced with several new methods of policy-making and implementation, such as non-binding decision-making, informal and unfixed networks of advice, lobbying, and new instruments to measure the processes, like benchmarking.<sup>38</sup>

A third step to approach the broad concept of governance concentrates on the fundamental questions of governance: “Who has the right to govern? Who has power and who has authority, and how are the two related<sup>39</sup>?” From this standpoint, governance focuses more on the decision-making process and its behavioral conventions.<sup>40</sup> Under this perspective, the idea of networks plays an important role. Networks are self-organizing and not limited to one organization but rather inter-organizational and a complementary.<sup>41</sup> Rosenau<sup>42</sup> made a distinction between government and governance, whereas governance’s authority is based on shared

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<sup>35</sup> Ibid., 2.

<sup>36</sup> Keohane and Nye, "Introduction", 12.

<sup>37</sup> David J. Bailey, "Governance or the crisis of governmentality? Applying critical state theory at the European level," *Journal of European Public Policy*, Vol. 13, No. 1 (2006), 22.

<sup>38</sup> Ibid., 23.

<sup>39</sup> Howell, "Governance Matters: Key Challenges and Emerging Tendencies", 8.

<sup>40</sup> Goldsmith, "Is Governance Reform a Catalyst for Development?," 165.

<sup>41</sup> Rhodes, "The New Governance: Governing without Government," 652.

<sup>42</sup> James N. Rosenau, "Governance, order, and change in world politics", *Governance Without Government: Order and Change in World Politics* (eds.) Rosenau and Czempiel, Cambridge University Press, 1992), 4, James N. Rosenau, "Approaches to Global Governance Theory", (eds.) Hewson and Sinclair, State University of New York Press, 1999).



goals.<sup>43</sup> This differs from government, which derives its legitimacy from formal authority. Four important differences can be discerned. Firstly, the state is no longer the lynchpin; rather, network systems between public, private and voluntary sectors have gained authority. Secondly, the new networks made it necessary to coordinate resources and communications. Thirdly, the rules shifted to game-like interactions which generated trust and regulations. And fourthly, the networks have a significant degree of autonomy from the state. However, the state is still able to steer the networks, albeit imperfectly and indirectly.<sup>44</sup> This point underlines an important characteristic of governance; governance is a (new) governing style, “in which boundaries between and within public and private sectors have become blurred.”<sup>45</sup> Within this concept, Czampiel<sup>46</sup> formulated his definition of governance distant from of the state-centered concept:

*[T]he capacity to get things done without the legal competence to command that they be done [...] From this point of view the international system is a system of governance.*

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<sup>43</sup> Rhodes, "The New Governance: Governing without Government," 657.

<sup>44</sup> Ibid., 660.

<sup>45</sup> Gerry Stoker, "Governance as theory: five propositions," *International Social Science Journal*, Vol. 50, No. 155 (1998), 17.

<sup>46</sup> Ernst-Otto Czempiel, "Governance and democratization", *Governance Without Government: Order and Change in World Politics* (eds.) Rosenau and Czempiel, Cambridge University Press, 1992), 250.

**Table 2: Government and governance as perspective in political science<sup>47</sup>**

	Government State vs. Market vs. Society	Governance State, Market and Networks as complex forms of steering
Polity	<ul style="list-style-type: none"> <li>• Focusing on the state</li> <li>• Democracy and hierarchy as most important institutions</li> </ul>	<ul style="list-style-type: none"> <li>• Institutional structure, which combines elements of hierarchy, negotiations systems, and mechanism of competitiveness</li> <li>• Networks</li> </ul>
Politics	<ul style="list-style-type: none"> <li>• Competition between parties for retaining power and between stakeholders for influence</li> <li>• Conflict settlement through decisions of state organs and enforcement of state decisions</li> </ul>	<ul style="list-style-type: none"> <li>• Conflict between governing and leading actors</li> <li>• Steering and coordination in a complex institutionalized system of rules</li> <li>• Negotiation between state and public actors</li> <li>• Adaption institutional systems of rules</li> </ul>
Policy	<ul style="list-style-type: none"> <li>• Legislation</li> <li>• Distribution public service</li> </ul>	<ul style="list-style-type: none"> <li>• Communication (in networks and communities), compromises, bartering</li> <li>• Coproduction collective goods</li> <li>• Network management</li> <li>• Politics of institutions (change management for institutions)</li> </ul>

Table 2 shows the analytical dimension of governance. In contrast to more common approaches state, market and society are not separated. The interactions are characterized by multi-dependency with an emphasis of rules in networks.

Governance is a concept used to understand and explain several problems. Depending on its definition, governance can be used to understand changes in a state's government.<sup>48</sup> Another example can be found in the fields of economics and political economics: decentralization, integration and federalism. With the factors of externalities, heterogeneity, and economies of scale scholars try "to determine the

<sup>47</sup> Arthur Benz, *Governance-Regieren in komplexen Regelsystemen: eine Einführung* VS Verlag für Sozialwissenschaften, 2004), 21.

<sup>48</sup> Rhodes, "The New Governance: Governing without Government," 666.

most efficient level of governance.”<sup>49</sup> In the end, a general definition of governance includes all of the abovementioned aspects. If we define governance “as the traditions and institutions that determine how authority is exercised in a particular country,”<sup>50</sup> most of the phenomena mentioned in this chapter will have been taken into account.

### 2.1.2. Good governance

Good governance signifies governance in a normative sense. That means that “the juxtaposition of ‘good’ augments the essentially evaluative nature of the concept.”<sup>51</sup> Good governance has become popular in several international institutions as a key tool to evaluate governments. Most notably, international financial institutions such as the IMF and the World Bank have applied good governance to evaluate institutionalizing processes in terms of effectiveness, efficiency, transparency and accountability of governments.<sup>52</sup> Financial institutions and Western governments were the first to link development assistance to governance issues.<sup>53</sup> With the idea of good governance, the international organizations aim to create processes and mechanisms for enhancing government quality. Good governance acts as a legal framework for development. Better accountability, transparency and decentralization are the key elements of this process. Some Western governments “interpret the term more broadly to embrace also the processes of democratization, respect for human rights, and socioeconomic equity.”<sup>54</sup>

In the normative aspect of good governance, ‘good’ refers to some rules that are considered necessary for sustainable development,<sup>55</sup> meaning that good governance

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<sup>49</sup> Lisa L. Martin, "The Leverage of Economic Theories - Explaining Governance in an Internationalized Industry", *Governance in a global economy: political authority in transition* (eds.) Kahler and Lake, (Princeton, New Jersey: Princeton University Press, 2003), 35.

<sup>50</sup> Cheung and Schott, "Governance and public sector reforms in Asia: paradigms, paradoxes and dilemmas", 4.

<sup>51</sup> Howell, "Governance Matters: Key Challenges and Emerging Tendencies", 1.

<sup>52</sup> Ibid.

<sup>53</sup> Howell, "Getting to the Roots: Governance Pathologies and Future Prospects", 233.

<sup>54</sup> Howell, "Governance Matters: Key Challenges and Emerging Tendencies", 1.

<sup>55</sup> Daniel Kaufmann and Aart Kraay, "Governance Indicators: Where Are We, Where Should We Be Going?," *International Bank for Reconstruction and Development*, (2007).

should be established.<sup>56</sup> The OECD<sup>57</sup> has defined six criteria of good governance: rule of law, accountability, transparency, efficiency and effectiveness, responsiveness, and forward-vision.

The idea that good governance leads to development and economic growth is widespread not only among scholars but also in development agencies. The “possibility that open and inclusionary institutions take more human and financial capital to run successfully<sup>58</sup>” is one of the assumptions. Grindle<sup>59</sup> has taken a different critical standpoint. According to Grindle, taking good governance as a guide to development is problematic for several reasons. Firstly, governments in developing countries have often low legitimacy and venal leadership. Civil society, to the extent that it exists at all, struggles with being disenfranchised and may be divided. Under such circumstances, the ideas of good governance are barely workable. “In such contexts, getting good governance as a route toward poverty reduction can overwhelm the commitment of even the most energetic reformers.”<sup>60</sup> Secondly, most of the policies proposed on the basis of good governance approaches are ahistorical and are in large measure incompatible with regional characteristics. Thirdly, the study of developed countries offers no evidence that good governance is an essential condition for development. Studies suggest “that economic development occurred long before countries had fully institutionalized democracies, professional bureaucracies, rules for corporate governance, modern financial institutions, and extensive social welfare services.”<sup>61</sup> The essential requirements of good governance of transparent and accountable institutions were not necessary conditions for economic and industrial development.

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<sup>56</sup> Goldsmith, "Is Governance Reform a Catalyst for Development?," 165.

<sup>57</sup> OECD, "China in the Global Economy: Governance in China", 43.

<sup>58</sup> Goldsmith, "Is Governance Reform a Catalyst for Development?," 182.

<sup>59</sup> Merilee S. Grindle, "Good Enough Governance: Poverty Reduction and Reform in Developing Countries," *Governance: An International Journal of Policy, Administration, and Institutions*, Vol. 17, No. 4 (2004), 525.

<sup>60</sup> *Ibid.*, 526.

<sup>61</sup> *Ibid.*, 531.

Instead of a 'full program' of good governance, Grindle has proposed a proper concept of 'good enough governance', which she defines as "a condition of minimally acceptable government performance and civil society engagement that does not significantly hinder economic and political development and that permits poverty reduction initiatives to go forward."<sup>62</sup>

A reduced agenda for good governance requires tackling the problem of choosing which reforms of good governance would be reasonable to introduce. That requires a broad knowledge of the possibilities of how particular goals, such as poverty reduction, can be achieved. The lack of sufficient information about how strategies can be implemented makes good governance for a wide range of countries only "a distant possibility"<sup>63</sup> of what can be done in actuality.

Grindle's concept of good enough governance has some implications for which part of development we should focus upon. The idea is that some governance deficits are less important and do not require too much attention. Grindle "suggested that good enough governance directs attention to considerations of the minimal conditions of governance necessary to allow political and economic development to occur."<sup>64</sup> Nevertheless, good governance remains an important guideline for a wide range of areas of the development community, despite the fact that numerous questions remain unanswered, especially the question of which institutions matter most. It is not likely that the World Bank and other lenders to the 'Third World' will change their policies regarding good governance any time soon.

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<sup>62</sup> Ibid., 526.

<sup>63</sup> Ibid., 543.

<sup>64</sup> Merilee S. Grindle, "Good Enough Governance Revisited," *Development Policy Review*, Vol. 25, No. 5 (2007), 554.

### 2.1.3. Corporate governance

Corporate governance, as the name suggests, applies the idea of governance to corporations. Like governance used in other fields, there is no set definition of corporate governance; how corporate governance is characterized depends, instead, upon the intention of the particular study.

In general, corporate governance has two principal perspectives. One is narrowly related to the corporate perspective and its investors. Shleifer and Vishny<sup>65</sup> have defined corporate governance in terms of how investors can protect their investments. The underlying idea is that suppliers of finance to corporations develop ways to ensure getting a return on their investments. It focuses on shareholders and measures the efficacy of corporate boards representing their interests.<sup>66</sup> According to this viewpoint, corporate governance answers three main questions: “How do the suppliers of finance get managers to return some of their profits to them? How do they make sure that managers do not steal the capital they supply or invest it in bad projects? How do suppliers of finance control managers?”<sup>67</sup> Although this overall point of view takes an investor’s standpoint, the public sphere is strongly involved.<sup>68</sup> The second perspective is related to the corporations’ stakeholders. Although by definition it includes its investors as stakeholder, various actors are related to corporations. Most prominent is the OECD’s definition of corporate governance: “Corporate governance involves ‘a set of relationships between a company’s management, its board, its shareholders and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance, are determined.’”<sup>69</sup> This approach focuses more on the “quality of accounting practices across countries.”<sup>70</sup> That implies that corporate governance is not directly concerned with how enterprises run their business, but rather with how enterprises incorporate

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<sup>65</sup> Andrei Shleifer and Robert W. Vishny, "A Survey of Corporate Governance," *The Journal of Finance*, Vol. 52, No. 2 (1997).

<sup>66</sup> Xun Wu, "Corporate Governance and Corruption: A Cross-Country Analysis," *Governance: An International Journal of Policy, Administration, and Institutions*, Vol. 18, No. 2 (2005), 161.

<sup>67</sup> Shleifer and Vishny, "A Survey of Corporate Governance," 737.

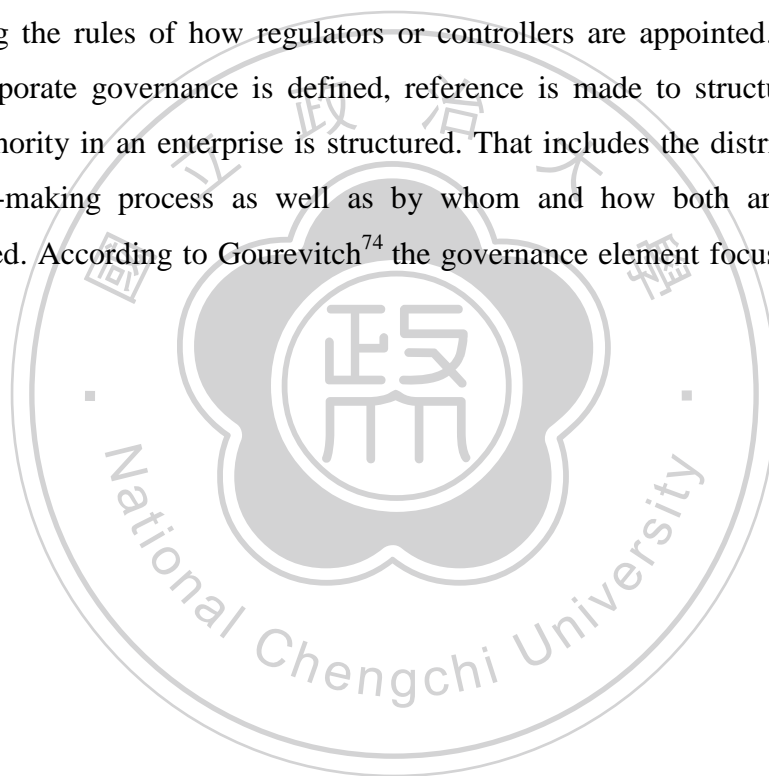
<sup>68</sup> *Ibid.*, 738.

<sup>69</sup> OECD, "China in the Global Economy: Governance in China", 43.

<sup>70</sup> Wu, "Corporate Governance and Corruption: A Cross-Country Analysis," 161.

tools and rules into their internal regulations to guarantee maintaining a relationship with their stakeholders under the “expectations for accountability and regulation by the interests beyond the corporate boundaries.”<sup>71</sup>

Definitions of corporate governance sometimes combine both approaches. In that case, the term is related to state and social influences that affect “institutional processes, including those for appointing the controllers and/or regulators, involved in organizing the production and sale of goods and services.”<sup>72</sup> It describes the relations within an economic system which enable the control or regulation of the corporations, including the rules of how regulators or controllers are appointed.<sup>73</sup> In all cases of how corporate governance is defined, reference is made to structures, specifically, how authority in an enterprise is structured. That includes the distribution of power, decision-making process as well as by whom and how both are controlled and monitored. According to Gourevitch<sup>74</sup> the governance element focuses on three main aspects:



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<sup>71</sup> Rhodes, "The New Governance: Governing without Government," 653.

<sup>72</sup> Shann Turnbull, "Corporate Governance: Its scope, concerns and theories," *Corporate Governance: An International Review*, Vol. 5, No. 4 (1997), 181.

<sup>73</sup> *Ibid.*, 182.

<sup>74</sup> Peter Gourevitch, "Corporate Governance - Global Markets, National Politics", "*Governance in a global economy: political authority in transition*" (eds.) Kahler and Lake, (Princeton, New Jersey: Princeton University Press, 2003), 307.

“[1.] Information institutions: accounting rules, audit procedures, standards-settings, and third-party analysis.[2.] Oversight institutions: boards of directors and the rules governing their fiduciary responsibilities.[3.] Control institutions: the degree of voice minority shareholders have in the case of contested control and the rules that govern such contests, including the rules of hiring, compensating, and firing senior managers.”<sup>75</sup> There are certain identifiable points of convergence between good governance and corporate governance. Some features, such as accountability and transparency, have been said to be necessary to both forms of governance. Like good governance, corporate governance occupies a prominent position in policymaking in developing countries. The expectations underlined in some studies suggest that “low corporate governance standards raise the cost of capital, lower the operating performance of industry, and impede the flow of investment.”<sup>76</sup> In other words, corporate governance is an important factor in boosting a country’s economy. The problems corporate governance faces are similar to those of good governance. It is a critical area of policy making which incorporates interactions between domestic politics, the private sector and even an international dimension.<sup>77</sup> It is difficult to demonstrate a direct correlation between growth and corporate governance. All this may lead to similar conclusion, namely that a ‘good enough corporate governance’ should be moved to the center stage of discussions.

#### 2.1.4. Public governance

Public governance can be seen as the concepts of corporate governance applied to public administrations. Just as governance and government have historically been considered to be synonyms, it can be argued that so are public administration and public governance. Osborne<sup>78</sup> has shown that theories of public administration management have passed through three paradigmatic stages. From the beginning of the 20<sup>th</sup> century through to the late 1970s and early 1980s, the preminent paradigm was that public administration had some similarities to the use of governance during the same period. This was followed by the new public management which enriched

<sup>75</sup> Ibid., 307.

<sup>76</sup> Wu, "Corporate Governance and Corruption: A Cross-Country Analysis," 151.

<sup>77</sup> Gourevitch, "Corporate Governance - Global Markets, National Politics", 325.

<sup>78</sup> Stephen Osborne, "The New Public Governance?," *Public Management Review*, (2006), 377.



public administration management with private-sector managerial techniques<sup>79</sup> and focused on entrepreneurial leadership within public service organizations. Mayntz's<sup>80</sup> and Mayntz and Scharpf's<sup>81</sup> actor-centered institutionalism (Akteur zentrierter Institutionalismus) theory argues that because in complex societies certain actors possess the de facto power of veto, the state is finding it increasingly difficult to implement public policies.<sup>82</sup> This development has led to the newest trend, which can be seen as a fusion of governance theories with existing administration management theories. The new public governance emerged as the predominant paradigm. From this perspective, it is clear that "‘governance’, and ‘public governance’, are not new terms and they themselves come with considerable prior theoretical and/or ideological baggage."<sup>83</sup> Like the various definitions of other uses of governance, the views related to how public governance is seen are not harmonized. For instance, Rhodes<sup>84</sup> has identified no fewer than seven different uses of governance in studying public administration: "governance; the new public management; good governance; international interdependence; socio-cybernetic systems; the new political economy; and networks." A definition proposed by the OECD is a good synthesis of these seven approaches: "Public governance has been defined as ‘the formal and informal arrangements that determine how public decisions are made and how public actions are carried out, from the perspective of maintaining a country’s constitutional’ values as problems, actors and times change’."<sup>85</sup>

The main concern of public governance is correlated to the public choice theory that tries to develop institutions to prevent people from misusing the state for maximizing their own benefit.<sup>86</sup> For that purpose, the older concept of new public management

<sup>79</sup> Ibid., 379.

<sup>80</sup> Renate Mayntz, *Soziale Dynamik und politische Steuerung: Theoretische und methodologische Überlegungen* (Campus, 1997).

<sup>81</sup> Renate Mayntz and Fritz W. Scharpf, "Steuerung und Selbstorganisation in staatsnahen Sektoren", *Gesellschaftliche Selbstregulierung und politische Steuerung* (eds.) Mayntz and Scharpf, (Frankfurt aM: Campus, 1995).

<sup>82</sup> Yannis Papadopoulos, "Governance, Coordination and Legitimacy in Public Policies," *International Journal of Urban and Regional Research*, Vol. 24, No. 1 (2000), 214.

<sup>83</sup> Osborne, "The New Public Governance?," 381.

<sup>84</sup> Rod A. W. Rhodes, "Governance and Public Administration", *Debating Governance: Authority, Steering, and Democracy* (ed.), Pierre, Oxford University Press, 2000).

<sup>85</sup> OECD, "China in the Global Economy: Governance in China", 43.

<sup>86</sup> Goldsmith, "Is Governance Reform a Catalyst for Development?," 166.

took the view that “society should be run as if it were a firm.”<sup>87</sup> Public governance overturns this view and focuses on designing institutions capable of influencing intrinsic motivation. Frei<sup>88</sup> has identified four aspects which are designated to fulfill these expectations: (1) Popular participation rights which generate a common identification and provide feedback to the system (2) Fixed position and income of officials encourage them to make suggestions for improvements and to criticize processes without fearing the disagreement of their superiors (3) Extensive selection processing of agents and (4) autonomy within the rules.<sup>89</sup> The tools of public governance are different from those of new public management in that the agents’ behaviors are influenced to achieve the principal goals. It is a global approach with a strong enhancement of “efficiency, outcome, competition, value-for-money, catalytic role, autonomy, partnership, and customer orientation.”<sup>90</sup>

#### 2.1.5. Global governance

Next, I discuss global governance, which is the latest application of the concept of governance as well as one that has drawn widespread attention. In contrast to the previous concepts, in which the focus was on institutions, global governance points to the sources and political implications of global change<sup>91</sup> and the implications linking private and governmental actors.<sup>92</sup> Global governance became increasingly popular simultaneously with the notion of economic globalization. It is not surprising that with the link to two general terms, global change and globalization, an enormous variety of global governance conceptions would follow.<sup>93</sup> Nonetheless, several distinct concepts of global governance must be recognized. Hewson and Sinclair<sup>94</sup>

<sup>87</sup> Bruno S. Frey, *Corporate Governance: What can we Learn from Public Governance* (Zürich: Institute for Empirical Research in Economics, 2003), 2.

<sup>88</sup> *Ibid.*, 5.

<sup>89</sup> *Ibid.*, 5-10.

<sup>90</sup> M. Shamsul Haque, "Significance of accountability under the new approach to public governance," *International Review of Administrative Sciences*, Vol. 66, No. 4 (2000), 600.

<sup>91</sup> Martin Hewson and Timothy J. Sinclair, *Approaches to Global Governance Theory* State University of New York Press, 1999), Martin Hewson and Timothy J. Sinclair, "The Emergence of Global Governance Theory", *Global Governance - Critical Concepts in Political Science* (ed.), Sinclair, (New York: Taylor & Francis, 2004), 227.

