



From Local Government-Led to Collaborative Governance: The Changing Role of Local Governments in Urbanization

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I INTRODUCTION

China has accelerated its urbanization since the 1990s, its urbanization rate leaping from 29.04% in 1995 to 57.4% in 2016. While driving the large-scale migration of rural population to cities, the urbanization has expanded urban entities and urban space. This round of urbanization is a typical local government-led urbanization. As legal subjects of land expropriation and transfer, the local governments levied the land from farmers with low compensation and resettlement costs on the one hand and transferred land use rights to land use developers to obtain extra budgetary income on the other hand. Meanwhile, land has become a key bargaining chip for regional “race-to-bottom” investment attraction as the local governments have deliberately lowered industrial land prices to attract foreign investment, promote local economy, and develop tax bases (Tao et al. 2009; Wang and Tao 2013). It is under this government-led “Land Expropriation—Land Selling” (LELS) Model that China boosted its urbanization and industrialization for more than a decade; therefore, China has become a middle-income country in its urbanization rate, industrial structure, and people’s income. However, two major dimensions of China’s urbanization, “population urbanization” and “space urbanization,” have shown severe contradictions and problems, and they are related to China’s traditional local government-led urbanization model, more or less.

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First, under the current land expropriation system, low compensation deprived the farmers, in particular the farmers in underdeveloped areas, of their means of survival when they lost their land, as it meant they lost employment opportunities. More seriously, the landless farmers did not benefit from value-added land benefits or the fruits of urbanization. So, how to compensate the farmers in the expropriation and demolition of land has been a social issue in recent years. Second, administrative power was mainly exercised on “land urbanization,” so “population urbanization” obviously lagged behind “space urbanization” in speed, leading to “land urbanization, not population urbanization.” It created many desolate cities, which are known as “haunted cities” in China, in urbanization as land resources were wasted to a large extent, and it hindered the flow of labor; therefore, much labor was still in the primary industry. Finally, in the LEIS Model, local governments tended to depend heavily on unsustainable land finance. Meanwhile, they were already in heavy debt with land loans, posing a huge risk for the entire financial system.

Governments at all levels have introduced a series of policies, laws, and reforms to address these problems in the land system; however, the focus was on changing the local government-led urbanization model. If the local governments continued to push forward urbanization as leaders with administrative forces, the LEIS Model would be maintained and the problems could not be properly tackled. We found out that the changes in government roles actually did not slow down urbanization but, rather, helped solve the problems in current urbanization. The new-type urbanization in the Zhejiang public-private partnership (PPP) model and the urbanization of spontaneous farmers and collaborative governance in the Nanhai Model are successful cases. The former found a solution for the local governments to alleviate their dependence on land finance as the collaboration between the governments and social capital compensated the capital shortage in urban construction, while the latter created a win-win situation for local governments and farmers as farmers benefited from value-added land benefits. It is our view that China’s urbanization would be more healthy and sustainable if local governments transformed from leaders to collaborators and governors to help form mutual promotion and governance between governments and the society.

2 LOCAL GOVERNMENT-LED URBANIZATION AND ITS DRIVING FORCES

2.1 *Local Government-Led “Land Urbanization”*

In China’s rapid urbanization, local governments played a leading role, which had a lot to do with China’s special land system. The urban land in China belongs to the country, the rural land to village collectives. Most of the land needed for urban expansion and industrial park construction came from rural collective land, which was expropriated by the governments before it could be

developed and sold. The 2004 Amendment to the Constitution endowed local governments with the rights to levy collective land from village collectives and farmers within public interests. Although China had a large population and scarce land, the unequal urban and rural dual land system facilitated local governments to forcibly expropriate land from farmers with low compensation. And due to the land expropriation rights granted by the law, local governments could compensate and place the landless farmers based on the original land uses, with compensation only equivalent to six to ten times the annual returns of farmland. The land expropriation system ensured enough land for construction, which prevented China from falling into economic stagnation with high land price due to land scarcity (Fig. 28.1). With the expansion of urban space and accelerated infrastructure construction since the mid- to late 1990s, more land was expropriated, leading to a huge number of landless farmers. China expropriated land annually that amounted to 2.4–3 million mu (1 mu equaling 0.067 ha) from 1999 to 2002, and about 2–3 million farmers lost or partially lost land each year. By 2006, the number of landless farmers in China was more than 40 million, and it would increase to 70 million in the next 10–15 years.

On the other hand, the local governments monopolized the primary market of land transfer, and the supply of construction land was manipulated by the local governments. The local government first expropriated the land at low cost and transferred the land use rights to land-using units after the leveling of land and building of infrastructure facilities. Between 2000 and 2015, the land for construction experienced an increase of about 35.09 million mu from 543.09 million mu to 578 million mu, that is, an annual increase of 2.34 million mu. Another means of urban expansion by the local governments included

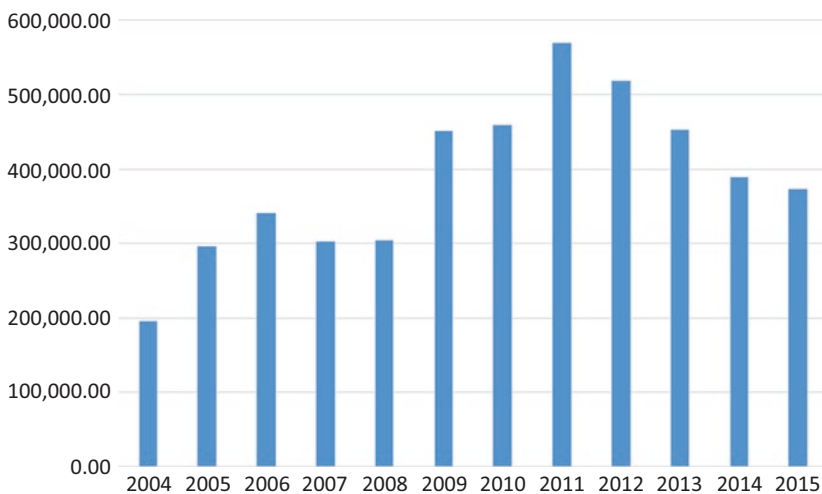


Fig. 28.1 National land expropriation in 2004–2015. Source: *China Land and Resources Statistical Yearbook*

rural and suburban areas into an urban planning circle to expand the urban area by planning revision and administrative division adjustment, namely “urbanization with the outward moving of the urban circle.” Between 2000 and 2015, the urban construction area expanded from 22,439.3 to 52,102.3 square kilometers, an increase of 132.2% (see Table 28.1).

In the land supply, the local governments showed a clear preference to industrial land as it would attract businesses and investment or rather, a key stake to attract foreign investment; therefore, a large amount of land was allotted to industrial use to ensure the rapid development of industry. Figures 28.2 and 28.3 show China’s land supply structure over the past decade, and it could be seen that the supply of land for industry, mining, and storage, occupying more than 20%, far exceeded that for commerce and services, as well as for residences. This kind of land supply structure led to two consequences. First, there

Table 28.1 China’s urban area and construction area in 2006–2015

Year	Urban area	Urban construction area	Year	Urban area	Urban construction area
2006	166,533.5	33,659.8	2011	183,618.0	43,603.2
2007	176,065.5	35,469.7	2012	183,039.4	45,565.8
2008	178,110.3	36,295.3	2013	183,416.1	47,855.3
2009	175,463.6	38,107.3	2014	184,098.6	49,772.6
2010	178,691.7	40,058.0	2015	191,775.5	52,102.3

