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Creative Destruction meets the Entrepreneurial State — China Through Schumpeterian Lenses

Leonardo Burlamaqui[1]

Abstract

This paper reconstructs Joseph Schumpeter's fragmented reflections on the state into a framework of the Entrepreneurial State, linked to his conception of socialism as a system where competition and corporations are preserved but subordinated to public interest. Beyond creative destruction, Schumpeter envisioned a political economy in which public authority acts as entrepreneur, venture capitalist, and manager of structural change. Socialism thus appears as managed creative destruction—innovation and rivalry not suppressed but redirected and disciplined by the state toward long-term developmental goals.

China's trajectory since the late 1980s closely approximates this model. State-led growth has combined public funding for innovation, industrial policy, and systematic management of creative destruction. From Zhu Rongji's banking and SOE restructuring to the disciplining of Ant Group and Evergrande, and from Huawei and Tencent's rise to BYD and CATL's leadership in green industries, the party-state has repeatedly fused finance, innovation, and competition to foster technological upgrading while containing financial fragility.

The analysis also addresses the political dimension. Drawing on Schumpeter's "second theory" of democracy (via Medearis, 2001), it argues that China embodies performance-based legitimacy, where innovation and transformation underpin goals like common prosperity and the development of "new quality productive forces." In this light, China represents a living case of Socialism with Schumpeterian Characteristics.

Keywords: Schumpeter; China; Entrepreneurial State; Managed Creative Destruction; Socialization of Investment, Socialism; Industrial Policy Transformative Democracy.

JEL Codes: B31; O25; O30; P20; P21; H11; E61; O53.

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1. Introduction

Joseph Schumpeter remains one of the most penetrating analysts of capitalist dynamics, yet his treatment of the state has long been considered marginal or even absent. This neglect has obscured what I suggest is a "hidden, or dispersed, agenda" in his work: scattered but powerful insights that allow us to reconstruct the contours of an Entrepreneurial State[2]. These insights, once systematized, reveal a conception of the state not merely as regulator or corrector of "market failures," but as market-maker, macro-strategist, venture capitalist in chief, and creative-destruction manager.

In this sense, Schumpeter provides more than a theory of innovation-driven capitalism; he also provides the building blocks of a political economy of socialism, understood in his own terms[3]. For Schumpeter, socialism did not mean the abolition of private property but a much more nuanced institutional architecture: an institutional pattern in which the decisive economic affairs of society belong to the public, rather than the private, sphere (Schumpeter, 1942,167) From this perspective, state entrepreneurship and the managed coordination of innovation could, under certain conditions, surpass capitalism itself in efficiency and growth[4].

This reinterpretation acquires renewed relevance in light of China's trajectory[5]. The Chinese party-state has become the most advanced experiment in *Schumpeterian*

[2] Schumpeter was among the first economists to cast the State in "entrepreneurial" terms (Schumpeter, 1918); an idea he left largely undeveloped until discussing Socialism, in Capitalism, Socialism and Democracy, as I will show. The contemporary revival of the "Entrepreneurial State" owes much to Mariana Mazzucato's pioneering work. Since the publication of her now-classic 2013 book, followed by a series of volumes that expanded and refined the theme, she has firmly established the state as a central actor in innovation and structural transformation. While her analysis does not rely on Schumpeter, and China is not her principal case, her arguments and policy prescriptions resonate strongly with my own framework.

[3] See Burlamaqui, Ch. 10 in Burlamaqui, L. and Kattel, R. (eds.), 2019, for an earlier and less developed attempt to explore China's Entrepreneurial State. The volume as a whole assembles a collection of essays advancing a "Schumpeterian Agenda" for the twenty-first century. Burlamaqui (2020) offers a slightly expanded incursion into the theme.

[4] Contrary to Marx, Schumpeter did not equate socialism with the abolition of private property, resulting from a proletarian revolution. For him, socialism meant something else entirely: "A system, an institutional pattern, in which the control over the means of production and over production itself is vested with a central authority—or, as we may say, in which, as a matter of principle, the economic affairs of society belong to the public and not to the private sphere." (Schumpeter: 1942, 167). For Schumpeter, socialism was not the abolition of capitalism's dynamics but its reorganization. Creative destruction, far from vanishing, could be institutionalized and disciplined under socialism (The full argument is laid out in Schumpeter, 1942 Ch17).

[5] See Burlamaqui 2015, 2020, for earlier attempts to explore this connection, and Burlamaqui, 2025a, and 2025b for extensions of the synthesis attempted here.

socialism: simultaneously centralizing strategic control, disciplining private capital, steering innovation, and managing both sides of creative destruction[6].

In this light, Deng Xiaoping's creation of Special Economic Zones, Zhu Rongji's sweeping overhaul of the banking system and state-owned enterprises (Ma, 2006; Burlamaqui, 2025a), the "three red lines" imposed on real estate and the disciplining of big tech, along with the state-led mobilization of financial, industrial, and technological resources for the green transition and the forging of "new quality productive forces," are not isolated reforms but elements of a coherent strategy. Taken together, they reveal how the Chinese state consciously- or not- enacts Schumpeter's vision of socialism: the deliberate management of creative destruction to secure innovation, political stability, and long-term structural transformation.

A second dimension, largely absent from contemporary debates on democracy and from discussions of China, yet present in Schumpeter's own work, is democracy understood in transformative rather than electoral terms. Beyond his well-known "thin" definition of democracy as merely competitive elections, Schumpeter also intimated that political legitimacy depends on a regime's capacity to foster material progress through innovation and structural transformation. John Medearis brings this dimension into sharp relief in his 2001 study, identifying it as Schumpeter's "transformative" theory of democracy, in which legitimacy springs not from procedure alone, but from a system's ability to deliver actual economic and social improvements (Medearis, 2001, Ch. 2).

