Size and Dynastic Decline:  
The Principal-Agent Problem in Late Imperial China 1700-1850  

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Abstract  
I argue that one reason for China’s relative economic decline in the 19th century was its size. A ruler governing a big country faces a severe principal-agent problem. Given his monitoring difficulties, his agents have strong incentives to extort from the taxpayers, especially the politically weak ones. To prevent over-exploitation that could foment rebellion, the ruler has to keep taxes low. The result is the paradox of low state revenue despite a heavy tax burden on the poor. Economic growth could further exacerbate the situation as it increases the incentives for corruption. I apply this model to late imperial China and find that its predictions are well supported by empirical evidence. The Qing state taxed lightly and official land tax burdens were especially low in regions far from the capital. Furthermore, the fiscal and managerial capacity of the Qing dynasty began to contract steadily during the prosperous 18th-century, sowing the seeds for China’s socio-economic problems of the 19th-century.

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1 Introduction

China poses many questions that standard economic theories seem unable to answer. This paper deals with one of them: why was China unable to take advantage of the opportunities presented by the Industrial Revolution to modernize its economy in the 19th century?

On surface, there is a simple answer: the Chinese emperor. Economists have often argued that dictatorships are antithetical to economic development due to the dictator’s propensity to expropriate at will (North and Weingast, 1989; DeLong and Shleifer, 1993). A prominent view, drawing from Marx, held that China’s development was hampered by the presence of an autocratic, managerial, and interventionist state (Wittfogel, 1957; Balazs, 1964; Landes, 2006). In the words of David Landes,

“...China lacked a free market and institutionalized property rights. The Chinese state was always stepping in to interfere with private enterprise — to take over certain activities, to prohibit and inhibit others, to manipulate prices, to exact bribes.”

However, the applicability of this argument on late imperial China is questionable even on theoretical grounds, for the Chinese emperor was a stable dictator. As Mancur Olson (1993) taught us, a stable dictator is a “stationary bandit” who understands that excessive exaction in the short run involves a long run cost, in terms of less future tax revenue and more political instability. He will therefore demonstrate self-restraint when he expropriates through taxation. He may even actively provide public goods to improve the economic well-beings of his subjects, since this will allow him to collect more taxes in the future.

The orthodox interpretation of Chinese history is further undermined by the empirical findings of China historians in recent decades. Although Kenneth Pomeranz’s claim in *The Great Divergence* that the levels of development in the Lower Yangzi delta and England were comparable in the 18th century is still a subject of intense debate, his book has helped foster an emerging consensus that the Chinese society and economy in the 18th century were well-developed in many ways. Commercialization, helped by the monetization of taxes and the inflow of silver from Japan and the New World, linked the lives of ordinary people to the world outside their villages (Li, 1998; Wu and Hsü, 2000). The social status of merchants improved during this period (Mann, 1987). There is also strong empirical evidence suggesting

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1The Japanese historian Naito Konan pointed out that the position of the Chinese emperor became more secure from the Song dynasty (960-1279) onwards. Usurpation became extremely rare as aristocratic power was suppressed through the introduction of the examination system to select officials (Miyakawa, 1955).

2See Huang (2002); Brenner and Isett (2002); Allen et al. (2005); Xue (2007); Allen (2009) for critiques of Pomeranz (2000).
that a high degree of market integration was present in China at the dawn of the Industrial Revolution (Li, 2000; Shiue and Keller, 2007).

Where political institutions are concerned, the notion of a despotic regime incapable of adopting “progressive” changes is also giving way to an acknowledgement that the Chinese state demonstrated certain “early modern tendencies” in the 18th century. Externally, the Qing dynasty (1644-1911) extended its domain into Tibet and parts of Central Asia through military conquests and diplomacy (Perdue, 2005). Domestically, the state was actively involved in the provision of public goods, including the construction and maintenance of a nationwide granary system to combat famine (Will, 1990; Wong and Perdue, 1983), as well as active flood control in North China (Leonard, 1996; Dodgen, 2001; Li, 2007).

These empirical findings have, in some sense, created more questions than answers. If all was well and fine with China in the 18th century, why was it incapable of mounting a more resolute response to the coming of the West in the 19th century? Was China’s relative economic stagnation in the 19th century merely a consequence of historical contingency, or can we find a theoretical explanation for the reversal of fortune?

This paper argues that the explanation to the puzzle can be found in China’s size. The geographic size of the Chinese empire created a severe principal-agent problem in the way it was governed. This in turn led to an inefficient tax and administrative system. Fiscal weaknesses of the state were initially masked by the huge tax base, which compensated for the low tax rate forced upon the state. Over time, however, economic expansion in the 18th century intensified corruption and put further squeeze on state finances. The result was the paradox of a weakening state despite an expanding economy. Subsequent cuts in public goods provision and growing political instabilities eventually put a halt to sustained economic growth in the early 19th century, and rendered China ill-prepared to handle the military and technological shocks from the West in the age of industrialization.

Specifically, size carries two dimensions in the hypothesis: geographic and economic.

Geographic size matters — partly in its own right and partly because it is highly correlated with other variables that have a direct bearing on agency costs. Since the cost of transmitting information over distance is non-zero, especially in a pre-modern world, geographic distance increases the difficulties for the ruler to monitor state agents dispersed across the country. In addition, a large geographic size is usually associated with wide regional diversity and heterogeneity, which introduces even more noise into the ruler’s information. Regional differences in climate, crops cultivated, per capita income, and other socio-economic conditions implies that some degree of flexibility is required when a policy designed by decision makers in the capital is implemented by agents at the local level. Yet this necessity also makes it harder for the ruler to determine whether an act of some agent is one of corruption or one driven by the
need to adjust to local conditions.

In a large (and stable)\(^3\) dictatorship, even if the interests of the ruler and the society are aligned due to the ruler’s long-term perspective, excessive exploitation can still come from his agents who have shorter decision horizons and less encompassing interests.\(^4\) While the ruler is motivated not to overtax the population to preempt rebellion, his agents have private incentives to expropriate rent and undersupply public goods. If the ruler is unable to keep corruption in check, he will have to keep the tax rate low and his bureaucracy small to mitigate this “tyranny at the bottom” effect.

The effect of economic size on state finances is more ambiguous. A bigger economic output enlarges the tax base, but it also increases the temptation for state agents to corrupt. The more costly it is for the ruler to monitor his agents, the more corruption will grow with output. To keep exploitation by the state and its agents sustainable, the ruler will then have to respond to economic expansion by adjusting the tax rate downwards. In an economy associated with severe monitoring difficulties within the government, economic growth can actually hurt the state, as the negative effect of growth (lower tax rate due to worsening corruption) is likely to overwhelm its positive effect (bigger tax base) eventually.

The issue of size is particularly relevant to China, given that for the last two millennia, the land mass between the Great Wall and the South China Sea was more often than not under the rule of a single central authority. Mao himself highlighted the importance of distance in shaping the performance of political institutions in China when he told Nixon during the latter’s visit to China, “I have not been able to change [China]. I have only been able to change a few places in the vicinity of Beijing (Kissinger, 1998, p. 60).”\(^5\)

In addition, China has consistently accounted for around one-quarter of humanity —\(^6\) give and take a few percentage points — since the birth of Christ. This in turn implies that for the best part of the pre-1850 world, China had been the largest economy in the world.\(^7\)

\(^3\)Unstable dictators behave like “roving bandits” since their horizons were too short for them to consider taking steps to nurture the economy so as to benefit from higher tax revenues in the future (Olson, 1993). Hence, geographic size is irrelevant to this class of dictatorships.

\(^4\)This paper does not examine non-dictatorships for the following reason: in a dictatorship, the ruler has limited scope to up the monitoring of his agents since his monopoly of power implies that monitoring can only be top-down, not bottom-up. Hence, if he sets up a new agency to monitor existing agencies, the newly created agency will require personal monitoring from him too. In a non-dictatorship, bottom-up monitoring is possible and this demands a different framework of analysis.

\(^5\)A field specialist noted that even in contemporary China, “...there is a feeling among many inhabitants that law is enforced rather arbitrarily. This increases with distance from the national capital and major regional cities (Edmonds, 1990, p. 61).”

\(^6\)The term is borrowed from the title of Lee and Wang (1999).

\(^7\)Since living standards in pre-modern societies were usually not very far from subsistence level, population will be used as a proxy to economic output for the rest of the paper. This is, however, not an assumption and it plays no part in driving the results of the model. Economic growth without population expansion would have delivered the same results, as long as the growth in output is not driven by technological advances that
To the rulers of the Qing, the last imperial dynasty of China, the challenges that distance and population posed to effective governance were more acute than ever. Qing China in 1800 is significantly bigger than China or the United States today. Even if we disregard the thinly populated regions of Manchuria, Mongolia, Tibet, and Xinjiang, the region known as China proper is still bigger than India and Pakistan combined, or ten times the size of California. Pre-modern communication technologies did not help. In 1853, when the Taiping rebels captured Wuchang, a major Middle Yangzi city about 1000 kilometers from Beijing, the news took 8 days to reach the capital. To send an official report of the highest priority between Beijing and Shanghai through the imperial postal relay stations would take 10 days (Xie, 2002).

Furthermore, the Chinese economy expanded substantially during the late 17th and the 18th centuries. A lack of technological breakthroughs implies that economic growth during this period was largely extensive in nature, powered primarily by demographic expansion. Nonetheless, it remained impressive. Between 1650 and 1850, the Chinese population grew by a factor of three, from less than 150 million to over 400 million (Perkins, 1969), with no evidence of a significant drop in the living standards of the average Chinese before the mid-19th century (Baten et al., 2010). As we shall see later, this was accompanied by the spread of corruption, which grew like cancer to impoverish the Qing state as the population expanded.

The predictions of the hypothesis are cross-checked with historical observations and empirical data. First, the relationship between distance and agency costs is tested by examining regional differences in land tax burdens, as well as the spatial distribution of administrative units in late imperial China. In line with the predictions of the hypothesis, I find that both the land tax per capita and the number of counties per square area were significantly higher in regions adjacent to Beijing than in regions far away from it, even after controlling for regional population and income disparities. This suggests that state building in regions far away from the capital was inhibited by costly monitoring.

Next, using hand-collected as well as published historical fiscal records of the Qing dynasty, I have reconstructed the Qing state’s tax revenues between 1650 and 1850. The time series depict a hump-shaped pattern. The Qing state’s fiscal capacity peaked early in the 18th century and began to contract steadily from then, even as the economy continued to power ahead through extensive expansion.

Finally, I provide historical evidence to demonstrate that the contraction of the regime’s fiscal capacity led to a gradual and sustained reduction in the supply of state-provided public goods. This development became evident in the second half of the 18th century, and it predated the military and socio-economic troubles which kicked in after 1796. The nature
and timing of these spending cuts strongly suggests that persistent fiscal problems on the revenue side affected the economy adversely, through the under-provision of public goods that protected property rights. Before the modern West began taking steps to open up China by force, the Celestial Empire was already sinking under its own weight.

The rest of this paper is organized as follows. Section 2 places the research in the context of the existing literature. Section 3 discusses the historical background. A model is set up in sections 4 and 5 to establish the hypothesis formally and show that in a big country, sustained economic growth could sow the seeds of its own demise by hurting the state fiscally and instilling political instability.

The empirical aspects of the paper are covered in the subsequent sections. Section 6 tests the relationship between geographic distance and agency costs. Section 7 presents empirical evidence on the paradox of economic growth and fiscal decline in China during the 18th century. Section 8 discusses the historical evidence on how fiscal weaknesses of the Qing state turned into a growing drag on the economy, so much so that by the early 19th century, China had become too preoccupied with its domestic problems to deal with the rise of the West proactively. Section 9 concludes.

2 Literature Review

A common theme in the literature is the proposition that democratic checks and balances are prerequisites for growth. North and Weingast (1989), Acemoglu et al. (2005), and many other works have argued that without constraints on predatory dictators, excessive taxation and redistributive policies would lead to economic stagnation — an often cited example being the failure of France and Spain to keep pace with England and Netherlands economically in early modern Europe.

This view has been disputed by other scholars, who pointed out that absolutist regimes like France and Spain actually taxed less than England and Netherlands (Mathias and O’Brien, 1976; Hoffman and Norberg, 1994; Dincecco, 2009). Some economic historians contended that the problem with these absolutist regimes was not arbitrary despotic power, but institutional fragmentation. According to Hoffman and Rosenthal (1997), the ability of the French rulers to impose new taxes was severely constrained by the “divided fiscal authority” within their regime. In the words of Stephan Epstein, “the practice of absolutist rule [was] contested at every turn by feudal lords, town councils, corporate entities and religious institutions” (Epstein, 2000, p. 14). This in turn led to the inability of the absolutist state to solve coordination problems and provide public goods efficiently.

Neither paradigm fit into the experience of late imperial China. As we shall see later, the
Qing state extracted relative little. Hence, China’s developmental woes cannot be attributed to a strong state. However, China had also overcome the problem of jurisdictional fragmentation by the 10th century. From the Song dynasty (960-1279) onwards, measures were painstakingly implemented to prevent independent centers of power from emerging within the realm. A non-hereditary bureaucracy replaced the aristocracy. Passing civil service examinations became the main avenue to joining the political elite. Accordingly, there were fewer incidents whereby the authority of the emperor was openly and directly challenged by the elite class. Late imperial China had a weak state, but the source of its weakness was not jurisdictional fragmentation, but a more classical principal-agent problem which arose due to the emperor’s inability to monitor his bureaucrats effectively.