<sup>92</sup> J. Humphrey and D. Messner, "China and India as emerging global governance actors: Challenges for developing and developed countries," *Ids Bulletin-Institute of Development Studies*, Vol. 37, No. 1 (2006), 107.

<sup>93</sup> Hewson and Sinclair, "The Emergence of Global Governance Theory", 229.

<sup>94</sup> *Ibid.*, 239.

have traced the concept back to three mainstreams: “One arises from the attempt to trace broad changes in patterns of international regimes. A second is concerned with the implications of contemporary changes for the world organizations’ capacities for addressing world problems. The third is concerned with identifying the ascendant political forces shaping the form of global governance.” All three issues are concerned with the effects of globalization on different levels and institutions. Global governance focuses further on three analytical dimensions: firstly, at the level of private or public institutions, global change has an influence; secondly, how the systems respond to the new challenges and the impact of democratic accountability and thirdly, the conflicts between convergence or divergence of the resulting policy products.<sup>95</sup>

Theories on global governance are related to globalization and governance, and rely on functionalist- or efficiency-based concepts.<sup>96</sup> They suppose that institutions involved in global change and globalization aggregate the preferences of these players into policies. Bargaining is the method they use when preferences are in conflict.<sup>97</sup> In either case, these processes became more important with the growing complexity of global politics. The problems were analyzed in different ways. A static model focuses on governance and the state, based on the concept of sovereignty. Global governance occurs in cases of power inequality. That permits some states to possess the additional ability to constrain others. Governance and international organizations focus on sites of authority and their relationships. That means that the authoritative power is not located in one place like the central state, but in particular entities, or between them. Furthermore, the model of transnational actors shifts the center of power to non-governmental actors. Their power relies on market power or on particular areas where such organizations have a broad influence. And lastly, policy networks is a model where actors are organized among networks rather than within organizational entities.<sup>98</sup>

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<sup>95</sup> Kahler and Lake, "Globalization and Governance", 8.

<sup>96</sup> Ibid., 16.

<sup>97</sup> Ibid., 24.

<sup>98</sup> Robert. O. Keohane and Joseph S. Nye, "Redefining Accountability for Global Governance", *ibid.*, 394-395.

### 2.1.6. International agencies and their use of governance

The International agencies that matter most in this context include but are not restricted to: the World Bank, the International Monetary Fund (IMF), the United Nations and its agencies, e.g. United Nations Development Programme (UNDP), the Organization for Economic Co-operation and Development (OECD) and the Asian Development Bank (ADB). It is no wonder that the concept of governance is widespread among international agencies which develop and implement a wide range of policies that, by definition, are concerned with these issues. A prominent example of the importance of governance to international organizations is the World Bank Institute's (WBI) large-scale 'Governance & Anti-Corruption' project.<sup>99</sup> What the WBI shows is that such organizations may have a strong preference for good governance. The OECD, for example, has defined three pillars as targets for development: economic growth, social cohesion and good governance.<sup>100</sup> Therefore, for the OECD "good governance is thus seen as a crucial element in addressing challenges and fault lines facing a nation, and to ensure sustainable development."<sup>101</sup> The best way to analyze how international organizations conceptualize governance is to distinguish between their use of governance and good governance.

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<sup>99</sup> The World Bank, *WBI Governance & Anti-Corruption* 2008).

<sup>100</sup> OECD, "China in the Global Economy: Governance in China", 11.

<sup>101</sup> *Ibid.*, 11.

## **Governance**

### OECD:

Basically, the OECD includes a “whole-of-government and a sectoral approach.”<sup>102</sup> In its definition, governance is recognized as critical to economic development and the achievement of a society’s objectives.<sup>103</sup>

### World Bank:

Governance is the process and institutions through which decisions are made and authority in a country is exercised.<sup>104</sup>

### IMF

The IMF distinguishes two spheres: (1) improving the management of public resources through reforms covering public sector institutions, including administrative procedures; and (2) supporting the development and maintenance of a transparent and stable economic and regulatory environment conducive to efficient private sector activities.<sup>105</sup>

### ADB

Governance for the ADB is the “vital connection between sound and responsive systems of public administration and the effective and equitable operation of the economy,”<sup>106</sup> as well as “the manner in which power is exercised in the management of a country’s economic and social resources for development.”<sup>107</sup>

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<sup>102</sup> Ibid., 11.

<sup>103</sup> Ibid., 11.

<sup>104</sup> The World Bank, *Good Governance and Its Benefits on Economic Development: An Overview of Current Trends* (The World Bank Institute, 1997), 3.

<sup>105</sup> International Monetary Fund, *Good Governance: The IMF's Role* (Good Governance 1997).

<sup>106</sup> Asian Development Bank (ADB), *Governance: Sound Development Management* (Manila: Asian Development Bank, 1995), 1.

<sup>107</sup> Ibid., 3, Burns, "Governance and public sector reform in the People's Republic of China", 68.

## **Good governance**

### OECD:

The OECD Public Management Committee has adopted a set of principles that explain the key components of good public governance: rule of law, accountability, transparency, efficiency and effectiveness, and forward-vision.<sup>108</sup> It is worth noting that the OECD combines good and public into the term good public governance.

### World Bank

For the World Bank, good governance takes place in three key areas: (1) selection, accountability and replacement of authorities (accountability and stability), (2) efficiency of institutions, regulations, resource management (regulatory framework; and government effectiveness), and (3) respect for institutions, laws and interactions among players in civil society, business, and politics (control of corruption and rule of law).<sup>109</sup>

### IMF

Promoting good governance is one of the IMF's goals, which include: ensuring the rule of law, improving the efficiency and accountability of the public sector, and tackling corruption.<sup>110</sup>

### ADB

According to the Asian Development Bank, governance values are primarily accountability, transparency, openness, predictability and participation,<sup>111</sup> which are necessary for effective management.<sup>112</sup> This is governance from the perspective of sound development management.<sup>113</sup>

<sup>108</sup> OECD, "China in the Global Economy: Governance in China", 43.

<sup>109</sup> The World Bank, "Good Governance and Its Benefits on Economic Development: An Overview of Current Trends", 7.

<sup>110</sup> International Monetary Fund, "Good Governance: The IMF's Role", (

<sup>111</sup> Asian Development Bank (ADB), *Governance* 2008).

<sup>112</sup> Asian Development Bank (ADB), "Governance: Sound Development Management", 3.

<sup>113</sup> *Ibid.*, 21.

### 2.1.7. Critique on the use of the term ‘governance’: normative implications

Although governance is widely used to describe processes of policy development and implementation, the use of governance is often criticized for its normative implications. When scholars and politicians speak about governance, they often do so with an emphasis on good governance, which is explicitly an evaluative and therefore normative value. I would argue, however, that governance itself is, in fact, descriptive and actually not necessarily normative. Next, I examine criticisms leveled by some scholars and international organizations of how governance is used.

#### **Governance as a challenge to democratic accountability**

It may sound contradictory to consider governance and accountability as being in conflict, especially because accountability is one of the pillars of good governance. Rhodes<sup>114</sup> remarks on the challenges of governance for democratic accountability in the British case is one case in point. Accountability between voters and private organizations poses a further question.<sup>115</sup> From a deliberative critical perspective, governance is biased to technocratic decisions and therefore a threat to public legitimization.<sup>116</sup> “The participatory criticism predicts that governance reduces citizen involvement and eventually jeopardizes community-building and solidarity.”<sup>117</sup>

#### **Governance does not help development**

Governance reforms are often initiated to boost a country’s development. Goldsmith<sup>118</sup> has concluded that governance reforms may not make a considerable contribution to development, and mentioned four reasons: (1) accountable institutions would be appreciated, but setting them up need not necessarily provide a perceptible jolt to development; (2) public institutions may be adequate for an upsurge in production and income; (3) good governance reforms are more the effect of rather than the cause of speed-up development; (4) a higher rate of development often brings an escalation in

<sup>114</sup> Rhodes, "The New Governance: Governing without Government," 667.

<sup>115</sup> Wälti, Kübler and Papadopoulos, "How Democratic Is "Governance"? Lessons from Swiss Drug Policy," 84.

<sup>116</sup> Cynthia Hewitt de Alcantara, "Uses and abuses of the concept of governance," *International Social Science Journal*, Vol. 50, No. 155 (1998), 113.

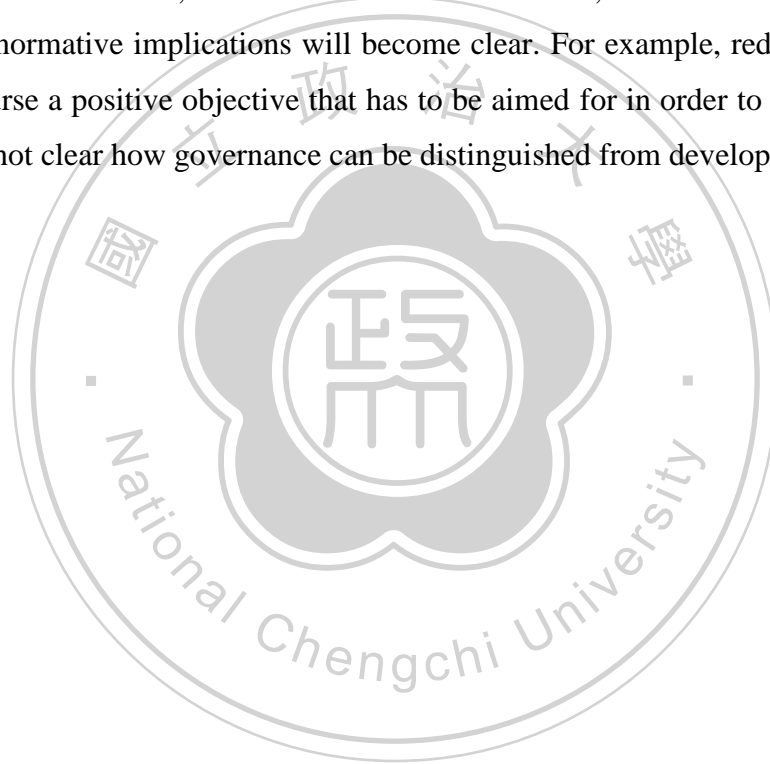
<sup>117</sup> Wälti, Kübler and Papadopoulos, "How Democratic Is "Governance"? Lessons from Swiss Drug Policy," 106.

<sup>118</sup> Arthur A. Goldsmith, "Is Governance Reform a Catalyst for Development?," *ibid.* Vol. 20, (2007), 181.

corruption.<sup>119</sup> The question hereby is: which part of governance or good governance has to be implemented first<sup>120</sup>?

### **Normative questions<sup>121</sup>**

The broad definition of governance and good governance makes it difficult to distinguish among descriptive, evaluative and normative views of what 'is' and what 'ought to be'.<sup>122</sup> In particular, if governance is used to ensure achievements of development like stable macroeconomic policy, reduction of poverty, openness to trade, decentralization, or efficient revenue collection, then democratic participation and the normative implications will become clear. For example, reduction of poverty is of course a positive objective that has to be aimed for in order to be achieved. "[I]t is often not clear how governance can be distinguished from development itself."<sup>123</sup>



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<sup>119</sup> Ibid., 181.

<sup>120</sup> Ibid, Grindle, "Good Enough Governance: Poverty Reduction and Reform in Developing Countries.", Grindle, "Good Enough Governance Revisited."

<sup>121</sup> David Williams and Tom Young, "Governance, the World Bank and Liberal Theory," *Political Studies*, Vol. 42, No. 1 (1994).

<sup>122</sup> Grindle, "Good Enough Governance Revisited," 555.

<sup>123</sup> Ibid., 555.



## 2.2. Definition of Governance

My preceding discussion of the different approaches of governance has shown the wide range of uses to which the term ‘governance’ is put. There is no common approach, neither in academic discourse nor among international organizations, to define governance. Governance can be seen as an ad-hoc concept that is defined for a specific research topic or as a set of values for a common ground for policy development in the case of international organizations. Nevertheless, governance is a concept that can be understood intuitively, but for which a clear definition is very hard to reach. In most cases, we see a very strong relation to the more narrow approach of good governance. It is also a widely held belief, though the correlation remains to be proven, that better governance improves a country’s performance in many different areas, such as medium to long-term economic development, social cohesion and environmental protection.

The aim of this paper is to evaluate whether governance theories are a helpful tool for answering the question whether the current reforms in China worsen China’s existing problems or whether China is on a good path. In view of the many governance theories, I propose to use an existing and broadly accepted concept of governance used by the World Bank<sup>124</sup>. Such a pragmatic approach has several advantages: It reflects better than the academic discussion, a broad agreement of set of values within the variation of definitions of governance theories. Although the World Bank may also have its critics and it is not a value-free organization, it is the leading institution where Western and Asian countries have been engaged in governance issues since the early 1990s.<sup>125</sup> But one of the main advantages in using the World Bank’s governance concept is its declared aim to measure governance changes over time. It combines a quantitative with a qualitative approach, which makes it useful to examine whether governance theories can be a useful tool to evaluate China’s future development.

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<sup>124</sup> Kaufmann and Kraay, "Governance Indicators: Where Are We, Where Should We Be Going?.", Daniel Kaufmann, Aart Kraay and Massimo Mastruzzi, *Governance Matters VI: Governance Indicators for 1996-2006* SSRN, (2007), Daniel Kaufmann, Aart Kraay and Massimo Mastruzzi, *Governance Matters VIII: Governance Indicators for 1996-2008* (2009), The World Bank, *Managing Development: The Governance Dimension* (Washington, D.C.: The World Bank, 1991), The World Bank, "Good Governance and Its Benefits on Economic Development: An Overview of Current Trends", (, The World Bank, "WBI Governance & Anti-Corruption", (, The World Bank, *WBI Governance & Anti-Corruption* (2010), World Bank Institute, *Country Data Report for CHINA, 1996-2006* World Bank Institute, (2007).

<sup>125</sup> The World Bank, "Managing Development: The Governance Dimension", (

In this thesis, governance will be defined as follow:

Governance is the (1) process of policy development and implementation, as well as (2) the manner in which economic, social and environmental resources are allocated and used. The (3) outcome of this process can be measured in three dimensions of 'Selection and Monitoring', 'Efficiency' and 'Respect'.

These three dimensions with which the outcome is measured also correspond to the most important characteristics of successful states. Put another way as Brinkerhoff<sup>126</sup> did, failed states confront three main problems: lack of legitimacy, security and effectiveness.

The following chapters are based on this conceptualization of governance. I will begin by focusing my discussion of governance on the case of China. In addressing the central questions of this thesis, my discussion will inevitably not rely solely on the definition, but will also include broader aspects of governance.

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<sup>126</sup> D. W. Brinkerhoff, "Rebuilding governance in failed states and post-conflict societies: core concepts and cross-cutting themes," *Public Administration and Development*, Vol. 25, No. 1 (2005), 5.

### 3. Governance in China

In this chapter, three main lines of governance in China are discussed, beginning with two different approaches to examine China's governance performance. In general terms, we can distinguish between a **negative outlook** expressed by Pei<sup>127</sup> and a **generally positive evaluation** presented by Yang.<sup>128</sup>

I will conclude this discussion with an evaluation of the strengths and weaknesses of China's governance capacity. Regarding the definitions, chapter 3.1 relies on the first section of the definition, which focuses on 'the process of policy development and implementation' and the 'manner how economic, social and environmental resources are allocated,' whereas chapter 3.2 is related to 'the outcome of governance processes.' Chapter 3.3 points out 'hotspots' in the actual discussion on governance topics.

#### 3.1. Different approaches to issues inherent in the governance framework

Regarding its governance, the early days of China's communist period the system was extremely simple: social organizations had no autonomy and were de facto branches of the government in Beijing.<sup>129</sup> The economic opening and the related reforms in the economic sphere spurred changes in China's system of governance. The CCP government moved away from its four types of organizations (industrial units, agricultural units, service units and administrative units) to a more complex, and therefore different, system of governance.

<sup>127</sup> Pei, "China's trapped transition the limits of developmental autocracy".

<sup>128</sup> Yang, "Remaking the Chinese Leviathan: Market Transition and the Politics of Governance in China".

<sup>129</sup> OECD, "China in the Global Economy: Governance in China", 13.

A brief reference to two scholars who present two different approaches will demonstrate the difficulties in evaluating the ongoing process of reforms and restructuring power constellations in China. The following debate about the specific topic of governance in China will offer a different understanding of how China's reforms influenced its governance capabilities and how governance theories may be a helpful tool.

### **Negative – China's Trapped Transition<sup>130</sup>**

Pei has drawn a pessimistic picture of the ongoing reforms in terms of handling the country's rising problems. He has analyzed the lack of structural reform in China's political institutions and concluded this with several indicators showing that China has a serious governance problem. He has developed the indicators from his two main theses that China's state capacity was eroding and that the CCP's capacity for political mobilization was declining. That would cause the declining ability of governance, which Pei has defined as the ability to provide public services, such as: public safety, health and environmental protection and the enforcement of laws. The main problem, according to Pei, was that China is a developmental autocracy incapable of reforming its institutions. Pei's thesis is that China will find itself in a transitional trap and will be harmed by low political accountability, unresponsiveness, collusion and corruption.<sup>131</sup> Three scenarios are possible to escape from the transitional trap: more democracy for more social groups, regime collapse, and a boost from local and regional institutional reforms.<sup>132</sup>

Pei's views on this topic have, in my opinion, several weaknesses. Although he uses statistical sources, he has failed to make an accurate analysis that accounts for change over time and draws comparisons with other countries. The other limitation of his conclusion is that he did not develop a broader concept of governance. For instance, the World Bank uses 6 main indicators in its worldwide governance project. China's

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<sup>130</sup> A. J. Nathan, "Present at the stagnation - Is China's development stalled?," *Foreign Affairs*, Vol. 85, No. 4 (2006), Pei, "China's trapped transition the limits of developmental autocracy".

<sup>131</sup> Pei, "China's trapped transition the limits of developmental autocracy", 208.

<sup>132</sup> *Ibid.*, 210-211.

performance, compared to other countries, did not change as much as one might have expected after Pei's prediction. Between 1996 and 2008, the biggest change occurred in the control of corruption, in which China dropped from 54.4 to the 41.1 percentile rank. But China remained more or less stable in the remaining five parts. China performed best in the area of 'government effectiveness' where it occupies the 63.5 percentile rank. That means that China did better than almost two third of all countries worldwide. Unsurprisingly, in terms of 'voice and accountability', China is among the worst performing countries. But is that enough to support Pei's pessimistic conclusion of a continuing deterioration of China's governance to the worst possible result?

### **Positive - Remaking the Chinese Leviathan**<sup>133</sup>

Yang,<sup>134</sup> like Pei, discusses the institutional reforms in China. His conclusion is diametrically opposite to Pei's. He has shown how institutional reforms have improved the interactions between citizens, corporations and the state. Yang refers explicitly to the reforms since the late 1970s in China as governance reforms.<sup>135</sup> Events like the SARS crisis helped China to make progress in terms of good governance. The events "spurred the spread of transparency and accountability to the area of public health."<sup>136</sup> One piece of evidence supporting Yang's contention that China's (governance) reforms are working is the fact that China's recent economic record is the best since the beginning of China's modern era.<sup>137</sup>

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<sup>133</sup> Margaret M. Pearson, "Review on Dali Yang, 'Remaking the Chinese Leviathan: Market Transition and the Politics of Governance in China,'" *Far Eastern Economic Review*, Vol. 168, No. 3 (2005), Yang, "Remaking the Chinese Leviathan: Market Transition and the Politics of Governance in China".

<sup>134</sup> Yang, "Remaking the Chinese Leviathan: Market Transition and the Politics of Governance in China".

<sup>135</sup> *Ibid.*, 290.

<sup>136</sup> *Ibid.*, 291.

<sup>137</sup> *Ibid.*, 303.

### 3.1.1. Reforms and its impact on the governance framework

This chapter briefly examines a couple of contentious issues on governance related reforms in China. The question is whether the reforms improved governance capabilities or whether the reforms were not carried out in an appropriate manner. China is not a unique case, in that it faces challenges similar to those of other centrally planned economies in Asia. Specifically, I will focus on the lack of an appropriate legal framework and skills to challenge the reforms.<sup>138</sup>

#### **Reforming the civil sector**

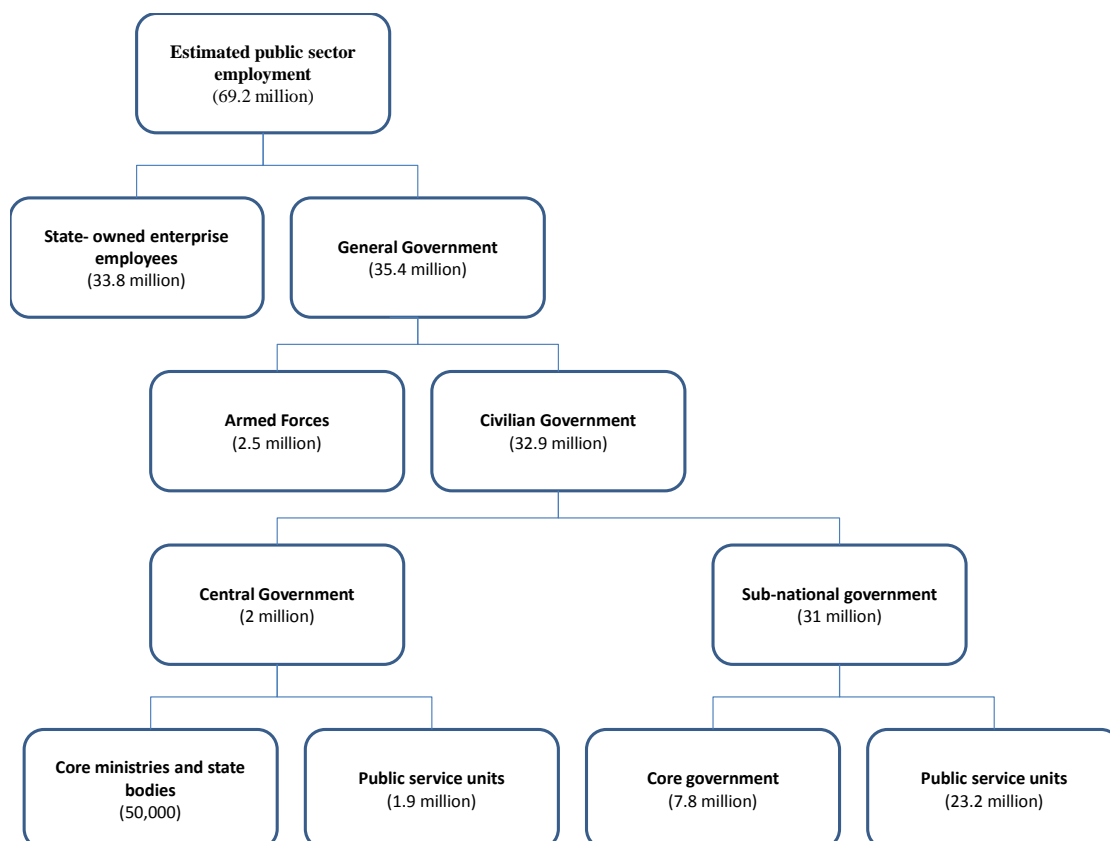
Given the strong position of the state in China, it is reasonable to consider one particular reform, the civil service reform in China's administration. Chinese leaders' attempts to improve China's governance capability mainly concerned reforms on the civil sector.<sup>139</sup> Talking about the civil sector involves some peculiarities; there are no precise numbers available regarding the extent of public sector employees in China. Estimations show that about half of the nearly 70 million employees are state-owned enterprise employees. The other half are employed by the general government, with most working for the sub-national government in public service units. Burns<sup>140</sup> has estimated the spread of civil employees in China as follows:

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<sup>138</sup> ANTHONY B. L. Cheung, "The Politics of Administrative Reforms in Asia: Paradigms and Legacies, Paths and Diversities," *Governance: An International Journal of Policy, Administration, and Institutions*, Vol. 18, No. 2 (2005), 259.