Source: *China Urban Construction Statistical Yearbook*

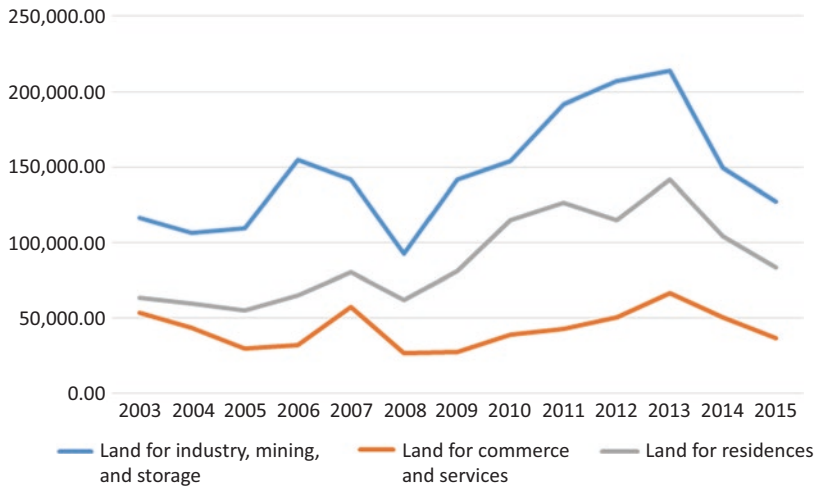


Fig. 28.2 Land supply for different uses in 2003–2015. Source: *China Land and Resources Statistical Yearbook*. Notes: 工矿仓储用地: Land for industry, mining, and storage; 商业服务业用地: Land for commerce and services; 住宅用地: Land for residences

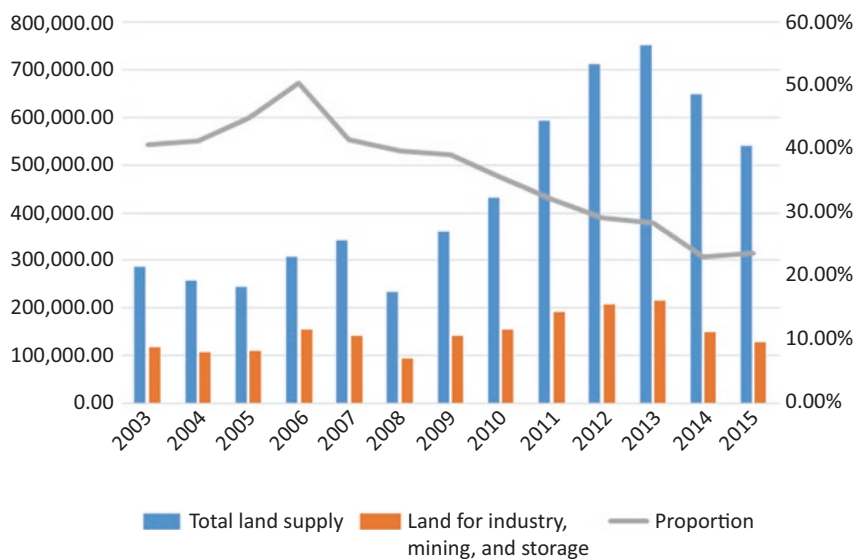


Fig. 28.3 The supply and proportion of the land for industry, mining, and storage in 2003–2015. Source: *China Land and Resources Statistical Yearbook*. Notes: 供地总量: Total land supply; 工矿仓储用地: Land for industry, mining, and storage; 占比: Proportion

is a lot of waste in industrial land. According to the statistics issued by the Ministry of Land and Resources in 2013, the integrated volume rate of national development zones was 0.83, having a building density of 29.28%, and the volume rate in some areas was much lower. Especially in the central and western regions, we saw that development zones had broad roads and good forestation but very light traffic. On the other hand, the local governments had to lower the prices of industrial land for attracting investment, so the prices of industrial land had no significant increase for more than ten years (Fig. 28.4). In fact, the transfer revenues of industrial land for some local governments could not even offset land development costs. In order to compensate that, the local governments had to tighten the supply of commercial land to ensure high-level commercial and residential land transfer revenues. The reduction in the supply of residential land led to output effects and substitution effects, the former decreasing the housing area, while the latter increasing the construction area as real estate developers used commercial capital instead of land. The actual supply of housing was affected by this decrease and increase. Our study showed that the substitution effect between land and capital was less than 1 in reality. In other words, more construction area from the increased investment of real estate developers could not effectively offset the reduction in construction area caused by the reduction in land supply. Such a chain reaction led to high housing prices since the government tightened the supply of residential land, and ultimately, the number of housings in the market became smaller.

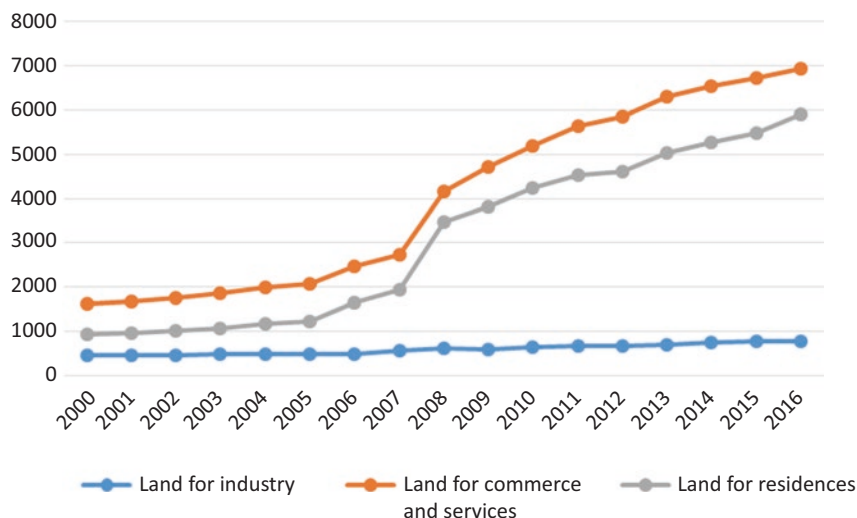


Fig. 28.4 Average prices for the land of different uses in 2000–2016. Source: *Land and Resources Statistical Bulletin* Issued by Ministry of Land and Resources. Notes: 工业用地: Land for industry; 商服用地: Land for commerce and services; 住宅用地: Land for residences

All in all, in the last round of economic growth, the big supply of construction land played a fundamental role. Cheap land expropriation ensured the low cost of land supply. In addition, the big supply of land ensured high investment; the lowered prices of industrial land protected high export. The investment attraction with land led to the accelerated industrialization and urbanization, thus facilitating the rapid growth of the local economy. Therefore, this government-led LELS Model has successfully maneuvered China's rapid urbanization, industrialization, and sustained economic growth.

2.2 The Driving Forces of Local Government-Led Urbanization

Urbanization under this government-led LELS Model embodied deep internal logic, which were the strategic responses of local governments as a weak force in the administrative system and a passive role in policies toward a series of institutional changes. Three motivations were concluded, namely fiscal incentives and development incentives of local governments as organizations and “political incentives” of government officials. In fact, the organizations and individuals, with the same goal and “incentive compatibility” reinforced this government-led LELS Model (see Fig. 28.5).

2.2.1 Fiscal Incentives

China's fiscal system has undergone several major changes since the reform and opening-up. China implemented a system of “serving meals to different diners

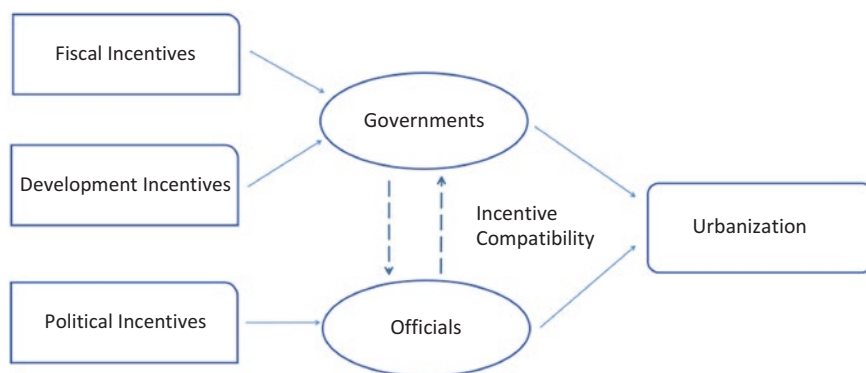


Fig. 28.5 The internal motivation of local governments in driving urbanization. Notes: 财政激励: Fiscal Incentives; 发展激励: Development Incentives; 政治激励: Political Incentives; 政府: Governments; 官员: Officials; 激励相容: Incentive Compatibility; 城市化: Urbanization

from different pots,” namely the system of dividing revenue and expenditure between the central and local governments and holding each responsible for balancing their budgets from 1980s to the beginning of 1990s. This system decentralized the power and profits to local governments; meanwhile, a high marginal sharing ratio enjoyed by the local governments in the budget stimulated them to advocate the policies of economic growth (Montinola et al. 1995; Oi 1992). However, this system led to a significant decline in two proportions—the share of fiscal revenue in the GDP (Gross Domestic Product), and the share of central fiscal revenue in total fiscal revenue—with the former falling from 28.4% in 1979 to 12.6%, the latter from 46.8% in 1979 to 31.6% in 1993 (Wu and Li 2010). In this context, in order to stop deteriorating fiscal revenues, the central government implemented a tax distribution system reform in 1994 featured by “the concentration of fiscal revenue rights while keeping the responsibilities of fiscal expenditure unchanged.” Local governments, on the one hand, had to pay a higher proportion of budget revenue; on the other hand, large-scale corporate restructuring at that time led to a substantial increase in actual expenditures. In the face of huge fiscal deficits, local governments had to seek new sources of income to relieve financial pressures.

