
Third Ways

Modern China

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Abstract

This article compares the Chongqing model of the “third hand” with various theories of the “third way” in late socialist Eastern Europe. The third hand is praised as an intriguing attempt to offer an alternative to the invisible hand of the free market and the redistributive hand of state socialism. Funding of public goods from capital gains from government-owned land and real estate is an innovative idea, but it is unclear whether it is a sustainable proposition. China may be developing a real estate bubble similar to the one that has recently burst in the United States and continental Europe. The key question is: can prices of land and real estate grow indefinitely faster than wages?

Keywords

third hand, third finance, third way, real estate bubble

As state socialism during the 1980s was entering the terminal stage of its economic ills a new specter haunted the world, the specter of the “third way.”

The idea of the “third way” was not all that new.¹ Its origins can be traced back to the nineteenth-century German notion of *Sonderweg*: a uniquely German way to modernity that escapes the individualism/anarchy of the English and French ways of development on the one hand and the despotism of Russia on the other. The intellectual and political history of the idea of *Sonderweg* is complex. During the nineteenth century and the first half of the

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twentieth century it was mainly nationalistic. It was even an inspiration for Nazi theory (which combined anti-bourgeois ideology with anti-bolshevism). After the Second World War many liberal German historians used the notion of *Sonderweg* to explain why modernization/embourgeoisement in Germany was blocked. *Sonderweg* was now blamed for the rise of Nazism. Eventually some—most eminently Jürgen Kocka—half rehabilitated the German *Sonderweg*. Kocka argued that Germany in fact found the golden middle path between the English and Russian roads to modernity (Kocka, 1987). In England, the march to modernity was led by a propertied bourgeoisie, in Russia by the state or state bureaucrats, while in Germany the major force of modernization was the “men of ideas,” the “cultural bourgeoisie” (*Bildungsbürgertum*). Hence German modernity has more culture or civilization and less greed and bureaucracy than the English or Russian version of modern society.

At the end of World War II, Polish, Bulgarian, and Hungarian left populists resented their countries’ being put before a false alternative: they either had to adopt the Western European/American model of capitalism or they had to convert to the Soviet version of communism. They insisted: there must be a “third way” that transcends Western greed and Soviet bureaucracy, a collectivist, egalitarian, free, and efficient system of the economic and social organization.

Third roaders or *narodniks* were arch enemies of the Bolsheviks²: being a “bourgeois liberal” might have been a lesser evil than being a “left populist.” So any talk about the “third way” was forbidden fruit until the system began to disintegrate. But in the 1980s, suddenly a great variety of “third way” theories emerged. In Europe these theories were short lived: by 1990 or so neoliberalism was hegemonic. “Populism” or “the third way” became a pejorative term, which was used to label out of discourse the critics of neoliberalism. “The third way is the road into the Third World” was the neoliberal slogan; being pro-business (“friends of business”) became the only rational attitude; populists (“friends of the people”) were fascist or at best proto-fascist.³

But let me return to the 1980s and to the epoch when the specter of third way haunted state-socialist Europe. During the 1980s I was teaching at the University of Wisconsin in Madison. I was doing research on the reemergence of small family farmers in Hungary (I called them “socialist entrepreneurs”—see Szelenyi, 1988). The Open Society generously funded two distinguished Hungarian agrarian scholars, Pál Juhász and Bálint Magyar, to spend a semester collaborating with me on my book on socialist entrepreneurs.⁴ They both became after 1990 members of the (Neo-)Liberal Party; Magyar served as Minister of Culture and Education for many years and became one

of the leaders of the party. But back in 1985 when they visited me they belonged to what I called “the socialist opposition.” I remember our very first conversation in Madison at the dinner party shortly after their arrival. Juhász and Magyar described to me what appropriate agrarian policies are and I was stunned by the extent of uses of private property and market mechanisms in their proposals. At that time I identified myself as a democratic socialist, so with probably a slight misgiving in the intonation of my voice I asked: “Are you recommending the restoration of capitalism?” Juhász was upset: “What is this nonsense of dichotomy between socialism and capitalism? Cannot we think about a third way?” As a socialist I had not before then given much consideration to the idea of the third way, but he persuaded me. Indeed what seemed to have been emerging in Hungary (and by the way, in China) in the rural sector during the 1980s was an interesting hybrid of socialism and capitalism—it appeared appropriate to describe it as a third way between the two competing systems. With due immodesty let me cite myself, in this much-forgotten book in 1986:

For a while it appeared that the sovietization of Eastern Europe in 1949 and the forced collectivization of agriculture had irreversibly closed off the possibility of a Third Road. But in different ways the idea is returning to the political and theoretical agenda in this part of the world. In Poland, most theorists of the Solidarity movement have emphasized that they seek an alternative to Soviet-style socialism which is also different from the Western socioeconomic system. In Hungary in particular, the resurgence of family entrepreneurship . . . can be interpreted as proof that is uniquely East European, Third Road development maybe, not just a theoretical fantasy, but a stubborn trend in history. (Szelenyi, 1988: 17)

And let me add one more citation from this book, which echoes some of the themes of Philip Huang’s article “Chongqing: Equitable Development Driven by a ‘Third Hand’?”:

Theorists of the political Left and Right both often presume that systems tend to develop toward their pure form or ideal types. . . . Mixed economies will not last too long: a little welfare-state activity in the West is “creeping socialism,” a little market activity in the East is “creeping capitalism.” In the last instance, countries will have to choose; there are no alternatives. . . . The idea of . . . a “Third Road” is often ridiculed as naïve or utopian. This book is about the viability

of that Third Road. Our story suggests that mixed economies can reproduce themselves, that more complex systems adapt more effectively to economic challenges. (5)

During the early 1980s, even economists who later became advocates of neoliberal capitalism usually did not see the world as divided into well-functioning capitalist and poorly performing socialist economies. When I read Kornai's most formidable 1980 book *Economics of Shortage* I believed I was reading an institutionalist economist who did not advocate market capitalism over socialist redistributive (or to use Kornai's terminology "bureaucratically coordinated"—see Kornai, 1984) economies. In my reading, Kornai offered what David Stark later called "mirrored comparisons" between capitalism and socialism (Stark, 1986). Yes, Kornai identified the tendency to produce chronic shortages under the socialist system, but he also showed that capitalist economies tend to produce crises of overproduction. While the book does not offer explicit policy recommendations, in my reading in 1980 Kornai was in favor of mixed economies in which the two crises-tendencies soften each other. When I wrote the above passage I believed I was on the same page with Kornai. Well, I either misinterpreted him or he might have changed his mind as history changed (Kornai, 1992).

Much like with the theory of the "third hand" in Chongqing today, the "concepts and features" of such a third way were "not yet entirely clear," to paraphrase Philip Huang. My "third way" was the way agrarian reform progressed in Hungary—what arguably might have been the model from Deng's agrarian reforms during the early 1980s. Here the initial idea was simple: keep the collective farms but let the peasants do whatever they want on their family plot—family work organizations and the thus emergent peasant entrepreneurship solved the chronic food shortages overnight. In such a "mixed economy," the state redistributive sector was dominant but it was complemented by a dynamic, expanding small private sector (later, in the book *Making Capitalism without Capitalists* I called this strategy "capitalism from below"—Eyal, Szélenyi, and Townsley, 1998). While the Hungarian system of the 1970s and 1980s was not identical to the Chinese reforms after 1978, they had many similarities.

But there were other visions of "third ways." One popular idea of the 1980s in Eastern European socialism was "market socialism" (which eventually had its impact in China as well): one should retain public ownership, but make state enterprises interact with each other via markets. The most radical form was the "holding system." The point of departure of the theory of generalized holdings was that nationalization is an irreversible process:

once property was nationalized it cannot be returned to private ownership. As a future neoliberal economist in the mid-1980s told me—with some sadness in his voice—“We know how to make fish soup from fish. But how can one make fish from fish soup?” The holding system theory recommended creation of competitive, though state-owned, commercial banks or holding companies. State-owned enterprises (SOEs) would be converted into stock-holding companies, but their stocks would be held and traded by government-owned banks or holding companies on the free market. Yasheng Huang claims in his *Capitalism with Chinese Characteristics* (2008) that most of the “privatization” of the public sector in China happened this way. What appears to be private ownership is not really private—most of the formerly SOEs’ stocks are held by “legal persons,” banks or holding companies owned by the government.