Propositions that the state plays an indispensable role in the promotion of a healthy economy can be broadly classified into two categories. In the weak form, the state has to acquire sufficient capacity to ensure the security of property and person (Smith, 1776; North, 1990). On the other hand, strong form arguments see a more proactive role for the state in economic development — either to resolve “coordination failures” (Epstein, 2000) and generate the big push in industrialization (Rosenstein-Rodan, 1943; Murphy et al., 1989), to reorganize property rights and remove inflexibilities in the existing property rights regime so that individuals and communities can take full advantage of the economic opportunities present (Bogart and Richardson, 2008), or to implement social policies (child labor laws, public education, and so on) that allow the society to escape from the Malthusian trap (Doepke, 2004). The hypothesis here focuses on the weak form view of the role of government, although it is not incompatible with stronger form arguments.

Empirically, there is some evidence suggesting that absolutist states often lack the capacity to manage economic development. Jones and Olken (2008) found that nearly all countries have experienced extended periods of economic growth. Autocracies do not lag behind democracies when it comes to triggering growth. However, they experience growth collapses that are often associated with monetary and political instabilities more frequently.

Worsening corruption was the main driver that generated the socio-economic instabilities in Qing China during the first half of the 19th century. The increasingly pervasive rent-seeking activities of corrupt state agents denied the late imperial Chinese state sufficient resources to maintain social order and protect the empire and its subjects against natural disasters, bad harvests, and foreign aggression. Within the literature on corruption, some authors have argued that corruption could improve economic efficiency, either by allowing entrepreneurs to bypass unnecessarily restrictive regulations or by incentivizing bureaucrats to work harder.

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8This is suggested in the Naito Hypothesis, formulated by the Japanese historian Naito Konan and widely cited by China historians (Miyakawa, 1955).
(Leff, 1964; Huntington, 1968; Lui, 1985). In this sense, this paper is more in line with the strand of the literature which emphasizes the overall harmful consequences of corruption (Rose-Ackerman, 1978; Shleifer and Vishny, 1993; Mauro, 1995; Bardhan, 1997).\textsuperscript{9}

Particularly, this paper highlights the regressive nature of corruption. High corruption in Qing China, which according to the estimates of Ni and Van (2006) consumed 22% of China’s agricultural output in 1873, did not affect all taxpayers equally. It was those with the least political and economic resources to protect themselves who suffered most from rapacious state agents. Section 4 constructs a model to demonstrate that this is not just a matter of equity, as it has efficiency ramifications too. In a fiscal system characterized by the ruler’s poor access to information, the state’s ability to tax hinges primarily upon the ability of the politically disadvantaged to pay.\textsuperscript{10} As corruption reduces the surplus of this underprivileged group available for the ruler to capture, it aggravates the state’s fiscal weakness and lack of capacity to solve collective action problems.

This paper is also related to the small literature on the size of nations. Alesina and Spolaore (1997) pioneered the use of cost-benefit analysis in studying the determinants of country size.\textsuperscript{11} Here, I leave out the discussion on the benefits that China might have reaped from its size, and focus entirely on the costs that size and centralized control imposed on the pre-industrial Chinese society and economy. As Owen Lattimore (1940), Ray Huang (1988), and others have pointed out, the need to coordinate defense efforts against nomadic incursions and to manage the flood-prone Yellow River might have generated impulses that pushed China towards early political unification. To keep the discussion focussed and its scope manageable, this paper takes a unified Chinese empire during the late imperial era as the point of departure, and leaves the question of why it was so to future research.

A strand of the literature emphasizes the importance of geography in shaping institutions, which in turn influence economic outcomes (Acemoglu et al., 2001, 2002; Easterly and Levine, 2003; Olsson and Hibbs, 2004; Rodrik et al., 2004; Galor et al., 2009). Within this literature, two recent works that deal with the issue of geographic size are of particular relevance here. Using cross-sectional data from 127 former colonies, Olsson and Hansson (2009) detected a strong negative casualty between territorial size and the rule of law. In addition, the average level of the rule of law tends to be lower in countries where the capital is not centrally located. Stasavage (2009) studied the evolution of representation in Europe across the five centuries
from 1250 to 1750 and showed that the effectiveness of representative institutions decreased progressively with the size of the polity in question, as high communication and travel costs created substantial obstacles for representative bodies in large territorial states to convene regularly.

Finally, turning to China-related research. Usher (1989) was the first to apply rational choice theory to explain dynastic cycles, which — according to classical Chinese historiography — characterized the history of China. In that work, a dynastic cycle emerges if the despotic state is fiscally weak. This paper builds on the observation and shows that fiscal weaknesses (and hence dynastic patterns) are the likely results of a severe principal-agent problem in government, which dooms the state to a small and declining share of the taxpayers’ surplus. Furthermore, I employ historical data to confirm the existence of a fiscal cycle in Qing China between 1650 and 1850.

On agency problems in historical China, Shiue (2004) and Shiue (2005) found evidence that the Qing government did not operate as a unitary and wholly coordinated entity, as provinces that received disaster relief from the central government frequently tended to take advantage of it by reducing their granary storage levels. Ma (2008) argued that bureaucrats and the general population in late imperial China withheld private information to tie the grabbing hands of the absolutist state, yet the same phenomenon also restrained the Chinese state’s ability to protect property rights and support economic growth.

With the exception of Kiser and Tong (1992), which applied agency theory to analyze the fiscal administration of pre-industrial China, none of the above papers explicitly relate high agency costs in late imperial China to the geographic size of the Chinese polity. This paper constructs a formal model and provides empirical evidence to show that agency costs and distance were indeed intrinsically linked. Furthermore, it argues that over time, economic expansion aggravated the impact of the principal-agent problem in China, so that what had been a manageable problem in the early 18th century became impossible to deal with by the first half of the 19th century. The last point is non-trivial, for it helps explain why economists and modern China historians hold such contrasting views over whether political institutions in late imperial China were capable of supporting economic growth.

3 Historical Background

The Qing dynasty (1644-1911) was the last dynasty of China. It was founded in 1616 by the Manchus, an ethnic minority group that originated in northeastern China. In 1644, the young empire captured Beijing, the capital of the Ming dynasty (1368-1644), and it would

12 The original name of the empire was “Jin” (or Later Jin). It was renamed “Qing” in 1636.
rule China for the next 267 years.

Until 1850, the Qing emperors had full control over the apparatus of government. In the 1850s and 1860s, widespread rebellion across the empire forced the imperial court to devolve substantial decision making power to provincial authorities to better deal with the crisis. The imperial court never fully recovered these powers after the rebellions were suppressed. For this reason, this paper focus primarily on the period until 1850, when institutions were fairly stable and political power firmly in the hands of the throne, to analyze how a severe principal-agent problem shaped the nature of imperial rule and the subsequent socio-economic outcomes.

A total of six emperors reigned in succession between 1644 and 1850, each being succeeded by one of his sons (see figure 1). The longest reign was that of the Kangxi emperor (61 years), and the shortest that of his fourth son Yongzheng (13 years). China historians usually divide the 206 years of rule under these six monarchs into three sub-periods. The first sub-period, the early Qing, is one of military conquest and political consolidation, and it ended in the 1680s after the imperial court suppressed a major revolt led by former Qing administrators in southwestern China.

With the restoration of peace, interregional trade resumed and flourished, and China entered a golden age known to the Chinese as “Kang Qian shengshi” (the flourishing age of the Kangxi and Qianlong reigns) and to the West as the High Qing. The High Qing officially ended in 1796, when a large-scale uprising erupted in Central China and exposed structural weaknesses of the Qing military as well as its civil administration.

The last sub-period, known as the mid-Qing, was characterized by rising socio-economic and monetary instabilities. Towards the end of it, China was handed a humiliating defeat by the British in the Opium War (1839-42). A bigger disaster arrived in 1850 with the outbreak of the Taiping Rebellion (1850-1864) which devastated the southern half of the country and very nearly toppled the Qing dynasty.

Structure of Government. The emperor sat at the pinnacle of the state apparatus. The core institutions in the central government included the Grand Council (the inner court privy-council) and the Six Boards or Six Ministries (namely: Board of Civil Appointments, Board of Revenue, Board of Rites, Board of War, Board of Punishments, and Board of Public Works).

Until 1850, all important decisions had to be approved by the emperor, who was advised by close aides in the Grand Council. Through the Board of Civil Appointments, he would appoint or ratify the appointment of every official from the county magistrate upwards. Through the Board of Revenue, he would regulate and audit the expenditures of the regional
Figure 1: Reigns and Major Events of the Qing Dynasty until 1850

1644: Peasant rebels toppled the Ming dynasty. The Qing empire, from Manchuria, took the opportunity to invade China proper.

1673 - 1681: Revolt of the Three Feudatories. Once these powerful regional warlords in south China were suppressed, there was no more independent centers of power within the realm capable of challenging the emperor.

1683: Taiwan annexed. Domestic peace fully restored.

1684: Lifting of sea ban.

1689: Treaty of Nerchinsk signed between China and Russia. Peace settlement between China and Russia. Russia ceded the Amur River basin but gained trade access to Beijing.

1720: Qing troops occupied Lhasa. The Qing court would later assume direct control of Tibet through its appointment of the "amban" (resident commissioner).

1750s - 60s: Qing conquest of Zungharia and the Tarim Basin in Central Asia.

1790s: Rise of piracy at sea.

1793: Macartney mission in Beijing. Lord Macartney asked Emperor Qianlong to ease restrictions on trade with Britain but was rejected.

1796 - 1804: White Lotus Rebellion. First large-scale commoner rebellion in Qing China since pacification.

1800s - 20s: Successive floods in North China.

1820s - 40s: Economic depression.

1839 - 1842: Opium War. China ceded Hong Kong and opened treaty ports after defeat.

1850 - 1864: Taiping Rebellion. More than 20 million people died. Qing court forced to decentralize power to provincial elites to deal with crisis.
and local governments, down to stationery expenses. Through the Board of Punishments, he would review judicial decisions made across the empire. All death sentences had to receive his sanction (Ch’u, 1962).

Outside the capital, civilian administration was handled by four layers of formal government: province, circuit, prefecture, county. Traditionally, the county was viewed as most critical to a regime’s effectiveness or viability, since it sat at the bottom of the formal state hierarchy and was therefore the layer of government that dealt with the subjects of the empire directly. In this sense, the other layers of government were no more than intermediaries between the center and the county (Watt, 1977, p. 360).

The Magistrate. There were about 1500 counties in Qing China, and the number stayed remarkably stable over time. Each county was headed by a magistrate, who was fully accountable to his superiors for all affairs concerning the administration of his jurisdiction.

As the population of China tripled between 1650 and 1850, an average county would govern slightly over 100,000 people in 1700, and nearly 300,000 people in 1850. Given this heavy workload, it was impossible for the magistrate to cover many aspects of government that we are accustomed to expect today. In practice, his job revolved around three themes: (1) the collection of land and miscellaneous taxes, which constituted the bulk of the Qing state’s tax revenue; 15 (2) the administration of justice, which required him to preside over all court hearings held in his jurisdiction, civil or criminal; and (3) the maintenance of social order.

The imperial court monitored magistrates across the country through several means. In a triennial exercise known as daji (grand review), the magistrate’s superiors in the central and provincial administrations would review his performance and mete out reward or punishment accordingly. 16 Failure to remit the taxes owed to the central government in full and in time, a huge backlog of civil cases in court, and the presence of unsolved murders and major robbery cases would cost the magistrate dearly during the review (Watt, 1977).

Apart from relying on higher authorities within the civilian bureaucracy to supervise downstream agencies, the late imperial Chinese state also established the Censorate to investigate and impeach shirkers and wrongdoers (Feuerwerker, 1976, p.49). At any one time, there were

15 Broadly speaking, there were five kinds of taxes collected in Qing China before 1850: the diding (land tax stipulated in silver), the grain tax (land tax stipulated in grain), the salt tax, customs duty, and miscellaneous taxes. The two land taxes together accounted for more than 80% of the Qing state’s tax revenue during this period, and it was the responsibility of the magistrate to collect these taxes and remit the portion owed to the central government promptly.

16 Punishments typically included pay forfeiture, fine, demotion, removal from office. Rewards usually came in the form of awarding merit points (jilu), or rank promotion (jiaji). Merit points could be used to write off future punishment at predetermined “rates”. For example, according to the 1764 edition of the Qing statutes, an official could use one merit point to cancel out pay forfeiture of six months (DQHD, 2006, QL - juan 6).
56 censors attached to the provinces to act – in the words of the Qianlong emperor – as the “eyes and ears” (er mu) of the imperial court.

The Local Elite. Not all inhabitants residing in his jurisdiction were equal in the eyes of the magistrate. Since the central government kept in touch with influential local households known as the gentry through the censors, the magistrate would need the goodwill of these households to ensure that no complaints about him would reach his superiors (Holcombe, 1895, p. 228).17

Put simply, the Qing society comprised of two classes, the gentry and the commoners.18 Also referred to in the literature as the local elite, a gentry member was one who held an official educational degree. Such a degree was a prerequisite to enter government service in late imperial China, and it could be obtained either by passing state-sponsored examinations or by purchase.

Many gentry members owned sizeable land holdings.19 Although only a small fraction of them ended up in officialdom,20 gentry members were granted social and legal privileges by the state to distinguish themselves from the commoners. They wore buttons on their hats as a symbol of their status. If a gentry member had committed a serious offense, punishment should not be applied before the provincial director-of-studies was notified and approval had been given to strip off the offender’s title. A magistrate who did not observe these procedures could be impeached (Zhang, 1955).

The privileged position of the gentry implies that even the most corrupt magistrate would not lay his hands on them. It was commoners who lacked the political means to protect themselves who bore the brunt of corruption by rapacious local state agents.