When combined with the Chinese leadership's commitment to "common prosperity," this broader understanding of democracy as a performance-based institutional arrangement complements the Entrepreneurial State framework, linking economic dynamism to social and political outcomes (Schumpeter, 1942, Ch.2; Bell, 2015)[7].

The paper proceeds in three steps. First, it reconstructs Schumpeter's scattered reflections on state action—across The Crisis of the Tax State, The Theory of Economic Development, Business Cycles, and Capitalism, Socialism and Democracy—to distill an analytical framework of an Entrepreneurial State, as well as his conception of Socialism. Second, it turns to China, where the party-state has acted simultaneously as financier, entrepreneur-in-chief, and manager of creative destruction. I argue that China constitutes both the closest real-world approximation to Schumpeter's vision of the entrepreneurial state and socialism, and a large-scale experiment in what John Medearis has called Schumpeter's "transformative" theory of democracy.

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[6] For an exploration of Schumpeter's analysis, in Capitalism, Socialism and Democracy, as a rupture with his earlier theoretical framework, and centered in the concept of creative destruction, instead of cycles, see Burlamaqui, 2023).

[7] Wolfgang Drechsler has offered a highly insightful essay tracing the Confucian roots of this line of thought (Drechsler, 2020); I am grateful to Rainer Kattel for drawing it to my attention.

Third, the paper concludes by suggesting that contemporary China provides a living case of Schumpeterian socialism in practice. More precisely, it advances the view that China's trajectory is best understood as a triad: a system where managed creative destruction, orchestrated by an entrepreneurial state, generates the institutional foundations of socialism with Schumpeterian characteristics. This framing captures both the continuity with Schumpeter's insights and the originality of China's political economy, in which innovation and rivalry are not abolished but disciplined, redirected, and mobilized to serve public goals.

The conclusion draws out the broader implications. Reintroducing the state into Schumpeter's paradigm of creative destruction does not dilute its analytical power; it strengthens and extends it. At the same time, it allows us to recast Schumpeter's conception of socialism—not as the abolition of competition or corporations, but as their reorientation under public authority.

The result is a richer theory of development, in which competition, innovation, public funding, state capacity, and transformative democracy are inseparable dimensions of long-term structural transformation.

2. Schumpeter, the State and Managed Creative Destruction

Schumpeter's early writings left little space for the state. In *The Theory of Economic Development* (1911; 1934), innovation is propelled by entrepreneurial activity and bank credit, while the state remains a fiscal appendage. Yet scattered, but coherent, remarks across his career suggest a deeper intuition: under certain circumstances, the state itself could perform entrepreneurial functions. These remarks, rarely systematized, provide the basis for reconstructing a Schumpeterian theory of the Entrepreneurial State.

The trajectory begins with *The Crisis of the Tax State* (1918). There, Schumpeter insists that fiscal policy has historically created and destroyed industries, even when unintentionally [8]. He distinguishes between "entrepreneurial" and "rentier" states, implicitly opening the possibility that public authority might foster innovation as much as private actors [9]. At the time, his conclusion still reflected an Austrian suspicion of intervention: taxation should not suffocate entrepreneurial profits. Yet the seeds of a broader conception of state leadership were already present.

His participation in the German Socialization Commission the following year pushed these seeds further. Although not a socialist, Schumpeter endorsed proposals for a public coal corporation designed to raise productivity and rationalize operations. This episode revealed how his thinking was evolving: entrepreneurial functions need not be embodied in heroic

[8] "Fiscal measures have created and destroyed industries, industrial regions, even where this was not their intent, and have in this manner contributed directly to the construction (and distortion) of the edifice of the modern economy" (1918 [1991]:101).
[9] "There is a great difference between …. *entrepreneurial and rentiers states*" (1918[1991], 111, my emphasis),

individuals alone but could also be performed by organizational forms, including the state itself, provided institutions supported efficiency and innovation. A socialization of investment—if guided by productivity, autonomy, and long-term horizons—could rival, and at times surpass, private entrepreneurship[10].

This was an important departure: it suggested that "entrepreneurship" was not reducible to individual genius but could be institutionalized, bureaucratized, and even socialized under the right conditions. Here lies the conceptual bridge between Schumpeter's early Austrian skepticism and his later, more expansive vision of state-led innovation.

Importantly, the contrast between entrepreneurial and rentier states resonates powerfully today[11]. In an era of financialized capitalism, Western governments often reinforce rentier logics by privileging financial markets, shareholder value, and asset-price inflation. By contrast, China's party-state has positioned itself as an entrepreneurial authority—mobilizing fiscal and financial resources to discipline speculation, direct investment, and accelerate technological upgrading.

The Schumpeterian question, then, is whether states act as rentier enablers or entrepreneurial organizers of creative destruction. The line Schumpeter first drew in 1918 thus anticipated the limits of financialized capitalism and underscored that capitalist outcomes remain malleable—shaped by whether public authority reinforces entrepreneurial dynamism or succumbs to rentier logics.

Placing the contrast in contemporary terms, we can see the rentier state as the hallmark of financialized capitalism—extracting value through asset inflation and debt pyramids—while the entrepreneurial state represents its antithesis: subordinating finance to innovation and long-term development. This dichotomy is central to the paper's comparative lens on China and the West.