The *Constitution* and *Land Administration Act* in 1988 endowed the local governments the rights to transfer state-owned land use rights, which was a new way for local governments to alleviate financial pressures. From a fiscal point of view, this land transfer brought two kinds of revenues for local governments. First during the land transfer, local governments collected land transfer payments from the land-using units, and the land transfer payments were deemed extra-budgetary income, over which the local governments had free discretion, and after the completion of the transfer, the local governments could levy taxes from the units. We only analyze the benefits from land transfer payments to local governments, that is, the “land finance” we refer to.

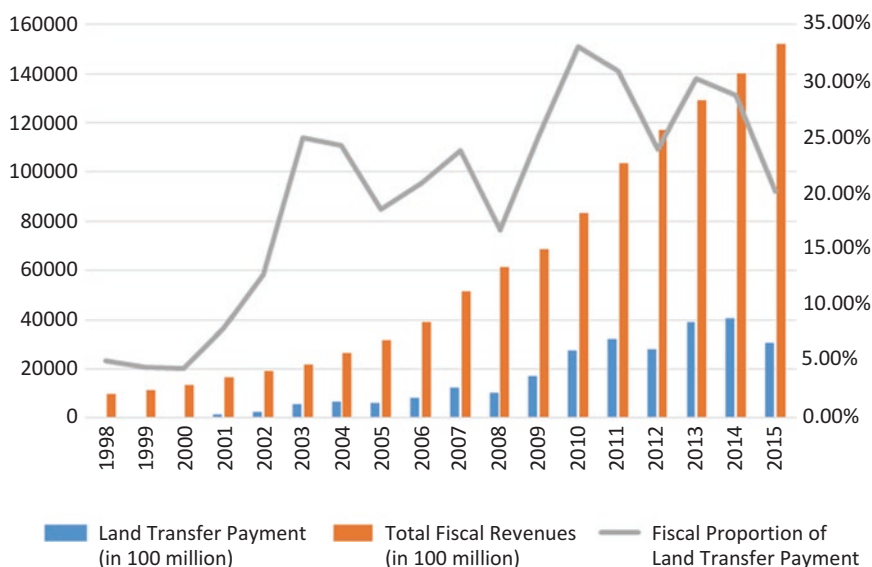


Fig. 28.6 National land transfer payment and its fiscal proportion in 1998–2015. Development incentives. Source: *China Land and Resources Statistical Yearbook* and *China Financial Statistics Yearbook*. Notes: 土地出让金(亿元): Land transfer payment (in 100 million); 总财政收入(亿元): Total fiscal revenues (in 100 million); 土地出让金占比: Fiscal proportion of land transfer payment

Figure 28.6 shows land transfer payment, total fiscal revenues, and the ratio of land transfer payment to total fiscal revenues between 1998 and 2015. At the start of the twenty-first century, land transfer revenues rose rapidly from 59.5 billion yuan in 2000 to 3078.38 billion yuan in 2015, even exceeding 4000 billion yuan in 2014. Simultaneously, land transfer revenues occupied a growing ratio in fiscal revenues, from less than 5% in 2000 to 20% in 2015, or exceeding 30% in some years. It can be seen that the sale of land did provide an important channel for the local governments to relieve financial pressure.

Apart from being a tool to “accumulate wealth,” land has become a key chip for local governments to attract investment after the mid-1990s. From late 1970s to early 1990s when China began to adopt its reform and opening-up policy, local governments were not keen on vying for such productive factors of mobility, for example, capital or labor, because the growth of secondary and tertiary industries then was mainly driven by the enterprises invested and controlled by the local governments, including rural community organizations. In other words, state-owned enterprises and township enterprises were the main forces of local economic growth. As owners sharing the resources and profits of the enterprises, the local governments were more motivated to support the development of local enterprises, rather than attracting foreign enterprises to local investment. On the contrary, some places even prevented foreign enterprises entering with local protectionism. Meanwhile, local governments could

also evade the central government's taxation by transferring the income of local firms (Che and Qian 1998). However, from the mid-1990s on, the model oriented by the development of local enterprises was no longer applicable, and the regional competition on manufacturing investment started; there are two reasons for this. First, as market-oriented reforms brought about fierce market competition, local governments could not resist market laws, and interregional trade fortresses gradually disintegrated, and local enterprises had to follow the rule of "survival of the fittest" to confront the challenges from the enterprises in domestic markets or even world markets. As a consequence, local state-owned enterprises and township enterprises could not earn more, and the enterprises as financial resources became negative assets of local governments. The second reason is the reforms on the tax division system. The establishment of a national tax system has strengthened the tax supervision system; so the gap for the local governments to evade central taxation by transferring local corporate income became much smaller (Bird and Wong 2005; Wong 1997), which also confined the local governments from supporting local manufacturing with tax tools.

As local governments could neither secure stable financial resources from state-owned and township enterprises nor evade central taxation by operating the government-controlled enterprises, they gradually shifted their attention to private investment and foreign investment, hoping to create a new economic growth point and cultivate new tax bases through foreign capital. So, the local governments would naturally face a problem of how to attract foreign capital to local investments. In addition to the commonly used means of reducing the requirements for labor and environmental protection, as well as providing preferential taxation and policies, a set of "race-to-bottom" capital attraction models by providing industrial land with low prices or even zero prices came to sight in the late 1990s; so land became a key chip to attract investment in the manufacturing sector. In the mid-1990s, when local state-owned and township enterprises completed their restructuring, the local governments began to build industrial development zones on a large scale in the late 1990s, which was most evident in the eastern coastal areas. In order to curb the "industrial zone heat," the State Council launched a national development zone clean-up and rectification in July 2003. The survey showed that there were as many as 6866 development zones with a planned area of 38,600 square kilometers within ten years, which, compared with only 2862 county-level administrative units, meant there are at least two development zones in every county. In most cases, the industrial development zones would first complete infrastructure construction and then provide other support preferential policies, in which governments' fanaticism in attracting investment could be clearly found.

It is worth noting that in the development zone boom at the beginning of the century, land preferential policies, including the agreements on selling industrial land at low prices, returning a certain amount of transfer fees based on investment, were inevitably covered in the investment-inviting policies. More often than not, the industrial land lasting for 50 years with complete

infrastructure was transferred to the hands of investors at nominal prices, or so-called zero prices. Figure 28.4 shows the prices of land for different uses from 2000 to 2016. For more than ten years, the industrial land maintained stable low prices, while the land for commerce or services and for residences increased several times. It needed high costs to deliberately control the prices of industrial land, as the local governments not only paid land expropriation costs but ensured sufficient infrastructure investment. Taking southern Jiangsu Province (including Suzhou, Changzhou, and Wuxi) as an example, our field survey showed that the industrial land with an average cost up to 200,000 yuan per mu for its expropriation and construction was sold only at an average price of 150,000 per mu, and even as low as 50,000 or 100,000 per mu in some areas. It was obvious that the local governments spared no efforts to sell their land for investment; however, it helped create the parallel development of high-speed industrialization and urbanization in the late 1990s.

