

# CHINA AND CAPITALISM

A History of Business Enterprise in Modern China

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# 1 Introduction

Towards the end of 1978 when the Chinese leadership decided to re-open the country to foreign trade and investment, the implications of the policy turn-around were neither as clearly set out nor necessarily as destined to succeed as it is sometimes now thought. Yet, overnight, it became clearly established that the aspiration towards modernization was to be fostered through China's taking its part in the international economy. Overnight, a generation in the writing of Chinese history was overthrown: gone was the foreign impact as a decided detriment on China's fortune and in its place was capital investment as a contribution to economic growth. Through the 1980s, social and economic historians writing within the People's Republic of China and accustomed to thinking about Chinese history in relation to capitalist oppression had had to grope for a new way forward, and that began a long process of rethinking China's history.

I shall not summarize the literature which went into this tortuous process. Readers who are interested in the outcome can read Xu Dixin and Wu Chengming's three volumes on the history of capitalism in China, or, for another strand in the argument, turn to the writings of Ma Min and Zhu Ying which deal with the shift in the Qing state's perception and treatment of merchants in the spate of reforms begun in the early years of the twentieth century.<sup>1</sup> The one line of thought traces the history of the market in China, and the other addresses the question of the rise of "civil society". The history of the market and the position of merchants are fundamental in understanding the history of Chinese business and these works in the 1980s may be cited as examples which cleared the ground for further research.

In the meantime, China's increasing importance in the world economy and a growing interest in incorporating China into world history has brought about a demand for generalizations about Chinese economic and social history. In my view, China historians — writing from within or outside China — are ill prepared to satisfy the demand. A few exceptions to the contrary, since the 1950s, little interest has been shown in examining China's historical statistics in any systematic manner; few studies have looked at the structures of Chinese business corporations, and hardly any China historian has examined the history of technology in the nineteenth and twentieth centuries.<sup>2</sup> Despite the pioneering effort on the history of accounting produced by two Chinese historians, the significance of that subject is poorly grasped.<sup>3</sup> Contemporary documents are always in short supply, but not even when they are abundant has research conducted been published, or, more often, been conducted at all. Moreover, a great deal of what is published is still available only in Chinese and remains inaccessible to most Western historians who are not also China specialists. A greater gulf exists between the China historian (whether or not ethnic Chinese) and his or her Western counterpart who is interested in drawing China into world history, than between the Chinese historian of the 1990s and earlier decades.

Language is such an obvious barrier in writing history that any warning for the non-Chinese reader in wrestling with Chinese history seems superfluous. However, it is necessary to point out the lack of critical analysis in a great deal that is written about China in the general vein. It is useful to be reminded of the saying "easy comes, easy goes", which applies to quick scholarship as it does to home finance. It sounds very old-fashioned nowadays to say that historians should learn to read the footnotes. When the footnotes refer to documents in languages which the reader cannot understand, it may be obvious but it needs pointing out that it is very easy for writers to take liberty with the documentation, and some do.

The only answer to shoddy documentation is, of course, more and more careful research. Yet, in republishing this small volume, I think it is worth presenting this history of Chinese business in outline even at this stage because I think in my short lectures of 1993, I

presented a view of Chinese history which, even now, goes somewhat against the grain of present scholarship. To my mind, the current discussion has, probably as a result of over-correction to charges of “orientalism”, underscored China’s cultural differences from the West. The Western-centred post-industrial world is too full of the importance of individual rights and liberties to appreciate the workings of a society ruled more by ritual than by law. In saying this, I am not defending the penchant for characterizing Chinese business by imputing to it strong affinities for “guanxi” (read “connections”) or “face”. I find these crude characterizations quite misleading as tools for understanding Chinese society. At heart, I think the ritual, rather than legal, definition of interpersonal relationships in business relates to the manner of incorporation, and that, in turn, is closely tied up with the control of property.

Let me state briefly my argument in this book. When the capital market in the fifteenth century did not take off, Chinese business advanced through patronage and incorporation facilitated by ritual (rather than law). The transformation of this structure came about under the Western impact in the second half of the nineteenth century. It had taken China all of the twentieth century to make the transformation and to this day, it is far from complete.