The insights on the State reappear with greater clarity in the English edition of *The Theory of Economic Development* (1934), where Schumpeter contemplates *selective credit policies by central banks* to shield promising innovations during crises. For the first time, state intervention is seen not as distortion but as creative-destruction management: buffering the destructive side of crises while preserving the creative potential of innovation[12]. This anticipates later Keynesian concerns with stabilizing

[10] Medearis traces the origins of Schumpeter's "second theory" of democracy from his participation in that commission (Medearis, 2001. Ch.1)

[11] The Western logic of "financialized capitalism" is well captured in Krippner,2012; Lazonick and Shin,2019; Hudson, 2015; Nesvetailova, and Palan, 2020; Greenwell, 2025 and Cristophers, 2020 and 2024.

[12] "But [instead of a policy of indiscriminate credit restriction] a credit policy is also conceivable – on the part of the individual banks as such, *but still more on the part of the Central Banks*, with their influence upon the private banking world – which would differentiate between the phenomena of the normal process of the depression, which have an economic function, and the phenomena of the abnormal process, which destroy without function. It is true, such a policy would lead far into a special variety of economic planning which would infinitely increase the influence of political factors upon the fate of individual and groups ... *Theoretically, it is of interest*

investment, yet Schumpeter situates the issue in terms of innovation and structural transformation rather than aggregate demand management—though Keynes, too, ultimately ties it to the 'socialization of investment [13].'

The historical outlines in *Business Cycles* (1939) expand this reasoning. Schumpeter notes that modern industry in Germany, as well as in other countries, was often initiated by the state, not private entrepreneurs[14]. He praises the entrepreneurial leadership of the German state in the 1930s for providing direction, financing, and pressure to accelerate innovation and rationalization [15]. Though politically problematic in retrospect, Schumpeter's positive evaluation was based strictly on economic grounds: state-led investment and selective intervention could sustain full employment, accelerate technological change, and smooth the business cycle. For him, the lesson was clear: the destructive volatility of capitalism could be mitigated by state leadership without undermining innovation[16].

By the 1940s, Schumpeter's thinking had evolved into a more coherent position. In *Capitalism, Socialism and Democracy* (1942), he redefines socialism as an institutional order in which the "economic affairs of society belong to the public sphere." Crucially, this did not mean abolishing private property but rather socializing investment, while preserving competition: systematically coordinating innovation, timing entry and

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to establish that such a policy is not impossible and is not to be classed with chimeras or with measures which are by nature unsuited to attain their ends" (Schumpeter, 1934, p. 254, my emphasis).

[13] It is worth underscoring the striking parallel between Schumpeter's vision of socialism—especially his notion of a "socialization of investment"—and Keynes's call, in the closing chapter of The General Theory (1936, Ch. 24), for a reformed capitalism built on precisely that principle.

[14] "Was it not – again, in Germany – the state rather than the entrepreneur which initiated modern industry? *The answer is…. in the affirmative, and with the dosing appropriate to each case, similar answers would have to be returned for other countries*. The German principality in many cases… directly filled the entrepreneurial function, particularly in mining. Beyond that it conditioned enterprise by reshaping the institutional framework (legal reforms and so on) and improving the environment (canal and road building and the like), and by fostering it in various ways, some of which in fact come within what we usually under- stand by mercantilist policy (1939, Vol. 2: 235, my emphasis).

[15] Schumpeter's most comprehensive endorsement for the entrepreneurial state, in the book, comes from his analysis of the "State-Directed Economy of Germany" between 1933 and 1938. There, he writes: "The outstanding feature is the rapid progress, practically without relapse, toward full employment of resources in general and labour in particular, in fact more than that: unmistakable symptoms of overemployment in our sense. ... In many industries, shortage of labour. (Schumpeter, 1939, vol. 2, p. 971). To which he adds a note specifically referring to the role of the State: "It gave leads. It exerted pressure. It helped in various ways in financing and promoting ... This active leadership was, of course, something very different from mere control or regulation, and also from mere conditioning" (ibid., p. 973, my emphasis).

[16] "Theoretically it is possible so to plan the sequence of innovations as to iron out cycles: but after strenuous periods of advance there will be recessions even in the corporate State: most of the symptoms of depressions, however, need not occur at all. ..." (1939. Vol. 2, p. 977).

exit, and reallocating resources from obsolete sectors to new ones[17]. Within this framework, the state emerges simultaneously as entrepreneur, coordinator, and manager of creative destruction[18].

This institutional vision resonates not only with Keynes's Chapter 24 proposals for the socialization of investment but also with later developmental state practices in East Asia. In this sense, Schumpeter anticipated both the postwar successes of Japan and Korea and the contemporary Chinese trajectory (Burlamaqui, 2020).

Taken together, these threads depict the state not as an impediment but as the central driver of structural transformation. Entrepreneurial leadership, the socialization of investment, and the deliberate management of creative destruction emerge as a coherent triad—one that foreshadows today's debates on the defining features of developmental states, strategically guided industrial and technological policy, and, most vividly, China's state-led structural trajectory[19].The unresolved question—and one that the rest of the paper addresses—is whether this Schumpeterian logic represents a viable socialist alternative, or whether it inevitably risks sliding back into rentier domination once financial accumulation reasserts itself.