2.2.2 *Political Incentives*

The political incentives faced by government officials reinforced the above model. The Chinese political institution after the reform and opening-up was mainly characterized by the decentralization of powers; so local governments had discretionary power in economic affairs of the areas (Huang 1997; Lin et al. 2005; Qian and Weingast 1997). Meanwhile, the power for the appointment and removal of local officials was in the hands of superiors. The promotion mechanism of Chinese officials was abstracted by Zhou (2004, 2007) as the theory of promotion tournament, which suggested that under China's centralized political system, superiors assessed and promoted inferior officials mainly based on economic growth of an area (Li and Zhou 2005). In this theory, local officials were considered "political people" who valued political interests, rather than so-called economic people in "fiscal federalism" proposed by Jin, Qian, and Weingast (2005). It was true that the political relations of officials had a significant impact on their promotion, but the relations could not be changed through the efforts of officials themselves; on the contrary, officials could exhibit their governance capacity by boosting local economy. Therefore, with measurable objective indicators and easy comparison of relative competition results, Li'an (2007) maintained that the promotion tournament could be effectively implemented. In addition, Li and Zhou (2005) discovered that the promotion probability of the officials could be predicted with the economic growth rate of a province; Xu (2011) attributed China's economic growth miracle to competitions among local officials. It was speculated that the organization departments of higher CPC committees were apt to measure the individual officials' capacity with the yardstick of the local economic growth rate, so as to influence the promotion of inferior officials.

In this context, local officials had strong incentives to develop local economy, which coincided with the "fiscal incentives" and "development incentives" of local governments. The work organized by the governments for their interests, such as driving urbanization, investing in development zones, and

attracting investment just accorded with the political interests of officials. If we viewed the governments as a client, and local officials as agents, both sides obviously had the same goal and incentive compatibility in driving industrialization of urbanization. Therefore, the political incentives of officials strengthened the logic behind the local government-led urbanization.

3 RETHINKING LOCAL GOVERNMENT-LED URBANIZATION

Driven by local governments, China embarked on a road to rapid urbanization. Local governments played a central role in urbanization, industrialization, economic growth, and raising people's living standards. However, some side effects of government-led urbanization emerged, such as the loss of rights and interests of landless farmers and the inefficient use of construction land. Some risks, though not breaking out, need more attention, such as growing local debts and unsustainable land finance. These problems impelled us to reflect on China's urbanization model and the role that local governments should play in urbanization.

3.1 *Protecting the Rights and Interests of Landless Farmers*

According to the *Constitution*, the government could expropriate land from farmers for public interests, but farmers need to be compensated. Land expropriation and compensation had gone through a historical process. In a planned economy and the start of reform and opening-up, the landless farmers were resettled by the land-using units; so they were recruited by the enterprises using their land. Monetary resettlement was gradually becoming a major one beginning from the mid- and late 1990s. China's "Land Management Law" stipulated that compensation for expropriated cultivated land shall include compensation for land, resettlement subsidies, as well as compensation for attachments and young crops on the requisitioned land. The compensation for the first two was respectively six to ten times and four to six times of the average annual yield value of the land in the previous three years. The lower limit of the sum of these two categories was 10 times, the upper limit 16 times, and the maximum of total compensation may not exceed 30 times, which implied that the maximum compensation was lower than 30,000 yuan if the annual yield value of farmland per mu is 1000 yuan. It was obvious that the *Land Administration Act* implemented the policy of "compensation based on the original uses of the expropriated land," which excluded the farmers from sharing the value-added benefits of farmland converted to other uses. Landless farmers in areas with developed economies could find new employments due to booming second and third industries, while those in underdeveloped areas lost not only land but the opportunities to make a living.

In the land expropriation, local governments acted as decision makers, organizers, and executors, but the image of government officials in the minds of farmers in recent years was seriously damaged in land expropriation, and government credibility was greatly reduced. In order to defend their land and basic

rights, the farmers had to rise against the governments. On the other hand, local governments were forced to expropriate land against all pressures, and sometimes resorting to tougher means, ultimately leading to collective confrontations between farmers and the governments. Our large-scale surveys on the 1200 land-expropriated farmers in 12 large and medium-sized cities in the four major metropolitan areas of the Bohai Sea, the Yangtze River Delta, the Pearl River Delta, and the Sichuan-Chongqing region between 2008 and 2009 showed that a total of 63 collective incidents (including obstruction of traffic, resistance, mass fights, demanding statements from the cadres, or police dispatched by superiors) happened. Among them, coming in the first place, 29 cases arose from the dissatisfaction with the compensation for land expropriation and demolition, 6 from unwilling land expropriation, 7 from disputes in land expropriation, and 10 from unsettled compensation placement. Only 11 cases were related to other factors, for example, poor village environments and village conflicts (see Fig. 28.7).

Land is increasing its value in urbanization; so the conflicts on the value-added land are inevitable. Disputes from land expropriation have become major reasons for petition. According to the National Bureau of Letters and Visits, 60% of the mass petitions were related to the land (Liu 2014). Although the compensation for farmers increased, and a social security system provided to landless farmers in recent years, the situation did not substantially improve, that

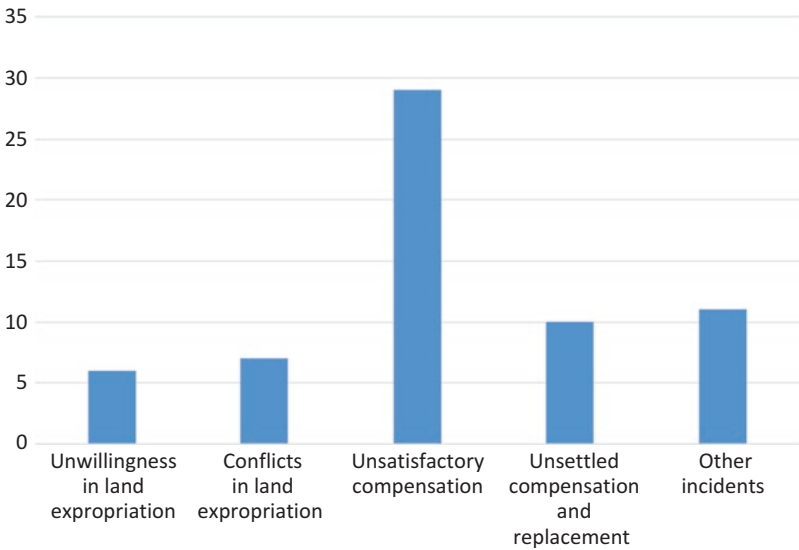


Fig. 28.7 Distribution of collective incidents based on conflict reasons. Source: According to the surveys of land-expropriated farmers in 2008 by authors. Notes: 不愿意征地: Unwillingness in land expropriation; 征地纠纷: Conflicts in land expropriation; 补偿不满: Unsatisfactory compensation. 补偿安置未落实: Unsettled compensation and replacement; 其他事件: Other incidents

is, the farmers were still excluded from the benefits of urbanization or the distribution of value-added land gains. Local development supported by land selling of the governments inevitably led to the conflicts between them and farmers or between officials and civilians. With accelerated industrialization and urbanization, land expropriation was rapidly expanding, depriving more farmers of their land and giving rise to social panic. On the other hand, because farmers had more awareness of power and rights, but were short of effective legal channels to resolve the conflicts, they had to express their demands in extreme ways, and such a large population and prolonged period would definitely endanger social stability. Undeniably, China's current land expropriation system has been a major support for economic development, industrialization, and urbanization. However, unfair distribution of land interests and low-cost forced land expropriation seriously endangered the interests of landless farmers.