<sup>139</sup> John P. Burns, "Civil Service Reform in China," *OECD Journal on Budgeting*, Vol. 7, No. 1 (2007), 58.

<sup>140</sup> *Ibid.*, 60.

**Table 3: Civil employees in China<sup>141</sup>**

As regards governance issues, we can maintain that most civil servants work in local government. They are employed in more than 2,800 counties.<sup>142</sup> For instance, the central government's core ministries and state bodies are staffed with about 50,000 employees. Another 7.8 million work in the same function but on a sub-national level. In other words, every central government official has 156 colleagues on a lower level.

The civil service system has been undergoing a reform process for more than 15 years. The Chinese government has taken significant steps to reform it.<sup>143</sup> A civil servant in China is still considered as occupying a prestigious position. The reforms have increased the requirements on the part of government employees.<sup>144</sup> At the central level, officials' mindset has changed in several important respects. The recruiting process has increasingly aimed to select more competent people (the best and brightest). The result was an increase in the number of leading cadres with a university degree since the 1980s, by a factor of 2 to 3 and finally reaching a rate

<sup>141</sup> Ibid., 60.

<sup>142</sup> Ibid., 63.

<sup>143</sup> OECD, "China in the Global Economy: Governance in China", 55.

<sup>144</sup> Ibid., 61.

above 80%.<sup>145</sup> A further attempt was the introduction of a culture of performance with performance standards, evaluation of performance and performance linked to rewards.<sup>146</sup> Another characteristic in this context is the increased awareness of the need to improve the efficiency and effectiveness of public resources.<sup>147</sup> The number of public employees has dramatically declined in recent years, mainly as a result of the decline of state-owned-enterprises.<sup>148</sup> Of the more than 60 million employees mentioned above, depending on public regulations, “only 4.98 million were formally classified as ‘civil servants’ according to China’s civil service regulations.”<sup>149</sup> The resulting improved capacity of the public sector over the past 10 years has not only been achieved by public sector reforms but, in all likelihood, also been influenced by the general improvements in China’s system of education.<sup>150</sup> That said, any attempt to evaluate the performance of the Chinese government’s reforms must begin with the difficult problem of assessing their results to date. The public sector is a good example. Yang<sup>151</sup> has praised the introduction of job-rotations among cadres on the center’s nomenclature and county magistrates as positive. He argues that the performance rose and corruption fell. Yang underlined the end-of-term audits for such officials, which “have become a crucial link in the enhancement of the cadre disciplinary regime.”<sup>152</sup> The same institutional reform can be seen completely differently. Pei described the rotations of cadres as new exit options which reduce the time horizon for carrying out responsibilities. Self-interest and rent seeking became more salient. Pei’s radically different view has led him to conclude that “the unintended effect of this institutional practice is to turn these officials, literally, into roving bandits.”<sup>153</sup> The problem of different interpretations can be found within statistics. Pei sees the problem of overstaffing as a risk inherent in a steadily growing Chinese state with immense costs and the reason why China became a predatory state. Pei stresses that the problem became worse during the 1990s. In particular, district and township governments employed significantly more employees than officially

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<sup>147</sup> OECD, "China in the Global Economy: Governance in China", 40.

<sup>148</sup> Ibid., 14.

<sup>149</sup> Ibid., 57.

<sup>150</sup> Ibid., 69.

<sup>151</sup> Yang, "Remaking the Chinese Leviathan: Market Transition and the Politics of Governance in China", 181.

<sup>152</sup> Ibid., 182.

<sup>153</sup> Pei, "China's trapped transition the limits of developmental autocracy", 153.



authorized. Underreporting and the lack of a standard classification of employees made it even worse. He compared the growth rates of state employees between 1953 to 1978 of 1.8% and 1979 to 1990 of 6.7% and the fact that the official figures for 2002 suggest double the number of employees as in 1978.<sup>154</sup> The same statistics can be read and interpreted very differently. Yang<sup>155</sup> believes that the Chinese state, at the local level, has recently been massively downsized. The plan to reduce 20% of its staff would firstly affect unauthorized staff. This different perception of the same phenomenon is not only caused by different observation periods (Pei focused on the long term and Yang more on recent events) but also by the difficulties in trying to measure the success of the reforms. Although there is no consensus how the reforms have affected the outcome of the governing process in general, there is some evidence that the reforms have had little effect on containing corruption and developing participative social structures but have, however, improved resource allocation efficiency.

### **Reforms toward transparency**

Beside the difficulties in the public sector reform, there are many other issues affecting governance in China. One significant case in point is the practice of reserving posts in the government for CCP members. In this respect, China does not differ much from past practice in other communist countries. China undertook several reforms which have led to greater transparency. One of them was the publication of these reserved posts.<sup>156</sup> This may be seen as minor improvement in transparency, but it shows that minor reforms can help remedy some weak points related to governance.

Reforms directed at transparency are oftentimes related to the issue of corruption. China undertook several efforts to strengthen and consolidate its instruments, mostly repressive instruments, to curb corruption. The redefinition of several offenses and improving documentation concerning the nature of corruption is another such minor step, which is necessary to improve governance capacity. The OECD conclusion was as follows:

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<sup>154</sup> Ibid., 136.

<sup>155</sup> Yang, "Remaking the Chinese Leviathan: Market Transition and the Politics of Governance in China", 47.

<sup>156</sup> OECD, "China in the Global Economy: Governance in China", 63.

*A lot remains to be done to complete a national ethics infrastructure and ensure that it functions in an effective and consistent manner. In addition to adjusting existing mechanisms in the public service, key challenges include how to implement and coordinate the new policy instruments.*<sup>157</sup>

The topic of corruption was not in the least related to the employees' salary with the benefits of corruption viewed as compensation. This led to a widespread tolerance of corruption, and makes it difficult to implement anti-corruption policies. The complicated CCP-State relationship affects the two dimensions which include the selection process of key-players in the process of policy development and implementation and the issues of corruption and its strong interdependencies.

### **Institutional reforms**

The public sector and civil employees are only one aspect of how reforms have influenced governance in China. Another general problem is related to the relationship between state and society and the development and implementation of policies. The most urgent measures, according to Howell, are “the need for political reform; processes of institution-building such as strengthening state capacity and improving the legal framework; enhancing regime legitimacy through the sharing of power at lower levels and promoting participation and voice through the development of civil society; and managing social discontent.”<sup>158</sup> Howell<sup>159</sup> identifies the roots of China's governance challenges in political, institutional, and economic factors in ways similar to Pei's.<sup>160</sup> The monopoly of power by the Chinese Communist Party is one of the key political determinants. The governance perspective reveals the imbalance between the incorporation of private entrepreneurs' interest and the expanded space for self-organization and expression.<sup>161</sup> Although this process harmed the legitimacy and authority of the Communist Party, the CCP has still been able to maintain and increase its membership.<sup>162</sup> The institutional problem has its roots in the very beginning of the PRC's institutions. The institutions are characterized, like other Leninist institutions, by vertical lines of command that result in insulated ministries

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<sup>157</sup> Ibid., 128.

<sup>158</sup> Howell, "Governance Matters: Key Challenges and Emerging Tendencies", 3.

<sup>159</sup> Howell, "Getting to the Roots: Governance Pathologies and Future Prospects".

<sup>160</sup> Pei, "China's trapped transition the limits of developmental autocracy".

<sup>161</sup> Howell, "Getting to the Roots: Governance Pathologies and Future Prospects", 228.

<sup>162</sup> Ibid., 229.

and agencies complemented by overlapping party and government structures. Mass organizations can be seen as extensions of the state and party with the primary mandate to promote their policies. The problems accumulate due to the lack of autonomous government institutions and an underdeveloped, constricted civil society. Participation is limited and repressed.<sup>163</sup> The economic factor has its roots in the fast economic development of China, which was not accompanied by the necessary reforms and thereby caused an imbalance within the society. Rural migrants, for instance, are poorly covered by the governance mechanism. On the other hand, while economic performance does not necessarily correspond with a better governance record, it may help the state to raise its capacity. Higher tax revenues can be an opportunity to fund existing policies. A comparison with other new post-socialist states puts the problems of corruption, fragmentation of authority, and unevenness of governance reforms, into perspective. Compared with them, the Chinese state is relatively strong and has a long history of state administration.<sup>164</sup> In addition, China enjoys relative political stability.<sup>165</sup>

Nevertheless, the highly fragmented structures in China have resulted in further problems in the decision and consensus making process. The political system makes “consensus-building central and the policy process protracted, disjointed, and incremental.”<sup>166</sup> With respect to governance issues, three particularities need to be kept in mind:

- 1) Problems tend to get pushed up the system where supra-bureaucratic bodies can coordinate their response, as they have sufficient leverage to bring together the different parties.
- 2) The fragmentation of authority means that at each stage of the decision-making process, strenuous efforts have to be made to maintain a basic consensus to move forward.
- 3) For a policy to be successful, it needs the concerted support of one or more top leaders. This fragmentation is accentuated because the party is no longer able

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<sup>163</sup> Ibid., 235.

<sup>164</sup> Ibid., 235.

<sup>165</sup> Ibid., 236.

<sup>166</sup> Tony Saich, *Governance and Politics of China* Palgrave Houndmills, Basingstoke, Hampshire, 2001), 213.

to perform the vital role of integrating the bureaucracy to improve both the formulation and the implementation of policy.<sup>167</sup>

Issues pertaining to governance and its outcome in China are not limited to a single, easily identifiable field, but involve much of China's political, economic and social landscape. Moreover, research on this topic is still limited: "after decades of research, we still do not really understand how things actually work in China."<sup>168</sup> Governance theories help to identify the important changes in its institutional framework and give with the evaluation of the outcome a tool to trace the changes. The following chapters will consider the evaluation of governance in China from quantitative viewpoint.

### 3.2. Measurement and evaluation of governance in China

Measuring and comparing governance in China and comparing the results with other countries is another concept finding a more comprehensive answer to the problem of understanding the impact of China's reforms on its governance capacity. In political science, indicators are made for almost every issue, and more than a few are broad concepts like governance. For instance, if democracy can be measured, the same should be possible for governance?

This chapter focuses on the Worldwide Governance Indicators (WGI) developed and published by the World Bank. It is the largest project ever undertaken to measure governance and enables a comparison of historical developments and changes among almost all countries. After discussing the advantages and limitations of the WGI, I will attempt to quantify governance performance in China.

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<sup>167</sup> Ibid., 213.

<sup>168</sup> King W. Chow and Laura Q. Luo, "Contending Approaches and Models for Rationalizing Chinese Public Organizations: The Case of Western China," *Public Organization Review*, Vol. 7, No. 1 (2007), 70.

### 3.2.1. Worldwide Governance Indicators (WGI)

One way to measure governance is to rely on existing indicators and studies on topics related to governance issues such as corruption. The World Bank started back in the 1990s with the Worldwide Governance Indicators (WGI) project, a long-term research program that measures governance in three dimensions (selection/monitoring, efficiency and respect) with the six key indicators: ‘voice and accountability’, ‘political stability and absence of violence’, ‘government effectiveness’, ‘regulatory quality’, ‘rule of law’ and ‘control of corruption’.<sup>169</sup> What makes the WGI an interesting approach is that it is designed as a set of indicators of different aspects of governance. Each of the indicators takes account of different facets of governance theories. Another interesting point is the nature of the indicators. The World Bank uses primary not only data but also indicators. The resulting governance indicators are an aggregated index of about “33 data sources produced by 30 different organizations worldwide.”<sup>170</sup> The result is an indicator encompassing more than 200 countries. The WGI is a useful tool to discover where the Chinese government is in its effort to reform the country and maintain its ability to sustain effective and efficient governance. In the publication accompanying the annual update of the WGI, Kaufmann and Kraay (2007) begin by stating the main problem encountered in every effort to measure governance:

*All governance indicators have limitations, which make them imperfect proxies for the concepts they are intended to measure. The presence of measurement error in all governance indicators that this implies is central to the rationale for constructing aggregate indicators.*<sup>171</sup>

The WGI is composed of six different governance indicators and can be seen in three dimensions:

<sup>169</sup> The World Bank, "Managing Development: The Governance Dimension", (

<sup>170</sup> The International Bank for Reconstruction and The World Bank, *A Decade of Measuring the Quality of Governance - Governance Matters 2007* (Washington: The World Bank, 2007), 1.

<sup>171</sup> Kaufmann and Kraay, "Governance Indicators: Where Are We, Where Should We Be Going?," 18.

Table 4: Six governance indicators<sup>172</sup>

<b>1. Voice and Accountability (VA)</b> – measuring the extent to which a country's citizens are able to participate in selecting their government, as well as freedom of expression, freedom of association, and a free media	Selection, accountability and replacement of authorities
<b>2. Political Stability and Absence of Violence (PV)</b> – measuring perceptions of the likelihood that the government will be destabilized or overthrown by unconstitutional or violent means, including domestic violence and terrorism	
<b>3. Government Effectiveness (GE)</b> – measuring the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation and the credibility of the government's commitment to such policies	Efficiency of institutions, regulations, resource management
<b>4. Regulatory Quality (RQ)</b> – measuring the ability of the government to formulate and implement sound policies and regulations that permit and promote private sector development	
<b>5. Rule of Law (RL)</b> – measuring the extent to which agents have confidence in, and abide by, the rules of society, and in particular the quality of contract enforcement, the police, and the courts, as well as the likelihood of crime and violence	Respect for institutions, laws and interactions among players in civil society, business, and politics.
<b>6. Control of Corruption (CC)</b> – measuring the extent to which public power is exercised for private gain, including both petty and grand forms of corruption, as well as the "capture" of the state by elites and private interests	

Since the World Bank supports countries with loans to improve their development efforts, it is not surprising that the method it uses to measure governance has a strong bias toward the concept of good governance. But as stated above, in order to evaluate governance it is a pragmatic approach.

The WGI itself consists of six different aggregated indicators of governance. Beside China, indicators are available for more than 200 countries. One of the advantages of the WGI is that the data is standardized, which allows for a comparison of the results

<sup>172</sup> Kaufmann, Kraay and Mastruzzi, "Governance Matters VI: Governance Indicators for 1996-2006", 2-3.

among these countries via a defensible method.<sup>173</sup> Every indicator aggregates data from different studies and from different organizations. For instance, the control of corruption indicator uses 13 different data sources<sup>174</sup>.<sup>175</sup> The following results are not absolute values. This means that a higher value does not mean that China has improved the particular field of governance, but a higher value does mean that compared with the other countries, it has improved its relative position.

**Table 5: Governance indicators for China (1996, 2006 and 2008) - Country's percentile rank (0-100)**<sup>176</sup>

	Voice and Accountability	Political Stability	Government Effectiveness	Regulatory Quality	Rule of Law	Control of Corruption
1996	5.7	38.0	64.5	50.7	48.8	54.4
2006	5.8	35.6	58.8	42.0	43.3	36.9
2008	5.8	33.5	63.5	46.4	45.0	41.1

Source: The World Bank (2010): WBI Governance & Anti-Corruption<sup>177</sup>

The changes in the last twelve years regarding China are very interesting in terms of direction. Detailed results are offered in the appendix.

<sup>173</sup> Shantayanan Devarajan, "Two Comments on "Governance Indicators: Where are we, where should we be going?" by Daniel Kaufmann and Aart Kraay," *International Bank for Reconstruction and Development*, (2008), 31.

<sup>174</sup> Business Environment Risk Intelligence Business Risk Service, Business Environment Risk Intelligence Financial Ethics Index Economist Intelligence Unit, Freedom House Countries at the Crossroads, Global Insight Business Conditions and Risk Indicators, Global Insight Global Risk Service, Rural Sector Performance Assessments, Institute for Management and Development World Competitiveness Yearbook, Merchant International Group Gray Area Dynamics, Political Economic Risk Consultancy Corruption in Asia Survey, Political Risk Services International Country Risk Guide, World Bank Country Policy and Institutional Assessments, World Economic Forum Global Competitiveness Report. Source: World Bank Institute, "Country Data Report for CHINA, 1996-2006", (

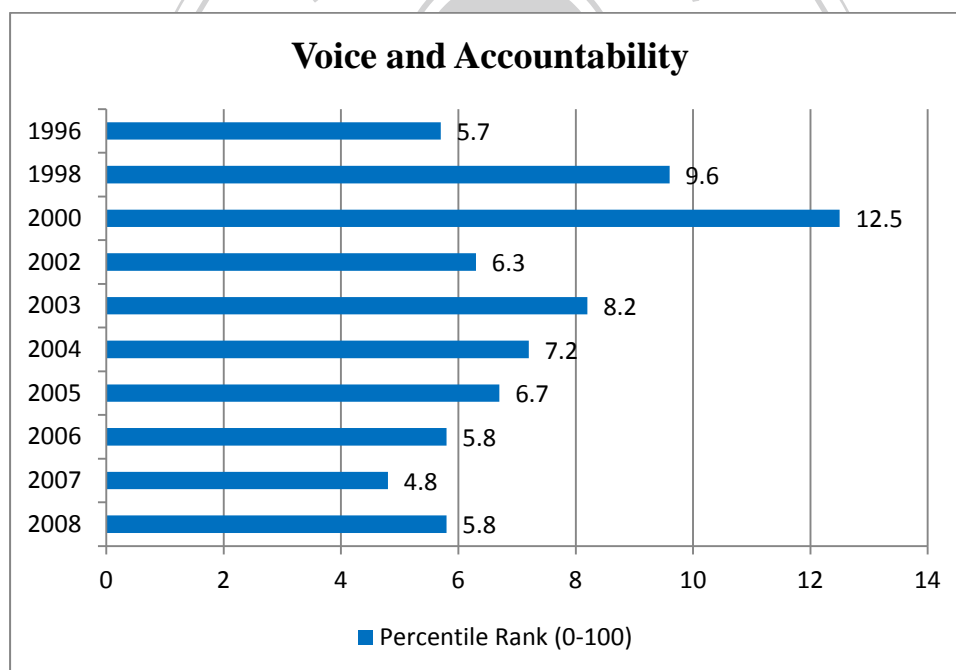
<sup>175</sup> Kaufmann and Kraay, "Governance Indicators: Where Are We, Where Should We Be Going?," 18.

<sup>176</sup> A value of 50 means that 50% of all countries in the sample at the corresponding indicator having a lower rank. For the full data, see Annex.

<sup>177</sup> Kaufmann, Kraay and Mastruzzi, "Governance Matters VIII: Governance Indicators for 1996-2008", The World Bank, "WBI Governance & Anti-Corruption", (

**Voice and Accountability:** The low percentile rank of 5.8 is not as astonishing as the low value may imply. Per definition, this indicator has a strong bias toward democratic values. The fact that 95% of the other countries in the surveys have a higher value tells us that China is definitely not a democracy, keeping in mind that the repressive capacity is essential to a “Leninist political machinery.”<sup>178</sup> The low values are without doubt very low, but a closer look at the data may lead us to reason slightly differently. The data for 2000 for instance has a value of 12.5. In addition, considering the standard error of the sample the values need to be slightly adjusted. What is inescapable is that governance (not only in terms of ‘good governance’) is China’s weak point. It is important to note is that the low values change dramatically if we compare China with the regional average. China’s relative rank jumps from the 5.8 to the 49.9 percentile rank in 2008.

**Table 6: WGI (China): Voice and Accountability - country's percentile rank (0-100)**



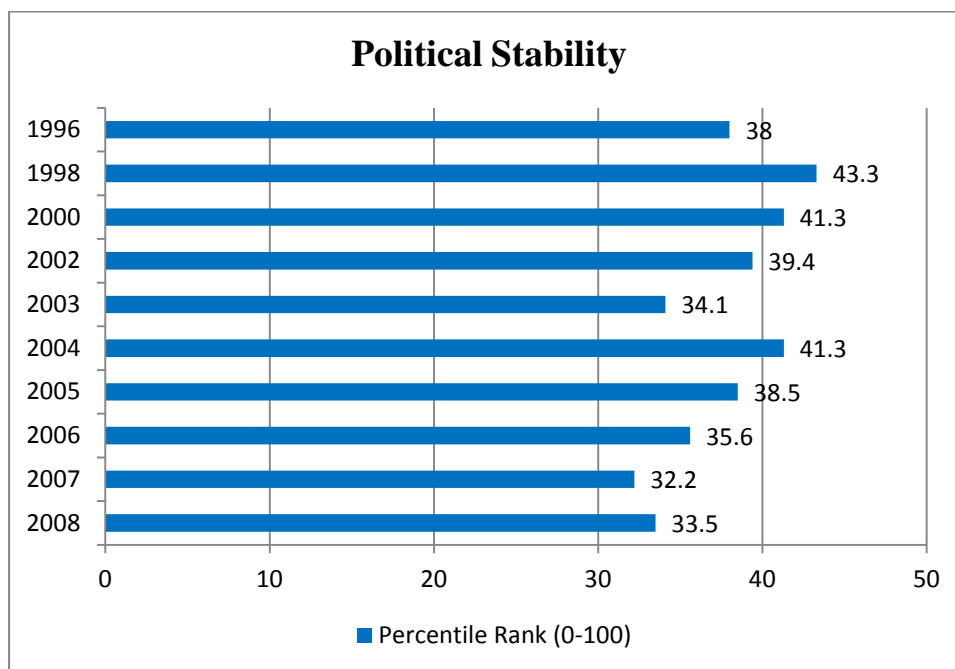
Source: The World Bank (2010): WBI Governance & Anti-Corruption.