To put this brief outline into context, it can be said that business practices in China had been shaped by the broader trends in the evolution of the Chinese state and society since 1500. To take the long view, it is necessary to recognize that three changes, in particular, provided for the backbone of long-lasting development in the late imperial state of the Ming (1368–1644) and the Qing (1644–1911) dynasties. Firstly, the economy was increasingly monetarized from the sixteenth century as silver was imported into China in large quantities from abroad (in return for Chinese exports). Secondly, the recruitment of a bureaucracy by examination, long instituted since the Tang dynasty, was consistently applied without any break from the early Ming into the last years of the Qing dynasty, and, whether or not the content of the examination shaped an efficient government, it created a class of administrators who prided themselves on their scholarship. The same sense of pride became a

basis for lineage organization in the richer parts of China which produced more than the average number of examination degree holders. Thirdly, the scholar-official class, from the 1500s, saw their political interests vested in the maintenance of ritual order which assigned all members of the state, including the emperor, rights and responsibilities. It is possible to read into this development the political agenda long raised by Neo-Confucians in the Song dynasty, but it was only from the sixteenth century, after various crises shattered the hold the emperor might have had on court officials, and a scholar-official class grew in number and wealth over many parts of the realm, that the scholar officialdom achieved the unity of purpose as a political force. In the background, it is important to draw attention to the vast size of the Chinese state even in 1500. When the emperor ruled over a population of 100 million, no officialdom was capable of enforcing the emperor's order except through the connivance of the local elite, which itself aspired to official status. Stability was maintained in late imperial China not by strict enforcement of law but by connivance between the officialdom and the local leadership to maintain the propriety of rituals.<sup>4</sup>

In Chapters 1 to 3 I shall describe how business was conducted under the late imperial regime. I shall argue that in the sixteenth century, with the exception of the salt trade, run as a government monopoly but in which merchant capital was drawn through a market in futures, Chinese business was conducted by merchants who, most of the time, were unregulated, and who transacted with one another with little resort to the law. As an aside, I shall also look briefly at the history of Chinese technology, especially with the view of coming to an understanding as to why it was so difficult for China to adopt steam technology in the nineteenth century, the answer for which question rested on the lack of a machine tool industry. This much should be common knowledge to the field. However, this characterization of Chinese business omits the very important need of incorporation. In other words, surely enough, Chinese people contracted, but when they did not contract as individuals, how did they do it? The answer I present in Chapter 3 argues that they did so as lineages, a term used in the literature on China to refer to

groups of people tracing common descent rather than the lines of descent themselves. Relationships in the lineage group were regulated more by ritual and patronage than by law, and for that reason, ritual and patronage had a strong place in Chinese business institutions.

From the end of the nineteenth century into the first half of the twentieth century, incorporation through ritual practices came to be challenged by practices introduced through Western law. That did not happen overnight, nor did it imply the immediate disappearance of the ritual corporations. Instead, in this period which went astride the end of the Chinese empire and the establishment of the Chinese Republic, rituals which were established in the late imperial period were increasingly pitched against what seemed Western and modern. A century-long process began whereby incorporation on the ritual basis had to be replaced by incorporation resting on the strength of law. Chapter 4 outlines the beginnings of the process in relation to the introduction of Company Law in China from the late nineteenth century (enacted in the British colony of Hong Kong in 1865 and in China by 1904), and Chapter 5 the resumption of the process from the last years of the 1970s after a break of four decades.

In the background, it is necessary to appreciate the momentous changes which came over Chinese society as the Qing empire drew to a close. The last word has not been said about the Revolution of 1911 which overthrew monarchy in China. Nevertheless, we know enough about it as historians to realize that it did not come about only because the government was inept and Westernized young people brought it about through their revolutionary parties.<sup>5</sup> The government was inept and seen to be so because it was defeated in war, first in 1840 to Britain (in the Opium War), and then, in 1895, to Japan (the Sino-Japanese War), and it could not deal with the inflation of the early 1900s which it had created by debasing the coinage. Some time in between those events, the central government in Beijing had come to financial ruins. The Taiping Rebellion in the 1850s and 1860s had undercut its ability to raise revenue from the land tax which it had depended on through the eighteenth century, and, so, through the last decades of the nineteenth century, but especially after 1895, it was increasingly burdened by war indemnity



and financial calls for military reforms. The inability of government to deliver cast doubt on the very ideology on which it had commanded respect in earlier centuries. The same scholarly tradition which had held the Chinese state together in the eighteenth century, by the end of the nineteenth century, appeared backward. By 1900, even the imperial court had accepted the need for a complete overhaul, and it was that effort which brought down the government.