3.2 “Space Urbanization, Not Population Urbanization”

Urbanization came in two major dimensions, namely “population urbanization” and “space urbanization.” In the local government-led urbanization model, “population urbanization” lagged behind “space urbanization,” which was manifested in two main aspects; one was that the growth rate of urban population was lower than the expansion of a constructed urban area, and the second was that the proportion of the primary industry in employment was lower than the decline in output value. World Bank statistics showed that in the last period, China expanded its cities at an annual average rate of 7%, while the average annual growth of urban population was only slightly higher than 3%. Figure 28.8 shows a comparison of urban area expansion and urban population

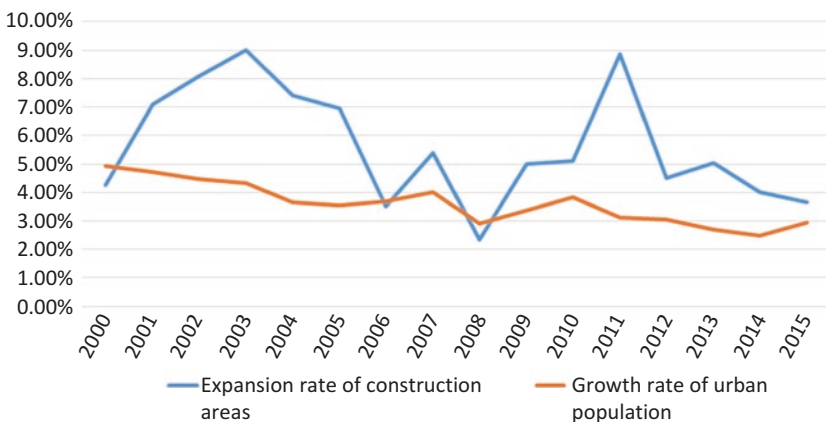


Fig. 28.8 China's “space urbanization” and “population urbanization.” Source: *China Statistical Yearbook* and *China Urban Construction Statistical Yearbook*. Notes: 建成区扩张率: Expansion rate of construction areas; 城市人口增长率: Growth rate of urban population

growth from 2000 to 2015, and our conclusion that land urbanization was faster than population urbanization was consistent with the results of the World Bank. This “Space Urbanization, Not Population Urbanization” was clearly not the essence of urbanization (Wen 2014), as in its real sense, urbanization should attract the rural population to settle in cities through strong agglomeration effect, and the population agglomeration should boost industry accumulation and the formation of scale economies. A lot of drawbacks were related to lagging population urbanization, and the urban-rural gap could not be diminished because cities were short of a constant attraction to rural farmers and traditional agriculture of low returns kept the average income of farmers at a low level. On the other hand, the nonmatching land urbanization and population urbanization made a large number of empty cities and ghost cities, leading to the low-efficient use of land and investment waste.

The declining proportion of the primary industry in employment lagging behind that in output value was another manifestation of “Space Urbanization, Not Population Urbanization.” The experience of developed countries was that the industrial structure would also be adjusted with industrialization and urbanization, exhibited in the declining proportion of the primary industry and the rising proportion of secondary and tertiary industries. Local government-led urbanization also showed the same pattern. The difference was that the transformation of the employment structure in China’s urbanization failed to keep up with the transformation of the industrial structure. In other words, the transfer of the labor force from the primary industry to the second and third industries was too slow. Figures 28.9 and 28.10 show the proportion of different industries according to output value and employment

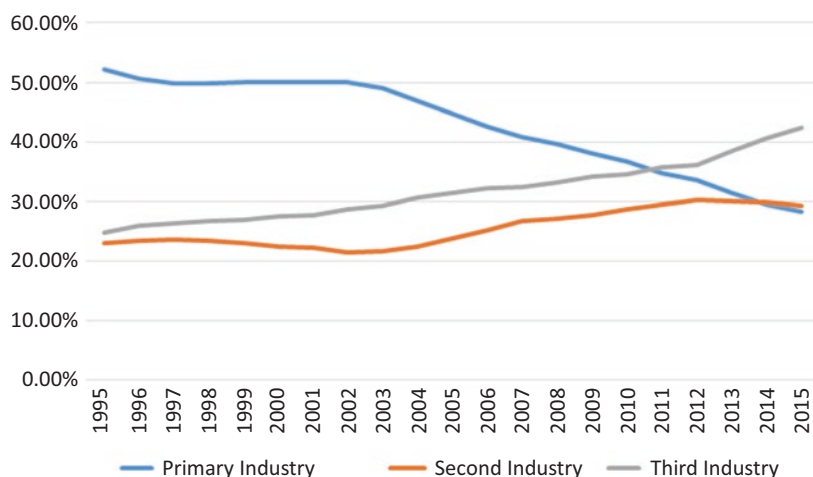


Fig. 28.9 Proportion of industries in China according to output value in 1995–2015. Source: *China Statistical Yearbook*. Notes: 第一产业: Primary industry; 第二产业: Second industry; 第三产业: Third industry

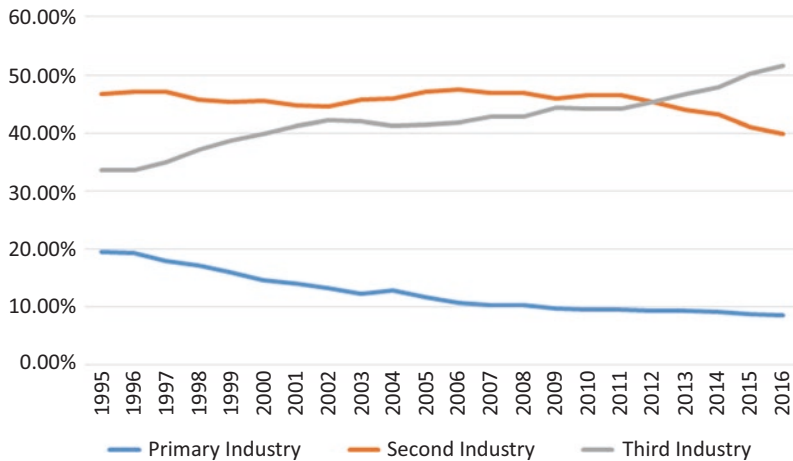


Fig. 28.10 Proportion of industries in China according to employment share in 1995–2015. Source: *China Statistical Yearbook*. Notes: 第一产业: Primary industry; 第二产业: Second industry; 第三产业: Third industry

share from 1995 to 2015. As shown in Fig. 28.9, the share of the primary industry in GDP fell from 50% in 1995 to less than 30% in 2015, while the proportion of secondary and tertiary industries steadily increased. However, the changes in employment share lagged far behind the changes in the output value structure, and the proportion of employment population in the primary industry dropped from 20% to 10% (Fig. 28.10). This meant that in industrialization and urbanization for more than 20 years, the transformation of the employment population failed to keep up with industrial transformation; a lot of labor was still maintained in the primary industry. Of course, the flow of population and labor was also related to the “semi-open” household registration system and the constraints of urban management systems (Knight et al. 1999; Cai 2000; Au and Henderson 2006), but we think our traditional urbanization model was also one of the key factors. Since the government-led urbanization could not attract enough population to cities, many of the people naturally lived in rural areas.

3.3 Unsustainable Land Finance

The value of land has increased with China’s rising urbanization in recent years, and farmers have become aware of their rights; so, the costs of land expropriation and demolition have significantly increased and the compensation to the farmers with expropriated land and demolished shelters improved remarkably. The proportion of related compensation costs rose from 42.03% in 2009 to 53.18% in 2015 in total land transfer revenues; in particular, under the “Regulations on the Expropriation and Compensation of Housing on State-

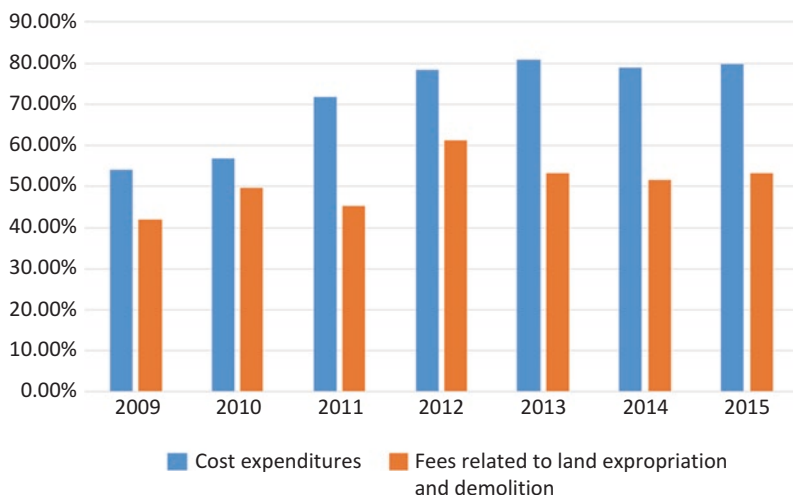


Fig. 28.11 Changes in China's land transfer costs in 2009–2015. Source: *National Land Transfer Revenue and Expenditure* issued by the Ministry of Finance. Notes: 成本性支出: Cost expenditures; 涉及征地拆迁相关费用: Fees related to land expropriation and demolition

owned Land,” costs in 2012 were even more than 60% (Fig. 28.11). At the same time, the expenditure prior to land development also increased. In recent years, the costs for land transfer only accounted for 80% of land transfer revenues. It is predictable that, in continuing urbanization, it will be more and more difficult to expropriate land with the compensation on original uses as the compensation costs for land expropriation and demolition continue to grow. It was most evident in the rural-urban continuum and urban expansion areas; so, China's urbanization would slowly bid farewell to the low-cost period supported by low-price land expropriation compensation. This meant the land transfer returns were getting smaller for local governments.