**Political Stability:** The data are more or less stable over the time period; values vary from a high of 43.3 (1998) to a low of 32.2 (2006) and 33.5 (2008). The percentile rank of 59.4 (2008) reflects China's best position in the regional average.

<sup>178</sup> Steve Tsang, "Consultative Leninism: China's new political framework," *Journal of Contemporary China*, Vol. 18, No. 62 (2009), 878.



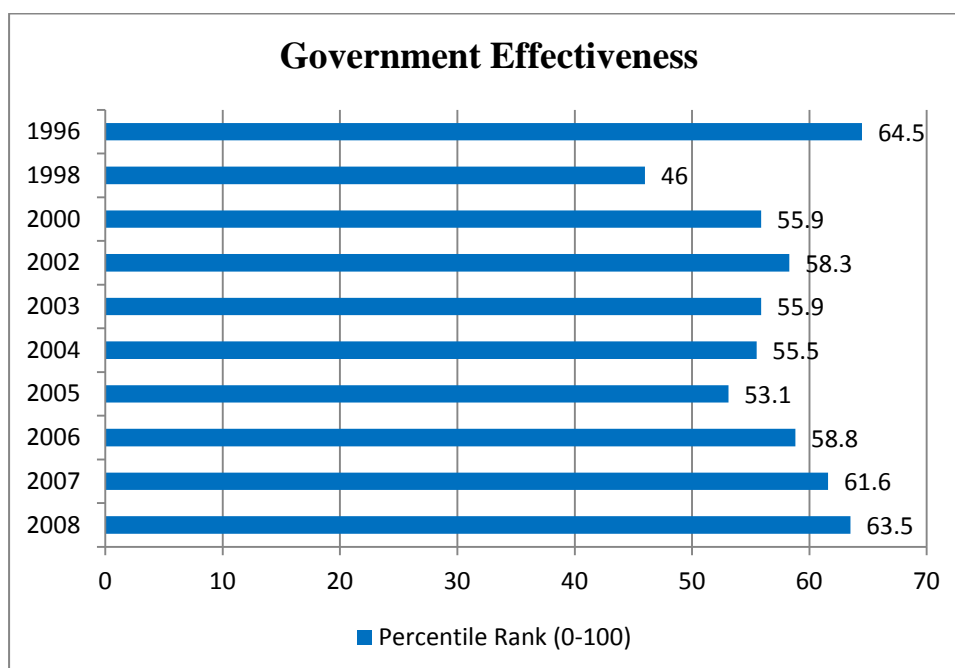
**Table 7: WGI (China): Political Stability - country's percentile rank (0-100)**



Source: The World Bank (2010): WBI Governance & Anti-Corruption.

**Government Effectiveness:** This indicator fluctuates over time. The value dropped between 1996 and 1998 almost 20 points from 64.5 to 46 points. In the following years, China's rank continually improved and by 2008 it reached more or less its starting value. Although we lack an explanation for the massive drop, we may conclude that over time China's record on government effectiveness massively improved at least for the last ten years.

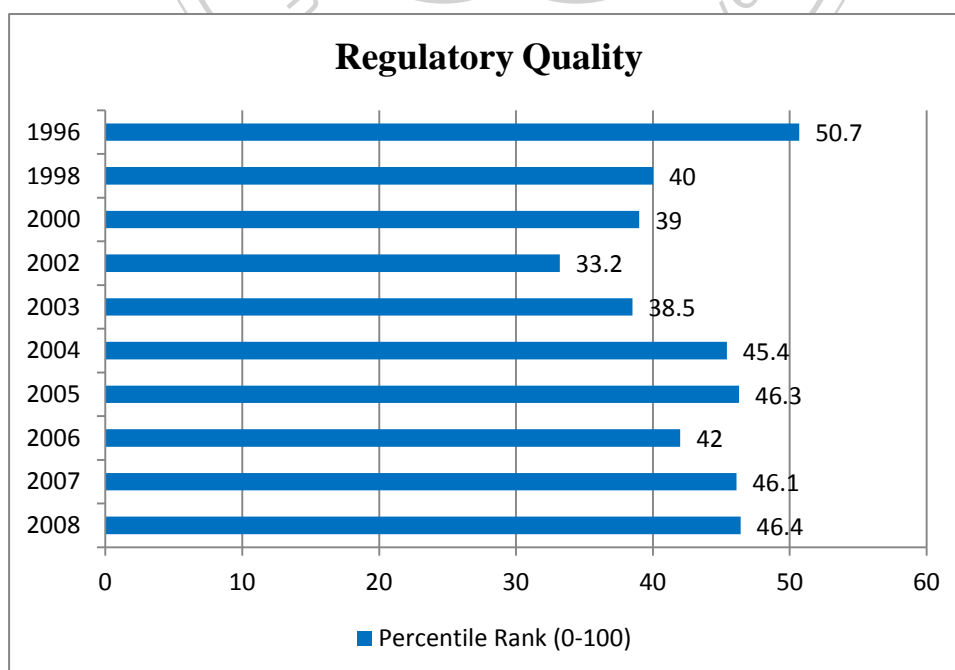
**Table 8: WGI (China): Government Effectiveness - country's percentile rank (0-100)**



Source: The World Bank (2010): WBI Governance & Anti-Corruption.

**Regulatory Quality:** In terms of regulatory quality, the data indicate an interesting development. China started from a relatively good level, reached a low point of 33.2 in 2002, and improved its quality in 2008 continuously to reach 46.4. In the regional comparison, the value of 42.1 points is the lowest of the indicators.

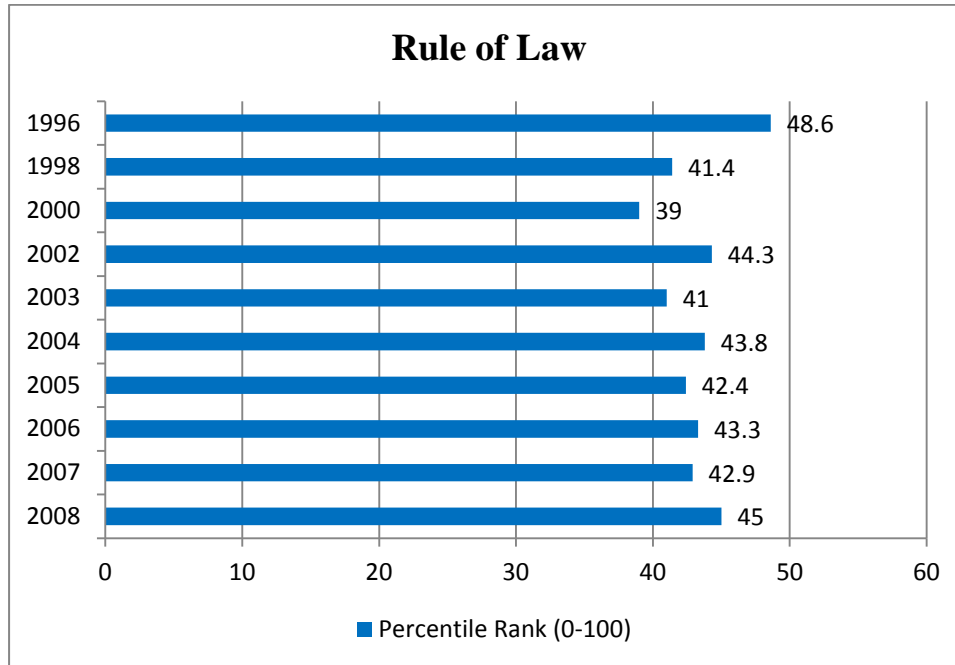
**Table 9: WGI (China): Regulatory Quality - country's percentile rank (0-100)**



Source: The World Bank (2010): WBI Governance & Anti-Corruption.

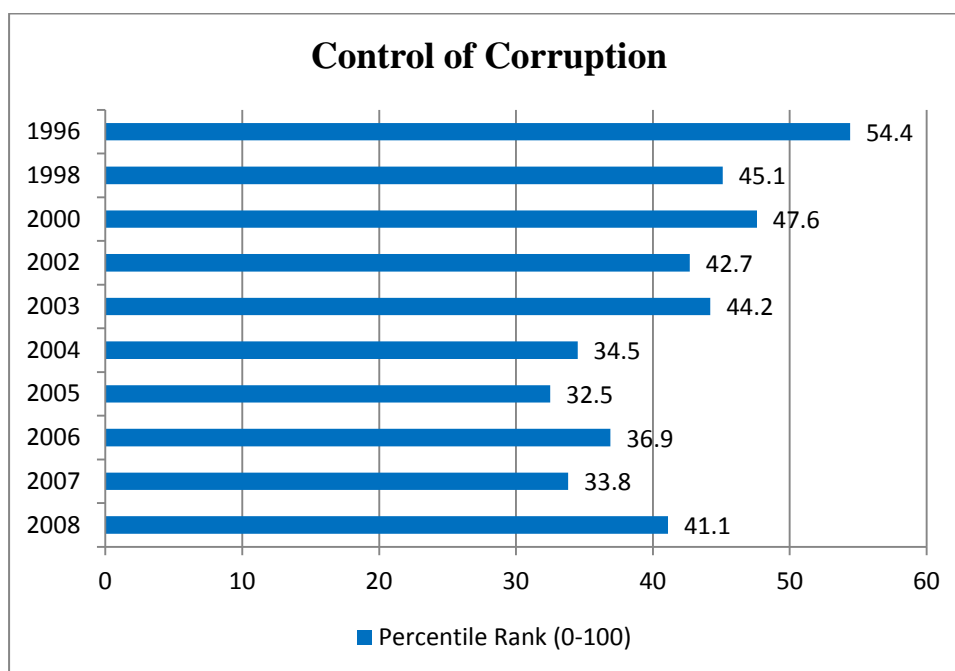
**Rule of Law:** The values indicate that in terms of law enforcement, China was stable and its government was able to guarantee a stable environment for the enforcement of the law.

**Table 10: WGI (China): Rule of Law - country's percentile rank (0-100)**



Source: The World Bank (2010); WBI Governance & Anti-Corruption.

**Control of Corruption:** Maybe the most significant change is the decline in the control of corruption, with a low point of 32.5 in 2005. But one has to keep in mind that the values may underestimate China's effective control of corruption. As a society begins to talk more openly about crimes, it is likely that the rate of these crimes rises because the society has become more aware of it. That means that even if corruption remains at the same level, because the topic has become more public, the value of 'controlling corruption' can be lowered. In the case of China's control of corruption, it is evident that in recent years corruption in China has emerged as one of the 'hot' topics. In the last surveys, the indicator rose slightly to 41.1 (2008).

**Table 11: WGI (China): Control of Corruption - country's percentile rank (0-100)**

Source: The World Bank (2010): WBI Governance & Anti-Corruption.

The data from the WGI allows one to compare the governance indicators with other countries with regional proximity and a similar income level.

**Table 12: Governance Indicators for China in comparison (2008) - country's percentile rank (0-100)**<sup>179</sup>

	Voice and Accountability	Political Stability	Government Effectiveness	Regulatory Quality	Rule of Law	Control of Corruption
China compared to the worldwide average	5.8	33.5	63.5	46.4	45.0	41.1
China compared to the regional average	49.9	59.4	46.5	42.1	52.9	45.1
China compared to the income category average	38.9	39.9	38.1	37.9	37.8	38.5
India	<b>58.7</b>	<b>16.7</b>	53.6	46.9	56.5	44.4
Russia	21.6	23.9	<b>45.0</b>	<b>31.4</b>	<b>19.6</b>	<b>15.5</b>
Italy	76.4	60.3	66.4	78.7	<b>62.2</b>	<b>62.3</b>

Source: The World Bank (2010): WBI Governance & Anti-Corruption

<sup>179</sup> A value of 50 means that 50% of all countries in the sample at the corresponding indicator having a lower rank.

**Regional Average:** The most important difference in the global and regional comparison can be found in the index of voice and accountability. China jumped from a level of 5.8 to 49.9 percentile rank. That means that China's performance in Asia is about average. Half of its neighboring countries' records are even worse than China's. Furthermore, except for government effectiveness, every indicator is much better. The perception of an unfavorable governance performance in China is not really justified when the focus is on Asia.

**Income Category Average**<sup>180</sup>: If we compare China to countries with a similar income average, the results are leveled similarly to the regional average. The levels are between a very small range of a percentile rank of 37.8 and 39. It is important to mention that the value of the voice and accountability is much higher in a global comparison. The difference between a global and an income category average is the highest of all variables.

**Selection of Countries:** **India** has some similarities to China. Like China, it has an immense population and a booming economy rising from a relatively low level; the biggest differences are its political system and history as a colony. It is not surprising that voice and accountability are much higher in India (58.7 compared to 5.8) than in China. But its political stability is considered much lower than in China. The other values differ only slightly. **Russia**, a former socialist state with a much more highly developed economy, has a higher value only in terms of voice and accountability. But with a value of only 21.6, it remains at a relatively low level. Perhaps surprisingly, China's rule of law value is more than double that of Russia's. And finally in **Italy**, a country from the developed world and a member of the European Union, all values are much higher than in China, as might be expected from a highly developed country and a founding member of the European Union.

My reasons for using the WGI to elucidate China's governance record are twofold. On the one hand, the WGI shows clearly where China has its strengths in terms of (good) governance. It has a relatively good governance effectiveness record, including public services and also policy implementation. Its biggest governance deficit is

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<sup>180</sup> The regional average (East Asia) includes the following countries: American Samoa, Brunei, Cambodia, China, Cook Islands, Fiji, Guam, Hong Kong, Indonesia, Kiribati, Laos, Macao, Malaysia, Marshall Islands, Micronesia, Mongolia, Myanmar, Nauru, New Caledonia, Niue, North Korea, Palau, Papua New Guinea, Philippines, Reunion, Samoa, Singapore, Solomon Islands, South Korea, Taiwan, Thailand, Timor-Leste, Tonga, Tuvalu, Vanuatu, Vietnam

undoubtedly related to democratic issues. The WGI can help to “identify the nature of the ‘governance problem’ in a country.”<sup>181</sup> On the other hand, even with the ranking of the WGI, the underlying reasons remain unclear. Devarajan<sup>182</sup> discusses the limitations of measuring governance with the example of Bangladesh. Although the WGI indicates a poor governance capacity, the country was able to improve the Bangladeshis’ social conditions much more than countries with better indexes. He uses this example to show that “governance indicators such as the WGI do not capture the multifaceted ways in which governance affects development in a particular country.”<sup>183</sup>



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<sup>181</sup> Devarajan, "Two Comments on "Governance Indicators: Where are we, where should we be going?" by Daniel Kaufmann and Aart Kraay," 32.

<sup>182</sup> Ibid.

<sup>183</sup> Ibid., 33.

### 3.2.2. The WHO indicator on governance in China in health care

Beside the holistic quantitative approach of the WGI, governance performance in China can be evaluated in regard to specific topics. The World Health Organization has published a report on the 'performance on health governance'.<sup>184</sup> China ranked 144 in its overall performance out of 191 countries. Pei<sup>185</sup> sees this placement as an indicator of China's poor performance on health system governance. He compares the result with other countries and claims that India (112), Indonesia (92) and Bangladesh (88) achieve considerable higher rankings. The problem with such ranking, however, is how it is interpreted. For instance, Pei's interpretation focuses on only two aspects, the 'overall performance' and the performance on 'overall goal attainment.' To that extent, China's ranking seems to lag behind those of other countries. What Pei fails to mention are other measurements in the report: If we evaluate the countries on their performance 'on level of health', China does much better. China (61) ranks much better than India (118), Indonesia (90) and Bangladesh (103), and even higher than some European countries such as Estonia (115), Hungary (105) or even New Zealand (80).<sup>186</sup> In my opinion, it makes little sense to extrapolate from particular and topic-specific rankings such as the WHO's to all aspects of governance. We can conclude, however, that China's health system, produced at the time of the report (2000) a relatively good level of healthcare but has a poor overall evaluation according to the WHO criteria. But to evaluate overall governance performance, the analysis should go further and include, for example, a weighted view based on China's health system policy. And this policy is distinctly different in terms of goals from the index used by the WHO.<sup>187</sup>

Other attempts to evaluate governance in China can be found, for instance by Howell (2004a). He argues that the fact that China is not aid dependent is a strong point in favor of how the governance system works. He buttresses this argument with the 'Human Development Index' where China ranked in 24<sup>th</sup> place out of 90 countries.<sup>188</sup>

<sup>184</sup> World Health Organization, *The World Health Report 2000* (World Health Organization, 2000).

<sup>185</sup> Pei, "China's trapped transition: the limits of developmental autocracy", 172.

<sup>186</sup> World Health Organization, "The World Health Report 2000", 152-155.

<sup>187</sup> J. A. Lauer, C. A. K. Lovell, C. J. L. Murray and D. B. Evans, "World health system performance revisited: the impact of varying the relative importance of health system goals," *BMC Health Services Research*, Vol. 4, No. 19 (2004).

<sup>188</sup> Howell, "Getting to the Roots: Governance Pathologies and Future Prospects", 236.

### 3.2.3. Other projects to measure Governance

The Sustainable Governance Indicators (SGI)<sup>189</sup> project approach to measure governance is different from the WGIs'. Instead of using an aggregation of existing reports and indicators, it relies on an institute's own census with 100 scholars acting as country experts. Another difference from the WGI is its scope. Where the WGI builds indicators for almost every country, the SGI is restricted to OECD countries and therefore excludes China. The motivation for creating the indicator is the thesis that the demand for structural reform will grow. The SGI helps to analyze the need for such reforms and the countries' capacity to respond to it. The SGI has two dimensions: need for reform and reform capacity, with two variables each. The first dimension includes 'status of democracy' and 'economic and policy-specific performance'; the second 'executive capacity' and 'executive accountability.' The variables have some similarities to the WGI but exclude 'stability and lack of violence' and 'regulatory framework.' The results of the SGI, in terms of the relative positions, seem very similar to those of the WGI<sup>190</sup>. The fact that measurement of governance (good governance) with two different methods leads to a very similar result supports the approach of the quantitative measurement of governance. This approach is also used in more state-centered indicators, such as the OECDs 'Government at a Glance,' which explicitly mentions the World Bank's governance indicators as a very good basis for evaluating governance issues.<sup>191</sup>

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<sup>189</sup> Leonard Novy, Martin Brusis, Andrea Kuhn and Daniel Schraad-Tischler, *Sustainable Governance in the OECD - An Overview of Findings Sustainable Governance Indicators 2009* Bertelsmann Stiftung, 2009).

<sup>190</sup> For Instance, Norway has the highest index value for both, the status index and the management index. In the WGI, Norway is at the top of two variables (voice and accountability and rule of law) and has very high values for the other variables. Countries with a lower position in the SGI tend to have a lower value in the WGI.

<sup>191</sup> OECD, *Towards Better Measurement of Government* OECD Working Papers on Public Governance 2007/1 OECD Publishing, 2007), 3.



### 3.3. Issues relating to China's governance performance

This chapter continues to evaluate China's governance performance from different angles. My aim is not to cover every aspect, but rather to focus on some 'hotspots' in China's recent reforms which affect the state's governance capacity.

The chapter follows the definition developed earlier in 0.

Governance is the (1) process of policy development and implementation, as well as (2) the manner in which economic, social and environmental resources are allocated and used. The (3) outcome of this process can be measured in three dimensions of 'Selection and Monitoring', 'Efficiency' and 'Respect'.

#### **The government (process of policy development and implementation)**

Although the concept of governance encompasses much more than the government's governing of the state, the government has still a predominant position. There are several aspects to how the organization of the government influences a country's governance capacity. The five territorial divisions: province level, prefecture level, county level, township level, grassroots level,<sup>192</sup> all have extended power structures and appropriate rules, a situation which has led to the highly fragmented authority of the Chinese state, which has long encouraged a politics of bargaining both between and within institutions at all levels.<sup>193</sup>

The OECD sees no less than a redefinition of the role of the state as the most salient challenge in China<sup>194</sup> and suggests that government activities should concentrate on issues where the market can not accomplish 'national objectives'<sup>195</sup> such as: (1) Increasing public expenditure in education, health and science and technology, (2) consolidating the institutional framework of the newly created SASAC and of other regulatory bodies, (3) redefining the role of the state and (4) rationalizing the administrative organizational structure and improving co-ordination.

#### **Policy making (policy development and implementation)**

<sup>192</sup> OECD, "China in the Global Economy: Governance in China", 16.

<sup>193</sup> Howell, "Getting to the Roots: Governance Pathologies and Future Prospects", 230.

<sup>194</sup> OECD, "China in the Global Economy: Governance in China", 39.

<sup>195</sup> Ibid., 40.

On the one hand, the fragmented structure of China's political system has led to fragmented and contradictory governance processes with regard to policy making. The "central government struggles to enforce national and uniform policies and laws,"<sup>196</sup> yet Saich<sup>197</sup> argued that it is China's size and diversity which make it necessary that China's policies remain flexible.<sup>198</sup> This fragmentation, according to the viewpoint of 'flexibility', causes a localized nature of governance in regard to outcomes and processes.<sup>199</sup> From a governance perspective, policy making in China leads to the conclusion that the process does not embody the primacy of rationality. Furthermore, the lack of "a direct relationship between the problem and the solution, and the policy outcome may not be an actual response to the problem that triggered the decision process."<sup>200</sup> Cheung and Schott (2003) have suggested that one solution is to produce better results in the sense of more coherent policies. To guarantee a more rational policy, which is independent of special interests, the states' capacity has to be raised. This "capacity-building is linked to governance in that one of the conditions for strengthening state institutions, according to most international and regional agencies concerned with public sector reform, is that they should be transparent, accountable, predictable, participatory, efficient and corruption-free."<sup>201</sup> In other words, the authors suggest strengthening China's 'good governance' capacity.

### **External effects (process of policy development and implementation)**

The important issues of external effects are evident in China's opening up of its economic policies; it automatically became increasingly subject to economic and social forces from the outside,<sup>202</sup> from private enterprises to NGOs, along with new pressure to take responsibility on global issues like global warming and the post-Kyoto process.

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<sup>196</sup> Howell, "Governance Matters: Key Challenges and Emerging Tendencies", 16.