Another attractive idea for a third way between capitalism and socialism was universalized private ownership with a small market, a kind of neo-Proudhonian dream: one should privatize the whole public sector but not via markets or competitive auctions. All public property should be split into vouchers and every citizen should get an equal share of public goods in vouchers. Even after the collapse of the socialist system, President Yeltsin used this populist-socialist ideology. When he announced mass privatization he proclaimed: we do not want a few millionaires, we want millions of owners.

The 1980s in socialist Eastern Europe was a decade of utopias. Every intellectual with some self-respect came up with a scenario of how to make socialism work by eliminating its bureaucratic structures but without converting the system into Western-style competitive and greedy capitalism.

Juhász and Magyar made me believe in the third way so much that I wrote an auto-critique (Szelenyi, 1986–1987). In my 1979 book *The Intellectuals on the Road to Class Power* (Konrád and Szelenyi, 1979)—written as a reflection of the 1960s reform era—I believed that the idea of rational planning has a fatal attraction for “intellectuals”; they are likely to prefer the rational order of redistribution over the anarchy of the market, hence they are ready for the big historical compromise with the ruling bureaucratic estate and constitute themselves as the new dominant class of the state socialist redistributive economy. I was expelled from Hungary in 1975 and when I was first allowed to return in 1982 I was astonished by the expansion of the small private sector. This was not the same system I left just seven short years earlier. My research on the emergent private sector in agriculture persuaded me that the new class emerging is not a techno-bureaucratic intelligentsia but rather a socialist petty bourgeoisie. The big winners of the early reforms were

peasants and workers who entered the rapidly expanding informal economy. Victor Nee in his 1989 path-breaking “A Theory of Market Transition” reported the same process in the first years of the 1980s in China (Nee, 1989). Hence I decided it was time to offer an auto-critique, which appeared in *Politics and Society* in 1986–1987, in which I conceded that the intellectuals are not likely to attain or even aspire to class power; rather, the new class coalition is more likely to be between the bureaucratic estate and the new class of socialist petty bourgeoisie.

But history wanted it to happen differently. It was the very bureaucratic estate that walked away from this class compromise in 1989–1991. The rulers of the ancient regime could not and did not want to rule the old way. They saw the new opportunities for themselves and their children in turning their systems into fully fledged market economies and at the same time enriching themselves. The ones who were “building socialism” took upon themselves the task of “building capitalism.” Petty capitalism built from below was suddenly abandoned; the big losers in the market transition were the socialist petty bourgeoisie and the big winners were the former communist cadres and their clients, and now capitalism was built from above.

It was time again for a second auto-critique. In my 1998 book *Making Capitalism without Capitalists*, I acknowledged that my 1986–1987 auto-critique was premature. In Eastern Europe the third way did not happen, the socialist petty bourgeoisie did not establish itself as a new class; rather, many of them were pushed into the sub-proletariat.

Which way China is going was and remains an important and controversial subject—and my earlier “commitment”⁵ to the third way is one of the reasons why I am so fascinated with the Chinese process of transformation. Is China the real exception? Is China indeed a formation that cannot be described with the capitalist/socialist dichotomy?

Most scholarly literature which analyzes the nature of the Chinese formation describes it as some variant of socialism or capitalism: the official doctrine calls it “socialist market economy”; Western commentators tend to see it as a version of capitalism: capitalism with Chinese characteristics (Huang, 2008), political or politicized capitalism (Nee and Opper, 2007), or a “hybrid formation” (Nee and Swedberg, 2005), capitalism from below—Nee’s latest version (2007) and my earlier terminology (Szelenyi, 2002). With the idea of the “third hand,” the theorists/ideologues of the Chongqing model are offering a refreshing new idea.

As Philip Huang points out, what exactly the “third hand” (or the “third finance”) is could be clearer, but in my reading it is undoubtedly a new variant of the idea of the Third Road.

Well, the notion of the first hand is clear enough: that of course refers to Adam Smith's invisible hand and to the institutions of liberal capitalism. The question of what the second hand is is more difficult to answer. The concept of the second hand is used either to describe "planned socialism" (as described in Philip Huang's article in this special issue), or "market socialism," may I say, hence the system in which the state intervenes to perfect the functioning of the market, and hence maximizes profit. In my reading, the second hand refers to different variants of socialism, either redistributive or market driven.