Another risk of relying on land finance was the volatility of land transfer revenues. The total contract price of land transfer in China increased from 60 billion yuan in 2000 to 3.56 trillion yuan in 2015, with an average annual growth rate of 35.62% (Fig. 28.12). Although the land revenue continued to increase at a stable rate for a longer period of time, it showed a large fluctuation between years, for example, more than 50% average annual fluctuation in land transfer revenues between 2000 and 2016. In particular, affected by a macro-economic situation after 2010, there were obvious fluctuations between years in land transfer revenues. The excessive reliance on land finance would transmit the volatility of land transfer revenues to local finance, which also threatened the stability of fiscal revenues.

As mentioned above, the significance of land to government finance was not only the land transfer revenues and consequent tax revenues but loan finances

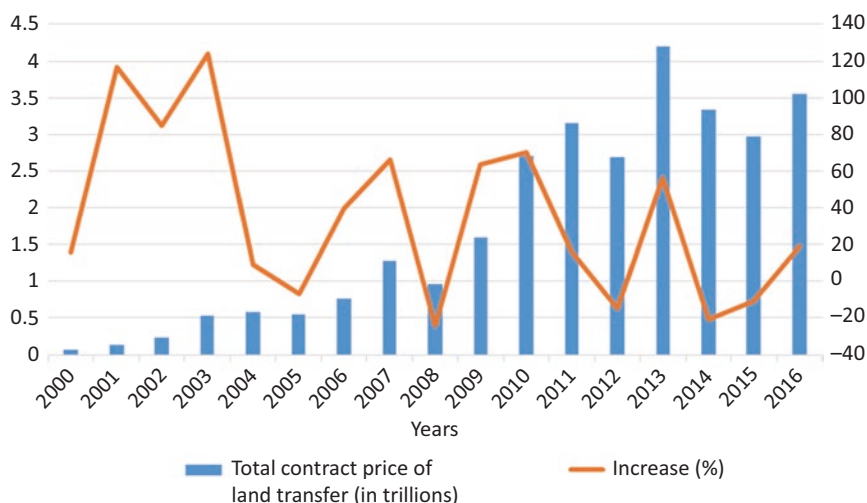


Fig. 28.12 Fluctuations of land transfer revenues in 2000–2016. Source: *Land and Resources Statistical Bulletin* issued by the Ministry of Land and Resources. Notes: 年份: Years; 土地出让合同总价款(万亿元): Total contract price of land transfer (in trillions); 增幅(%): Increase (%)

for local governments with land as collateral. In recent years, China has shown a dramatic increase in its land mortgage area and land mortgages. From 2009 to 2015, the land mortgage area of 84 key cities in China grew from 217,000 ha to 490,800 ha, with an average annual increase of 21%; land mortgage loans increased from 0.259 billion yuan to 1.133 billion yuan, its average annual increase of up to 56.3% (see Fig. 28.13). Land mortgage increased from 6.5% in 2009 to 12.1% in 2015 in total RMB loans from national financial institutions, an increase of about 100%.

The risk of land mortgage loans was first manifested in local debts. According to the report of the National Audit Office, China's local government debt reached a balance of 17.2 trillion yuan at the end of 2016, accounting for 23.1% of GDP in 2016, and if the public sector debt and the financial bonds issued by policy financial institutions were taken into calculation, China's total public debt rate reached 55%. Although this figure was still lower than 60% of the GDP, a warning line set by the European Union, the situation in some areas was not optimistic; especially in China's western areas, the local debt was as high as 36.4%, far more than 16% of the local government debt ratio line set by the United States.

In fact, local governments relied on land for this round of loans, and debt borrowing and paying were both heavily dependent on the land. According to the report released by the National Audit Office in 2014, local governments needed to pay 10.89 trillion yuan for their debt by the end of June 2013, of which 40% was promised to be paid from the land selling and even more than

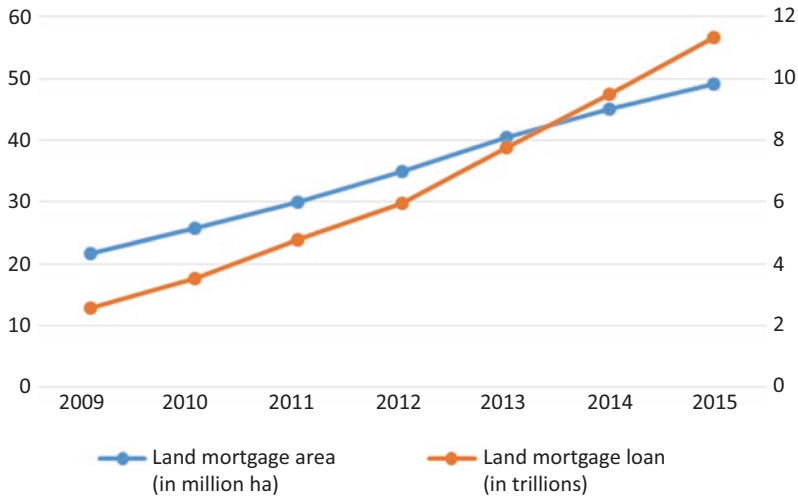


Fig. 28.13 China’s land mortgage area and land mortgage loan in 2009–2015. Source: *Land and Resources Statistical Bulletin* issued by the Ministry of Land and Resources. Notes: 土地抵押面积(万公顷): Land mortgage area (in million ha); 土地抵押贷款(万亿元): Land mortgage loan (in trillions)

50% in some areas, for example, close to 65% in Zhejiang and Tianjin. On the other hand, the borrowing with land as the subject matter also increased the financial risk of banks. More than 50% of the total government loan of 10.89 trillion yuan came from bank loans. Local governments would be unable to pay the debt once the land transfer payments continued to fall. Unfortunately, as we mentioned earlier, the net income of local governments from land transfer has declined significantly in recent years, and land transfer revenues were rather unstable; so local governments were bound to have potential debt risk with the declining earning power and unstable land transfer revenues as a major source of debt payment.

4 GOVERNMENT TRANSFORMATION: FROM LEADERS
TO COLLABORATORS AND SUPERVISORS

When we reflect on the history of the social governance model of humans, we find out that the social governance structure since modern times tended to regard governments as the only subject of governance, which led to the domination of the social forces from the governments. The governments, as the core of governance of public affairs, provided institutional arrangements to the society and managed social affairs. With the diversification of management subjects in the post-industrial era, nongovernmental organizations (NGOs) have become key participants in social governance and have collaborated with governments in social governance. This governance model was characteristic of

cooperative governance. O'Leary et al. (2006) defined it as a common model of collaboration between two or more government agencies, private sectors, and civic groups for addressing the public policy challenges that government agencies were unable to solve on their own. Successful co-governance should satisfy the following points:

1. **Consultation among collaborators:** As Roberts (2016) pointed out, consultations need to be listened to, collaborators' views need be considered, and joint decisions need to be made concerning public affairs.
2. **Effective participation:** A cooperative group should invite the representatives that have different goals, relationships, identities, or institutions to solve problems and resolve conflicts (Lulofs and Cahn 2000).
3. **Abilities of joint action:** A cooperative group should enhance their abilities, and of others, through formal and informal agreements, as well as the designs and rules for institutions to achieve common goals.

Cooperative governance basically eliminated government centralism, which broke the centralist structure of public participation in government affairs by voluntary behaviors of equal subjects. One key point that distinguished co-governance from traditional government-centered social governance was that it broke the singularity of political goals in public policies and put policies out of the single-line linear responsibility for political institutions. One of the inevitable consequences of co-governance was that public policies were influenced by the multiple values of different interest groups. As pointed out by Downs (1967), in the governance system of an industrial society, because the government was the only subject of governance monopoly, internal department measures were taken for the acquisition and allocation of resources, while in cooperative governance, a cooperative organization could make a variety of choices based on its own function, size, and participants, and such a flexibility led to higher efficiency and more equitable results.