Corruption in The Land Tax Collection Process. Theoretically, land tax liabilities in Qing China were computed at the household level, based on the size and grade of the land that each household owned. The tax liability of a land-owning household was expressed as a fixed sum per plot of land regardless of how much the land actually produced that year. In practice, it was impossible for the imperial court to keep track of how much land taxes every

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17 The Veritable Records of the Qing Dynasty listed many instances where magistrates were demoted or dismissed due to “unfavorable public sentiments” (yuqing bu qia), which in most cases means that they were ousted by the local gentry.
18 According to Zhang (1955, p. 139), the gentry class – including their immediate family members – accounted for 1.3% of the total population during the first half of the 19th century.
19 Although it is true that a landlord was not necessarily a member of the gentry, a wealthy landlord could always purchase the status of an Imperial Academy student (jiansheng) from the state. As such, wealth and gentry status had the tendency to go hand in hand.
20 During the early 19th century, there were slightly over a million gentry members but only 20,000 official positions to fill up at any one time (Zhang, 1955, p. 111, Table 8).
landowning household should pay given the enormous amount of information that it would have to process to do so. Instead, it could only keep track of tax liabilities down to the county level. Each county was assigned a tax quota according to the cultivated acreage and land quality of the county. It was the responsibility of the county magistrate to ensure that taxes owed by residents in his county were collected fairly in accordance to actual ownership.

This created enormous opportunities for the magistrate and his underlings to profit from the tax collection process. As long as they were careful to pick only victims who lacked the political means to resist extortion, and as long as long the taxes due to the central government were always remitted promptly and in full, such actions were unlikely to catch the attention of the imperial court.

The magistrate could over-collect from the taxpayers either directly or indirectly. The easiest way to do so was to manipulate tax notices by adding an minute extra amount to the tax liabilities of every household. The act would usually go unnoticed. Those who did find out would not find it worthwhile to question the claim. Given the size of an average county in late imperial China, this practice of feisa or “spraying” could usually return a sizeable yield (Zelin, 1984, p. 49). Another commonly practised approach was for the magistrate to demand that taxes be paid in copper coins instead of silver or grain. He would then set the commutation rate at a level higher than the prevailing market rate to profit from arbitrage.  

Many magistrates used their underlings as proxies to avoid directly engagement in extortion. Clerks and runners assigned to receive tax payments often used the pretext that the tax silver or grain presented by a taxpayer was of inferior quality to demand addition payment (Huang, 1694, juan 8). It was customary for them to share their profits with the magistrate, who would then forward some of what he received to higher officials in the form of gifts (Xia, 1935, p. 411). Ch’u (1962, p. 29) cites a case where the extra silver collected from land tax payments was shared among the magistrate and his underlings in the ratio of 60% to 40%.

The Qing statutes prescribed harsh punishments for corruption. An official who extorted less than one tael of silver could be sentenced to 60 blows of the heavy bamboo. However, it was relative uncommon for such punishments to be meted out. Of the over 400 officials impeached for corruption between 1736 and 1795, very few were prosecuted (Park, 1997, p. 973, 996).

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21Late imperial China operated a bimetallic monetary system. Silver bullion was used for tax payment and large transactions, while alloy coins known as “copper cash” (tong qian) were used in retail transactions. The state controlled the supply of copper coins through its mints, while the economy relied heavily on running trade surpluses to augment its silver supply due to the scarcity of silver deposits in China. Copper coins and silver bullion could be exchanged in the market at market determined rates.

221 kuping (treasury) tael is equivalent to 37.3 grams of silver, theoretically 1000/1000 fine (Vogel, 1987). In 1800, it would take about 6.8 taels to feed and clothe an average person. See the discussion on figure 7 in section 7 for how this figure is derived.
As Shiue (2004, p. 106) has pointed out, part of the problem lies with the difficulty in ascertaining whether an act was one of corruption. The difficulty was exacerbated by wide regional diversity in China. As stipulated taxes in late imperial China represented the amount that should eventually enter the state coffers, the imperial court had to allow some form of over-collection by local state agents to compensate them for the cost of tax collection. Standardization of these surcharges was practically impossible given regional differences. Predictably, most magistrates took the opportunity to demand more than what was necessary.

How serious was the problem of corruption? Zhang (1962, p. 32) calculated that during the first half of the 19th century, an average magistrate fetched an extra 30,000 silver taels annually, on top of his regular salary of 45 to 80 taels and official salary supplement of 400 to 2259 taels. By this estimate, the extralegal income of the 1500 Chinese magistrates (45 million taels) exceeded the amount of tax silver that entered the state coffers each year (around 40 million taels in the 1840s). This is before we consider the extralegal income of the provincial governors (180,000 taels), circuit intendants (75,000 taels), prefects (52,500 taels), and other officials. According to Ni and Van (2006), the extralegal income of Qing officials, which peaked in 1850, consumed 22% of China’s agricultural output in 1873.

These estimates, outrageous as they appear, are in line with contemporary observations. The French missionary Père Amiot noted in 1782 that corruption was so deep-rooted in the Qing bureaucracy that “it is rare among the Chinese to find anyone in an official post who does not enrich himself” (Park, 1997, p. 999). Chester Holcombe (1842-1912), an American diplomat, commented that,

“The grave point of weakness and danger in the Chinese financial system, or lack of system, lies, so far as the government revenues are concerned, in the free opportunities which are afforded for extortion, illegal exactions from the people, and every form of officer robbery. It is safe to say that no tax is collected and paid over to the treasury in the exact amount stipulated by law. The subject invariably pays more than he ought, and the Emperor as invariably receives less than his due. And if the exact total of all sums collected for public purposes from every source in any year could be compared with the corresponding total actually

23 The Kangxi emperor once mentioned in private that he would consider a magistrate who imposed a surcharge rate of no more than 10% on the regular tax an honest official (Ch’u, 1962, p. 219).
24 This was attempted during the reign of Yongzheng (1723-35), when the Qing court legalized the collection of a “silver meltage fee” on top of the regular land tax to help pay for the cost of regional and local administrations. The sanctioned rates varied from province to province, with a nationwide average of about 12% on the regular tax (Wang, 1973, p. 70). Over time however, uneven inflation eroded the effectiveness of this reform so that legitimate claims could again be made to collect surcharges beyond the sanctioned levels (Zelin, 1984).
25 About 6.8 taels were required to feed and clothe an average person in 1800. See footnote 22.
devoted to public purposes in the same period of time, the enormous divergence between the two sums would astonish the world (Holcombe, 1895, p. 348-349).”

The discussion here and the model presented in the next section focus on only one form of corruption — the extortion of taxpayers. In reality, corruption can present itself in many ways. For example, quid pro quo deals between state agents and a subgroup of taxpayers (primarily the gentry families) were a huge concern in Qing China. However, this (and other forms of corruption) can be treated as a special case of extortion — if the magistrate waived the tax of some powerful local family for a bribe, he would have to cover the subsequent shortfall in taxes by over-colllecting from other taxpayers. Hence, while equating corruption with extortion is a simplification of reality, it does capture the essence of the historical situation in our context.

4 The Model

4.1 The Basic Model

Consider a single period game of taxation involving a ruler, a tax collection agency of measure \( B \), a representative local elite, and a homogenous peasantry of measure \( N \).

Let \( Y_E \) denote the income of the local elite, and \( Y_P \) the aggregate income of all peasants. Furthermore, let \( y_P \) denote the income of each individual peasant, so that \( Y_P = N \cdot y_P \).

The aggregate peasant output is a function of the peasant population, and is subject to diminishing returns, so \( Y_P = Y_P(N) \), and \( Y^P(0) = 0 \), \( Y^P(N) > 0 \), \( Y^P(N) < 0 \). For now, \( Y_E \) and \( N \) are exogenously determined.

The ruler taxes the local elite and the peasants at tax rate \( \tau \). However, due to the constraints of time and distance, he cannot collect taxes himself. Instead, he entrusts tax agents to collect \( \tau \cdot Y_E \) from the local elite and \( \tau \cdot Y_P \) from the peasants on his behalf.

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26 Although Holcombe was appalled by the level of corruption in 19th century China, he was also deeply impressed by the mechanisms in place to check corruption. Commenting on the Censorate system, he praised that “...few nations have such a complete civil service as China, or one in which the checks and guards against injustice, oppression, and every form of maladministration have been so carefully, and with such apparent wisdom, wrought out (Holcombe, 1895, p. 223).” The contradiction in his statements reflects the practical difficulties of fighting corruption in a country as big as China.

27 To keep the analysis simple, I assume that the ruler can perfectly observe the incomes of the taxpayers. In reality, a state that suffers from a more severe principal-agent problem is less able to observe taxpayers’ incomes. Incorporating this observation will strengthen the results.

28 With reference to the discussion in the last section, \( \tau \) represents the taxes that the imperial court explicitly authorized the magistrate to collect, as well as the amount of surcharges collected by the magistrate which the imperial court was willing to tolerate. Surcharges collected by the magistrate to provide local public goods would be counted into \( \tau \).

29 The results will not change qualitatively if we allow the ruler to set different tax rates for the local elite and the peasants. Nonetheless, when informational problems are severe, it is unrealistic to allow the ruler to set different tax rates for different groups of taxpayers if these groups live in the same locality and are engaged
**Tax Agents.** During the process of tax collection, a tax agent may abuse his authority by asking the taxpayers to pay an additional surcharge \( \epsilon \), which goes to his own pocket. However, he will never collect a positive amount of surcharge from the local elite as the latter can report the abuse to the ruler directly. Hence, the peasants are the only victims of bureaucratic extortion. Each of them faces an effective tax rate of \( \tau + \epsilon \), while the local elite pays only the stipulated tax rate \( \tau \).

Abuse of authority is not risk free to the agent. After taxes are collected, the ruler conducts a performance evaluation which gives him a signal for every tax agent whom he has hired. The signal can only take two values: positive or negative. If an agent collects a surcharge of \( \epsilon \), there is a probability \( q(\epsilon) \) that his signal will turn out to be positive, where \( q(0) > 0 \), \( q'(\cdot) > 0 \), and \( q''(\cdot) > 0 \). The probability of a corrupt agent being caught red-handed increases at an increasing rate with the level of corruption.\(^{30}\)

The ruler punishes any agent associated with a positive signal by deducting \( U \) from the latter’s utility. For now, let \( U \) be exogenously determined.\(^{31}\)

The tax agent’s problem is to pick an optimal surcharge rate that balances the benefit of corruption with the risk of detection and punishment. Mathematically, it is given by:

\[
\max_{0 \leq \epsilon \leq r^P} V^A = \epsilon \cdot Y^P(N) - q(\epsilon) \cdot U
\] (4.1)

**The Ruler.** The ruler is self-serving and he wishes to set \( \tau \) as high as possible. However, his ability to do so is constrained on two fronts. Powerful local elite may resist his demands. Peasants who lack political voice may also resort to armed violence if the tax rate is too high.

Let the ruler’s bargaining power vis-à-vis the local elite be measured by \( r^E \), where \( 0 < r^E < 1 \). The ruler is politically incapable of taxing away more than \( r^E \) fraction of the local elite’s income. Hence, \( \tau \leq r^E \). If the ruler is despotic and there are few explicit checks on his power, \( r^E \) takes a value close to 1.

\(^{30}\)An easy way to motivate a monitoring technology of this form is to suppose that whenever agent \( i \) collects a surcharge of \( \epsilon_i \geq 0 \), the ruler will receive a signal \( \hat{\epsilon}_i \), where \( \hat{\epsilon}_i \) has a normal distribution \( \mathcal{N} (\epsilon'_i, \sigma^2) \) that is bounded between 0 and 1 (i.e. a truncated normal distribution). The ruler punishes the agent whenever \( \hat{\epsilon}_i \) is greater than some threshold value \( 0 < m < 1 \). It is easy to check that \( q(0) > 0 \) and \( q'(\cdot) > 0 \) are implied by this setup. Ignoring corner solutions, it can further be verified that the agent will never set \( \epsilon_i \) beyond \( m \). This in turn implies that we can focus on the values of \( \epsilon_i \) which correspond to \( q''(\cdot) > 0 \). Here, \( \sigma \) measures the quality of the ruler’s information. The higher is \( \sigma \), the noisier his information.

\(^{31}\)Since \( q(0) > 0 \), the ruler’s signal is imperfect and punishment may be wrongly meted up. This will be important when we endogenize \( U \) later.

in the same mode of production. In Ming-Qing China, peasant households who owned very small plots of land were sometimes granted certain tax exemptions or relief. Some rich landowning households took advantage of this by dividing their landholding into multiple tiny plots and registering them under different names to qualify for the lower tax rates. To cite another example, tax exemptions were initially granted to the families of bureaucrats during the early Qing. This encouraged other households to collude with these families and report their properties under the latter’s name. Consequently, these privileges were withdrawn.
Similarly, to avoid peasant revolt, the ruler has to ensure that the effective tax burden on the peasants does not exceed \( r_P \). So \( \tau + \epsilon \leq r_P \), where \( 0 < r_P < 1 \).

Apart from setting \( \tau \), the ruler also determines the value of \( B \), the size or coverage of his tax agency. Here, \( B \) is normalized so that \( 0 \leq B \leq 1 \). For example, if \( B = 1 \), the ruler taxes the entire economy. If \( B = 0.5 \), the ruler can only extract taxes from half of the economy, and so forth.\(^{32}\)

Maintaining a big tax agency is costly as intermediate layers of government are required to manage the tax agents. Let the cost be represented by \( C(B) \). Given the pyramid structure of hierarchies, \( C(B) \) is a convex function, and \( C'(.) > 0, C''(.) > 0 \).\(^{33}\)

Summing up, the ruler’s problem is given by:

\[
\begin{align*}
\max_{0 \leq \tau \leq 1, 0 < B < 1} & \quad V^R = \tau \cdot B \cdot [Y_E + Y_P(N)] - C(B) \\
\text{s.t.} & \quad \tau \leq r_E \\
& \quad \tau + \epsilon \leq r_P
\end{align*}
\]

(4.2) (4.3) (4.4)

The timing of events is as follows. First, the ruler determines \( \tau \) and \( B \). After which, tax agents individually select a value of \( \epsilon \) to maximize their individual payoffs. They then proceed to collect taxes from the local elite and the peasants. Upon the completion of tax collection, the ruler punishes those agents associated with positive signals.