It is much clearer what the third hand is. The novelty of the third hand is that it combines public ownership with an economy that aims at the satisfaction of public needs, not maximization of redistributive power (as under the state socialist redistributive economy) nor maximization of profits of publicly owned enterprises (as is the case in market socialism).

To put it differently: the goal function of liberal capitalism is maximization of individual profit. Socialism had historically two versions: state socialism, or a socialist redistributive economy in which the goal function was maximization of redistributive power; and market socialism, where the goal function was maximization of publicly owned firms (or arguably occasionally even state subsidies for private firms to maximize their profits, as in the case of welfare capitalism). The third hand represents a fundamentally different formation: while public ownership remains dominant, the goal function of the economy is social equity (people's livelihood), which is achieved by the use of market mechanisms.

But can the circle be squared? As Philip Huang correctly notes, Kornai, at least in his work since the mid-1980s, argued that market efficiency cannot be achieved under the conditions of public ownership. There is a selective affinity between forms of ownership and integrative mechanisms: private ownership is necessary for the efficient functioning of a market economy; public ownership coincided with bureaucratic (or redistributive) coordination. In economic policy we can only have a "prix fixe menu" (not "à la carte")⁶: if you chose markets, you have to opt for private ownership. For the later Kornai, market socialism in the sense spelled out in official Chinese ideology or in Oscar Lange's use of the concept is a contradiction in terms (Lange, 1936–1937). Publicly owned firms could not even maximize firm-level profits; much less are they likely to achieve social equity or serve the livelihood of the people. How is it possible to combine what at least in principle is declared as the goal function of socialism with the idea of market efficiency?⁷ Even the theorists of market socialism did not claim this can be achieved; even they did not believe that "liberal socialism" is a possibility.

The Chongqing model claims it can square the circle and achieve this aim. The critical step in this direction is “third finance.” Jean Oi’s concept of local state corporatism was an interesting attempt to combine the welfare purposes of local authorities with their private business, market-supporting role (Oi, 1999). The theory of local state corporatism (reflecting the realities of the early 1990s in non-metropolitan China) claimed that in China local authorities achieved a kind of corporatism agreement with local business and local population interests. Local private business was ready to support various welfare programs (construction of local infrastructure, schools, etc.) for the license of achieving private profits. What the theory of local state corporatism did not explain is, is this system sustainable? If most or all localities want to encourage private business, would they still insist that private businesses use at least some of their profits to promote the collective good? Or is just the opposite likely to happen: localities will be competing for private businesses and give them “tax breaks,” let them off the hook to fund public projects?

The third hand and third finance provide an answer to this question. In the spirit of Henry George, land remains public property and capital gains in the increases of land value can be used for the satisfaction of public needs. If I understand the Chongqing model correctly, the public financing of the Chongqing municipal authority comes from the capital gains of the land held in public ownership. While Philip Huang’s article is not specific in this respect, I suppose the Chongqing municipal authority is using something similar to “mortgage-backed securities”: it issues municipal bonds, which are backed by the increasing values of the land held by the municipality. Since the leadership of the municipality (Bo Xilai and Huang Qifan) is socially committed, these resources are used to promote social equity and the livelihood of the people.

This indeed sounds like a wonderful “third way” between neoliberal capitalism and bureaucratic socialism. But this argument has an Achilles’ heel. Philip Huang states, “given China’s severe scarcity of land and abundance of surplus labor, it seems unavoidable that, with marketization and urbanization, development land values would rise far faster than wages.” This is a BIG assumption and I am afraid the sustainability of the Chongqing model depends on the validity of this assumption. I tend to believe that *in the long run*, prices of development land cannot be increased faster than wages in any of the sub-markets. They can do so for many, many years or even decades, but this is how bubbles are created and eventually *those bubbles not only tend to but have to burst*.

It appears that China is building a gigantic land/real estate bubble and once that bubble bursts municipalities, such as Chongqing or Wuhan (see Barbosa, 2011), may find that the actual market value of the land they

borrowed against is less than their debt. Thus, these municipalities may find themselves in a situation not unlike the homeowners who borrowed subprime mortgages or borrowed heavily on home equity credit lines in the United States during the first decade of the twenty-first century.