It was easy to find that traditional Chinese urbanization was mainly characterized by government-led administrative power. As we have described above, China's urbanization and industrialization from the late 1990s onwards were achieved by government-led LELS Model with legitimate rights. However, many drawbacks were debunked in this model. From the perspective of social governance, these drawbacks may only embody the evils inherent in urbanization from the government-centered governance model. For example, landless farmers lost their rights just because they did not have the power of discourse in land expropriation and the policies were only responsible to government agencies. So the best corresponding solution was transforming government governance to collaborative governance, which required the transformation of local governments from leaders to collaborators and governors in urbanization. However, a common concern was that, with the lessening urbanization in general in China, if the governments reduced stimulation to urbanization, urbanization might be stagnated; in fact, this concern was unnecessary. The

successful experience of urbanization in Western countries told us that, apart from administrative powers, urbanization was propelled by market forces more, and urbanization could still be achieved without government leadership. On the contrary, market-oriented urbanization would be more conducive to its real meaning, that is, rural population was attracted to settle down in cities with strong agglomeration effect of cities. The chapter provides two cases in Zhejiang and Guangdong to prove that the transformation of local governments' roles will not hinder urbanization; instead, it will lead to a more healthy and sustainable urbanization in China.

4.1 New Urbanization Under the PPP Model

We mentioned that the major cause for China to have embarked on such a local government-led urbanization was that local governments were facing heavy financial pressure; so, they either sold land to collect land transfer payments or sold industrial land at lower prices to attract investment as tax sources, and then urbanization followed. Meanwhile, the infrastructure construction in cities also needed a lot of investment, so local governments had to depend heavily on land finance. In fact, this vicious circle revealed a problem, that is, "where the money is from" faced by local governments in urbanization. In the expropriation of land transfer revenues in the traditional model, the local governments were also responsible for heavy urban construction expenditure; so the governments of some cities depended on loans to drive urbanization. We think the root cause was that local governments were the leaders monopolizing land, selling it, and constructing the cities. The new urbanization under the Zhejiang PPP model offered a good case in which the local governments no longer served as leaders; instead, they were "collaborators" and "guides."

The PPP model was traced back to the toll road construction in the eighteenth century in Europe, but in a modern sense, it was born and developed out of the market reforms where the private sectors were invited to be active participants of public services in the new public management movement. In order to alleviate the tight financial pressure by the economic recession in the 1970s, Britain and America vigorously introduced private sectors into public projects to operate jointly with government capital, which promoted PPP. To stimulate economy after the debt crises in moderately developed countries in the mid-1980s, many countries managed to lessen their financial burdens by introducing social capital (e.g., Turkey introduced Build-Operate-Transfer (BOT) to build nuclear power plants, which was also a PPP model). With the continuous improvement of norms, PPP has gradually become a key operation model for governments to adopt the joint cooperation of multiple subjects in public construction.

In recent years, the PPP model has been implemented in the urbanization of Zhejiang Province to facilitate the collaboration of government capital and private capital in urban construction. It is written in the "13th Five-Year Plan for Economic and Social Development in New Urbanization in Zhejiang" that "operational fields shall be open legally for the development, construction, and

management of markets. Quasi-operational fields are open to social capital with the collaborative mechanism of investment, subsidy, and price based on the PPP model and equity cooperation.” A wide range of urban investment projects were involved in the PPP, including the investment in infrastructure roads, municipal green environment, and high-end smart cities. It is worth mentioning that PPP has played a key role in the development of several characteristic towns well-known in China in recent years. In particular, social capital and private capital were quite conducive to those financially weak areas and the areas lacking substantial and continuous capital inflow.

Although the PPP model could provide more funds for urban construction and was a possible alternative for local governments to alleviate financial difficulties, the pivotal question was how to attract private capital in urban construction. It is self-evident that private capital was oriented toward markets and profits, so its participation in urban construction projects was motivated by profits. However, there were obstacles for private capital to flow into PPP at present, and they are shown in the following. First, there lacked a sound legal foundation for private capital to flow into urban infrastructure investments. Second, there were government default risks. As urban construction was featured by large investment and a long payback period, most of the enterprise investment returns were from the financial payment of governments; the enterprises would be in deep waters if governments failed to pay. Currently, local governments were “leaders” in urban construction, so local governments faced rather low penalty costs. Third, there was a shortage of risk-sharing principles. Similarly, since the current governments were “leaders,” they were used to shirking their responsibilities while authorizing one project to private investors, which put private investors in unfavorable positions.

We believe the key is that the governments have to change from “leaders” to “collaborators” and strengthen their contract spirit by setting up a contract system. With a sound contract system, the government responsibilities are regulated, penalty for the contract breach made clear, and effective governments monitoring conducted by private departments to dispel the worries of private capital. On the other hand, local governments should play the role of “guides.” Through policy guidance, enterprises are given certain tax reductions and land preferential policies, so the investment costs of enterprises are diminished to attract social capital into urbanization. Zhejiang Province did a good job in this area. A professional PPP investment committee, as a platform for the consultation of government and private sectors, was set up in Zhejiang Province in July 2015 to serve the urbanization strategies of the governments.

This kind of government-enterprise cooperation scored achievements in promoting urbanization and urban construction. Ningbo was one typical example. 42 PPP projects with a total social capital of 45.6 billion yuan were approved in Ningbo in 2015, of which, more than 10 projects were included for national demonstration and pilots. For a long time, urbanization and urban construction have been operated by the government alone and the investment on municipal facilities carried out by public sectors, which not only brought

heavy financial burdens to local governments but led to low efficiency in urban construction—for example, jelly-built projects due to a government monopoly. Social capital provided sufficient funds for urban construction and also alleviated the governments from heavy construction funds. Meanwhile, with a clear division of responsibilities of government and social capitals stated in contracts, risks can be reduced and distributed so as to share benefits and risks together.

The model of encouraging social capital and private capital into urbanization inspired us a lot. First, local governments can be lifted out of the vicious cycle of “financial pressure–land selling–urbanization–financial pressure,” as the governments act as guides to develop reasonable policies to attract private capital for sharing costs, risks, and benefits, without the need for public finance to bear all the construction funds. Second, the Zhejiang model also makes us realize that the key to the above changes is the transformation of local governments in their roles. The local governments would inevitably return to the LELS Model and bear the high cost of urban construction if they promoted urbanization as leaders. On the contrary, if the local governments participated in urbanization as collaborators and guides, it would effectively make up for the funds, resolve the debt crisis, and alleviate them from dependence on “land finance.” More importantly, because the urbanization is no longer driven by administrative power alone, but by market forces as well, it will help redress the “land urbanization, not population urbanization,” leading urbanization to its true meaning.

4.2 “Nanhai Model”: Spontaneous Urbanization from Farmers

Nanhai District in Foshan City, located in the heart of the Pearl River Delta, occupies an area of 1073.82 square kilometers. As of 2015, the district had a total population of 3 million with a disposable income of 39,625 yuan per capita, of which urban residents had disposable income per capita of 40,148 yuan and rural residents had net income of 25,909 yuan. Different from the LELS Model, Nanhai stepped onto urban-rural joint development for rural prosperity by inviting farmers to participate in urbanization with their land. The Nanhai Model was mainly characterized by the industrialization and urbanization carried out on collective construction land. According to the results of the second national land survey, Nanhai had a construction area of 797,500 mu, of which 71% (that is, 565.500 mu) was the rural collective construction land.

A large number of enterprises came to Nanhai to look for land and invest in factories in the early 1990s. For satisfying their needs, collective economic organizations at the village and group levels of the Nanhai District applied for land for the establishment of township enterprises, prepared relevant land use right certificates, and then rented the land to the enterprises seeking investment. The establishment of enterprises on collective land avoided national land expropriation; so the land was directly put into industrialization. Most importantly, the differential benefits from the nonfarming land use were kept

within the villages, and the farmers could enjoy the value-added land benefits as they had land ownership as a collective. According to statistics, Nanhai District reaped a total industrial output value of 422.6 billion yuan in 2012, and more than half of the industrial land was provided by the collectively constructed land.