<sup>197</sup> Saich, "Governance and Politics of China".

<sup>198</sup> Ibid., 214.

<sup>199</sup> Howell, "Governance Matters: Key Challenges and Emerging Tendencies", 16.

<sup>200</sup> Saich, "Governance and Politics of China", 212.

<sup>201</sup> Cheung and Schott, "Governance and public sector reforms in Asia: paradigms, paradoxes and dilemmas", 4.

<sup>202</sup> Howell, "Governance Matters: Key Challenges and Emerging Tendencies", 16.

### **State-Owned Enterprises (SOEs) (the manner how economic resources are allocated)**

State-owned-enterprises play an important role when it comes to governance in China. Before the reforms, SOEs functioned as an extended arm of the Chinese state. The reform processes separated the state-owned-enterprises from the administration. Since then, the responsibility for a wide range of policies, for example for welfare service policies, has shifted from the state-owned enterprises to local governments.<sup>203</sup> The loss of this power, along with a diversification of ownership systems, has weakened the influence of the Communist Party, and as a consequence, the influence of the state itself. As a follow-up to corporate governance reforms, the separation of management and organization rights became the basis for large SOEs to gain autonomous management.<sup>204</sup> “The main damage inflicted here has been on the capacity of the Party/state to mobilize support, to persuade, and to maintain authority at the microlevel,”<sup>205</sup> which in other words is a loosening of governance capacity in China. The importance of corporate governance reform is related to tackling corruption. According to Wu,<sup>206</sup> corporate reforms in the sense of strengthening the stakeholders’ rights may be one of the most important contributions to curb corruption. Shifting power to local governments is a major reallocation of the governance framework, the outcome of which has to be determined with concrete cases. A general conclusion seems to be inappropriate.

### **Participation (allocation of social resources and the outcome of the process in regard the dimension of ‘selection and monitoring’)**

Participation is not necessarily related to democracy. The main idea is that the field of actors in the process of policy development and implementation is based on a broad basis. The idea of governance, as the definitions show, is that the political arena is not centered on the state. It includes variety actors at different levels, with the state, parties, enterprises and civil society ‘participating’ in the process of governing the state, and formulating and implementing policies. This may be one of the weakest points when it comes to governance in China, as effective “participation also implies

<sup>203</sup> OECD, "China in the Global Economy: Governance in China", 14.

<sup>204</sup> Seung-Wook Baek, "Does China follow "the East Asian development model"?", *Journal of Contemporary Asia*, Vol. 35, No. 4 (2005), 489.

<sup>205</sup> Howell, "Getting to the Roots: Governance Pathologies and Future Prospects", 230.

<sup>206</sup> Wu, "Corporate Governance and Corruption: A Cross-Country Analysis."

the existence of a 'robust civil society' that includes more or less autonomous groups, including NGOs that can 'help to identify people's interests, mobilize public opinion in support of these interests, and organize action accordingly'.<sup>207</sup> China's current political leaders are reluctant to extend political choice, because they fear that an opening in participation would be likely to alter the influence of the central government on local governance. There is a strong preference on the part of the leadership to maintaining the status quo but that "might well pose a more pessimistic scenario of rapidly declining legitimacy and spiraling social unrest."<sup>208</sup>

### **Corruption (outcome, dimension of 'respect')**

Corruption is strongly related to the outcome of the governance framework. Most prominently, good governance epitomizes to a great extent the issue of corruption. The OECD, for instance, sees corruption as one of the most important problems in China today,<sup>209</sup> not only in terms of 'good governance' but also in regard to the instinct of self preservation on the part of the Communist Party. Curbing corruption plays an essential role, as corruption undermines the legitimacy of the party and could affect "the party's ability to survive."<sup>210</sup> Corruption in China may have several causes. For Pei<sup>211</sup> the roots can be found in the economic conditions and also in China's institutions, with their massive incentive system for corruption opportunities. Less radical explanations argue, for instance, that due to the low salary base of civil servants, the high rate of corruption serves as financial compensation<sup>212</sup> for civil servants or is even an incentive to join the civil service in the first place. Corruption is so widespread that a large number of official positions are filled through corruption<sup>213</sup>; people have to pay a superior to be employed. Another factor is that as the economy becomes stronger, more money is involved. Larger financial transactions "undertaken during the course of the restructuring process may lead, in the absence of functioning control mechanism, to the siphoning off of assets; the shift from traditional control to systems of accountability does not pass without frictions; and the utility of material wealth has increased, given the availability of consumer goods and the perception of

<sup>207</sup> Burns, "Governance and public sector reform in the People's Republic of China", 70.

<sup>208</sup> Howell, "Governance Matters: Key Challenges and Emerging Tendencies", 9.

<sup>209</sup> OECD, "China in the Global Economy: Governance in China", 30.

<sup>210</sup> Saich, "Governance and Politics of China", 299.

<sup>211</sup> Pei, "China's trapped transition the limits of developmental autocracy", 212.

<sup>212</sup> OECD, "China in the Global Economy: Governance in China", 68.

<sup>213</sup> *ibid.*, 64, Saich, "Governance and Politics of China", 303.

wealth as a symbol of success.”<sup>214</sup> Solutions to curb corruption are mostly related to the concepts of ‘good governance, particularly concerning improvements in transparency and accountability. The latter implies that efforts for governance reforms include establishing criteria to measure the performance of civil servants,<sup>215</sup> compare them and introduce incentives so that the performance may be enhanced. Other propositions, like government officials authorities being required to regularly rotate their positions, are highly controversial. As previous mentioned, Yang<sup>216</sup> considers job-rotations as a instrument to curb corruption while Pei<sup>217</sup> argues strongly that such systems are a cause of corruption. Such reforms may be a part of a broader solution which requires far-reaching reforms and more ‘checks and balances,’ such as the implementation of audits for leading officials, their offices, and their families which are in programs of job-rotations.<sup>218</sup> Corruption is clearly generally seen as very negative outcome of a governance system and as a strong indicator of an unhealthy governance system. But we should not overestimate corruption in China as one of its main problems. Compared with other countries, China’s record of curbing corruption might not be as bad as the WGI suggests. Moreover, the topic is under scrutiny by the government and the CCP.

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<sup>214</sup> OECD, "China in the Global Economy: Governance in China", 105.

<sup>215</sup> Burns, "Governance and public sector reform in the People's Republic of China", 69.

<sup>216</sup> Yang, "Remaking the Chinese Leviathan: Market Transition and the Politics of Governance in China", 181.

<sup>217</sup> Pei, "China's trapped transition the limits of developmental autocracy", 153.

<sup>218</sup> OECD, "China in the Global Economy: Governance in China", 70.

## 4. Case study – energy policy

The case study in this thesis aim to demonstrate China's governance challenges. The thesis focuses on China's energy policy to demonstrate the strengths and weaknesses of governance in China and the influence of its outcome. When it comes to energy in China, most people think of China's rush for oil around the globe. News that the rising oil prices are caused by China's hunger for energy seems to underline that fact. The reality is different from the common perception. It is neither oil, uranium nor the giant Three Gorges Dam project which are crucial for China's supply with energy. China's solution is coal.

**“No other country relies on coal to the extent that China does, and, in China, no other industry relies on coal to the extent that electricity does.”<sup>219</sup>**

My examination of the issue of energy policy will, therefore, be limited to the aspect of China's governance related to coal-fired power plants. There are several reasons why China's energy policy is a good choice in analyzing its general governance performance. The development and implementation of energy policies in terms of coal offers a perspective on all aspects of governance, but limits the impact of foreign policies. A discussion about oil shifts the main determinant to geo-strategic considerations. Due to the historical importance of coal in China and its immense reserves such impacts are limited. Although China has emerged as one of the major actors in global energy and environmental problems, the “real problem in China today, and the most important driver of the nation's energy and environmental footprint, is not geostrategic ambition, but rather a glaring deficit of governmental regulatory and administrative capacity.”<sup>220</sup> Corporate governance is important when it comes to experimenting with new forms of ownership and deregulations.<sup>221</sup> Global governance became an issue not only since the beginning of the discussions on global warming, but more intensively since China became the world's biggest emitter of carbon

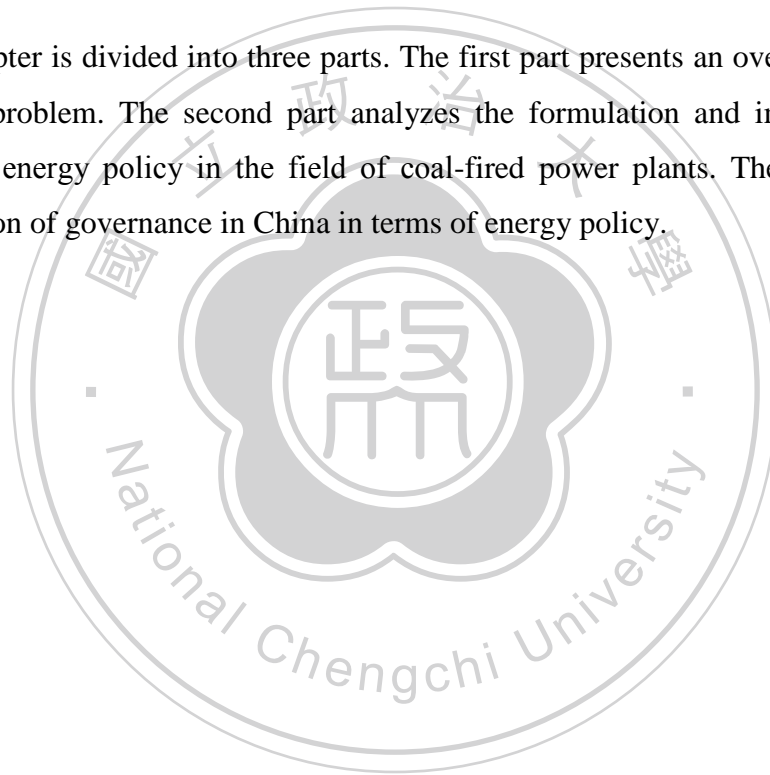
<sup>219</sup> Bing Wang, "An imbalanced development of coal and electricity industries in China," *Energy Policy*, Vol. 35, No. 10 (2007), 4659.

<sup>220</sup> Richard Lester and Edward Steinfeld, "China's Real Energy Crisis," *Harvard Asia Pacific Review*, Vol. 9, No. 1 (2007), 35.

<sup>221</sup> Pei Yee Woo, *China's Electric Power Market: The Rise and Fall of IPPs* Working Paper 45 (Palo Alto, CA: Program on Energy and Sustainable Development, Stanford University, 2005), Yanrui Wu, "Deregulation and growth in China's energy sector: a review of recent development," *Energy Policy*, Vol. 31, No. 13 (2003).

dioxide. Good governance can be applied in new projects. It encompasses several questions such as fuel choice, technology choice, infrastructure development, and environmental protection, which are all highly political. It involves numerous conflicting interests among several stakeholders.<sup>222</sup> All these questions and problems are the essence of the concept of governance. Furthermore, the governance perspective has another advantage in this case. The “blurred distinctions between public and private and governmental and commercial characteristic of the Chinese system as a whole<sup>223</sup>” make the governance perspective an appropriate perspective from which to analyze China’s energy policy. This policy is ideally qualified to analyze China’s governance framework and its outcome.

The chapter is divided into three parts. The first part presents an overview of China’s energy problem. The second part analyzes the formulation and implementation of China’s energy policy in the field of coal-fired power plants. The third part is an evaluation of governance in China in terms of energy policy.



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<sup>222</sup> Lester and Steinfeld, "China's Real Energy Crisis," 35.

<sup>223</sup> *Ibid.*, 35.

#### 4.1. China's energy Problem – the roots of the need for a better energy policy

China's rise in energy usage can be illustrated with some impressive facts:

- In 1973, China consumed 7.9% of the world's primary energy. The percentage jumped to 14.2% by 2005, following the USA as the second biggest energy consumer.<sup>224</sup>
- In only four years (between 2003 and 2006), China raised its electricity production by nearly a third.<sup>225</sup>
- In 2005, the newly installed capacity of electricity production was the equivalent of nearly the entire UK power grid.<sup>226</sup>
- In 2004, 43.41% of the primary energy was used to produce electricity.<sup>227</sup>
- China decreased the number of persons without access to electricity from 245 million in 1979 to around twenty million in 2004.<sup>228</sup>
- China has the world's highest SO<sub>2</sub> emission<sup>229</sup> and overtook the United States in the emission of CO<sub>2</sub> and will 2060 have the world's largest cumulative emissions of CO<sub>2</sub>.<sup>230</sup>
- Since 1989, China remains the world's largest producer and consumer of coal.<sup>231</sup>

These data points show that in recent years, China has experienced an enormous change and expansion of its energy and electricity environment. What were the driving forces behind all these changes?

<sup>224</sup> Edward Steinfeld, "Energy Policy", *China Urbanizes - Consequences, Strategies, and Policies* (eds.) Yusuf and Saich, (Washington D.C.: The International Bank for Reconstruction and Development / The World Bank, 2008), 125.

<sup>225</sup> Ibid., 126.

<sup>226</sup> Lester and Steinfeld, "China's Real Energy Crisis," 36.

<sup>227</sup> Qingyu Zhang, Tian Weili, Wei Yumei and Chen Yingxu, "External costs from electricity generation of China up to 2030 in energy and abatement scenarios," *Energy Policy*, Vol. 35, No. 8 (2007), 4295.

<sup>228</sup> Chi Zhang and Thomas C. Heller, "Reform of the Chinese electric power market: economics and institutions", *The Political Economy of Power Sector Reform: The Experiences of Five Major Developing Countries* (eds.) Victor and Heller, Cambridge University Press, 2007), 76.

<sup>229</sup> Zhang, Weili, Yumei and Yingxu, "External costs from electricity generation of China up to 2030 in energy and abatement scenarios," 4295.

<sup>230</sup> OECD, *OECD Economic Surveys: China 2010* (Paris: OECD, 2010), 22.

<sup>231</sup> C. P. Andrews-Speed, *Energy Policy and Regulation in the People's Republic of China* (The Hague: Kluwer Law International, 2004), 3, Elspeth Thomson, *The Chinese Coal Industry: An Economic History* Routledge, 2003).



#### 4.1.1. Rising demand for primary energy

A comparison of China's energy production and consumption between 1991 and 2005 shows that the consumption of the five different energy products: coal, oil, gas, hydro-electricity and nuclear-electricity had at least doubled.

**Table 13: Energy production and consumption in China between 1991 and 2005**

Primary energy production	1991	2005	Change (in %)
Raw coal (million tons)	1,087.41	2,204.73	102.6
Crude oil (million barrels)	14,099	18,135	28.6
Natural gas (10 <sup>8</sup> m <sup>3</sup> )	161	493	206.2
Hydro (10 <sup>8</sup> KWh)	1,251	3,970	217.3
Nuclear (10 <sup>8</sup> KWh)	0	531	-
Energy consumption	1991	2005	Change (in %)
Raw coal (million tons)	1,104.32	2,167.23	96.3
Crude oil (million barrels)	12,384	32,535	162.7
Natural gas (10 <sup>8</sup> m <sup>3</sup> )	159	479	201.3
Hydro (10 <sup>8</sup> KWh)	1,251	3,970	217.3
Nuclear (10 <sup>8</sup> KWh)	0	531	-

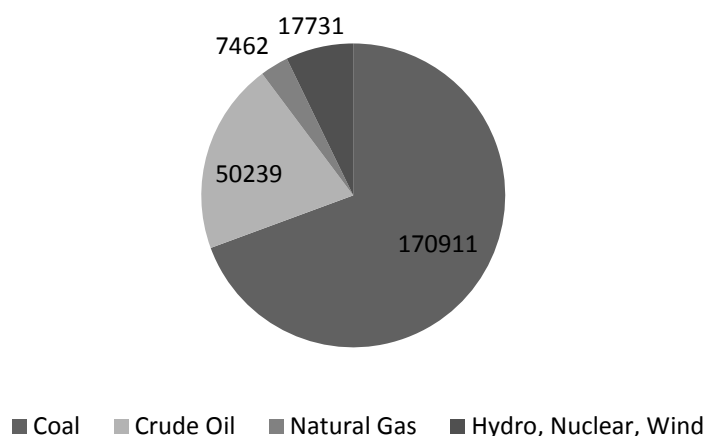
Source: Steinfeld<sup>232</sup>

Domestic production provided the biggest part in response to the additional demand. The production of raw coal doubled in production and consumption. The only exception was crude oil, where the domestic production could not be expanded in tandem with increased demand.

<sup>232</sup> Steinfeld, "Energy Policy", 128.

**Table 14: Consumption of primary energy in China in 2006**

**Consumption of primary energy in China in 2006  
(in 10,000 tons of Standard coal equivalent)**



Source: OECD and IEA 2009<sup>233</sup>

Although China can supply its domestic coal demand with domestic production, its involvement in the international coal market began in the early 1980s. Exports grew rapidly. The overproduction of state-owned mines led them to become involved as coal exporters as a means to survive and selling its overstock. The exports reached a peak in the early 2000s, with exports of more than 80 million tons<sup>234, 235</sup>. Although China became an important market player, compared with the domestic total production and demand, exports account for only a few percentages. Although exports fell until 2008 to 47.4 million tons, China is still the world's 7<sup>th</sup> largest coal export nation (compared with Australia with 252.2Mt).<sup>236</sup> In the early 2000s, imports became increasingly important. The rising production costs in China and lower world market prices for coal imports became more attractive. Until 2008, China imported (45.6Mt) almost the same amount that it exported and rose to the 6<sup>th</sup> largest coal import nations (compared to Japan with 185.6Mt).<sup>237</sup> It is expected that China will turn into a net import country, which will have an important impact on the coal world trade market.

<sup>233</sup> International Energy Agency, *Energy Balances of non-OECD Countries* (Paris: 2009a), International Energy Agency, *Energy Statistics of non-OECD Countries* (Paris: 2009c), OECD, *Eco-Innovation Policies in The People's Republic of China* Environment Directorate, OECD, 2009a), 12.

<sup>234</sup> Throughout this thesis, "tons" refers to "metric tons."

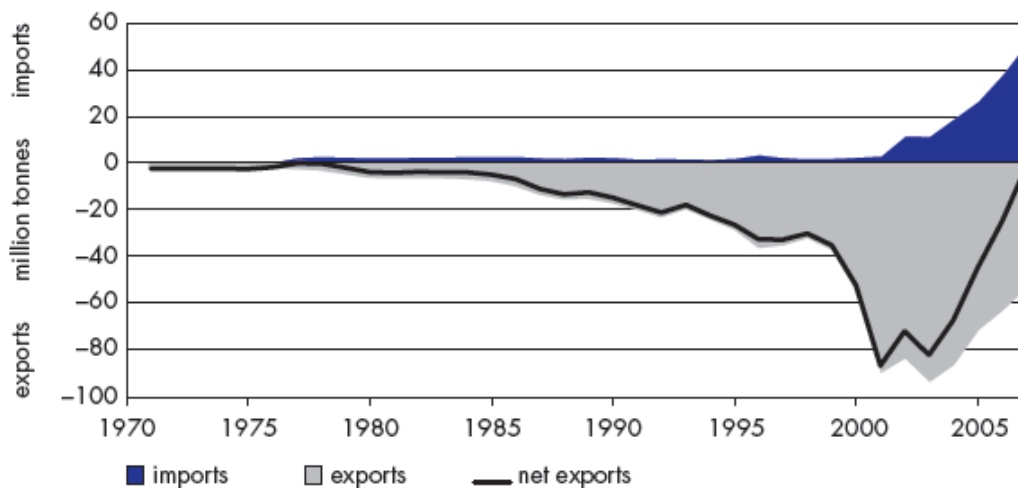
<sup>235</sup> International Energy Agency, *Cleaner Coal in China* (Paris: OECD/IEA, 2008a), 136-138.

<sup>236</sup> International Energy Agency, *Coal Information 2009* (Paris: OECD/IEA, 2009f), 17.

<sup>237</sup> *Ibid.*, 17.

Nevertheless, the share of import and exports on domestic consumption and production will remain marginal.

**Table 15: China's coal imports and exports**



Source: IEA database (World Coal Statistics.ivt available at <http://data.iea.org>).

#### 4.1.2. Determinants of the rising energy demand

The reason for this immense growth cannot be explained simply as stemming from the strong economic growth over this period. Other factors played an important role as well in China. Three aspects should be underscored:

##### **Urban and rural demand for electricity**

Since the initiation of the economic reforms, China's urban population rose from 16.9% (1980) to 27.4% (1990) and then to 42.9% (2005). Although urban population growth is a common phenomenon in Asia, China has witnessed one of the greatest historical immigration movements from rural to urban areas. In absolute numbers, over the last 25 years, at least 350 million people have left rural areas and immigrated to urban areas.<sup>238</sup> The better infrastructure in urban areas, combined with a rapid urbanization, have caused the demand for energy to soar.<sup>239</sup> But at the same time, China has developed the rural areas as well. Seventy percent of China's rural population in 1978 consumed only 13.3% of the national power (27.5 TWh). The

<sup>238</sup> Shahid Yusuf and Kaoru Nabeshima, "Optimizing Urban Development", *"China Urbanizes - Consequences, Strategies, and Policies"* (eds.) Yusuf and Saich, (Washington D.C.: The International Bank for Reconstruction and Development / The World Bank, 2008), 2.

<sup>239</sup> Edward Steinfeld, "Energy Policy", *ibid.*, 125.

development of the rural areas raised this percentage massively but per capita consumption was still only one eighth that of an urban citizen. Nevertheless, between 1992 and 2001, 12 million people every year gained access to electricity.<sup>240</sup>

## Industry

In its development, China's industrial structure has experienced periods of unbalanced energy intensity. Theory predicts that at an early stage of the transition from an agricultural to an industrial production an economy needs more energy to raise its GDP. At a later stage, the ratio should fall. Between 1991 and 2000, the ratio (tons coal equivalent / GDP) fell from 5.12 to 1.40 but remained at this stage during the following years. China needs considerably more energy to produce a unit of GDP than other comparable economies do, and has one of the highest ratios in the world.<sup>241</sup> Steinfeld<sup>242</sup> has shown that China's production for the global market relies on these energy-intense goods which boost China's need for more primary energy and electricity as well.