There was, of course, a technological gap between China and its invading powers, but China's inability to fill it had to do with the weaknesses of its social institutions in mobilizing resources. Some of these weaknesses could justifiably be attributed to conservatism. The scholars who looked upon the imperial examination as their preserve were hardly likely to look favourably at a new syllabus to be adopted from the West over which they had no expertise. However, many more weaknesses had to do with the lack of a commercial tradition rooted in law. Until Western law came to be applied in China – more of that in Chapter 4 — China did not have any law which dealt with the business company. When the imperial government launched into railway building, therefore, and permitted the provinces to raise capital for it through joint-stock operations, the mechanisms were not present to hold the company promoters accountable to shareholders. In inland Sichuan province, the railway company went bankrupt before the railway was built, and shareholders were aggrieved to find the central government demanding the railway nationalized without providing for compensation. Multiply such confusion manifold as government abolished the imperial examinations, increased tax, founded new schools, instituted police forces, and implemented many more new policies, all at a time the debased coinage was fostering inflation in the market place, and one can understand why it was so popularly thought by 1908 that the imperial government was inept. When in 1911, a portion of the army stationed in Wuchang revolted, the government found it had to deal with not only that localized incident, but a crisis of confidence that was widely felt throughout the country.

The Republican government which was formed in the wake of the success of revolution in 1911 did not ever have the chance to

succeed. Implementing a constitutional government by popular election in 1912 was too drastic a change to comprehend for any but a tiny fraction of China's newly educated elite. The central government, which was ruined financially before then, depended on foreign loans to survive, and, so, secret negotiations for loans which were to benefit only the parties involved in negotiation eroded any further confidence in government. Power devolved very soon to military commanders, dubbed "warlords" by their opponents, while the country fragmented. Significantly, political fragmentation was not accompanied by economic disaster. Despite continual wars between army factions, for reasons that will be given in Chapter 4, which had to do with the devolution of political patronage of business, the economy boomed from 1900 to the early 1930s. A nascent working class coming from the mines, the railways and new-found urban industries, gave enough of a hint that the new industrialization might be the course for further revolution to enable the Comintern to foster revolutionary cells in China. One of these was the Chinese Communist Party, which was to be fostered within the Guomindang Party which the Comintern also had a strong hand in re-organizing. It will be too much of a detour in this account to describe the very important transformation of Chinese politics introduced by these two parties. Suffice it to say that when the Guomindang Party defeated the northern warlords and set up a government in Nanjing in 1927, it re-established the authority of a centralized regime. Its decade of rule from Nanjing, a nightmare scenario for any government, fraught with internal and external wars, depression and considerable internal dissension, saw the beginnings of a government policy which was increasingly concerned with centralizing its control on the economy. War with Japan came in 1937, followed by civil war between the Guomindang Party and the Chinese Communist Party from 1945 to 1949. Effective centralized government was re-established only in the People's Republic in 1949.<sup>6</sup>

Between 1949 and 1978, despite the occasional shifts in policy — which were real and consequential — it may be said that the economy was increasingly put under a command regime. Central planning, however, did not ever produce the plans which allowed

effective central control, and by the Cultural Revolution, which broke out in 1966, the planners themselves were no longer in place, let alone the plan. The very marked features of the Chinese economy, therefore, were not produced by planning, but by some very drastic measures which put enormous strain on the central government for driving the economy. Inheriting runaway inflation and substantial debts from the previous government, the People's Republic in 1949 moved towards closing the economy to the outside world, effectively by abrogating foreign debts, introducing strict exchange controls, rationing and restricting the movement of its people abroad. For three decades, increasing radicalization of political and economic policies totally squeezed out the market. By the Great Leap Forward in 1959, no private enterprise was in operation in China and practically all farmland was held by communes, and by the Cultural Revolution beginning in 1966, even accounting was regarded as a bourgeois indulgence and suspended in many state and communal enterprises. The net result was an initial spurt in heavy industry in the 1950s and a stagnant economy thereafter. Economic policy took an about turn towards the end of 1978, when in recognition of the need for both political and economic reform, the Chinese government took the bold step of requiring the communes to contract land out to farmers, permitting individual business enterprises — at first on a small scale, but the scale of operation grew very rapidly — and promoting foreign investment in coastal cities designated as “special economic zones”. Back in 1978, no-one foresaw the extent to which privatization might go. Throughout the 1980s, the opening of the Chinese economy to world trade and investment was called into question with every political upheaval. However, by the 1990s, it was widely recognized that economic opening had become irreversible.<sup>7</sup>