4.2 Analysis

Consider the two constraints in the ruler’s problem. It is easy to see that out of (4.3) and (4.4), only one will bind in equilibrium. Which one binds depends on the nature of the regime. If the problem of fragmented jurisdiction is severe and the ruler’s ability to set the tax rate is constantly contested by powerful feudal lords or urban oligarchies, (4.3) is likely to bind.

On the other hand, if the ruler is vested with absolute power, (4.4) will likely be the binding constraint. This is especially so if corruption is severe and \( \epsilon \) is high in equilibrium.\(^{34}\)

---

\(^{32}\)Think of this setup as follows: Suppose the geographical size of the ruler’s domain is \( \pi \) square distance. Given technological limitations, the maximum area that a tax agent can physically cover on duty is \( \mu \) square distance, where \( \mu << \pi \). Hence \( B = 1 \) if the ruler employs \( \frac{\pi}{\mu} \) tax agents.

\(^{33}\)For example, suppose every two officials require 1 intermediate supervisor. To hire 4 tax agents, the ruler will need to hire 2 supervisors. To hire 8 tax agents, 6 supervisors are required. Here, doubling the number of tax agents requires a tripling of supervisors.

\(^{34}\)The use of efficiency wages to incentivize agents is not considered here because when monitoring is costly and the probability of detecting an act of corruption is low, paying efficiency wages is inefficient (Besley and McLaren, 1993). A simple example will make this clear: A tax agent has the opportunity of extorting $1000 from a taxpayer with a 0.2 probability of getting caught. For simplicity, suppose \( U = 0 \). We can calculate that the efficiency wage paid to the agent must exceed $4000 to ensure that his payoff of not engaging in corruption.
From now on, I shall only consider the case where (4.4) binds, which I call the case of a despotic state (as opposed to the case of fragmented jurisdiction).

A key determinant that drives the results of this model is the slope of the \( q(.) \) function, which represents the degree of the principal-agent problem that confronts the ruler. If \( q(.) \) is relatively flat, the ruler does not enjoy access to accurate information and acts of extortion are more likely to escape his detection. Hence, let us define the severity of the principal-agent problem as follows:

**Definition 1.** The principal-agent problem is more severe in Country \( X \) than Country \( Z \) iff:

\[
q'_X(\epsilon) < q'_Z(\epsilon) \quad \forall \quad \epsilon \geq 0
\]

**Result 2.** The more severe the principal-agent problem, the higher the level of corruption:

\[
\epsilon^*_X > \epsilon^*_Z \quad \text{if} \quad q'_X(\epsilon) < q'_Z(\epsilon) \quad \forall \quad \epsilon \geq 0
\]  

**(4.5)**

**Proof.** The agents’ problem gives us the following first order condition:

\[
Y^P(N) = q'(\epsilon^*) \cdot U
\]  

**(4.6)**

This condition plus definition 1 and the property \( q''(.) > 0 \) together imply result 2.

Result 2 also implies that fiscal inequality is higher where the principal-agent problem is more severe. Even though everyone faces the same stipulated tax rate, the peasants always pay more due to bureaucratic extortion. If agency cost is particularly high, the de facto regressiveness in the tax system is likely to be especially acute.\(^{35}\)

**Result 3.** The more severe the principal-agent problem, the weaker the ruler’s ability to tax:

\[
\tau^*_X < \tau^*_Z \quad \text{if} \quad q'_X(\epsilon) < q'_Z(\epsilon) \quad \forall \quad \epsilon \geq 0
\]  

**(4.7)**

**Proof.** Since we are analyzing despotic states, constraint (4.4) binds in equilibrium. Hence, result 3 follows directly from result 2.

Results 2 and 3 predict that where the principal-agent problem is most severe, corruption is most prevalent and the tax rate is lowest. That a severe principal-agent problem leads to a

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\(^{35}\)This is in line with the findings of recent empirical papers on corruption and inequality, which point to a significant correlation between the two variables. See Lambsdorff (2007) for a review of these papers.
weak state does not imply that peasants pay less taxes in these regimes. Instead, we have a paradoxical situation whereby the ruler taxes little but the burden on the peasants is heavy.

Furthermore, since constraint (4.4) binds for a despotic state, the ruler’s ability to collect more taxes is constrained by the peasants’ ability to pay. If the principal-agent problem is severe ($\tau^*$ is low), even if the general economy prospers, the ruler may not be enriched in any meaningful way.

This observation may help explain why the Chinese imperial court was more interested in maintaining political stability than in promoting economic development, and why it showed more enthusiasm in fostering agricultural growth than in encouraging commercial expansion (Mokyr, 1990, p. 237-8). The late imperial Chinese state’s emphasis on light taxation and care for the people had greatly impressed Enlightenment thinkers such as Leibniz, Voltaire, and Quesnay, who praised the emperor’s annual rite of plowing a furrow of soil to show his care for the common people’s livelihood, and the Chinese state’s effort to maintain a nationwide granary system to provide famine relief to its subjects (Pak, 1974; Perdue, 2004). The results here suggest that the emphasis on benevolent rule in the Chinese political culture may be driven by rational motives.

**Result 4.** The more severe the principal-agent problem, the smaller the bureaucracy:

\[
B^*_X < B^*_Z \quad \text{if} \quad q'_X(\epsilon) < q'_Z(\epsilon) \quad \forall \quad \epsilon \geq 0 \tag{4.8}
\]

**Proof.** The first order condition of the ruler’s problem is given by:

\[
\tau^* \cdot [Y^E + Y^P(N)] = C'(B^*) \tag{4.9}
\]

This condition, result 3, and the property $C''(.) > 0$ together imply result 4. \qed

An international comparison of the size of pre-modern governments provides some anecdotal evidence that geographic size is indeed positively correlated with agency costs. In 1750, there was on average one civilian official per 11,250 people in Qing China, and one per 10,000 people in Tsarist Russia (Pintner, 1980, p. 192). The direct tax system of Louis XIV’s France alone hired 3,000 officers, or one in every 7,700 people (Collins, 2009, p. 208 and 245). England, traditionally a nation of small government, already had one royal official for every 4,000 people by the 16th century (Sacks, 1994, p. 36). The smallness of the Chinese state is evident by comparison.\footnote{As Needham and Huang (1974) put it, “Chinese bureaucratic government always appeared impressive in breadth while remaining shallow in depth”.

At some level, result 4 echoes the claim made in Banks and Weingast (1992) that politicians
would not set up agencies that are particularly difficult to monitor. Intuitively, since managing a bureaucracy is costly, the ruler will try to keep it small unless a bigger bureaucracy brings him more tax revenues. Simple as this result may appear, it actually provides important insights into the difficulties of state-building in countries plagued by high agency costs.

4.3 The Dynamic Model

We now consider the game under a multi-period, infinite horizon environment. Only the ruler and the local elite are long run players. The tax agents are short run players as their positions are non-hereditary. The peasants make their own reproductive decisions, and each generation is replaced by their offsprings in the next time period. \( N \) is therefore now endogenously determined. Otherwise, all previous settings are preserved.

The timing of events at time \( t \) can be summarized as follows:

1. The ruler sets tax rate \( \tau_t \) and size of tax agency \( B_t \) to tax the local elite and \( N_t \) peasants;
2. Each tax agent chooses his optimal rate of extortion \( \epsilon_t \) and proceeds to collect taxes;
3. Tax collection ends. The ruler evaluates all tax agents and punishes those associated with positive signals;
4. Peasants make private decisions on how many children to produce. These decisions collectively determines \( N_{t+1} \);
5. \( t \) ends and \( t + 1 \) begins.

The ruler and the tax agents solve the same respective problems as before.\(^{37}\)

**The Peasants.** Every peasant derives utility from his consumption as well as from the number of children he produces. To him, the two “goods” are complements, and each is subjected to diminishing marginal utility.\(^{38}\)

At time \( t \), a peasant’s problem is given by:

\[
\max_{c_t^P, n_{t+1} > 0} u_t^P = u_t^P(c_t^P, n_{t+1}) \quad (4.10)
\]

\[
s.t. \quad c_t^P + n_{t+1} \leq [1 - r^P] \cdot y_t^P \quad (4.11)
\]

\(^{37}\)This presupposes that both the ruler and the agents will not or cannot influence population growth. For the ruler, this condition is satisfied as long as the principal-agent problem is severe enough so that there is no room for him to cut taxes below the level that binds the no-revolt constraint (4.4), even if he wishes to do so. As for the tax agents, this condition is met since they are short-run players.

\(^{38}\)This setup is modified from Hansen and Prescott (2002).
where \( u_1^P(.) > 0, \ u_2^P(.) > 0, \ u_{11}^P(.) < 0, \ u_{22}^P(.) < 0, \ u_{12}^P(.) > 0. \)

The above implies that the peasant population will evolve according to:

\[
\frac{N_{t+1}}{N_t} = \frac{N_t \cdot n_{t+1}}{N_t} = g([1 - r^P] \cdot y_t^P) \quad (4.12)
\]

where \( g'(.) > 0. \)

Condition (4.12) implies that the direction and rate of population growth depends on the peasant’s net income per capita. This is in the spirit of Malthus. However, the story here is not a Malthusian one. As will be clear soon, in this model, population growth leads to suboptimal outcomes not because it triggers subsistence crises, but because demographic and economic expansion erodes fiscal and political stability by promoting corruption.

Let \( y_s \) denote the subsistence level of income, or the net per capita peasant income which corresponds to \( \frac{N_{t+1}}{N_t} = 1. \) As illustrated in figure 2, if the initial population size is small, net per capita peasant income is high. Therefore, population will grow until net income level falls to \( y_s. \) On the contrary, if the economy suffered from overpopulation to begin with and net per capita peasant income is below the replacement level, population will shrink until net per capita peasant income rises to \( y_s. \)

**Figure 2: Converging to The Steady State Population Level**

**Result 5.** Corruption worsens with population growth: \( \frac{de^*}{dN} > 0. \)

**Proof.** This follows from the tax agents’ optimality condition (4.6). \( \square \)

Since the ruler has to ensure that the peasants are not overtaxed, result 5 and the no-revolt constraint (4.4) in turn imply that:
Result 6. The equilibrium tax rate $\tau^*$ falls with population growth: $\frac{d\tau^*}{dN} < 0$.

Population growth has two effects on the ruler’s finances, one positive and the other negative. On the positive side, it increases the aggregate output (and hence the tax base), but at a diminishing rate. On the negative side, the growth of the economic output $Y^P(N)$ encourages corruption. This decreases the tax rate or the fraction of the economic surplus available for the ruler to capture. The next result shows that in the case of a severe principal-agent problem, the negative effect of growth could eventually dominate its positive effect, so that growth actually hurts the ruler.

Result 7. If $q'''(.) \leq 0$, there exists a population $N^{Max}$ such that if $N < N^{Max}$, the ruler’s revenue increases with population growth. If $N > N^{Max}$, the ruler’s revenue decreases with population growth.

Proof. The ruler’s period revenue at time $t$ is given by:

$$v_t^R = \tau_t \cdot B_t \cdot [Y^E + Y^P(N_t)] - C(B_t) \quad (4.13)$$

By envelope theorem, we have:

$$\frac{dv^R}{dN} = \frac{\partial v^R}{\partial N} = \frac{d\tau}{dN} \cdot B^* \cdot [Y^E + Y^P(N)] + \tau \cdot B^* \cdot Y^P_N$$

$$= [-q'(\epsilon) - \frac{Y^E}{q''(\epsilon) \cdot U} + \tau] \cdot B^* \cdot Y^P_N \quad (4.14)$$

Since $q''(.) > 0$ and $q'''(.) < 0$, $\frac{q'(\epsilon)}{q''(\epsilon)} + \frac{Y^E}{q''(\epsilon) \cdot U}$ increases in $N$ while $\tau$ decreases in $N$. Let $N^{Max}$ represents the population level where $\frac{q'(\epsilon(N))}{q''(\epsilon(N))} + \frac{Y^E}{q''(\epsilon(N)) \cdot U} = \tau(N)$. If $N > N^{Max}$, growth leads to a contraction of state revenue.

Recall that $q'(.)$, $q'''(.) > 0$. The more severe the principal-agent problem, the less sensitive $q(.)$ is to changes in $\epsilon$, and the more likely $q'(.)$ will increase with $\epsilon$ at a constant or diminishing rate. If indeed it is the case that $q'''(.) \leq 0$, corruption will grow substantially as output expands.

As shown in Figure 3, population and economic expansion will always be beneficial to the ruler only if the principal-agent problem is negligible. Otherwise, the more severe the principal-agent problem, the earlier the tipping point where population growth turns from a boon to a bane for the ruler will arrive.

By combining figure 2 and figure 3, we have a theory of why and under what circumstances dynastic decline may emerge.

\[\text{Under the setup laid down in footnote 30, this condition is satisfied as long as } \sigma \text{ is sufficiently high (as}\]
As figure 4 illustrates, dynastic patterns emerge only if corruption has the tendency to worsen substantially in the face of population and economic expansion. Starting at a point where $N < N_s$, since the peasants are living above subsistence after taxation, population will grow. This in turn leads to a fall in the per-capita income of the peasants due to diminishing returns. If the principal-agent problem is mild, population growth will eventually come to a halt when the after-tax per-capita peasant income falls to $y_s$. At this point, the economy enters a steady state and will stay there until some exogenous shock occurs to knock it out of the steady state.