## Politics

The third peculiarity of China's rising energy demand is deeply rooted in Marxist politics. As Saich<sup>243</sup> notes:

*Marxist lack of concern for the environment and the privileging of production over all other factors. This perspective was enthusiastically adopted by Mao Zedong who saw nature as something to be conquered and tamed and did not appreciate that there were natural limits that resource endowment places on growth. Not only did the development strategy favour rapid exploitation of natural resources to build up the heavy industrial base, but also the associated policy of below-cost pricing for water, coal and other inputs contributed further.*

These three factors do not represent all factors but they do play a decisive role in driving China's rapidly rising energy demand. The following chapters will focus on several aspects of energy production and consumption.

<sup>240</sup> Chi Zhang and Thomas C. Heller, *Reform of the Chinese Electric Power Market: Economics and Institutions* Program on Energy and Sustainable Development (Stanford: Stanford University, 2004), 19.

<sup>241</sup> Steinfeld, "Energy Policy", 127-131.

<sup>242</sup> Ibid.

<sup>243</sup> Saich, "Governance and Politics of China", 294.

### 4.1.3. China's energy production and supply

#### **Fossil primary energy**

##### **Coal**

Coal is China's most important energy resource. Not only has China an immense domestic coal reserve which according to estimates is either 118 billion tons, the third largest,<sup>244</sup> or 188.6 billion tons, the second largest,<sup>245</sup> and about 20% of all known coal reserves. Estimates for coal resources (the potentially accessible coal in the ground) are as high as 334.2, with an additional 686.9 billion tons that could potentially be exploited with advanced technology. Coal reserves are spread across China but mainly in the provinces of Shanxi, Inner Mongolia, Shaanxi and Ningxia, which account for two third of all proven reserves. Obstacles to the coal industry are the difficult circumstances of mining. Most of the reserves cannot be exploited by opencast mining. The average mining depth is expected to be 500 meters in 2010. One third of the proven reserves lie within 300 meters of the surface, about the half between 200 and 600 meters. And the remaining reserves are located at depths of as much as to 1000 meters.<sup>246</sup> The world share of production reflects the highly developed coal mining sector. China's share in world production of coal rose from 18.7% (1973) to 46.2% (2006) and 47.2 in 2008.<sup>247</sup> In 2005, 76.4% of its primary energy production came from coal.<sup>248</sup>

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<sup>244</sup> Andrews-Speed, "Energy Policy and Regulation in the People's Republic of China", 17.

<sup>245</sup> Wang, "An imbalanced development of coal and electricity industries in China," 4961.

<sup>246</sup> International Energy Agency, *Cleaner Coal in China* (Paris: OECD/IAE, 2009d), 37.

<sup>247</sup> International Energy Agency, *Key World Energy Statistic* (Paris: International Energy Agency, 2007), 14, International Energy Agency, "Coal Information 2009".

<sup>248</sup> Steinfeld, "Energy Policy", 140.

**Table 16: Major hard coal producers [Mt]**

	2006	2007	2008e
PR of China	2320.2	2466.4	2761.4
United States	991.5	981.7	1006.6
India	428.2	454.4	489.5
Australia	299.7	323.8	325.4
Russia	310.4	217.9	247.1
Indonesia	195.8	230.2	246.2
South Africa	244.8	247.7	235.8
Kazakhstan	92	93.5	104.4
Poland	95.2	88.3	84.3
Colombia	65.6	69.9	78.6
Ukraine	61.4	58.7	59.3
Vietnam	38.9	42.5	39.9
Canada	29.9	32.8	32.2
DPR of Korea	27.2	23.9	28.6
Germany	23.8	24.2	19.1
Other	84.4	86	85.9
<b>Total</b>	<b>5209</b>	<b>5441.9</b>	<b>5842.3</b>

Source: IEA, Coal Information 2009<sup>249</sup>

The table highlights the importance of the coal industry for China's primary energy supply. In only one year between 2007 and 2008, the expansion of its coal production was equivalent to the world's fourth largest producing country Australia. In only two years between 2006 and 2008, the expansion amounted to more than 440 million tons a year, which is approximately the yearly production capacity of the world's second largest producing country India. Production will have to be expanded even further. The IEA estimates a yearly average growth of 2.7% per year between 2007 and 2030 for Chinese coal demand and 2.5% for the production.<sup>250</sup> This higher rate of demand indicates that China will become a major net coal importer.

<sup>249</sup> International Energy Agency, "Coal Information 2009", 16.

<sup>250</sup> International Energy Agency, *World Energy Outlook 2009* (Paris: OECD/IEA, 2009b), 90.

Coal has always been the main source of energy in China. For a long time coal was the main energy resource for electricity, railroad transportation and heating.<sup>251</sup> To date, its importance remains unchanged for the electric power sector.<sup>252</sup> During the first stages of the development of the coal industries in the PRC, “the township and village-run mines emerged as the major force of coal production.”<sup>253</sup> Coal shortages caused by the exploding demand for energy changed China’s policy, allowing local government, collective and private-owned coal mines to establish new mines.<sup>254</sup> The energy policy focused on promoting the growth of coal production.<sup>255</sup> This policy shift has dramatically shifted the production structure. Although the output of central government owned mines (CGMs) increased from 344 million tons in 1980 to 1.03 billion tons in 2005, the percentage declined from 55% to 47%. The rest was produced by the mushrooming small mines, LGMs, and village, town, and private-owned mines (VTPMs). These mines are small in size but, with 20,000 legal and several tens of thousands of illegal mines, large in number. Wu (2003) estimates that by 1998, the total number of mines in China was as follows:

“In August 1998, there were 94 large state-owned coal companies, 2,500 local government-owned mines and 75,000 township and village-run small mines [...]. By September 2000, however, about 30,000 small mines were forced to close their businesses due to environmental and safety concerns.”<sup>256</sup>

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<sup>251</sup> Thomson, "The Chinese Coal Industry: An Economic History", 1.

<sup>252</sup> Steinfeld, "Energy Policy", 135.

<sup>253</sup> Wu, "Deregulation and growth in China's energy sector: a review of recent development," 1417.

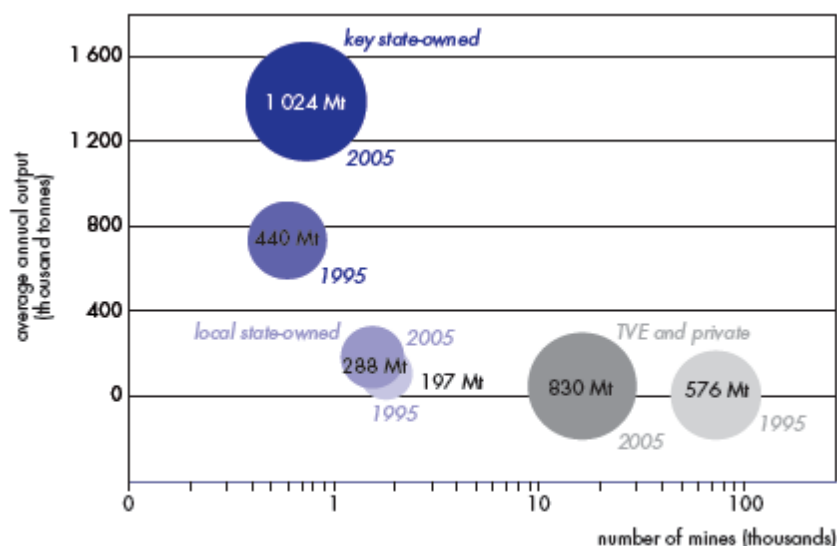
<sup>254</sup> Bing Wang, "An imbalanced development of coal and electricity industries in China," *ibid.* Vol. 35, No. 10 (2007), 4961.

<sup>255</sup> Yanrui Wu, "Deregulation and growth in China's energy sector: a review of recent development," *ibid.* Vol. 31, No. 13 (2003), 1417.

<sup>256</sup> *Ibid.*

It should be noted that illegal mines do not mean that private persons run these mines. Township and village-operated mines can be illegal in that they lack permits from the central-government.

**Table 17: Coal mine categories: number of mines and average production per mine, 1995 and 2005<sup>257</sup>**



Sources: 1995 data: Ye and Zhang (1998); 2005 data: CNCA (2007).

Coal for electricity plants is still the first choice for many municipalities. Due to the demand and the policy target for high economic growth, these conventional coal-fired power plants are built as fast as possible.<sup>258</sup> The question of how the pollution can be reduced involves several aspects. The coal in China is of relatively poor quality and causes an above average pollution, which worsens the pollution problem. The lack of adequate technology to clean the exhaust gases and the high costs contribute considerably to the poor air quality. In 2001, it was estimated that only 5% of the coal burned in Beijing could be considered clean.<sup>259</sup> Proposals to reduce these problems have no common denominator. “[S]ome rue the rapidly growing contribution of China’s coal industry to global climate change, while other express alarm over the efforts of China’s commercial entities to source cleaner liquid fuels from abroad.”<sup>260</sup>

<sup>257</sup> International Energy Agency, "Cleaner Coal in China", 43.

<sup>258</sup> Lester and Steinfeld, "China's Real Energy Crisis," 38.

<sup>259</sup> Saich, "Governance and Politics of China", 295.

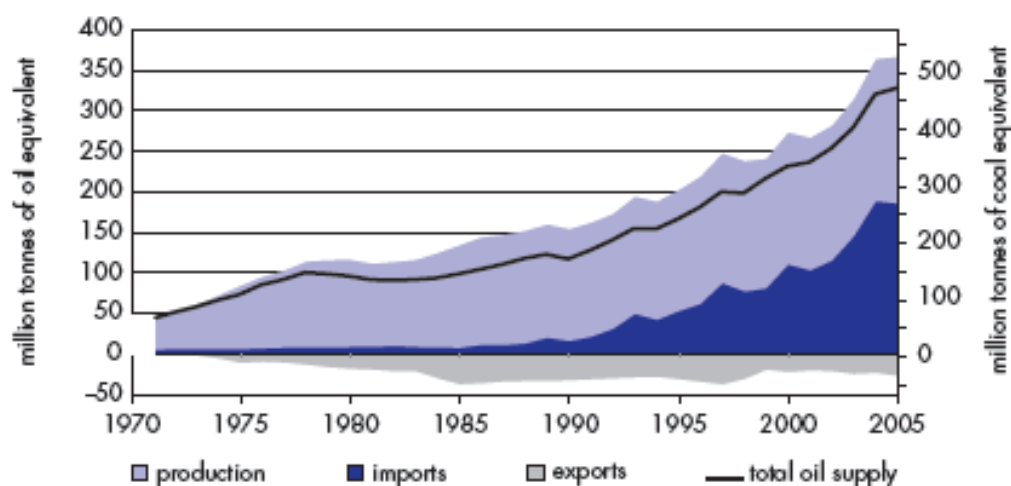
<sup>260</sup> Lester and Steinfeld, "China's Real Energy Crisis," 38.



## Oil

Crude oil domestic production in China is no longer large enough to meet the demand. With a share in 2005 of 12.6% of all primary energy, oil remains at a very low percentage.

**Table 18: Oil production, consumption and trade in China since 1971**



Source: IEA database (wed\_bal.ivt available at <http://data.iea.org>).

Oil in China is important for China's transportation sector but only to a minor extent for its electricity production. The 'oil-challenge' for China is mostly related to its foreign policy. Oil dependence has made China an active player in the world market, in particular in the Middle East, and has left little room for ethical considerations in its resource-based foreign policy.<sup>261</sup> It is likely that external pressure from competing big players will continue to rise. In the past, China was a net oil export country. The rising demand was larger than the domestic enlargement of oil production. In the mid 1990s, China became a net oil importing country. This is reflected in a high level of import dependency which will surpass 50% in 2010. Estimates for 2030 are as high as 75%.<sup>262</sup> Despite its low share in total primary energy supply, as far as the rest of the world is concerned, oil will become an even more significant component of China's energy policy.

<sup>261</sup> David Zweig and Bi Jianhai, "China's Global Hunt for Energy," *Foreign Affairs*, Vol. 84, No. 5 (2005).

<sup>262</sup> International Energy Agency, "Cleaner Coal in China", 78.

## Natural Gas

In the 1990s, China discovered several large natural gas fields, which boosted proven reserves to 1.88 trillion cubic meters and about the same amount of unproven reserves. Natural gas accounts for only 3% of its primary energy consumption but is seen as supplement to its energy mix. Because domestic production started from a very low level, most gas was imported. In April 2007, the 11<sup>th</sup> Five-Year Plan for Energy Development proposed improving the natural gas supply by means of better infrastructure such as stations for importing liquefied natural gas (LNG) and the exploration of Chinese offshore oil. The plan estimated an annual growth rate of 11-13% over the next 15 years, reaching a yearly consumption of 200 billion cubic meters of gas by 2020, of which 100bcm are expected to originate from domestic production.<sup>263</sup>

## Nuclear

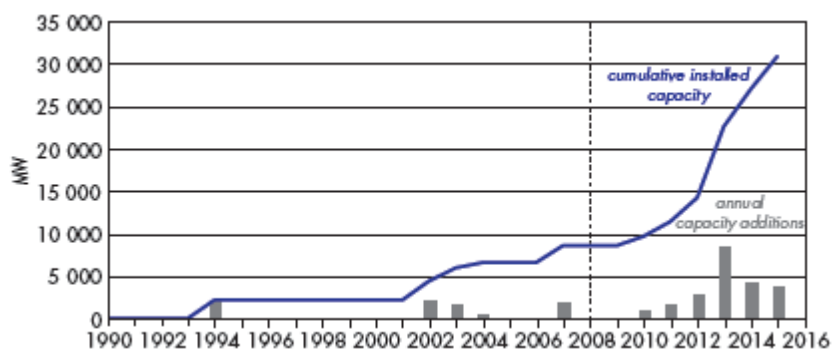
China has ambitious plans to develop its nuclear industry. Even with the plan to add an additional 40 GW capacity by 2020,<sup>264</sup> the total amount of produced electricity by nuclear power plants will only account for 4% of total electricity production.<sup>265</sup> Nuclear energy is not only considerably more expensive than coal, but numerous problems relating to it remain unsolved. Although it does not have the disadvantage of polluting emissions, the nuclear waste problem and complex security challenges are significant and have not yet been solved anywhere in the world. Although China has uranium reserves estimated at 48,800 tons, it depends heavily on uranium imports. Domestic production reached 750 tons in 2007, but China's nuclear power plants' consumption was double that. The new plants' uranium fuel will mostly be imported from Kazakhstan, Australia, Canada and Niger.

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<sup>263</sup> Ibid., 81.

<sup>264</sup> Steinfeld, "Energy Policy", 144.

<sup>265</sup> Lester and Steinfeld, "China's Real Energy Crisis," 37.

**Table 19: Nuclear power generation capacity in China**

Source: IEA (2009)

## Hydropower

Water is today China's most important renewable energy. Although China, with 108 GW, has the world's highest installed capacity in hydro electricity,<sup>266</sup> hydro power production accounts for only a fraction of the total energy production. It is estimated that only 25% of China's potential hydropower is exploited.<sup>267</sup> China's Energy Research Institute estimates a feasible capacity of up to 400 GW.<sup>268</sup> Experience from past mega-projects, notably the Three-Gorges Dam, has demonstrated the immense social costs inherent in such projects, mainly as a result of forced migration and resettlement programs,<sup>269</sup> as well as huge environmental risks.<sup>270</sup>

## Other renewable energies

As a result of falling prices in alternative energy production, in particular wind turbines, clean energy will doubtlessly play an important role in the future. China has an enormous potential to save energy by better insulating buildings and the use of solar energy for heating water. In recent years, several policies have been developed to promote renewable energy, notably the Renewable Energy Law implemented in

<sup>266</sup> International Energy Agency, "Key World Energy Statistic", 19.

<sup>267</sup> Wang, "An imbalanced development of coal and electricity industries in China," 4961.

<sup>268</sup> International Energy Agency, "Cleaner Coal in China", 83.

<sup>269</sup> Michael M. Cernea, "For a new economics of resettlement: a sociological critique of the compensation principle," *International Social Science Journal*, Vol. 55, No. 175 (2003), Paul K. Gellert and Barbara D. Lynch, "Mega-projects as displacements," *International Social Science Journal*, Vol. 55, No. 1 (2003), Gørild Heggelund, "Resettlement Programmes and Environmental Capacity in the Three Gorges Dam Project," *Development and Change*, Vol. 37, No. 1 (2006), Jun Jing, "Rural Resettlement: Past Lessons for the Three Gorges Project," *The China Journal*, No. 38 (1997).

<sup>270</sup> R. Fuggle and W.T. Smith, *Experience with Dams in Water And Energy Resource Development in The People's Republic of China* World Commission on Dams (WCD), 2000).

2005 to subsidize the industry with guaranteed feed-in tariffs for renewable energy power<sup>271</sup> and to lower VAT on small hydro power or wind energy (6% / 8.5% instead of 17%)<sup>272</sup> or the promotion for eco-cities.<sup>273</sup> Although China will play an important role in installing new wind and solar power capacity, the contribution of clean energy sources to the nation's energy demand will be marginal.

**Table 20: Renewable energy targets in China's medium and long-term development plan**<sup>274</sup>

	Total installed capacity/annual production	
	By 2010	By 2020
Wind power	5 GW	30 GW
Solar power	0.3 GW	1.8 GW
Hydropower	190 GW	300 GW
Biomass	5.5 GW	30 GW
Biomass use for fuel	1 million tonnes	50 million tonnes
Biogas use	19 billion cubic metres	44 billion cubic metres
Bio-ethanol use	2 million tonnes	10 million tonnes
Bio-diesel use	0.2 million tonnes	2 million tonnes

Source: NDRC (2007).

## Electricity

Electricity plays a critical role. In 2004, China used 43.4% of all of its primary energy to produce electricity, considerably above the world average.<sup>275</sup> Coal is the single largest contributor to the production of electricity. Although available data are out of date and the electric generating capacity has nearly doubled, the relative share of power plant types has changed not dramatically. According to the National Bureau of Statistics of China, the electricity generated nearly doubled between 2002 and 2007 to 3,271 TWh. More than 80% of all electricity is produced by thermal power.<sup>276</sup> Thermal power became even more important during this period. Between 2002 and 2006, the consumption of coal rose on average more by than 15%, whereas oil (-

<sup>271</sup> International Energy Agency, "Cleaner Coal in China", 83.

<sup>272</sup> OECD, "Eco-Innovation Policies in The People's Republic of China", 15(

<sup>273</sup> Ibid., 26.

<sup>274</sup> International Energy Agency, "Cleaner Coal in China", 87.

<sup>275</sup> Zhang, Weili, Yumei and Yingxu, "External costs from electricity generation of China up to 2030 in energy and abatement scenarios," 4295.

<sup>276</sup> International Energy Agency, *Electricity Information 2009* (Paris: OECD/IEA, 2009e), 206, National Bureau of Statistics of China, *China Statistical Yearbook 2008* 2008), Paul A. Steenhof and Whitman Fulton, "Factors affecting electricity generation in China: Current situation and prospects," *Technological Forecasting and Social Change*, Vol. 74, No. 5 (2007).

22.2%) and gas (-42.6%) had a negative growth in 2006.<sup>277</sup> The installed power generation capacity surpassed 2007 700 GW.<sup>278</sup>

**Table 21: Fuel shares of generating capacity and output in China in 2002**

Power Plant Type	Electric Generating Capacity		Electricity Generated	
	Amount	Share	Amount	Share
Coal-Fire Power	252.1 GW	66.50%	1281 TWh	74.40%
Gas or Oil-Fired	12.1 GW	3.20%	61 TWh	3.60%
Large Hydropower	84.6 GW	22.30%	271 TWh	15.70%
Other Renewable	26.0 GW	6.90%	83 TWh	4.80%
Nuclear Power	3.7 GW	1.00%	25 TWh	1.50%
Total	378.5 GW	100.00%	1721 TWh	100.00%

Source: APERC<sup>279</sup>

Coal has the greatest share of capacity, by a wide margin. Total production reached three-quarters. Even if we take account of the full capacity of the Three-Gorges Dam, which will be completed in 2009 and will raise the hydropower capacity to 18.2 GW,<sup>280</sup> hydropower's share of the total electricity generation remains low. The growth in China's electricity consumption is very impressive. For instance, to meet its additional need for electricity of 102 GW in 2007,<sup>281</sup> China should have built more than five Three-Gorges Dams. The additional demand for electricity production capacity by 2030 is estimated at 1,326 GW, which accounts for 28% of the world's new installed capacity.<sup>282</sup>

<sup>277</sup> OECD, *China - Defining the Boundary Between the Market and the State* OECD Reviews of Regulatory Reforms (Paris: OECD, 2009b), 244.

<sup>278</sup> *Ibid.*, 235.

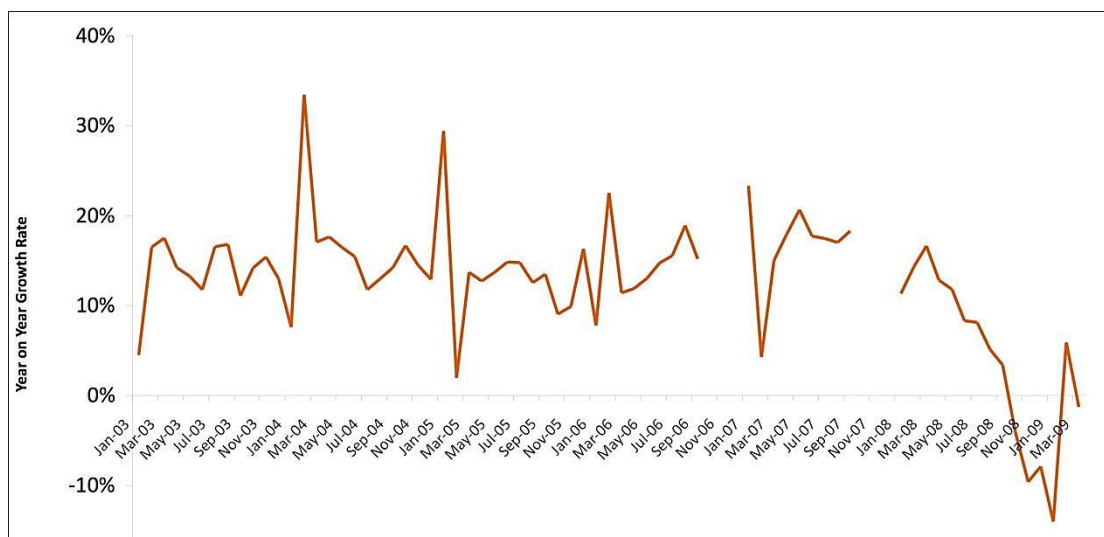
<sup>279</sup> APERC (Asia Pacific Energy Research Centre), *Energy in China: Transportation, Electric Power, and Fuel Markets* (Tokyo: Institute of Energy Economics, 2004), 54.