The process whereby law overtook ritual as the foundation of business took most of the twentieth century and to this day, the process is far from complete. That should be no surprise. After all, it took ritual three centuries (from the sixteenth to the eighteenth century) to be firmly established as the fundamental political principle whereby society might be held together. A great deal more

historical research is needed to flesh out in full the implications of this argument, but there is enough, on the basis of published research, to shape a general outline. In the long term, we are probably only now, in the early years of the twenty-first century, able to perceive in broad outline the new China that was taking shape. Business behaviour which rested on ritual and patronage differs in significant ways from that regulated by law, and in Chapter 6, the concluding chapter, I ponder on what these differences might be.

# 6

## Conclusion

This broad sweep of the business history of China highlights the following aspects of traditional Chinese business institutions:

- Written contracts relating to land were commonly employed.
- Chinese corporations emerged from a ritual context.
- Patronage took paramount importance in all businesses, and political patronage in businesses of scale.
- Traditional Chinese accounting lacked the means to calculate capital.
- The transformation of Chinese institutions from the nineteenth to the twentieth century required the adaptation of business to commercial law.
- Traditional business was limited to knowledge of capital within the group, and the legal basis for business institutionalized transparency in corporate governance.

This is not meant to be an exhaustive list. It is a list that is arrived at by positing contracts, accounting, incorporation, and financing as major elements of business. In the process, I have related these features of Chinese business to the sixteenth-century commercial revolution, when the lineage as a corporation came into its own and when the sale of salt tickets collapsed and with that, the end of any chance for the evolution of a capital market. China did not follow the course of events which the Western world went through: no law guaranteeing individual ownership of property was instituted, but instead, the practice of holding properties in the names of ancestors and deities became paramount. As long as business enterprise required limited capitalization, the ritual institutions were sufficient for the task of raising capital. The shortfall came when nineteenth-

century industry, introduced by the West, called for investments on unprecedented scales in the Chinese experience. Chinese institutions were unable to rise to the need.

Major changes were made to this manner of business by the last decades of the nineteenth century, many of which were associated with the erosion of China's political sovereignty under the threat of war and political turmoil. From the last years of the nineteenth century to the whole of the twentieth century, it may be said that:

- Chinese firms increasingly took on the character of companies as defined in successive versions of the Company Law.
- Banks remained the weakest link in the business chain but signs may be detected of an impact being made by banking practices.
- Since the 1930s accounting has evolved as a profession but the enforcement of accountability has not yet been settled.
- Families continued to wield power within the framework of the public company.
- Patronage remained a requirement in the world of business.

Some of these features can be traced to legislation and its enforcement in China proper and in areas where Chinese businesses proliferate. Some features have continued not because of any tenacity of tradition but because twentieth century governments have adopted policies similar to their nineteenth-century predecessors. The finance market has wielded a much stronger impact on the practice of businesses, but the jury is still out as to whether Chinese firms might be made accountable to their shareholders to the same degree as Western firms might be. In none of these changes did Confucianism as an ideology have any bearing.

I have little to quarrel with Kenneth Pomeranz in searching for a "great divergence" with the West to elucidate China's experience in economic development. He has a point in locating some of that in the control of the oceans by the West. Yet, I would describe the divergence in very different terms. I think he has brushed aside too summarily the differences in the business institutions of China and the West, in particular, the manner by which corporations might be founded and maintained. Or, in other words, were property to be held by a group, rather than an individual, how it might be held.

It goes without saying that the process of incorporation holds a central place in the history of business. Were comparison to be made with the Western European and North American experience, the history of business incorporation would embrace the history of partnerships, the chartered companies, the banks, limited liability, shareholding, credit-bearing instruments (commercial papers, in the form of drafts and bills), paper currencies, public debt, and associated with these practices, the emergence of commercial law and standard accounting practices. It is true that a great deal of this development came within the nineteenth and twentieth centuries, and the point of comparison, were it to contribute to an explanation of divergence in economic growth, would have to pertain to the eighteenth century. It is also true that the history of many of these institutions in China is a great deal hazier than it is in Europe and North America, not only because historical documentation has been in short supply, but also because the Chinese experience has not been told in institutional terms.