On the other hand, if the principal-agent problem is severe, state revenue dwindles fairly quickly as $N$ approaches $N_s$ from the left. If state revenue drops to 0 before the after-tax per-capita peasant income falls to $y_s$, the regime goes bankrupt and collapses before it enters the steady state. Here, we observe a clear pattern of dynastic rise and fall. The establishment of the dynasty brings order and stability initially. This allows economic expansion to take place. However, in a paradoxical manner, the regime finds itself increasingly incapable of managing the prosperity which it helped create, and growth leads to collapse.\textsuperscript{40}

Historians generally concur that corruption grew over time in Qing China (Fairbank, 1992; Naquin and Rawski, 1987; Rowe, 2009), and that the Qing rulers seemed increasingly unwilling

\textsuperscript{40}That a society under despotic rule could evolve into a stationary state or into a dynastic cycle was first proposed in Usher (1989). This paper builds on the insight to show that agency costs are likely to determine which of the two outcomes will prevail.
Classical Chinese historiography attributes this to the gradual loss of moral vigor among the ruling class. However, this view has been challenged by modern China historians, who have pointed out that the traditional consensus that the 19th century emperors were uninspiring and conservative was unduly colored by the problems that emerged during their reigns which these leaders could do little about. As the

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41See the discussion in Mann and Kuhn (1978) on the Jiaqing emperor’s reluctance to take the steps necessary to tackle the problem of corruption.

42The late Qian Mu, perhaps the best known classical Chinese historian of the twentieth century, claimed that the decline of the Qing dynasty was caused by: (1) the deterioration in the leadership qualities of successive Qing emperors; (2) the increasingly corrupt behaviors of the officials and their underlings; and (3) sustained population growth (Qian, 1940, p. 865-870).

43Li (2007) portrays a competent Jiaqing emperor who successfully orchestrated a flood control and famine relief campaign when a massive flood hit northern China in 1801. Dodgen (2001) sees Jiaqing’s successor
model suggests, a rise in corruption need not imply less vigilant rulers. State affairs in 19th century China had simply become intractable and would have overwhelmed even the ablest and most dedicated ruler.

5 Model Extensions

5.1 When and why the ruler shows tolerance towards corruption

This extension endogenizes $U_t$, the punishment that the ruler metes out to tax agents suspected of corruption. It shows that although corruption is detrimental to the ruler’s interest as it directs a portion of the society’s surplus that could be captured by him to the private pockets of corrupt tax agents, a rational ruler may — ironically — show more leniency towards corrupt officials as corruption worsens.

Suppose there are now two types of tax agents: the corrupt type and the honest type. As before, the corrupt type weighs the benefit of corruption against the risk of punishment to decide his best course of action. On the other hand, the honest type is incorruptible and never abuses office.

ω fraction of tax agents belong to the corrupt type and 1 − ω fraction belong to the honest type at any time. ω is exogenously determined and the precise value it takes does not matter to our analysis, as long as 0 < ω < 1.44

Suppose that the ruler cannot distinguish which type a particular tax agent belongs to but he has to keep honest people in the bureaucracy.45 These two conditions are non-trivial, for they imply that the ruler cannot punish his servants freely.

Let the payoff function of an honest tax agent serving at time $t$ be:

$$v_t^{Honest} = H - m \cdot U_t - K(N_t)$$ (5.1)

$H$ in the above equation is a strictly positive normalizing constant. It can be taken to represent a sense of warm glow felt by the tax agent for acting in an unselfish manner. $K(N_t)$ represents the tax agent’s cost of performing his duty.46
At time $t$, an honest tax agent will only serve the ruler if $v_t^{\text{Honest}} > 0$. Given that $q(0) > 0$, there is a small but strictly positive probability that he may be wrongly accused of corruption. To prevent honest tax agents from opting out of service ex-ante, the maximum level of punishment that the ruler can mete out ex-post is:

$$U_t = \frac{H - K(N_t)}{q(0)}$$  \hspace{1cm} (5.2)$$

If $N < N_s$ to begin with, population will grow over time. To keep honest tax agents in the bureaucracy, the ruler will have to lower $U_t$ progressively so that equation (5.2) is not violated. As to be expected, his apparent indifference towards maladministration will in turn encourage corrupt agents to up the ante according to optimality condition (4.6).

To sum up, if the ruler does not have access to accurate information on his agents’ actions, a vigorous campaign on corruption could appear arbitrary, for it penalizes not only the corrupt agents, but the honest ones as well. The higher is $q(0)$, the more likely individual agents could be punished for crimes that they did not commit, and therefore the more circumspect the ruler has to be in meting out punishment.

5.2 Reversal in capital accumulation

To see how a fiscal crisis could spill over to the real economy, I now introduce investment into the model to endogenize $Y^E$. This extension yields a simple and straightforward result: long run fiscal and political uncertainties could lead to reversals in capital accumulation by undermining public confidence. A state that taxes too little, like one that taxes too much, could cause economic stagnation and a lack of investment.

Suppose the local elite’s income $Y^E$ is determined by the amount of capital stock $K$ that he owns at time $t$. Let $Y_t^E = Y^E(K_t)$, where $K \geq 0$, $Y^E(0) = 0$, $Y^E'_K(.) > 0$ and $Y^E_{KK}(<) < 0$.

In each time period, the investor loses a fixed fraction $\delta$ of his productive assets due to depreciation, but he can also make a non-negative investment to increase his capital stock. At time $t$, if he invests $I_t$, his capital stock at time $t+1$ will be:

$$K_{t+1} = (1 - \delta) \cdot K_t + I_t$$ \hspace{1cm} (5.3)$$

An important determinant of the investor’s decision is his discount factor $\beta$. This in turn depends on how confident the investor feels about property rights protection in the future. Given that the collapse of a regime is likely to result in insecure property rights due to war and anarchy, if the investor regards a regime collapse in the next time period as a high probability
event, he will discount the future more, and invest less today.

To reflect variations in the investor’s confidence towards future property rights protection, suppose that the ruler receives a public goods expenditure shock $W$ at the end of every time period. The shocks are randomly drawn from a distribution function. Mathematically, let $W_t = |X_t|$, which has a cumulative distribution function $F(.)$ with mean 0 and variance $\sigma^2$.

At time $t$, after $W_t$ has been realized, if it turns out to be bigger than the period payoff of the ruler $v_t^R$, the regime goes into fiscal crisis and collapses. When this happens, the game ends and the capital stock ceases to reap future rewards for investors who owned them at time $t$.

The investor therefore discounts the future by the probability of the game not surviving into the next period. His discount factor is given by:

$$\beta_{t+1} = F(v_t^R) - F(-v_t^R)$$  \hspace{1cm} (5.4)

As the above condition suggests, $\beta_{t+1}$ moves in the same direction as $v_t^R$. The higher is $v_t^R$, the more stable the regime is and the more forward looking an investor will be.\(^{47}\)

At time $t$, the local elite makes his investment decisions after taxes are collected and before the realization of $W_t$. Otherwise the timing of events is exactly the same as before:

1. The ruler sets tax rate $\tau_t$ and size of tax agency $B_t$ to tax the local elite and $N_t$ peasants;
2. Each tax agent chooses his optimal rate of extortion $\epsilon_t$ and proceeds to collect taxes;
3. Tax collection ends. The ruler evaluates all tax agents and punishes those associated with positive signals;
4. Peasants make private decisions on how many children to produce. These decisions collectively determines $N_{t+1}$. The local elite determines $I_t$;
5. The public goods expenditure shock $W_t$ is realized;
6. If $W_t > v_t^R$, games ends. Otherwise, $t$ ends and $t + 1$ begins.

The ruler, the tax agents and the peasants solve the same respective problems as before.\(^{48}\)

\(^{47}\)A local elite can influence the discount factor through his investment decisions, but for this to happen, he must coordinate his action with other members of his class. It is possible that setting up a legislative assembly or introducing democracy may facilitate the coordination process. As this model does not consider the possibility of institutional innovation, he is assumed to take the value of $\beta_{t+1}$ as given here.

\(^{48}\)Again this presupposes that these players will not or cannot influence $\beta_{t+1}$. One may suspect that under certain circumstances, it is in the ruler’s interest to commit at time $t$ that he will set $\tau_{t+1}$ below the level that binds the no-revolt constraint (4.4) to stimulate investment. However, such a commitment is unlikely to be credible as the ruler also has the incentive to renege on his promise at time $t + 1$ and increase $\tau_{t+1}$ to the level
The local elite’s allocation problem at time $t$ is given by:

$$\max_{C_{t+j} \geq 0, I_{t+j} \geq 0} V_t = \sum_{j=0}^{\infty} \prod_{k=0}^{j} \beta_{t+k} \cdot U(C_t^E)$$ (5.5)

subject to

$$C_{t+j} + I_{t+j} \leq (1 - \tau_{t+j}) \cdot Y_E(K_{t+j})$$ (5.6)

where $\beta_t = 1$ at time $t$, $U^E(.) > 0$, $U^E_{cc}(.) < 0$.

His Euler equation is therefore given by:

$$\frac{U^E_c(C_t)}{U^E_c(C_{t+1})} = \beta_{t+1} \cdot [1 - \delta + (1 - \tau_{t+1}) \cdot Y^E_E(K_{t+1})]$$ (5.7)

This setup is almost identical to that of the standard neoclassical growth model. The only difference is that instead of assuming the discount factor $\beta$ to be a constant that is unchanging over time, here it is allowed to vary from period to period to reflect variations in investor confidence over future property rights protection.

From (5.7), if $\beta$ is assumed to be exogenous, it is natural to conclude that a weak state is always good for the economy, for a low $\tau_{t+1}$ encourages investment for the future.49

However, once $\beta$ is linked to political stability, the picture becomes more ambiguous. Now a weak state (typified by a low $\beta$), like a strong one (typified by a high $\tau$), could hurt investment, since a fall in $\beta$ affects investment in the same direction as an increase in $\tau$ in equation (5.7).

Combining the Euler equation (5.7) with result 7 gives us:

Result 8. Sustained population growth could lead to a depressed economic environment.

The scenario only emerges when the principal-agent problem is severe. If this condition is present, sustained demographic and economic expansion will generate rational expectations among investors when a fiscal crisis is imminent. As the economy moves closer to the twilight of the dynasty, a vicious cycle whereby political uncertainties and sluggish economic performance reinforce each other is likely to appear.

The setup here only allows the local elite to invest. This is admittedly arbitrary as there is no reason why others (the peasants) cannot do so. It is done nonetheless to deliver the point

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49The higher is $\tau$, the bigger is $U^E_c(C_t)$ relative to $U^E_c(C_{t+1})$, and therefore the more the local elite consumes and the less he invests today given that $U^E_{cc}(.) < 0$.
that political stability is no less important than low state exaction in encouraging investment. The local elite here do not suffer from local state oppression. In fact he enjoys a low tax rate thanks to the presence of local state oppression. Yet even someone as privileged as he is may not invest as long as there exists huge uncertainties to the security of his property rights (which arose due to the society’s inability to solve collective action problems).

In the model, $W_t$ is assumed to be randomly drawn and independent of $v_t^R$. As we shall see in section 6, in reality expenditure shocks are likely to be positively related to the fiscal health of the state — floods become more frequent when the impoverished state cut corners in river control projects, monetary instabilities increase with fiscal difficulties, uprisings erupt readily when there are insufficient resources to maintain the social safety net or to keep the military effective, and foreign powers turn more aggressive when they sense the presence of a weakened prey. The political and economic downswing, once set in motion, could be more pronounced than the model predicts.

6 Empirical Evidence: Distance and Agency Costs

This paper argues that the severity of the principal-agent problem in a dictatorship increases with geographic size. Specifically, results 3 and 4 offer two testable hypotheses to ascertain the validity of this claim.

First, given that the no-revolt constraint (4.4) binds in equilibrium, if indeed agency costs increases with distance, stipulated tax rate per capita across regions should differ, with regions faraway from the capital enjoying lower stipulated tax rates to account for higher levels of corruption in these weakly monitored regions.

Similarly, the ruler’s optimality condition (4.9) predicts that $B$ is positively correlated to $N$, and negatively correlated to the severity of the principal-agent problem. In other words, holding population density constant, the presence of civilian administration should be more keenly felt in regions adjacent to the capital than in faraway regions. Given that the county was the lowest level of formal administration, and that it was held responsible for the collection of land taxes in late imperial China, if this hypothesis holds true, the number of counties per square area should be higher in the vicinity of Beijing and lower elsewhere, after controlling for population density.

Data. Three sets of information are used here to test the predictions, of which the first two are prefectural-level data sets. The first data set is GIS-based.\textsuperscript{50} It provides the demarcation of prefectures in 1820 China, as well as the area and the number of counties administered by

\textsuperscript{50}CHGIS, Version 4, Cambridge: Harvard Yenching Institute, January 2007
every prefecture. The second data set, drawn from the *Grand Gazetteer of the Qing during the Reign of Jiaqing*,\(^{51}\) gives us the number of inhabitants as well as the stipulated tax quota of every prefecture in 1820. Finally, I have plotted the imperial postal relay routes based on the descriptions in the Yongzheng edition of DQHD (figure 5a). The imperial postal relay system ran errands between the capital and the provincial capital, and the imperial court relied on it to maintain communications with the rest of the country.