<sup>280</sup> Hongliang Yang, *Overview of the Chinese Electricity Industry and its Current Uses* 2006), 5.

<sup>281</sup> Steinfeld, "Energy Policy", 126.

<sup>282</sup> International Energy Agency, "World Energy Outlook 2009", 102.

**Table 22: China's power generation growth rates January 2003 – April 2009**



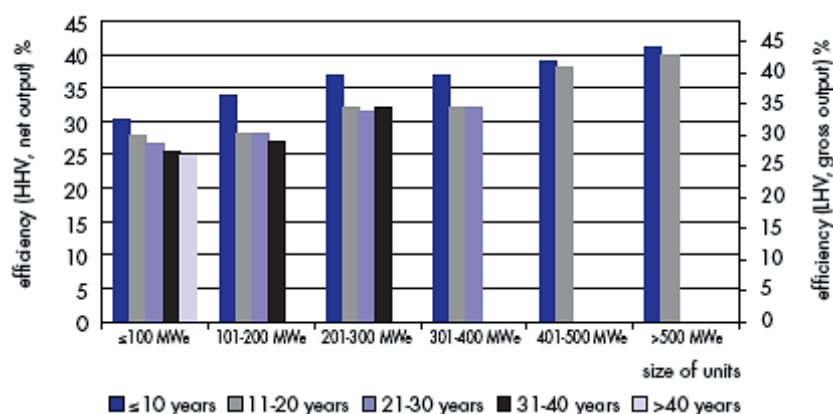
Source: R. K. Morse (2009)<sup>283</sup>

It is clear that China needs other resources in addition to hydro. Most of the new projects are coal-fired power plants. They are not only built very quickly, but in their simplest (but dirtiest) form of pulverized coal power generation, at about 3.5 U.S. cents per KWh, are also the cheapest of all alternatives.<sup>284</sup> In order to optimize its cost structure and environmental footprint, newer coal fired power plants are much more efficient and need less coal for producing the same unit of electricity.

<sup>283</sup> Richard K. Morse, *A drop in Chinese electricity production, for now* Program on Energy and Sustainable Development, Stanford University, (2009).

<sup>284</sup> Yang, "Overview of the Chinese Electricity Industry and its Current Uses", 38(

**Table 23: Average efficiencies of coal-fired power plants in China by age and unit size**



Source: IEA (2009)<sup>285</sup>

After the founding of the PRC in 1949, the Communist Party considered electricity production to be an important policy and nationalized its production.<sup>286</sup> The initial fast development of electricity production slowed down when China broke diplomatic ties with the Soviet Union in 1960. Russian technological assistance was discontinued and China was forced to build low-technology and small-sized power plants under central planning.<sup>287</sup> Today's structure is a result of these events. The new reforms initiated in the late 1980s placed a strong emphasis on the development of the electricity sector.<sup>288</sup> For example, until 1985 ownership of generation was the central government's monopoly. Reforms allowed local governments, SOEs and to some extent even private investors to develop their own generating facilities.<sup>289</sup> The liberalization continued in 2003 as the government announced its plan to develop regional wholesale power markets and an efficient exchange of power between regions.<sup>290</sup> The fruits of the reform included a dramatic growth in the power sector where, for instance, between 2004-2006 generating-capacity grew by nearly one third.<sup>291</sup> But the costs of this fast growth were immense. The coal-fired power plants are extremely dirty and produce vast amounts of health damaging emissions (SO<sub>2</sub>,

<sup>285</sup> International Energy Agency, *Energy Efficiency Indicators for Public Electricity Production from Fossil Fuels* (Paris: OECD/IEA, 2008b), 51.

<sup>286</sup> Zhang and Heller, "Reform of the Chinese Electric Power Market: Economics and Institutions", 9(

<sup>287</sup> Zhang and Heller, "Reform of the Chinese electric power market: economics and institutions", 85.

<sup>288</sup> Wu, "Deregulation and growth in China's energy sector: a review of recent development," 1417.

<sup>289</sup> Xiaochun Zhang and John E. Parsons, *Market Power and Electricity Market Reform in Northeast China* MIT Center for Energy and Environmental Policy Research, (2008), 1.

<sup>290</sup> Ibid., 2.

<sup>291</sup> Lester and Steinfeld, "China's Real Energy Crisis," 35.

NO<sub>2</sub>, and PM10) and cause a number of other external costs.<sup>292</sup> However, emission free production such as the hydropower from the Three-Gorges Dam has social, political and environmental consequences that help to “create enormous challenges for a government bent on rapid economic development at any cost.”<sup>293</sup>

#### 4.2. Coal fired power plants and energy policy in the governance theory framework

In this chapter, I focus on the problem of China’s energy supply and its implications for energy policy and governance issues. As I demonstrated earlier, China is heavily dependent on coal as primary energy source which is also the main energy source for producing electricity. Electricity itself is one of the crucial factors for China’s further economic growth. Consequently, I will turn my attention to coal-fired power plants and related issues. This chapter follows two major concerns: on the one hand, energy policy in general in terms of development and implementation and the allocation of resources and, on the other hand, the outcome of this process.

The chapter follows the definition developed earlier in 0.

Governance is the (1) process of policy development and implementation, as well as (2) the manner in which economic, social and environmental resources are allocated and used. The (3) outcome of this process can be measured in three dimensions of ‘Selection and Monitoring’, ‘Efficiency’ and ‘Respect’.

<sup>292</sup> Zhang, Weili, Yumei and Yingxu, "External costs from electricity generation of China up to 2030 in energy and abatement scenarios," 4298.

<sup>293</sup> Howell, "Getting to the Roots: Governance Pathologies and Future Prospects", 227.



#### 4.2.1. The policy development and implementation process

Ding<sup>294</sup> proposes three approaches to explain policy implementation problems in China. The 'factional approach' focuses on the top of Chinese politics. It argues that a defining characteristic of the system as a whole is its fragmentation and disjointedness. Policy development mainly depends on the outcome of factional quarrels. The provincialism approach suggests that the central government has vision of future development in competition with the provinces' own vision. The third, 'national integration approach,' sees China's centralization as a means to strengthen national unity.

In cases where the central government considers a policy not as a major objective, the policy is locally often not correctly implemented.<sup>295</sup> The problems are acute when it comes to coal fired power plants and their environmental impact. In terms of environmental protection, legislation is considered as sufficient but its implementation as inadequate, a fact that is reflected in the large number of violations of environmental laws and weak law enforcement.<sup>296</sup> The shortcomings of governmental institutions are increasingly remedied by citizens actions that play a "crucial role in improving pollution regulation and controlling severe pollution."<sup>297</sup>

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<sup>294</sup> Xiaojiong Ding, "Policy Implementation in Contemporary China: the making of converted schools," *Journal of Contemporary China*, Vol. 19, No. 64 (2010).

<sup>295</sup> *Ibid.*, 360.

<sup>296</sup> Benjamin van Rooij, "The People vs. Pollution: understanding citizen action against pollution in China," *ibid.*No. 63, 55.

<sup>297</sup> *Ibid.*, 57.

### **Struggle in energy policy development; economic preferences still dominates**

According to Steinfeld,<sup>298</sup> China's energy policy is like those of other large consuming countries: confused and uncoordinated. Nevertheless, the energy policy is no exception in its institutional reform efforts. Most significant are the central administration reorganizations in 1998, which focused on improving efficiency and strengthening the government's regulatory role by relinquishing it from business operations.<sup>299</sup> For the coal-based electricity industry, one of the most significant changes in recent years has been the coal price liberalization, which had two effects: the government reduced its subsidies to the coal sector and the management of producing plants began to implement more energy efficient methods.<sup>300</sup> The success of the reforms is reflected the industry's profitability. From 1980 to 2000, the coal industry faced financial losses of up to 6 billion Yuan (1991) annually. The turnaround happened in 2003, with a gain of 14 billion, which rose to 56 billion Yuan in 2005.<sup>301</sup> Since the reforms were launched, most power plants belong officially to one of five major state-owned national energy corporations, which are enterprise groups that answer to the central government, at least in theory.<sup>302</sup> In practice, however, most of decisions are made locally. The reforms in the electricity sector have had similar. After State Power of China was broken up into several regional companies,<sup>303</sup> it became a profitable business.

The future of China's energy policy will involve meeting several challenges. "Coal, for example, appears inexpensive in the near term for China. But if coal is burned without environmental cleanup mechanisms, flue gas desulfurization systems, and related technologies, it imposes a costly public health toll."<sup>304</sup> Policy development has to find answers to this problem. However, energy policy cannot be viewed in isolation. Steinfeld notes that energy policy is greatly influenced by national industrial policy and macroeconomic growth policy; even non-economic policies like environmental regulatory policy and health care policy are more or less strongly related to energy

<sup>298</sup> Steinfeld, "Energy Policy", 144.

<sup>299</sup> Wu, "Deregulation and growth in China's energy sector: a review of recent development," 1417.

<sup>300</sup> Ibid., 1419.

<sup>301</sup> Bing Wang, "An imbalanced development of coal and electricity industries in China," *ibid.* Vol. 35, No. 10 (2007), 4964.

<sup>302</sup> Lester and Steinfeld, "China's Real Energy Crisis," 36.

<sup>303</sup> Woo, "China's Electric Power Market: The Rise and Fall of IPPs", 2(

<sup>304</sup> Steinfeld, "Energy Policy", 134.

policy and finally to the underlying economic policy.<sup>305</sup> To be successful, energy proposals have to overcome several hurdles: “(1) associated benefits of the proposed decision for other policy problems; (2) presence of a consistent ‘issue champion’; (3) strength of mobilized and united ‘veto players’, i.e. those political actors who have the ability to decline a choice being made; (4) vertical and horizontal support; and (5) clear policy preferences of the leadership.”<sup>306</sup> A further important aspect of energy policy is that it significantly affects decisions in the domain of economic growth and is often in conflict with local circumstances.<sup>307</sup> All these aspects have a strongly negative influence on governance issues in the coal industry where overlapping interests exist.

That is particularly the case for energy decisions. Kong<sup>308</sup> speaks of a ‘leadership vacuum’ in China’s energy policy where “decisions are driven by projects promoted by localities or industries rather than being guided by a coherent national energy policy.”

A wide range of actors and institutions are involved in China’s energy policymaking and implementation process. Policy development is not limited to the central government or to the party; the process is complex and the involved parties are characterized more by an “obscurity that revolves around the modes of interaction amongst them<sup>309</sup>” than by a transparent arrangement. The result is a consensual form of decision making for formulating energy policies which results in a lengthy process “to gain support of all the related ministries” and has an undesirable result of “regulations that are often outdated by the time of their final approval.”<sup>310</sup> The struggles in the process of policy development have a direct impact on the process of policy implementation.

Possibly the most important characterization of the energy policy development is that since the economic reforms were first launched, China’s energy sector has largely

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<sup>305</sup> Ibid., 145.

<sup>306</sup> Bo Kong, "China's Energy Decision-Making: becoming more like the United States?," *Journal of Contemporary China*, Vol. 18, No. 62 (2009), 790.

<sup>307</sup> Ibid., 790.

<sup>308</sup> Ibid.

<sup>309</sup> Michal Meidan, Philip Andrews-Speed and Ma Xin, "Shaping China's Energy Policy: actors and processes," *ibid.*No. 61, 595.

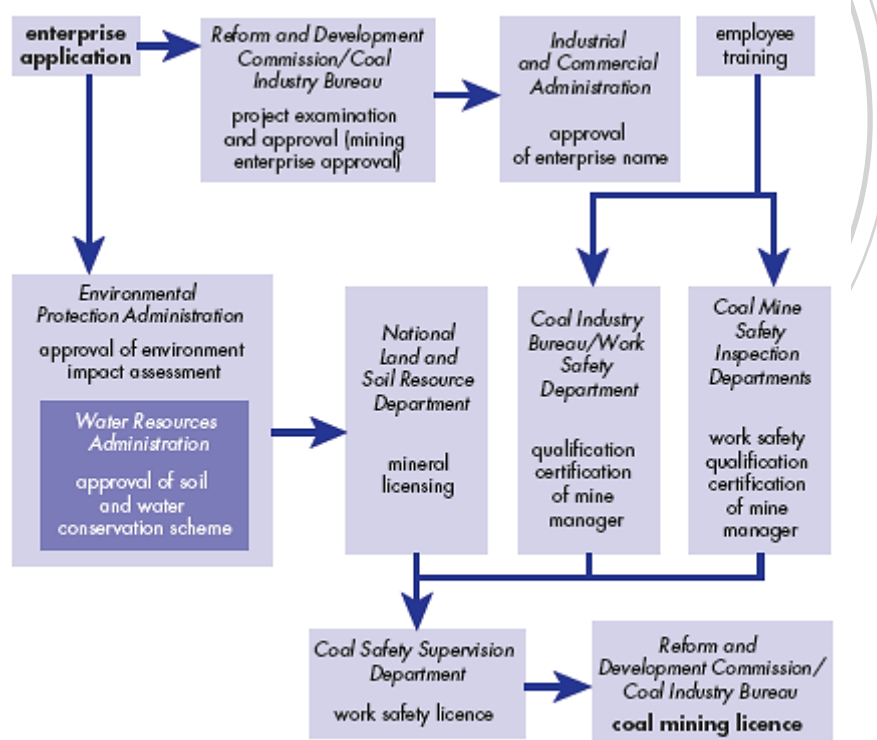
<sup>310</sup> Ibid., 592.

been driven by wider economic concerns, priorities and policies.<sup>311</sup> The political and ideological vision may in recent years have undergone a change. Some authors have observed a deemphasis of economic priorities in favor of “social equity and a more balanced growth pattern, as manifested by slogans such as ‘the Moderately Well-off Society’, the ‘Harmonious Society’ and ‘Scientific Development’.”<sup>312</sup>

### Struggle in energy policy implementation

Coal fired power plants require a long chain of national and provincial policy implementation. The example of licensing coal mines demonstrates the different layers of agencies involved in the process. Each of them has a critical position not only as veto power for approval. Their importance can be seen even more in the implementation of China’s main objective of energy policy: “supply security, economic efficiency, social equity, environmental protection.”<sup>313</sup>

**Table 24: Coal mine licensing procedures**<sup>314</sup>



Source: CCI.

<sup>311</sup> Ibid., 606.

<sup>312</sup> Ibid., 594.

<sup>313</sup> Ibid., 594.

<sup>314</sup> International Energy Agency, "Cleaner Coal in China", 63.

The aim of the 2008 government reforms was also a better policy implementation capacity. The reforms introduced five super-ministries. One of them is the Ministry of Environment, which replaced the State Environmental Protection Agency.<sup>315</sup> Early research on these reforms indicates that energy policy implementation has not yet improved. It has been suggested that the National Development and Reform Commission (NDRC) still has a dominant position in the implementation process, which prevents a more equal consideration of issues not directly related to economic interests. The NDRC has a very “powerful authority to record, verify, and approve a variety of investment projects. This allows the NDRC to dominate the right to review, approve, and finance grandiose infrastructure investment projects.”<sup>316</sup> In terms of energy policy, for example, one of the key powers of the NDRC is to approve coal mine licenses and new coal fired plants. Its approval is needed “because without a filing confirmation letter from the NDRC, projects could not be started.”<sup>317</sup>

Lieberthal and Oksenberg’s<sup>318</sup> study of large energy projects in China analyzed the policy-making process and its implications for their implementation. They concluded that governance for national policies can be seen as a bargaining process in central-provincial relations where “individual bureaucratic units have the capacity to pursue strategies which reduce control by superiors.”<sup>319</sup> That makes it difficult for the central government to implement a common policy. Steinfeld<sup>320</sup> has interpreted this conclusion, twenty years after Lieberthal and Oksenberg’s study, as modularized power arrangements. His conclusion is that for a country like China with a highly varied geographic, demographic, and development landscape, modularized power arrangements may be a suitable model. The governance system produces some striking outcomes. On the national level, the attempt to impose a national tax on high-sulfur coal, which accounts for a vast amount of pollution, is one of the new impulses of the central-level. In the run-up to the Olympic Games in 2008, for example, Beijing established a coal-free zone. Regional programs were established for pollution-rights

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<sup>315</sup> Yukyung Yeo, "Remaking the Chinese State and the Nature of Economic Governance? The early appraisal of the 2008 'super-ministry' reform," *Journal of Contemporary China*, Vol. 18, No. 62 (2009), 731-732.

<sup>316</sup> *Ibid.*, 733.

<sup>317</sup> *Ibid.*, 736.

<sup>318</sup> Kenneth Lieberthal and Michel Oksenberg, *Policy Making in China: Leaders, Structures, and Processes* (Princeton University Press, 1988).

<sup>319</sup> *Ibid.*, 389.

<sup>320</sup> Steinfeld, "Energy Policy", 145.

trading programs and some municipalities shifted public buses to cleaner burning fuels.<sup>321</sup> Like the energy policy case, energy governance was not decided at a higher level and led to fragmented results. The shift of power to lower-level institutions mentioned above can be attributed in particular to the understaffing of central-level organizations. The decision making power has shifted to an ad hoc basis and primarily to grassroots actors; unsurprisingly, these actors' incentives to follow the policies formulated by the center are weak. They do not follow a 'big picture' but rather the needs of local governments, local fuel and power producers and local industrial concerns.<sup>322</sup> A good example is the discrepancy between allotted power generating capacity and the actual installed capacity. About one fourth of the 440 gigawatts of generating power capacity is derived from 'illegal' power plants, "plants that never received construction approval by the responsible central government agency."<sup>323</sup> Besides the understaffing of central-agencies, local governments also face a conflict of goals. Their work is judged mainly in terms of economic growth. The actors involved in power governance systems have strong incentives to fulfill these expectations and create even greater pressure for more, and cheaper, electricity. In addition, energy projects are mainly financed through two channels. Loans from state banks and investments from municipal or provincial energy development corporations support the governance system to channel its decision making to a very quick construction approval, to "get the plants online as quickly as possible."<sup>324</sup>

Besides the governance privilege actors on lower levels, the overall number of actors exercising "de facto decision-making power"<sup>325</sup> is large and hard to analyze properly. For instance, Lo and Leung<sup>326</sup> have observed that the Municipal People's Congress (MPC) and the Municipal People's Political Consultative Conference (MPPCC) together with the mass media have become important sources of policy input. In a case study of public participation in environmental issues in Guangzhou, the authors concluded that the opening of governance structures to non-state actors may be an effective way to support government policy.

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<sup>321</sup> Ibid., 145.

<sup>322</sup> Lester and Steinfeld, "China's Real Energy Crisis," 35.

<sup>323</sup> Ibid., 36.

<sup>324</sup> Ibid., 36.

<sup>325</sup> Ibid., 38.

<sup>326</sup> Carlos Wing Hung Lo and Sai Wing Leung, "Environmental Agency and Public Opinion in Guangzhou: The Limits of a Popular Approach to Environmental Governance," *The China Quarterly*, No. 163 (2000), 703.

The enormous demand for electricity and the limits of accurate planning and construction of new power plants has led to another remarkable development. An opt-out from the governance process can be observed among corporations and major energy consumers. Instead of trying to participate in the process, they have taken self help steps by installing their own diesel-fired generators. It is virtually impossible to estimate how much petrol will be used this way to produce electricity. According to Lester and Steinfeld<sup>327</sup> “Generator manufacturers estimate that ten percent of China’s total electric power consumption is supplied by these ‘within-the-fence’ units.” Once installed, the political instruments will fail to regulate these facilities.

To summarize, energy and related environmental policies are constrained by several factors, including: “the vague and contradictory nature of the relevant laws and regulations; the nature of economic incentives for local government officials to prioritize economic growth at the expense of energy efficiency and the environment; the weakness of formal legal mechanisms; the close relationship between business and government; and the deep-rooted belief across society of the need for and desirability of economic advancement.”<sup>328</sup>

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<sup>327</sup> Lester and Steinfeld, "China's Real Energy Crisis," 37.

<sup>328</sup> Meidan, Andrews-Speed and Xin, "Shaping China's Energy Policy: actors and processes," 615.

#### 4.2.2. Allocation of economic, social and environmental resources

One way governance is defined is the manner in which economic, social and environmental resources are allocated and used. Since coal-fired power plants are relevant to a wide range of governance issues, the following analysis of the three ‘resource-dimensions’ represent a selection of relevant aspects.

##### **Use of economic resources**

There are two aspects to studying the use and allocation of economic resources in the context of coal-fired power plants. Energy is the main economic resource, with an input (primary energy) and an output (electricity). First, power plants mostly rely on domestic coal supplied from the “main coal mines in the north and northwest, while energy demand is greatest in the eastern and south-eastern coastal areas.”<sup>329</sup> The negative impact of using coal for electricity is found both in coal mining and in burning coal in the power plants for generating electricity. Since electricity is most cost effectively produced near the electricity demand, the negative impact is not limited to the mining location. Nevertheless, the positive economic impact is hard to determine, as mining operations have virtually no demand for employees with high qualifications and do not contribute to developing an advanced economy. The use of economic resources has some several shortcomings which at least has a limited global impact. The exception is, of course, the emission of CO<sub>2</sub> during coal burning, which falls outside the scope of this discussion.

Second, on the output side, since the breakdown of the central government’s monopoly, its supply and distribution of electricity has ended. Ownership of power plants is mostly state controlled. But attempts to create an inter-provincial wholesale market have shown initial results,<sup>330</sup> including the privatization of SOEs and opening the market to international corporations. To protect the periphery, wholesale tariffs for electricity have been politically set below the market value, but this has had not influence on other issues such as corporate governance, environmental regulation or end-user price.<sup>331</sup>

<sup>329</sup> International Energy Agency, "Cleaner Coal in China", 47.

<sup>330</sup> Zhang and Parsons, "Market Power and Electricity Market Reform in Northeast China", (

<sup>331</sup> Zhang and Heller, "Reform of the Chinese Electric Power Market: Economics and Institutions", 86(



### Use of social resources

Perhaps the most prominent social issues of coal-fired power plants is their negative impact on environment and health. As previously discussed, domestic coal mines have a complex ownership structure with poor governmental control and a liability to corruption. The safety record on coal mines is a good illustration of the use of social resources. Pei<sup>332</sup> uses it as a key argument for his pessimistic outlook for China's further (social) development.