3. China's State-Business Ecosystem through Schumpeterian Lenses

China's transformation since the late 1970s is by now a familiar story, but it remains analytically underappreciated through a Schumpeterian lens. Within four decades the country has moved from poverty and isolation to the world's second-largest

[17] "There may also be a supervising and checking authority—a kind of *cour des comptes* that could conceivably even have the right to veto particular decisions. As regards the second point [competition. LB], *some freedom of action must be left, and almost any amount of freedom might be left, to the "men on the spot," say, the managers of the individual industries or plants*. For the moment, I will make the bold assumption that the rational amount of freedom is experimentally found and actually granted so that efficiency suffers neither from the unbridled ambitions of subordinates nor from the piling up on the desk of the minister of reports and unanswered questions" (1942,168, my emphasis).

[18] "...the planning of progress, in particular the systematic co-ordination and the orderly distribution in time of new ventures in all lines would be incomparably more effective in the prevention of bursts ... and of depressive reactions ... than any automatic or manipulative variations of the interest rate or the supply of credit can be... And the process of discarding the obsolete, that in capitalism – specially in competitive capitalism – means paralysis and losses that are in part functionless could be reduced to what discarding the obsolete actually conveys to the layman's mind within a comprehensive plan providing in advance for the shifting to other uses of the non-obsolete complements of the obsolete plants or pieces of equipment." (1942, 200, my emphasis).

[19] "…the whole of our argument might be put in a nutshell by saying that *socialization* means a stride beyond big business on the way that has chalked out by it or, what amounts to the same thing, that socialist management may conceivable prove as superior to big-business capitalism has proved to be to the kind of competitive capitalism of which the English industry a hundred years ago was the prototype" (Schumpeter, 1942, 196).

economy [20], largest manufacturer and exporter, and a central player in global technological competition (Zhou, 2024; Zhou, Lazonick and Sun, 2016; Kroeber, 2020; Naughton, 2021, Westad and Chen, 2024). This trajectory did not follow the Anglo-American script of liberalization and market supremacy. It unfolded under the guidance of a state that has consistently acted as financier, entrepreneur-in-chief, and manager of creative destruction[21].

Equally important, China has not suppressed competition; it has redefined and redirected it. In Schumpeter's framework, mature capitalism operates not via pure shifts price competition among atomistic firms, but trough competition by means of innovation among large corporations. China has institutionalized this shift. The Party-state disciplines financial excess and monopolistic abuses, but it deliberately fosters rivalry among firms — state-owned, private, and hybrid — in strategic sectors (Lan, 2024). This is precisely the "managed rivalry" Schumpeter alluded to: competition is not extinguished but redirected into innovation races, while destructive liquidation is contained by public authority[22].

Huawei, Tencent, BYD, CATL, Lenovo, and Haier exemplify this hybrid model, where public finance and policy guidance enable firms to scale rapidly, yet competition among them remains intense. BYD's overtaking of Tesla in 2023 as the world's largest EV seller — with over 3 million units sold compared to Tesla's 1.8 million — is emblematic of this model (Wang, Jia, Liu, and Wang, 2022; Proença and Burlamaqui, 2023). By shielding innovation from speculative destruction while preserving rivalry in technology and markets, the Chinese state embodies Schumpeter's principle that competition is not to be extinguished but oriented towards productivity-enhancing innovations.

The Chinese party-state exemplifies Schumpeter's three dimensions of the Entrepreneurial State. *First,* in finance it has maintained a banking system dominated by large state-owned banks and development banks, able to channel credit strategically toward structural transformation (Burlamaqui, 2020, Naughton, 2021). The China Development Bank (CDB), with assets exceeding US$ 2.4 trillion by the

[20] Or, more properly, the first. China is roughly 20%-25% larger than the U.S economy when using PPP adjusted GDP figures.

[21] Even The Economist—a traditional bastion of economic liberalism—implicitly acknowledges Schumpeter's vision in its assessment of China's rise: "Firms around the world face ever more intense competition from their Chinese rivals. China is not the first country to industrialize, but none has ever made the leap so rapidly and on such a monumental scale. Little more than a decade ago Chinese boom towns churned out zips, socks and cigarette lighters. Today the country is at the global frontier of new technology in everything from mobile payments to driverless cars" (The Economist, September 24, 2017).

[22] But there are risks. This is precisely the substance of today's debate on "involution" within China's policy circles: how to rein in excessive competition that fuels deflation, while preserving the innovation-driven rivalry that has powered growth over the past decade—without, at the same time, unsettling investors, triggering price deflation on corporate balance sheets, or reintroducing financial fragility and heightened uncertainty.

mid-2010s, pioneered innovations such as local-government financing vehicles, making possible the largest urbanization drive in history(Cousin: 2011; Sanderson and Forsythe, 2013).Unlike the U.S. subprime bubble, these mechanisms were embedded in a public financial architecture that could absorb losses, recapitalize banks, and prevent systemic collapse (Lardy, and Subramanian, 2011; Tooze, 2018 Ch.5; Vague, 2019) .

This illustrates how socialized banking and investment, in Schumpeter's sense, can serve as the backbone of transformation rather than a drag upon it. Yet here lies a vulnerability: China's local-government debt overhang and the opacity of its shadow banking sector show that creative-destruction management does not eliminate fragility—it contains and manages it. While past episodes demonstrate that financial fragility has been impressively contained and even removed, this track record offers no guarantee that future challenges will be managed with equal success.

Already in the 1990s, under Premier Zhu Rongji, China had rehearsed this logic. Confronted with insolvent banks weighed down by non-performing loans and state-owned enterprises on the brink of collapse, Zhu launched a sweeping financial restructuring. Four Asset Management Companies—Huarong, Cinda, Great Wall, and Orient—were created to cleanse bank balance sheets. Between 1999 and 2003 they absorbed more than RMB 1.4 trillion in bad loans; banks were recapitalized with state support, and thousands of SOEs were merged or shut down (Ma, 2006; Vague, 2019; Burlamaqui, 2025a). Unlike Western crisis management, this process did not culminate in wholesale privatization. Instead, the state reasserted its command over the "commanding heights" of finance while carefully introducing market mechanisms under its supervision.