Figure 5 presents the information using maps. Figure 5a depicts the imperial postal relay routes (marked by black lines), as well as the location of the county seats (represented by red dots). Figure 5b illustrates population density in 1820 China. County density, or the number of counties per square area, is given in Figure 5c.\(^{52}\) Put together, the three maps provide suggestive evidence that distance from Beijing matters — county density was generally higher in the north than in the south. Furthermore, county density also appears to be positively associated with population density, since both county density and population density are generally higher in the east than in the west.

**Empirical specification and result.** OLS and IV regressions are employed here. First, I regress the *diding* — or the land tax stipulated in silver — per capita (*TAX*, prefectural *diding* quota divided by prefectural population, in grams of silver) on distance from Beijing (*D*, in 1,000 kilometers).\(^{53}\) As an alternative specification, I then use population density (*Y*, inhabitants per square kilometer) as a proxy for agricultural productivity per capita, and regress *TAX* on *D* and *Y*, or:

\[
TAX = \beta_0 + \beta_1 \cdot D + \beta_2 \cdot Y
\]  

(6.1)

The outputs of the two OLS regressions are shown in columns (a) and (b) of table 1. They support the prediction in result 3 that \(\beta_1 < 0\), and are statistically significant at 1% level.

One may worry that the imperial postal relay routes might be designed to pass through regions of high county densities. To correct for this potential endogeneity of *D*, I use direct (straight-line) distance between prefectural seat and Beijing as an instrument variable for *D*. Given that there is seemingly no plausible reason for direct distance to be correlated to *TAX* other than through *D*, and that it is highly correlated with *D*, it appears to be a good choice as an instrument variable. In column (c), the high value of the first-stage F-statistics

\(^{51}\) *Jiaqing Chongxiu Yitong Zhi* as republished in Liang (2008) and Cao (2000).

\(^{52}\) This is calculated by dividing the number of counties in a prefecture by the area of the prefecture.

\(^{53}\) *D* represents the sum of two components: direct distance from prefectural seat to provincial capital, and actual distance by imperial postal relay routes from provincial capital to Beijing.
Figure 5: County Density and Population Density in 1820
on excluded instruments shows that direct distance pass the weak instrument test, and the coefficient of $D$ is still negative at 1% significance level.

To test the prediction of result 4, I replace $TAX$ with $CD$, the number of counties per 10,000 square kilometers, as the dependent variable, and regress it on $D$ and $Y$, or:

$$CD = \beta_3 + \beta_4 \cdot D + \beta_5 \cdot Y$$

(6.2)

Result 4 predicts that $\beta_4 < 0$ and $\beta_5 > 0$, which is consistent with what we see in column (d). Next, to correct for the potential endogeneity of $D$, I again use direct distance as an instrument. As shown in column (e), it passes the weak instrument test with ease. The coefficient of $D$ remains negative, and that of $Y$ positive, at 1% significance level.

Table 1: Effect of Distance on Land Tax Burden and Administrative Presence, circa 1820

<table>
<thead>
<tr>
<th></th>
<th>(a)</th>
<th>(b)</th>
<th>(c)</th>
<th>(d)</th>
<th>(e)</th>
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<tr>
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<td>OLS</td>
<td>IV</td>
<td>OLS</td>
<td>IV</td>
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<tr>
<td>Dependent Variable</td>
<td>TAX</td>
<td>TAX</td>
<td>TAX</td>
<td>CD</td>
<td>CD</td>
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<tr>
<td>$D$ (Distance from Capital)</td>
<td>$-2.18^{***}$</td>
<td>$-2.05^{***}$</td>
<td>$-1.87^{***}$</td>
<td>$-1.21^{***}$</td>
<td>$-0.98^{***}$</td>
</tr>
<tr>
<td></td>
<td>(0.20)</td>
<td>(0.23)</td>
<td>(0.22)</td>
<td>(0.26)</td>
<td>(0.27)</td>
</tr>
<tr>
<td>$Y$ (Population density)</td>
<td>0.0020*</td>
<td>0.0024**</td>
<td>0.018***</td>
<td>0.019***</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(0.0011)</td>
<td>(0.0011)</td>
<td>(0.002)</td>
<td>(0.002)</td>
<td></td>
</tr>
<tr>
<td>$N$</td>
<td>269</td>
<td>269</td>
<td>269</td>
<td>271</td>
<td>271</td>
</tr>
<tr>
<td>$R^2$</td>
<td>0.38</td>
<td>0.39</td>
<td>0.52</td>
<td></td>
<td></td>
</tr>
<tr>
<td>$F$ on excluded instrument</td>
<td></td>
<td></td>
<td></td>
<td>2444.0</td>
<td>3238.1</td>
</tr>
</tbody>
</table>

Robust standard errors in brackets. * significant at 10%, ** significant at 5%, *** significant at 1%.

7 Historical Evidence: Fiscal Decline

The previous section establishes the empirical link between geographical size and the severity of the principle-agent problem. This section presents historical evidence to show that consistent with the predictions of results 5, 6, and 7, state finances in Qing China began to deteriorate in the first half of the 18th century (section 7.1) as corruption rose (section 7.2) in the face of population growth.

7.1 Falling tax revenues

Result 7 predicts that economic expansion could hurt a regime plagued by a severe principal-agent problem. This is consistent with the pattern in figure 6, which illustrates
...the Qing state’s tax revenue between 1650 and 1850. Although the prosperous age of the High Qing did not end until late in the 18th century, in real terms, the Qing state’s tax revenues reached a peak as early as in the 1720s, and fell steadily from there.

Figure 6: Estimates of the Late Imperial Chinese State’s Tax Revenue

Notes and sources:
(1) Includes taxes collected in silver (the *ding* [the land tax stipulated in silver], the salt tax, customs duty, and miscellaneous taxes) as well as the grain tax (the land tax stipulated in grain).
(2) Tax revenue refers to the actual amount that entered state coffers, plus estimated cost of collection. It covers the tax revenues of all levels of government (central, provincial, local), but excludes illegitimate incomes obtained through office. I assume that for every of tael of silver collected, tax collectors could legitimately collect 0.25 tael of silver to write off their costs (see the discussion on land tax collection in section 3, especially footnote 24). Since grain is more costly to transport and store, the costs of grain tax collection are set at a higher rate of 37.5%.
(3) Silver-to-grain conversion is based on the rice price series in column 5, Table 1.1 of Wang (1992). Since a portion of the grain tax was denominated in cheaper grains such as beans, this actually overestimates the silver value of the grain tax.
(4) The base numbers from QSL series are drawn from the *Veritable Records of the Qing dynasty* (QSL). This is a collection of records compiled after the death of every Qing emperor, which documented in chronological order the important monarchic decrees and court activities during each emperor’s reign.
(5) There is no information on receipts from customs stations in the *Veritable Records*. As such, I assume that the customs receipts amounted to 1.2 million taels of silver in 1652 and the number grew at a constant rate until it reached 1,219,782 silver taels in 1685 as recorded in the Kangxi edition of DQHD (2006). Justification for doing so comes from QSG (1927, juan 125), which stated that “Peace began to return by the 9th year of the Shunzhi reign (1652)…customs duties exceeded more than a million silver taels”.
(6) Other sources included Board of Revenue records that are either published or are kept in Chinese archives, as well as QSG (1927). Specifically, the base numbers for 1661, 1685, 1724 and 1753 are drawn from DQHD, 1811-12 from SLXK (1930), 1823-24 from DGCRQD, 1838-48 from DGJMZC. For 1749, the annual aggregate silver tax revenue was mentioned in a Board of Revenue President’s memorial to the throne ZYCZ, vol. 1. The amount of land tax collected in 1766 was published in QCWXTK (1787), a work commissioned by the Qianlong emperor. The amount of salt tax, customs duty, and miscellaneous taxes for that year was mentioned in QSG (1927, juan 125). The 1791 base numbers also came from QSG (1927, juan 125).
(7) Information on the tax grain is incomplete after 1766. Information on the grain tax in 1753 is well documented in Li and Jiang (2008, p. 38-39). However, there is scant information on the remaining portion of the grain tax. This missing portion, known as *bingmi* (literally “rice-for-soldiers”), was consumed within the province of origin by imperial garrisons stationed there. Since the size of the Qing army remained fairly stable throughout this period, here it is assumed that the actual amount of *bingmi* collected after 1753 remained at the 1753 level (Alternatively, we can assume that the ratio of *caoliang* to *bingmi* stayed at the 1753 level after 1753. Since the *caoliang* figures were falling during this latter period, this assumption would cause a steeper decline in state revenue after 1766).

If we take basic standard of living to represent an annual consumption of $3\frac{1}{3}$ shi of grain per capita,\(^{54}\) the Qing state’s tax revenue would be sufficient to feed and clothe 9.6% of the population.

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\(^{54}\)This would cover expenditure on clothing, food, and food supplements such as oil and salt (Huang, 2003,
Figure 7: Tax-to-GDP Ratio: China and Britain (%)  

Sources: figure 6; O’Brien (1988, p. 3).

Figure 8: Fiscal balance with and without sale of official titles

Source: Hand-copied Board of Revenue Income-Expenditure Records kept in Chinese Academy of Social Sciences.

p. 158).
Chinese population in 1685, 7.7% in 1724, 5.4% in 1753, 4.1% in 1791 and 2.3% in 1848. By this measure, state extraction ratio fell by three-quarters in slightly over one-and-a-half century. Compared to Britain, the contrast is illustrative (figure 7).

The trend in figure 7 is also consistent with result 6, which predicts that tax rates would decline over time. In practice, however, the Qing state did not adjust tax rates on a regular basis. Where the land tax is concerned, the tax liability of a household was expressed as a fixed amount of silver per plot of land. This stipulated nominal sum hardly changed over time. During the early and mid-18th century when inflation was positive (figure 9a), the decline in the real tax rate was automatically achieved through rising price levels. It was only when the long term price trend reversed itself during the late 18th and early 19th century that the Qing court had to grant tax waivers (juan mian) or postponements (huan zheng) to relieve the tax burden of the peasants.

Figure 8 depicts the fiscal balance of the Qing state in the 18th and 19th centuries. It offers us a slightly different angle to examine the steady deterioration of the Qing state’s finances.

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55 The percentages for England are drawn from O’Brien (1988). The percentages for China are calculated using the fiscal estimates in figure 6 and the population estimates in Perkins (1969, p. 216) (missing years are filled up by interpolation). Recalculating figure 7 using alternative population estimates in Ho (1959), Lee and Wang (1999), or Cao (2000) would not change the pattern observed. Similarly, replacing rice with cheaper grains would not alter the trend in figure 7.

56 Both juan mian and huan zheng were relatively uncommon in the 18th century. In 1812, 1824, and 1848 respectively, 14.1%, 6.2%, 14.2% of the land tax were waived or exempted nationally based on my calculation.
As tax revenues dwindled over time, the state undertook stop-gap measures such as holding campaigns to sell official titles, transferring surpluses of the inner court to the state treasury, and so on to narrow the widening funding gap. Because of these efforts, the downward trend in figure 8a is mild and hardly noticeable. However, once these extraordinary revenues were excluded, the depth of the Qing state’s fiscal problems is self-evident (figure 8b).

How do the other competing hypotheses measure up to the above fiscal evidence?

First, the empirical patterns do not square with the argument that unchecked monarchic power was the root of China’s developmental problems. Serious political and socio-economic troubles emerged in China at the turn of the 19th century (figure 1), but state revenue shrunk steadily from the early 18th century onwards. In fact, state extraction was at its lowest in the early 19th century, when domestic unrest and foreign threats were about to shake the very foundation of Qing rule.

Second, classical Chinese historiography blamed a succession of increasingly incompetent rulers for China’s woes in the 19th century — a view that is not dissimilar to Keynes’ belief that “third-generation men” were responsible for Britain’s industrial decline in the 20th century. However, as the evidence above illustrates, the steady contraction of the Qing state’s fiscal capacity began before Jiaqing and Daoguang — the “weak” rulers of the early 19th century — were even born. There is a growing consensus among modern China historians that the leadership qualities of these two emperors have been grossly underrated (Leonard, 1996; Dodgen, 2001; Li, 2007; Will, 2008).\footnote{See footnote 43.} This view finds support in the fiscal evidence above.

Third, it has been suggested by some scholars that China’s contrasting fortunes before and after 1840s were the result of a contingent of events. Rosenthal and Wong (2009) argue that there was nothing fundamentally flawed with the political institutions of late imperial China. After all, they had proven to be capable of delivering economic success in a pre-modern world. China’s path to industrialization would be far more straightforward if not for the political and military problems of the 19th century which the West and Japan were partly responsible for. A variant of this argument blames the inflexibility of Chinese institutions in adapting to the age of industrialization for its relative decline in the 19th century (Li, 2003), but it still implies that China would have done fine if the coming of the West did not occur.

There is much merit in this line of argument, but in light of the fiscal evidence above, it is clear that China’s developmental problems in the 19th century cannot be entirely attributed to exogenous events. State finances in Qing China began to worsen long before the negative events of the late 18th and early 19th centuries took place. This indicates that there were fundamental structural weaknesses in the late imperial Chinese political system. External
shocks did aggravate China’s plight in the 19th century, but it was the sustained enfeeblement of the Chinese state which began in the 18th century that denied China the collective ability to deal with these shocks effectively in the first place.

Finally, some China historians see the Qing state’s fiscal weaknesses as a direct consequence of its adherence to the Confucian ideal of benevolent rule. According to this argument, the Qing emperors were keen to distinguish themselves from the last rulers of the preceding Ming dynasty, who were toppled by a peasant uprising in 1644 after they raised the land tax three times in less than thirty years. As such, the Qing emperors were reluctant to raise taxes. In 1713, the Kangxi emperor even announced a permanent freeze on the head tax, as it was found to be excessively regressive in practice.