This all really boils down to whether “given China’s severe scarcity of land and abundance of surplus labor, it seems unavoidable that, with marketization and urbanization, development land values would rise far faster than wages.” If indeed in China land values will indefinitely rise faster than wages, the “third financing” of the “third hand” can also go on indefinitely. But if there is already a real estate bubble in China, the third finance may collapse and that can have fatal consequences for the municipalities that funded their development and social programs this way.

Western experts have been crying wolf too many times when commenting on China, and the “inevitability” of the collapse of China has been predicted far too often. But this time the evidence about an overheated real estate market seems to be overwhelming. And we should remember: in the West we believed far too long that real estate prices can only go up and they can never go down. So far real estate prices in the United States have adjusted by some 30 percent and we might not have reached the bottom yet (so at least Robert Shiller—who knows more about real estate than anybody else and who predicted the current slump—seems to believe).

There is another point where the Chongqing model is vulnerable: that is, leadership and the vision of leadership. Philip Huang points out that Chongqing is particularly lucky to have two “exceptional leaders,” Bo Xilai and Huang Qifan. Let me add, Bo Xilai and Huang Qifan may be also lucky that they lead Chongqing when Hu Jintao and Wen Jiabao lead China, two leaders who are committed to the ideology of “social harmony” and who try to correct the excessive growth obsession of the decade of Jiang Zemin. Even if—big IF—land prices keep outpacing increases of wages, a change of leadership at the national or local level may lead to a different strategy for using capital gains from ever increasing land values. Some commentators—for instance, Yasheng Huang—suggest that China has overbuilt its infrastructure, and so the sustainability of continued infrastructural development can also be questioned. China may opt in the future—at least for a while—for a policy that reduces investments in general and increases consumption and investments into the productive sphere instead. A return to the policies of the 1990s with more emphasis on domestic consumption—which would be similar to policies of neoliberal market capitalism—is not inconceivable.

The social achievements of the Chongqing experiment are impressive and they indeed offer solid evidence that there is an alternative to bureaucratic socialism and to the neoliberal push for a full-fledged transition to

liberal market capitalism. But whether this new version of the third way, the Chongqing third hand and third finance, is sustainable has to be tested by history.

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Notes

1. In this article, I will not deal with the two Tonys' (Giddens and Blair) reincarnation of the "third way." During the 1990s the "third way" implied Labour politics, which borrowed heavily from the Conservatives. The original idea of "third way," much like the "third hand" in Chongqing, meant a third alternative to profit-seeking capitalism and bureaucratic socialism.
2. Lenin, as early as 1894, attacked the left populists in his pamphlet "What the 'Friends of the People' Are and How They Fight Social Democrats."
3. When my book *Socialist Entrepreneurs* (written in 1986) was belatedly (after the fall of socialism) published in Hungary in 1992 under the cautious title *A Third Way?*, my neoliberal reviewer of the book called me "subjectively of good intention" (to acknowledge my early contribution to reformist opposition), but objectively proto-fascist since while I did not advocate a "third way" or an alternative to liberal capitalism I did claim it is a conceivable future for the post-communist world. I also have to concede that by 1990 the idea of a third way was transformed into the ideology of the far right; it had become the twentieth-century version of "Sonderweg."
4. The English version of this book was published in 1988 by Polity Press. At that time Tony Giddens was Polity Press. I submitted the book to him and in 24 hours he sent me an email and accepted it without revisions. I am still wondering, was it the idea of a "third way" that captured his imagination? The word was all over my book and was not used yet in social democratic discourse.
5. I need to qualify this. I have been sufficiently committed to the bourgeois notion of "objectivity in social sciences" that I did not describe the third way as the best way. All along I claimed I was proposing an "ironic theory" of the third way. The point was not to suggest that the third way is better than capitalism or socialism; I merely wanted to show that it is different from both hegemonic forms and it is a historical possibility.

6. This is Perry Anderson's insightful distinction (Anderson, 2005).
7. Whether the goal function of a Stalinist or Maoist economy was equity or livelihood of the people is a subject for debate (Philip Huang seems to believe it was; see his article in this issue). I was a skeptic. In my book *Intellectuals on the Road to Class Power* (Konrád and Szelényi, 1979), I speculated that the actual goal function of the Stalinist or Maoist formation was maximization of redistributive power, and that equity, or the livelihood of people, was just a legitimating ideology, just as love, freedom, equality, and brotherhood are a legitimating ideology of profit-seeking capitalism.

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