In fact, an array of problems appeared in the spontaneous urbanization of the Nanhai District in more than 20 years, such as excessive land development, lack of planning guidance, decentralized layout, and low land use efficiency. In facing these problems, the government played an active role as a governor. With the innovation in the land system and mechanism of profit distribution, a community of shared interests between the government, collective, and farmers was constructed and moderately complete institutional arrangements were made for effective intensive land use, industrial upgrading, and urbanization.

The first step in the cooperative governance of urbanization was to confirm the rights of rural collective land, which ensured its legal use and transaction. First, it was confirmed that collective land included not only the rural collective land except cultivated land, rivers, tidal flats, and fish ponds but nonfarming land for industry and tertiary industry. The second was to define the property rights left over by history. The land that had become collective land but not obtained legal formalities before January 1, 1999, confirmed its rights if only it was the land within the construction land area of overall planning. Third, the certificates of rights were conferred on rural collective economic organizations and landowners after the rights confirmation, and land ownership certificates were conferred directly on the villages in line with the provisions. As of 2013, more than 90% of the collective construction land had confirmed its rights. Clear subjects of rural collective land property laid a foundation for the transfer of collective construction land use rights.

The second step was to standardize rules for the land transactions. In order to standardize and promote the transfer of collective construction land, Guangdong Provincial People's Government introduced the "Methods on the Management of Collective Construction Land Use Rights Transfer in Guangdong Province" in 2005. Based on that, Nanhai District formulated "Methods on the Management of Collective Construction Land Use Rights Transfer and Rent in Nanhai District, Foshan City" and "Methods on the Management of Collective Construction Land Use Rights Transfer, Sublease, and Mortgage," specifying the "same nature, same price, and same rights" of rural collective construction land and state-owned construction land and allowing rural collective construction land to flow into markets through selling, transfer, rental, mortgage, and so on. As for the state-owned reserved land, if the persons owning land use rights did not change or the land did not change its uses, original users had the rights to handle the land, not subject to public transactions. If the rural collective construction land was used for real estate development projects, the procedures were necessary for the transfer of the collective to the state-owned land and for public transaction.

The third step was to draw up the methods for transferring collective to state-owned construction land. Collective construction land in industrial zones was transferred to state-owned construction land within village collectives with legal transfer formalities. Original owners (i.e., original village collectives) whose collective land was transferred to state-owned land could enjoy the distribution and share-holding of property, so their rights were protected. It facilitated the transfer of collective land to state-owned land without the expropriation from local governments.

Fourth, a benchmark land price system was established to regulate the transfer market of collective construction land. Nanhai District spent two years from early 2011 to 2013 in setting up the benchmark land price system for collective construction land. At the beginning of 2013, Nanhai District People's Government promulgated the "Notice on Implementing Benchmark Land Price for Collective Construction Land in Nanhai District," which included the benchmark land price and benchmark rent of collective construction land in existing and planned areas. When a perfect market was not nurtured, the establishment of a benchmark land price system provided an effective reference for the transaction of collective construction land.

Under the abovementioned norms, collective construction land was not only transferred legally but protected technically by the governments. With the establishment of transaction platforms for collective town and village assets, a collaborative pattern of the collectives owning land, farmers enjoying benefits, and governments assisting governance was formed, so that villages and farmers enjoyed the fruits of urbanization and value-added land benefits. Collective land rent increased from 2.26 billion yuan in 2008 to 3.02 billion yuan in 2012; dividends per capita in villages and groups rose from 2347 yuan in 2008 to 3516 yuan in 2012. Farmers' net income per capita grew from 11,158 yuan in 2008 to 25,909 yuan in 2015, an average annual increase of 18%; the urban-rural income ratio was narrowed from 2.33:1 in 2008 to 1.54:1. On the other hand, the economic strength of villages and groups was greatly enhanced. By 2012, their collective assets amounted to 30.6 billion yuan, of which 16.1 billion yuan was reaped by economic communities and 216 villages had a total income of more than 100 million yuan.

The "Nanhai Model" provided a way for farmers to share the value-added land benefits in urbanization, giving rise to a win-win for government and farmers, and urban and rural development. This case made us rethink the roles of governments in urbanization. We believe that the governments did not necessarily play a leading role in urbanization, nor pioneer the way for rapid urbanization. On the contrary, we feel the bottom-up economic vitality of rural collectives in the Nanhai Model. Of course, this spontaneous urbanization was often characterized by collective irrationality, which may lead to the overexploitation of land, the lack of planning, and low utilization. But interestingly, due to the "malfunction" of spontaneous forces, it was essential for the governments to participate in urbanization; however, the governments were not "leaders" at this time but rather "governors." With more talented people,

richer resources, and stronger power, the government could develop a series of norms to help village collectives form a complete system of land transfer.

Compared with government-led urbanization, the success of government-governed urbanization was reflected in two aspects. First, the farmers in the Nanhai Model shared the fruits of urbanization. As mentioned above, the urbanization driven by local governments led to a large number of landless farmers, who only received very low compensation and were excluded from value-added benefits of farmland transfer, which tended to become the focus of social contradictions. However, in the Nanhai Model, farmers enjoyed the benefits of urbanization and industrialization, instead of losing their land. Second, because this model was propelled by bottom-up market forces, urbanization was coming along with the transfer of farmer employment; “population urbanization” did not lag behind “space urbanization.” To sum up, the Nanhai Model addressed many problems in the urbanization effectively, for example, damaged interests of landless farmers and imbalanced population and employment structures.

5 CONCLUSIONS AND PROSPECTS

This chapter explored the role of local governments in the traditional urbanization model and the correct role for the governments. We note that China’s urbanization since the late 1990s was obviously government-led, that is, the local governments promoted rapid industrialization and urbanization through the LELS Model. Specifically, the local governments first collected farmland from farmers with land-expropriation rights, sold the land to land use units after transferring farmland to state-owned land, which triggered China’s industrialization and urbanization. There were fiscal and development motives behind this government model. On the one hand, low-cost land expropriation provided adequate construction land to local governments; low price and sufficient supply of industrial land attracted foreign investors. On the other hand, pressed by fiscal burdens, local governments had to decrease the supply of land for commerce and services to keep its transfer prices at a high level. Meanwhile, motivated by promotions, the officials as the agents of governments were eager to attract foreign investment and boost local economy, which was compatible with the governments as consignors in the incentives. The government-led LELS Model was intensified as the governments and officials had the same goal and compatible incentives.

However, the government-led urbanization pattern exposed many drawbacks. The low-price compensation to landless farmers based on original land uses stirred severe dissatisfaction among farmers and social instability. The “population urbanization” far behind “space urbanization” in speed prevented the potential labor from entering the markets, resulting in sluggish employment transformation and low inefficient land use. In addition, the dependence of local governments on unsustainable land finance, as well as large urban

construction investment, accumulated heavy local debts, posing latent risks to the country's financial systems.

The key to stepping out of the traditional urbanization model lay in the transformation of government roles. In the traditional urbanization model, the local governments drove urbanization as leaders, inevitably resulting in many of the problems stated above. However, there was a misconception among many people that China's urbanization would be stagnant without government forces, so the governments delayed in using "visible hand" to promote urbanization. In fact, the spontaneous bottom-up market behaviors could also push forward urbanization, and the Nanhai District in Guangdong Province was a case in point in its urbanization of collective construction land. The governments as governors curbed irrational collective behaviors, for example, overheating land development and lacking planning. This kind of urbanization with spontaneous farmer behaviors and government participation was not only superior to the government-driven urbanization, but more importantly, it created a win-win situation for the governments and farmers, as farmers were entitled to enjoy the fruits of urbanization and value-added land benefits. The participation of governments as collaborators was a new type of urbanization under the PPP model in Zhejiang. The investment in urban construction from government capital, social capital, and private capital eased the shortage of funds and helped local governments alleviate the financial burden from urban construction. Moreover, the urbanization model with the governments and individuals sharing costs, risks, and benefits avoided blind urban expansion driven by administrative power. Generally speaking, we think that only after the transformation of local governments from leaders to collaborators and governors to help form a collaborative governance of governments and the society, as well as governments and markets, can China step onto a healthy road to urbanization, which is also the correct orientation for future urbanization.

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