There is nothing contradictory between the above view and the hypothesis in this paper, unless one sees the Qing emperors’ emphasis on benevolent rule as one of choice rather than of necessity. A closer look at historical evidence suggests that although the Qing emperors’ decision to keep taxes low and fair was couched in ideological terms, it was clearly very much driven by practical needs.

For one, Ray Huang (1974) have shown that the average tax burden during the late Ming dynasty was nowhere near exorbitant even after taking into account the three tax hikes. The tax hikes were oppressive only because they were regressive. Given that a seemingly reasonable amount of tax increase could easily translate into an exorbitant jump in the poor’s burden, the Qing state had to keep taxes low to ensure that the exploitation of the weak and poor was sustainable.

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58 For example, see Rowe (2009, p. 66).
59 Ironically, the tax hikes were imposed to shore up border defenses against the newly founded Later Jin (Qing) empire.
60 Furthermore, no national land survey was ever conducted during the 268 years of the Qing dynasty. The Qing court took over the land records of the Ming dynasty and relied on provincial and local officials to update the Board of Revenue on the amount of land newly reclaimed each year. Agency problems played a part in the Qing emperors’ unwilling to deal with the problem of unreported acreage. There were many instances of reported abuse when small scale land surveys were conducted during the early years of the Qing dynasty (Wang, 1973, p. 27). It was found out that local officials and their underlings took the opportunity to extort fees from the people. When the Yongzheng emperor made officials compete with one another to report newly reclaimed land, it led to a wave of false reporting and taxpayers were made to shoulder the taxes on lands that never existed (Rowe, 2009, p. 94-5). Consequently, the policy had to be abandoned.
61 The topic of junding (equalizing the head tax) was widely discussed in HCJSWB, juan 30. Kangxi’s successor Yongzheng took the additional step of merging the head tax into the land tax to shift the tax burden away from the poor.
62 The Ming state collected 25-30 million taels of silver from land taxes and service levy before 1600 (about 10% of the agrarian output). The tax increases in the early 1600s amounted to no more than 21 million taels a year. Huang argued that “the tax increases were to a large extent illusory” as prices rose by 40% during this period (Huang, 1974, p. 175, 183, 308).
7.2 Rising corruption

Only anecdotal evidence is available to inform us about the trend of corruption in late imperial China, but there is an abundance of it. In line with the hypothesis, it is widely observed that corruption worsened over time in Qing China, and it was the have-nots in society that bore the brunt of growing maladministration.

Major corruption scandals took place infrequently during the reigns of Shunzhi (1644-61), Kangxi (1662-1722), and Yongzheng (1723-35). By the Qianlong’s reign (1736-95), they became a regular occurrence. Out of the 139 people who served the Qianlong emperor as provincial governors or governors-general, 30 of them, or over 20% of the total, were implicated in corruption scandals (Park, 1997, p. 968). In 1799, Heshen, the grand councillor and the de facto prime minister, was famously impeached and sentenced to death. An imperial censor lamented in 1803 that even county government clerks were dressing so luxuriously that it was no longer possible to tell their status from their appearance (Mann and Kuhn, 1978, p. 112). The scholar Hong Liangji (1746-1809) remarked that when he was young, magistrates could retire with enough to provide for his family for generations. When he grew older, that surplus had increased tenfold as corruption worsened (Ch’u, 1962, p. 31).

At the local government level, surtaxes unauthorized by the central government proliferated over time. In the province of Shanxi, 12 surtax items were imposed between 1735 and 1795, 7 additional items were imposed between 1796 and 1820, and 15 more between 1821 and 1850 (Wang, 1973, p. 59). In the southern province of Guangdong, where peasants were asked to pay their grain tax in silver, the commutation rate fixed by officials rose from 2 silver taels per shi of grain in the second half of the 18th century to more than 7 taels per shi by the mid-19th century, an increase that was far more than inflation could justify (Lin, 1997).

One type of “squeeze” that became prevalent was the practice of discounting the value of grain commoners submitted for tax payment (zhekou). When a taxpayer submitted 1 shi (10 dou) of grain as tax payment, county agents would count the grain for less than that. In the early years of the Qianlong’s reign, the prevailing discount rate was no more than a few percentage points. By the second half of the 18th century, 1 shi of grain would only count as 7, 8, or 9 dou during tax submission. It fell further to 5, 6 dou during the first half of the 19th century (QSG, 1927, juan 121).

Not all taxpayers were affected by these practices in the same way. The rich and powerful households could always rely on their political patronage to protect themselves against local state oppression. Although the Qing court explicitly banned the classification of tax

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63 shi was a volume measure, equivalent to 103.5 liters or 2.94 bushels (Rawski and Li, 1992).
64 Ch’u (1962, p. 141) citing Wang Huizu, who served as a magistrate during the latter years of the Qianlong’s reign.
payers into “big households” (da-hu) and “small households” (xiao-hu), this practice became increasingly common over time. In northern Jiangsu during the 1840s, it was observed that “small households” were paying 6000 to 16,000 wen for every shi of rice that they owed in taxes, while “big households” were charged the market rate of 2000 to 3000 wen per shi of rice (Wang, 1973, p. 38).

As observed by the scholar-official Feng Guifen (1809-1874), although tax liabilities were supposed to be computed at the household level based on the amount and quality of land each household owned, in practice one’s effective tax rate was always inversely related to his wealth and influence in local society. There were gentry families who owned huge plots of land but “never knew how paying taxes felt”, while commoner households could end up paying three to four times more taxes than their legal obligations (Feng, 1876, juan 10).

8 Historical Evidence: Reduction in Public Goods Provision

The model extension in section 5.2 shows that persistent fiscal weaknesses undermine the economy as the state becomes increasingly unable to pay for essential public goods that protect property rights. In this section, we see how the sustained deterioration of the Qing state’s finances actually led to the under-provision of public goods. By the late 18th century, the signs were clear that the once proud Qing state no longer had the ability to contain foreign threats and natural disasters, mitigate social tensions in local societies, and maintain monetary stability in a proactive and effective manner.

Table 2 provides a glimpse at the Qing state’s role in the economy of late imperial China. It suggests that the regime contributed to the economy’s well-being mostly in an indirect manner — through the protection of property rights. Through its military, the regime provided peace, which was crucial for economic exchanges to take place. This was reinforced by the civilian administration, which administered justice as well as maintained social order. The Yellow River conservancy sought to prevent flooding and the subsequent loss of lives and properties along the heavily silted Yellow River, the second longest river in China. Arguably, only the imperial mints — which consumed less than 1% of the state budget — facilitated economic exchanges directly by manufacturing copper coins used as mediums of exchange.

Due to its small budget, the minimalist Qing state adopted a largely hands-off approach in the provision of local public goods and the promotion of economic growth (Perkins, 1967; Myers, 1982; Feuerwerker, 1984). With the notable exception of trade along the Grand Canal, most long distance trade was carried out among regions either well served by natural inland waterways or along the coast. Land transportation, which would require investment in infrastructure, appears to have been underdeveloped. As a result, overland transport was sig-
Table 2: Estimates of the Qing State’s Silver Expenditure (1766)

<table>
<thead>
<tr>
<th>Item</th>
<th>Amount (1000 taels)</th>
<th>Share (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Military (Peace time)(^a)</td>
<td>24,880</td>
<td>60.6</td>
</tr>
<tr>
<td>Civilian administration(^b)</td>
<td>9,620</td>
<td>23.4</td>
</tr>
<tr>
<td>Yellow River conservancy</td>
<td>3,850</td>
<td>9.4</td>
</tr>
<tr>
<td>Imperial post stations(^c)</td>
<td>1,950</td>
<td>4.8</td>
</tr>
<tr>
<td>Imperial mints(^d)</td>
<td>240</td>
<td>0.6</td>
</tr>
<tr>
<td>Palace expenses(^e)</td>
<td>270</td>
<td>0.7</td>
</tr>
<tr>
<td>Miscellaneous(^f)</td>
<td>250</td>
<td>0.6</td>
</tr>
<tr>
<td>Total</td>
<td>41,060</td>
<td>100.0</td>
</tr>
</tbody>
</table>

Sources: QCWXTK (1787, juan 40), QSG (1927, juan 125).

Notes: (a) This can be further broken down into 5.03 million taels of silver (troops deployment in Beijing), 1.45 million taels (Manchuria), 17.5 million taels (rest of China), 0.81 million taels (wage supplements for military officers), and 0.08 million taels (horses, camels, and other animals).
(b) Including wages, wage supplements, and other administrative outlays incurred by the civilian bureaucracy.
(c) QSG (1927) lumped the expenditure on imperial post stations and other civilian administrative outlays in 1766 together as one single item. The amount cited here is estimated based on the Jiaqing edition of DQHD (1812).
(d) This amount reflects the outlays of all state mints in the capital and the provinces. QCWXTK (1787) only reported the expenditure of the two Beijing mints. The production costs of the provincial mints are estimated based on the production figures reported in Lin (2006, Table 1.2).
(e) This includes the expenses incurred by the Imperial Silk Manufactory, which oversaw the purchase or manufacture of textile consumed in the palace, as well as stipends paid to princes and other nobles.
(f) About half of this amount (0.12 million taels) was spent on building and repairs of boats used to transport grain to the capital. According to QSG (1927), this item consumed 1.2 million taels in 1766. However, this figure is too large to be true. A simple calculation will make this clear: there were 6969 such boats in operation around the time (according to the Qianlong edition of DQHD). The imperial court stipulated that annual maintenance expenses should be capped at 7.5 taels per boat (DQHDZL, juan 42). Furthermore, boats could be retired only after 10 years of service and the cost of a new boat should not exceed 78 to 298 taels, depending on its type (DQHDZL, juan 39). Even if all new boats were constructed at the unit price of 298 taels, the total annual construction and repair costs would not have exceeded 0.26 million taels. Hence, I assume here that the 1.2 million taels contains an extra zero by mistake, and adjust the figure accordingly.

Significantly more expensive relative to water transport in China compared to Western Europe (Shiu and Keller, 2007).\(^{65}\)

Proponents of the “Big Push” theory may argue that industrialization in China was hampered because the Qing state was too weak to coordinate investments across sectors and push the country out of the no-industrialization trap — for example, it did too little to invest in education or basic infrastructure such as roads, harbors, and (later) railways.\(^{66}\) Even if we reject this strong form view that the state has a direct role to play in the promotion of economic development, and judge the Qing dynasty entirely on the weaker criteria of a night watchman state, it is clear that its performance in the realm of property rights protection had turned increasingly disappointing from the second half of 18th century onwards.

\(^{65}\)Traditionally, the Board of Public Works ranked last in the six central government ministries. A popular saying described the Six Boards as the “wealthy” Board of Revenue, the “noble” Board of Civil Appointments, the “prestigious” Board of Punishments, the “mighty” Board of War, the “impoverished” Board of Rites, and the “lowly” Board of Public Works — or \(fu\), \(gui\), \(wei\), \(wu\), \(pin\), \(jian\) in that order (Xu, 1917).

\(^{66}\)This argument was made, for example, in Li (2003).
Military. The defense of the Qing empire during this period depended on two military systems: the Eight Banners and the Green Standard Army.\textsuperscript{67} The Eight Banners garrisoned Beijing as well as the strategic approaches to the capital, while the Green Standard troops were deployed to defend the provinces.

There were about 112,600 banner soldiers in 1634. By the mid-18th century, the number grew to about 200,000 (Feuerwerker, 1976, p. 54-55). To cut state payroll, measures were taken during the reign of Qianlong, for example, to decommission Han Chinese bannermen \((chu \, qi \, wei \, min)\).

On the other hand, the size of the Green Standard Army stood at around 600,000 (Wang, 1890). Table 3 illustrates the size of the Green Standard troops deployed in four provinces in South China.

Table 3: Troop Deployment in Four Southern Provinces

<table>
<thead>
<tr>
<th>Year</th>
<th>Guangdong</th>
<th>Fujian</th>
<th>Zhejiang</th>
<th>Guangxi</th>
</tr>
</thead>
<tbody>
<tr>
<td>1689</td>
<td>73,100</td>
<td>69,726</td>
<td>43,450</td>
<td>20,000</td>
</tr>
<tr>
<td>1764</td>
<td>72,565</td>
<td>66,566</td>
<td>41,529</td>
<td>24,166</td>
</tr>
<tr>
<td>1785</td>
<td>68,094</td>
<td>63,119</td>
<td>40,037</td>
<td>23,588</td>
</tr>
<tr>
<td>1812</td>
<td>69,007</td>
<td>63,324</td>
<td>39,009</td>
<td>23,408</td>
</tr>
<tr>
<td>1821</td>
<td>69,181</td>
<td>63,096</td>
<td>36,830</td>
<td>23,101</td>
</tr>
<tr>
<td>1849</td>
<td>68,322</td>
<td>61,675</td>
<td>37,565</td>
<td>22,472</td>
</tr>
</tbody>
</table>

Population (1766) 6,938,855 8,094,294 16,523,736 4,706,176
Population (1820) 21,558,239 18,546,446 26,422,380 7,416,287


These provinces are of particular interest because the main battles of the Opium War (1839-42) were fought along the coastal provinces of Guangdong, Fujian, and Zhejiang, while the Taiping Rebellion (1850-64) originated in Guangxi. In each of the four provinces, the size of its military shrunk over time before disaster struck.