In brief, it can be said of Chinese business history that China underwent a commercial revolution, very much as Western Europe did, in the sixteenth century. Out of the commercial revolution, business traditions developed which incorporated many instruments which serviced trade and investment. Contracts were commonly used, many of them written even though many more must have remained oral. Partnerships were formed. Moreover, even though membership to corporations did not go very far beyond circles of relatives and acquaintances, property was held in the name of the group as a body and maintained an independent existence beyond the lifetimes of the individuals who might make up the group. However, despite these similarities with the West, eighteenth-century China did not have as much as a nascent stock market nor did its government acquire a national debt. For that reason, China did not have banks which were experienced in dealing with a national debt or paper currencies issued on that basis. These similarities and differences are vital in the explanation of China's divergence from the West by the time of the iron-and-steel industrial revolution. Chinese people continued to excel in commerce where small groups of merchants networked

through friends and family, but came to grieve in capital-intensive enterprises such as running steamships, mines and railways.

Pomeranz is correct, therefore, to draw attention away from the ubiquitous reference to “culture” in the China literature towards institutional differences. Yet, the concept of cultural differences — not necessarily a Confucian East pitched against a Christian West — must creep back in the comparative context. After all, a comparative study is only meaningful when history is not regarded as a descriptive course of events, but as a series of twists and turns all of which could have led to alternative courses of development. What might have happened if the Ming emperors had been more successful in building up a national debt denominated in salt? Probably not enough of a background to allow any reasonable conjecture that it would lead to the beginnings of a paper currency backed by a reserve. But what if the kings of England in the first half of the seventeenth century were as powerful as the Ming emperors and might abrogate their debts? There would not have been a Bank of England. The national debt founded on salt tickets proved to be a blind alley, and so the Ming government, and the Qing government to follow it, took the course of “government supervision and merchant management”, euphemism for business under political patronage.

If the capitalist road of the salt ticket proved a dead end, not so the other institutions for trade and investment from the sixteenth-century commercial revolution. Here, again, some details are needed for the difference between China and the West to be understood. The corporations which served as the instruments of investment in eighteenth-century China had long been known to China historians but few had recognized in them the economic vehicles which they had become. Unlike Western Europe, where by the eighteenth century business incorporation was increasingly governed by a law with the explicit recognition that gaining a profit was rightful and legal, eighteenth-century Chinese corporations remained ritual entities, established not directly to serve the interests of their members, but ostensibly to provide sacrifice for gods and ancestors. Compared to Europe, the Chinese corporation would have been akin to the medieval monastery, built for a religious purpose but



maintained as a powerhouse of economic growth, managing land and hostels, providing services — not without charge — for living and dead, and networking with kings and peasants. The analogy creates its own problems, of course, there being no church in China equivalent to the religious establishment of Western society, the very diversified and decentralized corporate entities which might be established around shrines and temples answered to no clergy. Through the Ming and the Qing dynasties, authority of interpretation as to what might or might not be proper behaviour at shrines and temples was claimed, not by the religious specialists, who might be thought of as village shamans, Buddhist monks and Daoist priests, but by the literati schooled in the Confucian classics.

The comparison with Europe necessarily breaks down, as the description of Chinese society skirts nearer the much publicized East Asian tenet to what counts as a unique culture under the name “Confucianism”. It would be necessary to strip of that idea any reference to Confucius, or any inkling that the ideology pervaded society to such an extent that it competed with “Daoism” or “Buddhism”. The moral tenets it advocated as an ideology were translated into action only to the extent that moral tenets might. It downgraded mercantile activities, but that is not to say that the governments of the time did not recognize the value of trade or that society was not pervaded by the pursuit of profit. Left standing would be the close identification of the local to the central in terms of a common ritual, the separation of the emperor’s personal religious faith from the religious rituals of the state, a four-century-long trend of upward social mobility demarcated by the acquisition of official status by examination and the production of a literati class which saw its fortunes closely entwined with its defence of state orthodoxy. This was the society which rested its order on ritual rather than law, which recognized group rather than individual responsibility, and which legitimized official patronage rather than legal rights in business. Call this “culture” if one must, for embedded in it were beliefs and social practices which did set China off from the West.