The guiding principle was clear: financial fragility could not be allowed to spread unchecked; it had to be contained, reorganized, and redeployed. In Minsky's terms, China avoided to let financial fragility escalate into financial instability and systemic crisis, engineering instead a "reverse Minsky trajectory" in which financial fragility was preemptively removed, and the banking system recapitalized and harnessed for further growth (Minsky, 1982; Rongji, 2018; Burlamaqui 2025a). This episode was an early demonstration of how the Entrepreneurial State could redesign the modes of interaction between public and private spheres, simultaneously stabilizing finance and restructuring industry — a practice that would recur in later decades.

China's financial plumbing has since been repeatedly redesigned to contain fragility and channel innovation. In the mid-2010s, shadow banking mushroomed through wealth management products (WMPs), trust vehicles, and peer-to-peer lending platforms that promised unrealistic yields and drew trillions of yuan in household savings. By 2016, the volume of outstanding WMPs had surpassed RMB 30 trillion—equivalent to nearly one-third of GDP—posing systemic risks (Elliott, Kroeber, and Qiao, 2015; Hsu, 2017). Regulators responded with a sweeping campaign: new asset-management rules introduced in 2018 forced banks and trusts to bring off-balance-sheet products back under regulatory oversight, while between 2016 and 2019 more

than 5,000 peer-to-peer platforms were shut down (Sheng, and Soon, 2015; Sheng, 2016).

This same logic of "controlled implosion" later guided the handling of the real-estate bubble. The "three red lines" policy, announced in 2020, imposed hard leverage caps on developers, leading to the managed unwinding of over-extended giants like Evergrande. Similarly, the abrupt suspension of Ant Financials' record-breaking IPO that same year signaled the state's determination to discipline fintech innovation, curbing monopolistic practices and excessive financialization while redirecting digital platforms toward strategic priorities (Ang, 2020; Linyu, 2022; Jin, 2024; Zhang, 2024).

From a Schumpeterian lens, this was the state assuming the role of "bankruptcy manager" in advance—pre-emptively containing speculative finance before it metastasized. Critics, however, might argue that such interventions generate regulatory uncertainty, potentially chilling innovation rather than channeling it. Thus far, this has not materialized, but the risk remains, and it underscores the need for regulators to exercise such powers with caution and precision.

These episodes reveal a pattern: rather than allowing speculative excess to metastasize or resolving crises through "Too big to mess with" guidelines, Chinese regulators have repeatedly intervened to re-engineer financial circuits, prune fragile structures, and align capital flows with long-term developmental goals.

Second, in industrial and technological policy, China has consistently exercised entrepreneurial leadership, acting as a "business ecosystem's enabler". Huawei's rise from a small supplier in 1987 to the world's leading telecoms equipment producer was propelled by state-backed finance: in 2004, the China Development Bank (CDB) extended a US$10 billion credit line to support Huawei's overseas expansion, followed by another US$30 billion facility in 2009. By 2022, Huawei was spending over US$20 billion annually on R&D—more than any U.S. tech firm except Alphabet (Tao, Cremer, & Chunbo, 2017; Dou, 2025).

Even after U.S. sanctions cut it off from advanced semiconductors and Google's Android ecosystem, Huawei survived through state-supported financing, accelerated investment in domestic chip design, and the creation of its HarmonyOS platform. In Schumpeterian terms, Huawei embodies the principle that crises can be harnessed as moments of "creative destruction" — where destructive shocks are buffered by state finance, allowing the firm to redirect its innovative capacity rather than collapse (Dou, 2025).

Tencent, for its part, grew from a messaging service into a sprawling conglomerate spanning payments, gaming, and artificial intelligence, with over 1.2 billion WeChat users by 2023. Its fintech arm became a cornerstone of China's cashless economy, while its AI and cloud capabilities increasingly fed into industrial upgrading. Yet Tencent's trajectory also reveals the dual role of the entrepreneurial state: while

nurturing its rise, the party-state later disciplined its market power and data dominance, imposing restrictions on gaming, fintech, and monopolistic practices (Chen, 2021). This illustrates a point not developed in Schumpeter's take on capitalism, but implicit in his conception of socialism: large corporations are both engines of innovation and potential threats to competition. China's entrepreneurial state has acted as a "creative-destruction manager" by disciplining Tencent's excesses[23].

A complementary illustration is Xiaomi, sometimes described as China's "Apple with Chinese characteristics." Founded in 2010, Xiaomi scaled with unprecedented speed, leveraging lean production, razor-thin margins, and iterative design to deliver affordable smartphones and an expanding Internet-of-Things (IoT) ecosystem. By 2020, Xiaomi had become the world's third-largest smartphone maker, supported indirectly by local governments and industrial policy in Shenzhen and the Pearl River Delta.

Like Tencent, however, Xiaomi's expansion also met the state's disciplining hand: regulatory authorities curtailed its fintech ambitions, steering it back toward manufacturing and hardware (Wanqiang, L., 2016; Jayadevan, 2021). Here we see another facer of managed creative destruction: the state encouraged Xiaomi's hardware dynamism while constraining financial diversification that could have turned speculative.