The military cuts were implemented not because of complacency. The Qing court was fully aware of its military weaknesses, especially at sea. Much has been made about the Qianlong emperor’s snubbing of the Macartney mission in 1793. However, as Waley-Cohen (1993) points out, Qianlong’s behavior had more to do with diplomatic posturing than to a lack of awareness towards Western technological superiority. Immediately upon Macartney’s departure, the emperor instructed coastal provinces to bolster coastal defence,

“That they (Britain) made such outrageous demands shows that we must make

\textsuperscript{67}The Eight Banners system was set up during the founding years of the Qing (Jin) empire. The Green Standard Army was later formed to absorb Han Chinese soldiers who surrendered to the Qing during its conquest of China proper.
preparations in case they harbor evil intentions. The defence of our coast is most critical. In recent years, our coastal patrol and surveillance have been lax, fighting ability has deteriorated, we must do something about it (QSL, reign of Qianlong, juan 1436).”

In 1834, five years before the Opium War, his grandson the Daoguang emperor made remarks in the same vein after two British warships intruded into Chinese waters and sailed up the Pearl River with ease (SLXK, 1930, v. 3, p. 231),

“It seems that our cannon platforms are as good as useless. How laughable and deplorable it is that we cannot even repel two barbarian ships. Our military had decayed so much. No wonder the barbarians are looking down on us.”

Yet nothing was done as Daoguang placed his priority on restoring his regime’s fiscal viability and would not welcome new expenditure commitment.68 The pressure on state finances was so severe that during the Opium War, Daoguang ordered troops along the coast to began demobilization as soon as the first round of fighting stopped “to cut costly outlays” (yi jie mi fei), before a peace deal had been concluded (CBYWSM, p. 473, 491, 512).

**Local Administration.** Even at the height of Qing power, the Qing society was “under-governed”. In 1724, there were only 1360 counties, or one county for nearly 150,000 Chinese (Ch’u, 1962, p. 2). This was woefully inadequate, as the county was the level of administration that dealt directly with ordinary people. The situation only got worse over time, as the Chinese population more than doubled between 1700 and 1850 while the numbers of counties barely increased at all.

Where the judiciary process was concerned, the magistrate was the only imperial officer in the county administration authorized to preside over court proceedings. The weak presence of the state in the Chinese society explains China’s traditional reliance on kinship based organizations to promote law-abiding behaviors (i.e. prevent cheating and free riding), as well as its dependence on the local elite to mediate disputes in local communities. As the economy expanded and geographical mobility increased over the course of the 18th century, there were signs that this system of relying overwhelmingly on informal institutions to sustain cooperative behaviors was put under increasing strain. By the 1760s, vagrancy had become a serious social concern as the society felt increasingly threatened by rootless people unbounded by community ties (Kuhn, 1990). However, the state was unable to take up the slack in maintaining order. Instead, available court resources per person fell further with the drastic

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68 To cut expenditure, the cost-conscious Daoguang even resorted to wearing patched imperial robes instead of making new ones.
decline in the county-to-population ratio. To stem the ever-growing tide of civil cases flowing into local courts, the Qing state even resorted to measures such as outlawing litigation masters (lawyers) (Macauley, 1998). 69

The under-government of volatile frontier societies was a particular threat to social stability. In 18th century China, demographic pressure and the introduction of new crops from the Americas led to a wave of immigration from plains and valleys to highlands (Naquin and Rawski, 1987, p. 132-4). Communal violence was relatively common in these frontier societies due to a combination of weak state presence and the absence of an established elite. Some of these societies became highly militarized. The revolt of the White Lotus sect (1796-1804), the first major commoner rebellion after Qing pacification of China in the 1680s, erupted in the highlands of Central China. Here, a steady influx of population took place over the course of the 18th century but strong political institutions were never established. 70 Similarly, the Taiping Heavenly Kingdom movement (1850-64), which almost overthrown the Qing dynasty, originated in the highlands surrounding the city of Guangzhou in South China.

As figure 10 illustrates, social order was gradually restored in China during the second half of the 17th century with the establishment of Qing rule over China. However, commoner rebellions reappeared in the 1770s and the frequency of occurrence picked up over time, culminating in the Taiping movement of the mid-19th century.

**Flood Prevention and Control.** On river management in North China, the Qing state was a prisoner of its own success. Effective hydraulic engineering during the 17th and the 18th century reduced the frequency of flooding in North China, especially along the notoriously flood prone Yellow River. As a result, agricultural settlements mushroomed along river banks.

Over time, streams and swamps that once served as safety valves that drained off river water during the rainy season disappeared due to human encroachment. This increased the engineering difficulties of river management and costs of flood prevention. It also guaranteed that when disaster struck, its human costs would be exorbitant (Li, 2007).

Driven partly by the fear that massive flooding in North China could threaten the security

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69 Due to data constraint, it is not possible to prove statistically that litigation rates went up over time in late imperial China. According to Macauley (1998, p. 62, 332), the number of lawsuits in a commercialized county could reach as many as 800 a year in the late 18th and early 19th centuries. However, only about one-third of the cases were resolved in formal court sessions. The issue of backlogs was a particular concern in the more commercialized regions.

70 In her dissertation, McCaffrey (2003) describes the region as being plagued by increasingly fragile ecological conditions, as population growth led to excessive land reclamation which narrowed the water channels and increased the risk of flooding. The Qing state understood the risk, but was unable to enforce its own decision to ban further reclamation activities. Neither was it able to coordinate dike maintenance activities among upstream and downstream communities, nor to mitigate rivalries between left-bank and right-bank communities along the Yangzi and its tributaries effectively.
of nearby Beijing, the Qing state poured an increasing amount of fiscal resources into the management of the Yellow River hydraulic system. 670,533 silver taels were spent on the Yellow River conservancy in 1730 (Dodgen, 2001, p. 28), and the amount rose to 3.8 million taels in 1766. An additional 40 million taels was spent on top of the conservancy’s regular budget in the 1830s to shore up the increasingly fragile Yellow River hydraulic system (QSG, 1927, juan 125). However, these outlays were still inadequate to meet actual needs. As a result, corners were cut even as the bed of the Yellow River continued to rise above its basin. Although the state responded resolutely when massive floods struck in 1824, 1841 and 1842 (Leonard, 1996; Dodgen, 2001), the withdrawal of its commitment was only a matter of time given the depth of its fiscal problems. In 1855, when the Yellow River again ruptured its dikes, the Qing court, with its silver reserves depleted, chose the course of inaction. The result, well documented in Pomeranz (1993), was the marginalization of inland North China into an isolated backwater.

**Monetary Policy.** The Qing dynasty inherited its bimetallic monetary system from the Ming dynasty. Silver was circulated in the form of bullion and was used for tax payment and wholesale transactions, while alloy coins known as “copper cash” (*tong qian*) were used in retail transactions. The supply of copper coins was largely determined by the state through its mints.

Counterfeiting of copper coins was punishable by death. However, as Lin (2006) has
pointed out, the Qing state was unable to halt the circulation of private coins even in its heyday. This was in part due to the state’s lack of social control, but it was also because of the mismatch between demand and supply — the output of state mints simply could not satisfy the needs of a huge and expanding population.

Figure 11: Amount of Copper Coins Cast by State Mints during the 18th century

The counterfeit problem worsened after state mints cut back production in the 1770s (figure 11). The Jiaqing emperor noted in 1796 that “in recent years, every province has had an abundance of (illegal) private mintage”. In 1801, it was reported that 30-40% of coins used in the Zhejiang province were counterfeits (Lin, 1989, p. 198). Vietnamese coins were circulated in southeast China (QSG, 1927, juan 124). This, plus the outflow of silver from the 1820s onwards, created significant monetary instability and confusion, which in turn led to serious repercussions for the real economy.

Famine Relief. The case with famine relief was similar. Under the auspices of the Qing emperors, a nationwide system of granaries was gradually built over time to act as a social safety net against unexpected subsistence crises. Research by Pierre-Etienne Will suggests

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1. During the first half of the 19th century, some provincial mints halted production completely to cut costs (Lin, 1989, p. 164).
2. Existing evidence suggests that the Chinese economy was in a period of stagnation or decline during the first half of the 19th century. The contemporary Qing scholar Jiang Gao observed that agricultural lowland in Songjiang county of Lower Yangzi used to be expensive due to low taxes. Before 1810, one mu of fertile land there could sell for 35,000 wen of copper coins (one mu is about one-sixth of an acre). But prices started falling after 1814. By 1833, the same plot of land could not be sold for 10,000 wen – a sign that “the rich households in the old days had become poor in our county” (Xue, 2007, p. 227). Bernhardt (1992, p. 51) reports a similar pattern in two other counties.

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that the Qing state’s capacity to mobilize resources in dealing with famines peaked in the mid-18th century, and the system visibly deteriorated in the last third of the 18th century (Will, 1990, p. 276).

This observation is in line with evidence from the central government’s granaries records. As shown in figure 12, the amount of grain reserves stored in Beijing’s state granaries reached a peak at around 1730, and fell steadily from there.

Figure 12: Grain Reserves in Beijing’s State Granaries


To sum up, economic and population expansion in late imperial China heightened the need for investment in crucial public goods such as a viable social safety net against bad harvests, a more sophisticated court system to adjudicate disputes, and a stable and expanding money supply. However, these could not be met with the state’s limited budget. In this regard, the gradual breakdown of social stability after 1796, the emergence of monetary instability, the apparent increase in the frequency of popular resistance to rents and taxes, the buildup in litigation backlogs, and the disastrous record in flood prevention along the Yellow River during the 19th century were all manifestations of the Qing state’s inability to manage the prosperity which it helped create.

The mounting problems created a looming sense of upheaval. By 1845, three years after Qing’s defeat in the Opium War and five years before the outbreak of the Taiping Rebellion, even the emperor of Vietnam noticed that the Qing dynasty was on the verge of collapse:

“Yesterday I read their Beijing Gazette. It is reported that the Qing’s coffers are almost empty after paying so much silver to England. Morality has been fading so much that even official positions and lawsuits can be recklessly purchased with
money. Robbery, hailstorms, and natural calamities have been frequent. I am thinking that these phenomena prefigure the fall of this dynasty.”

9 Conclusion

The late imperial Chinese state is a puzzle at first glance. It was absolutist, yet weak. It taxed lightly, yet the effective tax burden on the peasant was relatively heavy. It seemed inefficient, yet it was able to survive for more than two centuries. It was able to support rapid Smithian growth, without which the more than doubling of the Chinese population during the 18th century would not have been possible, yet it imploded when the opportunities and challenges of industrialization knocked on its door. This paper argues that these contradictions can be understood if we fully appreciate how geographical size had shaped China’s fiscal and organizational possibilities.

One may suspect that establishing a parliament could be a way to mitigate the principal-agent problem. As Banks and Weingast (1992) have pointed out, well organized constituents could assist their political representatives in limiting agency exploitation by acting as sources of information for the politicians. A parliament could act as the platform to foster this process. It allows direct and repeated interaction between the state and its constituents, and by granting provincial elites access to the center, enables the center to incorporate provincial and local inputs into its decisions (Mokyr, 2009). Furthermore, constitutionalism could serve as a means to facilitate cooperation among the powerful (Greif, 2008).

Nonetheless, the effectiveness of representative institutions may decline as the size of the polity in question increases, since smaller groups are likely to be better than larger ones in organizing themselves to solve collective action problems (Olson, 1965). David Stasavage (2009) shows that this was the case in medieval and early modern Europe due to the high communication and travel costs in the pre-modern age. Representative institutions have never taken root in China, and geographical size may explain why this is so.

Another institutional change which could lower agency costs is decentralization. This was the path that China took after 1850, when the Taiping Rebellion swept the southern half of the empire and forced the Qing court to devolve decision making power to the provincial governors and governors-general. Fiscally, devolution meant that the provincial government replaced the imperial court as the residual claimant of the tax revenue collected within the

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74 As shown in the model, there are mutual benefits to be exploited if the ruler, his agents, and the local elite could coordinate their actions. For one, the catastrophe of dynastic collapse could be avoided.
75 To be sure, in Stasavage’s analysis, the main role of the parliament is to serve as a check on monarchic or executive power, not as a vehicle for the central government to lower agency costs.
province. In return, the central government in Beijing would receive a fixed amount of silver annually from each province to finance its expenditure in the capital region. In terms of the model, the “ruler” becomes the provincial governor, the size of the polity shrinks, the degree of the principal-agent problem is lessened, and (provincial) state finances improves.

Indeed, decentralization allowed the Qing state to mount a more effective response to the social and military crises of the mid-19th century. Following the suppression of the Taiping Rebellion by provincial militias, a successful campaign led by provincial governors and governors-general of the affected provinces was launched to reduce the effective tax burden of the peasants without decreasing the income of the state (Xia, 1935; Rowe, 1983). Research by Stephen Halsey (2007) also shows that as provincial leaders took over from the central government in initiating major reform efforts, the Qing state’s extractive capacity expanded significantly after 1850. Without this, the Qing dynasty would not have survived into the 20th century.

Yet decentralization also created coordination problems in the provision of public goods at the national level. When the Sino-Japanese war broke out in 1894, it was observed that only Manchuria and the province of Zhili were mobilized. In 1911, the imperial court’s announcement of a new railway nationalization initiative intensified the political tension between central and provincial authorities so that when a revolt took place in Central China that year, most provinces took the opportunity to declare their independence of the Qing regime. Put simply, it was not just revolution, but also decentralization, that brought down the Qing dynasty.

From then on, China oscillated between defragmentation (in the 1910s and 1920s) and unification (1925-1940), centralization (1945-1979) and decentralization (1979-) in its search for the right balance between having the center maintain vertical control, and allowing some degree of local state building without the local state becoming too oppressive. The details of the causes and legacies of these historical developments are beyond the scope of this paper. However, the role that size plays in shaping China’s institutions and hence the path of its recent history should be self-evident.

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76 The inaction of other provincial leaders during the war was criticized by contemporaries such as the philosopher and reformist Liang Qichao.


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