More than the oceans and the inner Asian deserts separated China from the West. East and West diverged in the innovations each

brought to the common problem of harnessing resources in the drive for wealth and power. It falls to the historian to identify the trajectories on which these innovations were set, and, thereby, provide an understanding for the varied experience of the very large numbers of people living on the opposite sides of the world.

# Notes

## Chapter 1

- 1 Xu Dixin and Wu Chengming, *Zhongguo ziben zhuyi fazhan shi* (A history of the development of capitalism in China), Beijing: Renmin chubanshe, 1985–1993, 3 volumes, of which volume 1 is available in English translation as Xu Dixin and Wu Chengming, eds. *Chinese Capitalism, 1522–1840*, Basingstoke: Macmillan, 2000; Ma Min and Zhu Ying, *Chuantong yu jindai de erchong bianzou: wan Qing Suzhou shanghai gean yanjiu* (Duet of tradition and modernity: A case study of the Suzhou Chamber of Commerce in the late Qing), Chengdu: Bashu shushe, 1993, and Ma Min, *Guanshang zhi jian: shehui jubian zhong de jindai shenshang* (Between the merchant and the official: The gentry merchant in a time of momentous social change), Tianjin: Tianjin renmin, 1995. Ma Min’s argument may be found in English summary in Ma Min, “Emergent civil society in the late Qing dynasty: The case of Suzhou”, in David Faure and Tao Tao Liu, eds. *Town and Country in China: Identity and Perception*, Basingstoke: Palgrave, 2002, pp. 145–65.
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- 3 Guo Daoyang, *Zhongguo kuaiji shi gao* (A history of Chinese accounting), Beijing: Zhongguo caizheng jingji chubanshe, 1982, 1988; and Gao Zhiyu, *Zhongguo kuaiji fazhan jianshi* (A concise history of Chinese accounting), Henan renmin chubanshe, 1985.

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- 5 Mary Clabaugh Wright, ed. *China in Revolution: The First Phase, 1900–1913*, New Haven: Yale University Press, 1968.
- 6 For description of social and political changes in the Republican period, see Henrietta Harrison, *The Making of the Republican Citizen: Political Ceremonies and Symbols in China 1911–1929*, Oxford: Oxford University Press, 2000, and John Fitzgerald, *Awakening China: Politics, Culture, and Class in the Nationalist Revolution*, Stanford: Stanford University Press, 1996.
- 7 Background of policy changes in the late 1970s and 1980s may be found in Joseph Fewsmith, *Dilemmas of Reform in China: Political Conflict and Economic Debate*, Armonk, NY: M. E. Sharpe, 1994; *China's Second Revolution: Reform after Mao*, Washington, DC: Brookings Institution, c. 1987.

## Chapter 2

- 1 Andre Gunder Frank, *Reorient: Global Economy in the Asian Age*, Berkeley, London: University of California Press, 1998; Kenneth Pomeranz, *The Great Divergence: China, Europe, and the Making of the Modern World Economy*, Princeton: Princeton University Press, 2000.
- 2 J. Y. Wong, *Deadly Dreams, Opium and the Arrow War (1856–1860) in China*, Cambridge: Cambridge University Press, 1998, pp. 337–60.
- 3 Raymond Dawson, *The Chinese Chameleon: An Analysis of European Conceptions of Chinese Civilization*, London: Oxford University Press, 1967.
- 4 On this interpretation of the classical economics background to *Capital*, see Louis Dumont, *From Mandeville to Marx: The Genesis and Triumph of Economic Ideology*, Chicago: University of Chicago Press, 1977.
- 5 Max Weber, *Economy and Society: An Outline of Interpretive Sociology*, Berkeley: University of California Press, 1978; Karl Polanyi, *The Great Transformation: The Political and Economic Origins of Our Time*, Boston: Beacon Press, 1957; Fernand Braudel, *Civilization and Capitalism 15th–18th Century*, transl. by Sian Reynolds, London: Collins, 1981.
- 6 The word “lineage” is used in Chinese social history to refer to groups of people of the same surname tracing ancestry from a common ancestor.

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