China's coal mine safety record is doubtlessly one of the world's worst and accounts for "80% of the total death in coal mine accidents worldwide."<sup>333</sup> Its fatality rate per million metric tons of coal is considerably higher than, for example, India's which was able to reduce its rate to 4% of China's in 2006.<sup>334</sup> Small and medium mines are mostly in the spotlight for improving the safety record. They use, on the one hand, more risky mining methods like room-and-pillar or shortwall compared to larger mines that use the safer longwall mining method. On the other hand, corruption is a severe problem in the coal-mining industry and especially within the smaller mines. Smaller coal mines are also considerably less mechanized (45% for small compared to 83% for the large key state-owned mines).<sup>335</sup>

**Table 25: Coal mining fatalities: annual total and rate per million tons of coal mined, 1949-2006**<sup>336</sup>

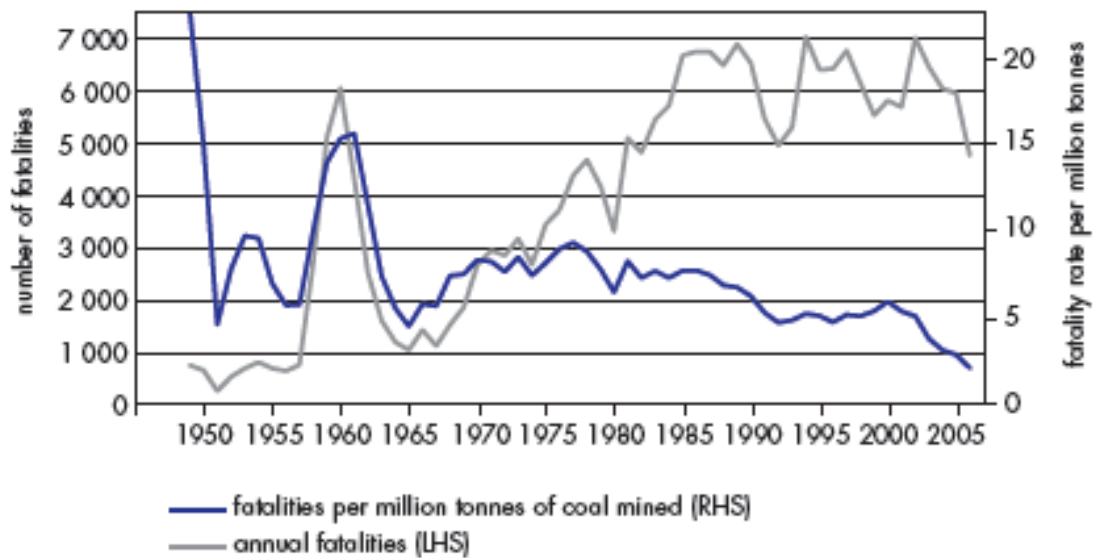
<sup>332</sup> Pei, "China's trapped transition the limits of developmental autocracy".

<sup>333</sup> Jianjun Tu, "Coal Mining Safety: China's Achilles' Heel," *China Security*, Vol. 3, No. 2 (2007), 38.

<sup>334</sup> *Ibid.*, 38.

<sup>335</sup> International Energy Agency, "Cleaner Coal in China", 44.

<sup>336</sup> *Ibid.*, 45.



Source: SACMS (2007).

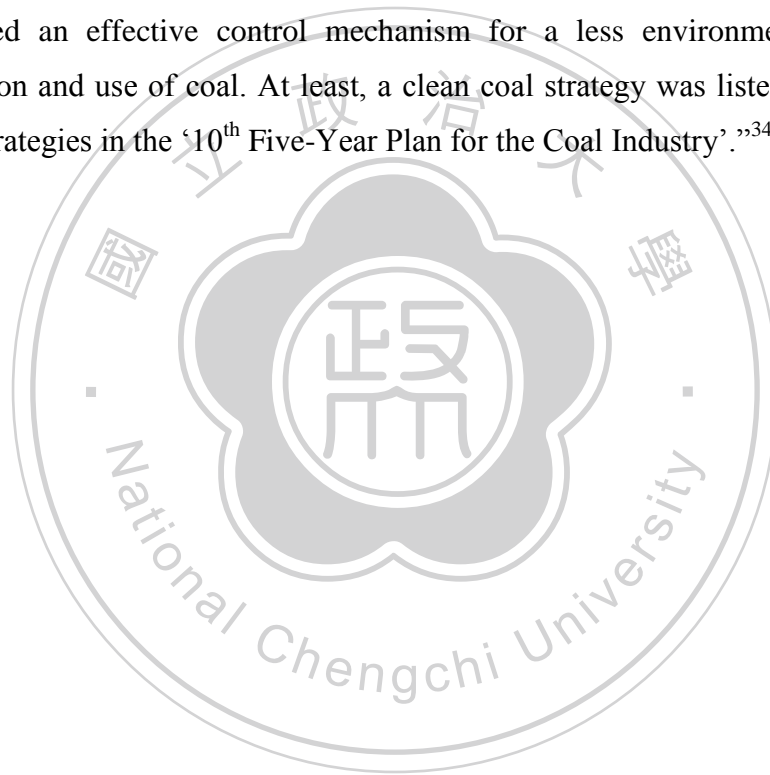
The current situation gives not much room for a positive interpretation of the use of social resources. But it may also not be as worse as most authors conclude. Although the absolute number of fatalities remains high and despite the fact that the data may be underestimated (media control, corruption, not reported illegal mines, etc.<sup>337</sup>), the fatality rate has been declining: by 2007 it was less than half what it had been in 2000. If this trend points to a turnaround toward a better safety record, the outlook can be considered to be slightly optimistic.

### Use of environmental resources

China's environmental policy at the national level has been mainly formulated by the State Environmental Protection Agency (SEPA, replaced in 2008 by the Ministry of Environmental Protection). Implementation and enforcement are delegated to the authority of provincial and municipal levels where the SEPA runs offices. With a governance perspective, the local SEPA has to face a trade-off between the goals formulated at the central level and the locality's main goal to achieve economic growth. The need for cheap electric power is generally given more weight than that of environmental enforcement. Furthermore, the financing of the local SEPA produces more conflicts. The SEPA "must rely either on the collection of local pollution emission fees or on handouts from the local governments [...]. Either [the SEPA] allows emitters to pollute or accepts payment from the local government in return for

<sup>337</sup> Tu, "Coal Mining Safety: China's Achilles' Heel," 38.

ignoring emissions entirely.”<sup>338</sup> The combination of these two facts made the enforcement of central policies very difficult. Lieberthal<sup>339</sup> observed similar effects as he studied the impact of China’s governing system on environmental policy implementation, and concluded that “much of the environmental energy generated at the national level dissipates as it diffuses through the multilayered state structure, producing outcomes that have little concrete effect.” The negative impact on the environment is immense both in coal mining, coal transport and coal burning in the power plants. Only for the mining, the “Government estimates of damage from coal mining, including wasted resources, environmental pollution, ecological destruction and surface subsidence, total about RMB 30 billion per year.”<sup>340</sup> China has not yet developed an effective control mechanism for a less environmentally damaging production and use of coal. At least, a clean coal strategy was listed as “one of four major strategies in the ‘10<sup>th</sup> Five-Year Plan for the Coal Industry’.”<sup>341</sup>



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<sup>338</sup> Lester and Steinfeld, "China's Real Energy Crisis," 37.

<sup>339</sup> Kenneth Lieberthal, "China's Governing System And Its Impact on Environmental Policy Implementation," *China Environment Series*, Vol. 1, (1997), 3.

<sup>340</sup> International Energy Agency, "Cleaner Coal in China", 46.

<sup>341</sup> *Ibid.*, 5.

### 4.2.3. Outcome of the governance framework

Having analyzed the process of policy development and implementation as well as the allocation of resources, my focus shifts to the aspect of measuring the outcome of governance. I described the definition of the three dimensions in chapter 3.2.1.

#### **Dimension “Selection and Monitoring”**

As mentioned before, China is not known for its strengths in citizens’ participation. The fact that the at least in the English literature virtually no studies can be found related to citizens’ influence on coal mining and coal-fired power plant decisions is a indicator of governance shortcomings. Much of the process depends on the Chinese Communist Party and how it manages its political, economic and social affairs.

The environmental and social threats from the coal industry are a growing risk as a destabilizing factor and the cause of a growing number of violent protests. In most of the protests are in the form of petitions and complaints, which are increasing at a rapid pace. In 2000 the Environmental Protection Bureau (EPB) received 247,741 complaints and petitions concerning pollution. Within only six years, complaints more than doubled to 616,122 in 2006. Air pollution accounts for about half of the cases.<sup>342</sup> This statistic allows no further breakdown of the sources of air pollution. Since coal mining produces a lot of toxic dust and coal power-plants in China often operate with unfiltered emissions, a large proportion of air pollution complaints are most likely linked to coal. Protests are likely to become even more widespread. The growing urban middle class is increasingly aware of governance shortcomings which affect their health and quality of life and its willingness to take political action may grow.<sup>343</sup> Protests are not a priori a negative indicator for the governance outcome. The fact that the resentments are expressed presents an opportunity to improve China’s governance capacity to compensate the shortcomings in direct participation.

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<sup>342</sup> van Rooij, "The People vs. Pollution: understanding citizen action against pollution in China," 62.

<sup>343</sup> Steinfeld, "Energy Policy", 15.

### Dimension “Efficiency”

According to the WGI, China performs best in the efficiency dimension, both in government effectiveness (GE) and regulatory quality (RQ).

Due to the nature of China’s electricity industry, which is mainly based on coal, environment regulations play an important role. Environmental awareness is not only a critical factor that determines the future of energy policies, but as the citizens of China become more affluent, they demand better quality living and hence become more aware of environmental problems.<sup>344</sup> It may harm the Chinese leadership’s “‘harmonious’ goals (i.e., environmentally friendly growth with some rudimentary social protection and effective political order).”<sup>345</sup> Nevertheless, legitimacy is derived from steady and rapid economic growth and job expansions. Measuring efficiency in energy and electricity governance shows two opposite results.

Given its primary economic goals, the outcome of China’s energy policy is impressive as there are no complaints of electricity blackouts or ever rising prices which would harm economic development. Although ‘guanxi’ (connections or personalized networks of influence) and corruption may have a negative impact, regulatory effectiveness in commercial transactions is still considered better in China than, for example, in India.<sup>346</sup> The good results can be related to poor outcome under ‘selection and monitoring.’ The limited existence of democratic institutions gives the Communist Party a “greater capacity for making decisions, and also greater policy integration and coherence across a large society, despite continuing change<sup>347</sup>” which can explain its strengths in efficiency.

As far as secondary goals such as environmental protection are concerned, efficiency has to be considered as very weak. One of the causes for this is how performance in policy implementation in China is measured. It is policy compliance that is measured but rather than the actual outcome of implementing government policies. An illustration of this problem is that local officials have been required to maintain a certain rate of local economic growth regardless of whether such growth is efficient or

<sup>344</sup> Wu, "Deregulation and growth in China's energy sector: a review of recent development," 1420.

<sup>345</sup> Pranab Bardhan, "India and China: Governance Issues and Development," *The Journal of Asian Studies*, Vol. 68, No. 02 (2009), 353.

<sup>346</sup> *Ibid.*, 354.

<sup>347</sup> Yongfei Zhao and B. Guy Peters, "The State of the State: Comparing Governance in China and the United States," *Public Administration Review*, Vol. 69, No. s1 (2009), 122.

sustainable. As long as local officials accomplish the growth policy goals, however, little attention is paid to how they have achieved the results.<sup>348</sup> “The massive tension between rapid environmental degradation and the strategic goal of maintaining high growth targets will undermine China’s environmental basis and affect health and well-being.”<sup>349</sup> A modification of environmental governance may be found in the growing relevance of grass-root level actors which the central level has empowered to a limited degree.<sup>350</sup> Although Lo and Leung<sup>351</sup> doubt any effective influence of major environmental organizations like Friends of Nature<sup>352</sup> and China’s Environmental Protection Foundation, they may have a positive influence in facilitating foreign assistance and mobilizing popular support for implementing the central-government’s environmental policies.

### **Dimension “Respect”**

The last dimension, ‘respect,’ includes trust in the legal system (RL) and control of corruption (CC). According to the WGI, we can expect a moderate result with some good and some bad sides.

The size of China’s electricity producing industry makes it one of the major global players. In that sense, issues concerning the legal system affect not only the domestic but also the global level. Since China is the world’s largest emitter of carbon dioxide,<sup>353</sup> without China’s efforts, ‘governing’ these issues will be much less effective. Coal burning in power plants accounts for most of the increasing emissions. The environmental problems in many cases affect not only one country but its neighbors and in the case of carbon-dioxide, the whole world. The negotiations on international treaties and agreements will move China even further into a process of global governance,<sup>354</sup> where the issues relating to ‘respect’ become even more important.

<sup>348</sup> Jie Gao, "Governing by goals and numbers: A case study in the use of performance measurement to build state capacity in China," *Public Administration and Development*, Vol. 29, No. 1 (2009), 27-28.

<sup>349</sup> Olivia Bina, "Context and Systems: Thinking More Broadly About Effectiveness in Strategic Environmental Assessment in China," *Environmental Management*, Vol. 42, No. 4 (2008), 731.

<sup>350</sup> Lo and Leung, "Environmental Agency and Public Opinion in Guangzhou: The Limits of a Popular Approach to Environmental Governance," 678.

<sup>351</sup> Ibid.

<sup>352</sup> Guobin Yang, "Environmental NGOs and Institutional Dynamics in China," *ibid.* Vol. 181, (2005).

<sup>353</sup> Steinfeld, "Energy Policy", 126.

<sup>354</sup> Howell, "Getting to the Roots: Governance Pathologies and Future Prospects", 227.

While protest (see ‘selection and monitoring’) against environmental pollution is rising, legal action has remained at a relatively low level. “Civil litigation against pollution is limited: the number of cases has fluctuated, with 2,136 cases nationwide in 2006, compared to 4,453 and 1,545 in 2004 and 2005, respectively.”<sup>355</sup> Although national and local rules, including rules on enterprise pollution, have improved, the legal system is not yet fully developed. “While this body of law has improved, studies show that existing rules continue to contain weak, unfeasible, unclear, and incomplete elements that limit citizen rights, and offer leeway for polluting enterprises and discretion to government institutions.”<sup>356</sup>

A problem in the legal system is the division of legislative power among central and local legislatures and powerful local governments, which has resulted in a “high degree of discretionary power at the local level.”<sup>357</sup> In large infrastructure projects, which most coal and electricity projects are, power is often abused, a problem that has resulted in local protectionism and a misuse of the legal system. Corruption and uneven application of laws are often related to energy issues. According to official estimates, as much as 10 to 14% of all procurements costs are either wasted, overpriced or frauds.<sup>358</sup> Moreover, emission fees paid by companies are collected without proper supervision or legal justifications, thus not only sowing the seeds of widespread corruption but also stoking popular discontent among the public.<sup>359</sup> As in other countries, this is associated with land deals, construction projects, bank lending, social security funds, and other activities.<sup>360</sup>

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<sup>355</sup> van Rooij, "The People vs. Pollution: understanding citizen action against pollution in China," 61.

<sup>356</sup> *Ibid.*, 68.

<sup>357</sup> OECD, *OECD Reviews of Regulatory Reforms - China - Defining the Boundary Between the Market and the State* (Paris: OECD, 2009c), 101.

<sup>358</sup> *Ibid.*, 164.

<sup>359</sup> Kong, "China's Energy Decision-Making: becoming more like the United States?," 791.

<sup>360</sup> Steinfeld, "Energy Policy", 14.

#### 4.3. Conclusion for energy policy and governance

China has a serious energy problem. It is not only the skyrocketing demand for oil and even more for coal as primary energy, but also the highly visible side effects during the transformation to the secondary energy 'electricity.' Environmental issues and the need in the global economy for ultra-cheap electricity, which is one of the fundamental requirements for China's economic development, produce goal conflicts that require a deliberated solution. It cannot be denied that China has a serious governance problem in formulating and implementing energy policies. The governance shortcomings in energy policy are conspicuously reflected in environmental problems.

Some argue that the problems reflect the transition of energy policies to public policy decisions which "touch on the essence of politics, namely who gets what when, where and how."<sup>361</sup> These problems do not stop at national frontiers. But an active participation by China in international environmental treaties is not very likely. Even if China's central government wanted to get more involved, the implementation of strict rules would be hindered by local authorities. In that sense, governance problems have multiplied. On a global level, China's integration in such processes will require adjustments in international diplomacy. The domestic governance challenges can be found mainly in the inability to enforce national policies. The best evidence for this is the uncontrolled growth of coal-fired power plants, 'illegal' coal mines and 'illegal' power plants.

Has China's energy governance failed? I would argue that it has not failed. Environmental problems are extremely harmful to people's health and contribute to global warming, but even a well-oiled governance situation would not automatically improve the environment. At the root of these problems are a series of trade-offs between economic development and environmental protection. It is not so much that governance has failed, but that central-level decisions must be adjusted at the local level to accord with priorities at that level. The fact that China has been able to raise its production so impressively over the last decade and build so many new electric power plants highlights the fact that governance requires a series of trade-offs. The question boils down to how much China is willing to pay to implement its policies.

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<sup>361</sup> Kong, "China's Energy Decision-Making: becoming more like the United States?," 790.



## 5. Conclusion

The very paradoxical result of this thesis is that China has a governance problem but it does not really matter. The final question should not be whether or not China has a governance problem. The question should be: how serious is the problem? In this thesis, I have examined different aspects of governance to analyze the problem of China's governance from different angles and I got different answers.

### **The problem is serious**

While China's governance problems are serious, they may simply be one piece of the puzzle of China's economic miracle. In the short run, governance deficits have boosted China's GDP. But governance deficits have a price, and in the case of coal-fired power plants, the costs can only be estimated but are certainly immense. Low environmental protection standards are made worse by the incapacity to implement regulations at the local level. People and the environment suffer from a steady deluge of pollution. The bill for this pollution will be paid later. Even if the governance system were 'fixed', the legacy of China's weak governance in the beginning of the 21st century will be felt for a long time.

### **The problem is not so serious**

But why bad governance in China is not the logical and appropriate conclusion?

- Firstly, governance indicators show that in recent years, China has at best been able to hold its position compared with other countries, but the general tendency is downwards.
- Secondly, governance reforms are one part of the ongoing reforms in China and cannot be evaluated in isolation. The problem is how we evaluate a reform process in terms of governance. Governance indicators are an obvious choice.
- Thirdly, if we factor out normative questions and analyze the outcomes such as the results of governance processes in the electricity market, our evaluation may be much more positive.

### **It doesn't matter**

Let us reformulate the question. Does China's governance problem matter? The example of the problems with coal-fired power plants shows that by ignoring central-government policies and processes China was able to supply its regions with plenty of new and cheap energy. China was able to raise its production and achieved one of its priority goals of rapid economic development. With more efficiently functioning good governance the supply of energy might have stagnated, which could have resulted in power blackouts and less foreign investment. In that sense the problems does not matter because the primary goal of improving the economic growth at almost any cost has not yet changed. There are good grounds for pessimism about China's future. Policy adjustments to the fast changes in China are too slow and harm many aspects related to China's future. But there are also good grounds to be optimistic about China's future. The dynamism found at the local-level attests to a degree of independence from the central level. That may prove very helpful to solve problems at the local level. Problems can quickly be adjusted according to the local needs. For instance, Shanghai citizens' protests over the potential health hazards, noise, and loss of property value resulting of the proposed Shanghai-Hangzhou Maglev train line succeeded in bringing about a suspension of the project in 2009. Even without a national electromagnetic policy and formal participation structures for the local people, solutions are possible.

How can the questions posed at the beginning of the thesis be answered?

- Firstly, governance theories may help to interpret governance indicators. This may be a paradoxical answer because governance indicators are based on governance theories. However, the variety of governance theories should make us cautious about the results of governance indicators. China's decline in the WGI's corruption indicator is not an absolute value. For instance, it does not include significant policy changes and their implications. A stricter corruption policy may lead to a lower value in such indicators, by causing a greater awareness among the people.
- Secondly, China's governance problems have many roots. The case of energy policies and the failure to implement them is an example of the problems. On the one hand, local governments simply ignore the policies and they are insufficiently evaluated on the basis of achievements. On the other hand, governance entails costs and someone has to pay for them. Without funding and supervision from the central government, it is unlikely that the problems will disappear quickly.
- Thirdly, governance reforms are a part of virtually every reform. The limits of governance reforms can be seen in their costs in the short run.
- Finally, a governance approach is, in my opinion, very fruitful for discussing China's future. Paradoxically, this thesis supports both approaches.

### 5.1. The limits of governance theories in China

The governance approach helps us analyze the development of China and facilitates a structured evaluation of general and specific issues. Nevertheless, we should be aware of the limits of applying governance theories to China. In my view, governance theories applied to analyze China have weaknesses in that they over emphasize democratic values and that governance normally turns attention to the status-quo and does not evaluate long-term planning and development visions. China may have its strengths in both. Neither governance theories nor most literature on China's development take due account of the China-specific concept of supraplanning (謀略 – mólüè).<sup>362</sup> Western democracies plan normally during legislative periods. China has no such limitations and has a tradition of supraplanning that combines a vision with strategic development over 10, 50 and even 100 years. Statements by the Chinese leadership that China will be a democratic country by 2050 are seen by many Westerners as an excuse on the part of China's elite for being undemocratic now and for their lack of commitment to democratic development. But we ought to be wary of ignoring the Chinese government's long-term development vision. China remains a communist country. In my opinion, the impact of that simple fact is greatly underestimated. The party leadership's program to achieve rapid growth and development by any means necessary is not because the Communist Party is convinced that capitalist methods are superior to a centrally planned socialist economy, but is a result of the principal contradiction with which China has to struggle. Since 1978, this principal contradiction has been the official doctrine of the Communist Party. Its commitment to undertake massive efforts to modernize China's agriculture, industry, national defense system, economy and science has deep roots in communist doctrine. Studies on Sino-Marxism (馬列 – mǎliè)<sup>363</sup> should be taken much more into account. This communist dialectic may explain why we have a gap between the poor results of policy formulation and implementation and the relative good evaluation of their outcome. In that sense, when it comes to governance in China, we have to think about governance in China with communist characteristics.

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<sup>362</sup> Harro von Senger, *Mouliè - Supraplanung. Unerkannte Denkhorizonte aus dem Reich der Mitte (Supraplanning: Non-Perceived Dimensions of Thinking in the People's Republic of China)* (München: Carl Hanser Verlag, 2008).

<sup>363</sup> Ibid.

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