More recently, Beijing has actively supported Xiaomi's entry into the electric vehicle sector, folding it into the strategic push for "new quality productive forces". Xiaomi's trajectory demonstrates how entrepreneurial dynamism is encouraged but ultimately redirected into sectors aligned with long-term national priorities (He, 2024).

The contrast with U.S. big tech is striking. Firms like Apple, Amazon, Meta, and Google have similarly grown into systemic infrastructures, but in the United States their financialization strategies—stock buybacks, tax arbitrage, and monopolistic acquisitions—have been left largely unchecked. Antitrust enforcement has been sporadic and belated, while speculative expansion into financial services and digital monopolies has not met the kind of structural discipline seen in China (Lazonick and Shin, 2019; Khan, 2017).

Where Washington treats platform power as a political problem at best, Beijing treats it as a systemic risk to be managed and redirected. This difference is crucial: in China, the entrepreneurial state nurtures champions but retains the authority to reorient their trajectories in line with developmental priorities. In the U.S., by contrast, the state largely adapts to corporate agendas (Scott, 2017).

[23] A critic, however, might argue, and many did, that such interventions risk politicizing competition and blurring the line between developmental discipline and arbitrary control.

Viewed as a whole, these cases illuminate the distinctive Chinese approach to industrial and technological policy: the state not only nurtures national champions but also intervenes decisively to redirect their trajectories, ensuring that innovation is harnessed for systemic resilience and strategic upgrading rather than captured by speculative rents. In Schumpeterian terms, this is socialism with entrepreneurial characteristics—creative destruction not left to markets alone but actively managed to serve collective developmental goals.

Third, the Chinese state has performed the function of creative-destruction manager with particular clarity in the green transition. Here, creative destruction is not simply contained but actively deployed as a lever for structural transformation. The aim is not only to curb emissions but to reconfigure the technological and industrial foundations of the economy (Wang, Yuan, and Gong, 2025; Dong, Zhao, and Taghizadeh-Hesary, 2023). Through subsidies, procurement mandates, directed credit, and infrastructure investment, Beijing has mobilized resources on a scale unmatched elsewhere, accelerating the displacement of carbon-intensive incumbents and cushioning the social costs of transition (Mathews and Tan, 2011, International Energy Agency (IEA), 2021).

The results are striking. In 2022 alone, China installed more renewable power capacity than the rest of the world combined (IEA, 2023). It now accounts for over half of global solar and wind deployment, and its manufacturers dominate the supply chains for photovoltaic panels, wind turbines, and grid equipment. In transport, the state's support for new energy vehicles (NEVs) has fostered a competitive ecosystem in which firms like BYD and NIO scaled rapidly, while CATL emerged as the undisputed global leader in EV batteries, with more than 35 percent of world market share by 2023. The milestone came in 2023 when BYD overtook Tesla as the world's largest EV seller, delivering more than three million units against Tesla's 1.8 million (Bloomberg NEF, 2024).

Crucially, this was not the result of protectionism alone. Firms such as BYD, CATL, and Huawei's new EV division have been exposed to intense domestic and global competition, forcing continuous innovation. What differentiates the Chinese model is the "financial and regulatory umbrella" of the state: cheap credit, assured funding, and coordinated regulation provided the stability necessary for firms to scale while buffering the risks of technological experimentation.

This illustrates Schumpeter's vision of a socialized investment process channeling innovation into systemic transformation. Yet the limits are real: overcapacity in solar, wind, and EVs already strains both domestic balance sheets and international trade relations, suggesting that state-managed creative destruction can also overshoot, creating new vulnerabilities.

The green transition also illustrates the state's ability to discipline old industries while fostering new ones. Coal still supplies the bulk of China's energy, yet the government has capped capacity expansions and directed investment flows into

renewables and electrification. Local governments have been tasked with managing labor adjustments and regional restructuring, preventing social dislocation while reallocating capital and skills toward strategic sectors. Instead of leaving structural change to market volatility, the Party-state has acted as a conscious arbiter of which industries decline and which one's scale (Atkinson, 2024).

From a Schumpeterian perspective, the significance is clear: China's green transition represents the most ambitious experiment yet in state-managed creative destruction. Innovation is steered collectively rather than left to market forces, with public authority orchestrating the pace, scale, and direction of transformation. This is socialism not defined by public ownership alone, but by the collective governance of innovation and structural change—a vision Schumpeter anticipated but never witnessed in practice.

4. Politics and Governance through Schumpeterian Lenses

A further dimension is political. Schumpeter's thin definition of democracy—as a method of leadership selection—offers a lens to view China's political system. Leadership turnover and competition occur within the CCP through institutionalized mechanisms of promotion and evaluation, rather than through multiparty elections. While this diverges from liberal democracy, it parallels Schumpeter's minimalist view of democratic process, albeit in a restricted form. Here, the tension lies in balancing efficiency with pluralism: planning priorities may override dissent, raising questions about long-term accountability (Bell: 2015).

This tension is highlighted eloquently by Richard McGregor's influential study The Party (2010). While Bell's political meritocracy highlights important advantages of China's governance model, McGregor's stresses its limitations[24]. His 2010's book underscores the opacity and pervasive control of the Chinese Communist Party (CCP), complicating the narrative that leaders rise solely by virtue of competence and administrative capacity.

McGregor argues that what appears as meritocratic promotion is often intertwined with factional loyalty, patron–client ties, and political maneuvering within the Party. The CCP maintains embedded control over all major institutions, blurring the line between state, market, and Party authority. This institutional dominance ensures that

[24] Bell also acknowledge limitations to political meritocracy. The system remains opaque to citizens, who cannot verify whether promotions are based on competence rather than factional loyalty. Risks of corruption and patronage persist, as personal networks may distort evaluations. Recruitment remains narrow, confined largely to Party cadres, limiting pluralism and excluding alternative perspectives. By emphasizing discipline and alignment, meritocracy can suppress dissenting or unconventional leaders. Finally, without broader electoral participation, meritocracy alone risks a legitimacy deficit—hence Bell's proposal for a comprehensive expansion of China's hybrid model of 'democracy at the bottom, meritocracy at the top.'(Bell, 2015, conclusion).

the leadership selection process, while technocratic in form, remains ultimately subordinated to Party discipline and survival imperatives (McGregor Ch. 1-3).

Moreover, corruption and factional balancing can distort the performance-based evaluations that Bell and Dickson emphasize. Although cadres must demonstrate competence, advancement may also depend on cultivating patrons and aligning with dominant political coalitions. This reduces the transparency and pluralism of the system, leaving open the question of whether meritocracy alone explains the leadership ladder (McGregor Ch.3-4).

Yet, as John Medearis has persuasively argued, Schumpeter also advanced a "second theory" of democracy[25], one grounded in capitalism's ability to deliver material progress and improved standards of living through innovation[26].

This perspective highlights the link between politics, democracy and performance: regimes derive legitimacy not simply from elections, but from their capacity to foster innovation, raise productivity, and improve well-being. Seen through this lens, China's emphasis on "common prosperity" and, more recently, on "new quality productive forces," embodies Schumpeter's second theory of democracy.

Legitimacy is tied not to formal electoral competition but to performance: the continuous delivery of rising living standards, social stability, and technological progress. In this sense, democracy as Schumpeter conceived it — thin in procedure

[25] Medearis's 2001 book title Schumpeter's Two Theories of Democracy is somewhat misleading. Schumpeter never explicitly elaborated a "second theory." What he did, in scattered passages—most notably in Chapter V of CSD—was to sketch a compelling vision of capitalism as a system of mass production and distribution in which the gains of productivity, efficiency, and quality eventually reached broad layers of the population. This perspective can be interpreted as a form of "performance-based" democracy, grounded in material outcomes rather than political procedures.

[26] A clear illustration of Schumpeter's "developmental" or "performance-based" conception of democracy can be found in his famous remarks: "Queen Elizabeth owned silk stockings. The capitalist achievement does not typically consist in providing more silk stockings for queens but in bringing them within the reach of factory girls in return for steadily decreasing amounts of effort" (1942, p. 66). He reinforces the point with another striking comparison: "There are no doubt some things available to the modern workman that Louis XIV himself would have been delighted to have yet was unable to have—modern dentistry for instance" (ibid., p. 67). These passages exemplify what John Medearis later identified as Schumpeter's second, "transformative" theory of democracy, in which legitimacy derives from capitalism's capacity to generate broad material improvements rather than from electoral procedure alone (Medearis, 2001, Ch. 2). It is important to clarify, however, that Medearis's account of Schumpeter's "transformative" democracy emphasizes the reshaping of institutions and social structures (2001, p. 209) more than their material basis. My own reading restores that material dimension: the structural transformation of the economy driven by competition through innovation. This, I argue, is fully consistent with Schumpeter's own writings, as the passages above make clear.

but thick in outcomes — is not absent from the Chinese experiment; it is reinterpreted through performance and social results (Bell, 2015, Dickson, 2016 and 2021).

Concrete evidence reinforces this claim. Over the past four decades, more than 800 million people have been lifted out of poverty, life expectancy has risen by more than a decade, and China has built the world's most extensive, and affordable, high-speed rail grid and an inclusive digital payment infrastructure. These achievements illustrate how innovation and structural transformation can underpin legitimacy without relying solely on electoral competition (Wang, Jia, Liu, and Wang, 2022).

At the same time, the political corollary of state-led creative destruction becomes visible: just as the entrepreneurial state channels and disciplines innovation, it must also translate those gains into broadly shared improvements. Performance legitimacy, in this sense, is the political counterpart to managed creative destruction. It is not enough to discipline Evergrande or steer Huawei's crisis response — legitimacy depends on ensuring that such restructuring delivers tangible benefits to households, workers, and communities.

Yet this model is not without risks. Performance legitimacy alone is fragile: it rises with growth but can erode quickly if economic outcomes falter. The property downturn, slower GDP expansion, and mounting local-government debt all threaten to narrow the regime's margin for maintaining transformative legitimacy. Critics would add that by tying legitimacy so closely to performance, the system leaves itself more exposed to downturns than electoral democracies, where procedural legitimacy provides a buffer[27].

This fragility is mirrored by the Western experience from the opposite direction: financialized democracies have, until recently, preserved procedural legitimacy but undermined performance legitimacy, privileging asset owners through shareholder value, buybacks, and rentier extraction. The result has been democratic discontent, populism, and declining trust in institutions (Philippon, 2019. Todd, 2024).

In this sense, the contrast is instructive: China has maximized performance legitimacy but lacks procedural guarantees, while the West has procedural democracy but often fails to deliver transformative outcomes.

From a Schumpeterian perspective, the Chinese case illustrates a structural duality. Bureaucratic organization rationalizes authority and institutionalizes competition by means of innovation, yet the same system constrains electoral political competition

[27] Stepen Roach and Ray Dalio are among the most preeminent skeptics here (See several Substack's by Roach and YouTube talks by Dalio). Furthermore, there is a huge, and angry, debate about those features of China's politico-institutional model. Here is not the place for extending it. The interested reader should look into Mc Gregor (2010), Bell (2015), Dickson (2016, 2021), Economy (2018 and 2022), Ang, (2020), and, for the West, performance-based Achen, C.H.; Bartels, L.M. (2016).

and entrenches decision-making within a Leninist party-state. The political dimension therefore mirrors the economic: genuine bureaucratic dynamism coexists with the imperative of Party control and regime preservation. In this light, Bell's defense of political meritocracy and McGregor's critique of Party dominance represent two complementary readings, *and tensions*, of the same hybrid order.

Seen in this light, transformative democracy completes the Schumpeterian triad: if the entrepreneurial state provides finance and direction, and if creative destruction is managed to preserve innovation, then results-based democracy supplies the political legitimacy that sustains the system. China's experiment thus suggests that Schumpeterian socialism has to be understood not only an economic architecture, but also a political one, in which legitimacy rests on the continuous delivery of innovation-driven improvements in social welfare (Wang, Jia, Liu, and Wang, 2022, Lan and Topp, 2024).

5. Global Projection

China's Entrepreneurial State has extended its reach to the global stage. The Belt and Road Initiative (BRI) originally launched as "One Belt, One Road," is no longer just an infrastructure and trade scheme. With over US$ 1 trillion in committed financing and projects spanning more than 140 countries, it functions as the external face of China's Schumpeterian socialism, combining public finance, industrial capacity, and strategic coordination on a transcontinental scale (Miller, 2017, CSIS 2024).

The global dimension of the BRI is not confined to bricks-and-mortar infrastructure. It has also become a platform for exporting technology and financial standards: Huawei's 5G networks, the BeiDou satellite navigation system, and cross-border digital payment systems linked to the digital yuan are emblematic. Increasingly, BRI projects also align with the green transition: Chinese firms are building solar parks in Pakistan, hydropower plants in Africa, and high-speed rail electrification across Southeast Asia (Hillman, 2021; Fang, Nolan, and Linggui, 2019).

In this way, China projects outward the same combination of socialized investment, mission-oriented industrial policy, and creative destruction management that defines its domestic model. The BRI is thus both developmental and geopolitical: it embodies Schumpeterian socialism not only within China's borders but as the organizing principle of an emerging Eurasian order (Maçães,2018, Duarte, Leandro, & Martínez Galán, 2023, and Diesen, 2024).

Framed through Schumpeterian lenses, the BRI is an internationalization of the entrepreneurial state — a deliberate projection of state-coordinated investment and managed creative destruction beyond national borders. But a devil's advocate would caution that many BRI projects have struggled with debt sustainability, governance problems, and local resistance, raising the key question of whether China's *Schumpeterian Socialism's* model scales well outside the domestic institutional framework.

Considered jointly, these features make China a living laboratory of Schumpeterian socialism. The state acts as the ultimate entrepreneur, directing finance, orchestrating innovation, and enabling business ecosystems. It tempers the limits of financialized capitalism, where rentier logics dominate, by ensuring that finance remains subordinated to development. It embodies the socialization of investment through its banking system and industrial policies. It operationalizes creative-destruction management not as an abstract theory but as day-to-day governance of property bubbles, digital platforms, and energy transitions.

6. Conclusion

What emerges from this exploration is not a simple juxtaposition of Schumpeter and China, but a profound resonance. Schumpeter's scattered insights—the entrepreneurial state, the socialization of investment, the malleability of competition, the management of creative destruction—cohere into a framework that China has, in its own context, made concrete.

China's trajectory is a rupture, but evolutionary rather than destructive: not the collapse of capitalism, but the realization of its most advanced possibilities. The party-state has shown that it is possible to fuse public finance with entrepreneurial initiative, to stimulate competition rather than suppress it, and to channel the destructive energies of innovation into constructive transformation.

Equally significant is a political dimension, almost never acknowledged in Western appraisals of China. Schumpeter's "second theory" of democracy, as emphasized by Medearis, located legitimacy in the ability to deliver rising welfare through the broad diffusion of innovation. From this angle, democracy is not absent from the Chinese experiment but reframed as performance legitimacy: the continuous provision of improvements in living standards and social stability. The pursuit of "common prosperity" and "new quality productive forces" can be read as the political counterpart to managed creative destruction, suggesting a model in which legitimacy rests less on procedure than on outcomes — an experiment still unfolding and awaiting further confirmation.

This perspective also sharpens the contrast with Western democracies. In the U.S. and Europe, procedural legitimacy, until recently [28], has endured, but financialized capitalism has hollowed out transformative outcomes, privileging rentier extraction over innovation and fueling disillusion with institutions. China, by contrast, maximizes transformative legitimacy but lacks procedural guarantees, leaving its political model vulnerable to economic downturns.

Taken together, these contrasts suggest that Schumpeterian socialism is not simply an economic arrangement but a new political economy: its sustainability hinges on

[28] Mann, and Ornstein., 2016 and Mair, 2023 provide good discussions of the "democratic discontent in the West.

aligning financial discipline, innovative competition, and performance-based legitimacy. Schumpeter once suggested that capitalism's greatest strength—its innovative dynamism—might also carry, along with "rationalization," the seed of its transformation. China demonstrates that this transformation need not be collapse or stagnation but can be the deliberate construction of a new political economy: socialism with corporations, competition, and entrepreneurial dynamism intact, yet subordinated to the public interest.

In sum, what Schumpeter glimpsed, China has operationalized. It represents not the end of his theory but its culmination: a living case of Socialism with Schumpeterian Characteristics.

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