

## Development of China (PRC)



---

---

---

---

---

---

---

---

## If you want to learn about modern China ...

- *Farewell my Concubine* (霸王别姬)
- *To Live* (活着)
- *Blue Kite* (蓝风筝)
- *The Wild Swans: Three Daughters of China* by Jung Chang



---

---

---

---

---

---

---

---

## Pre-1949 period

- Traumatic experience with foreigners
  - Series of defeats and interventions
  - 1840-42 – Opium War
  - 1894-95 – Sino-Japan War
  - 1911 – Collapse of the Qing Dynasty
  - Mid-1850s through 1930s – imperial powers semi-colonized China through occupying “concessions”; no effective government in control
  - 1937-45 – Sino-Japan war

---

---

---

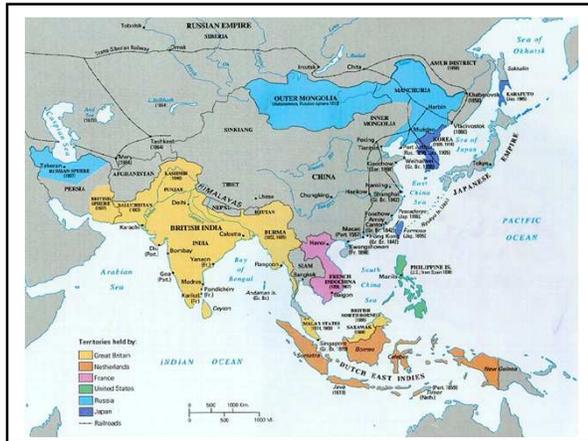
---

---

---

---

---




---

---

---

---

---

---

---

---

## Semicolonized China

Asia as of 1942



Tianjing (天津) in 1937




---

---

---

---

---

---

---

---

## 1949: Birth of PRC under Mao Ze Dong (毛沢東)

- People were
  - Starved
  - Tired of anarchy
  - Angry at those who accumulate wealth
  - Angry at foreigners
- CCP
  - Is much less corrupt than the Nationalists
  - Is better organized
  - Attracted more people with its communist platform

---

---

---

---

---

---

---

---

### Formation of the communist rule

- 1950-53 – land reform
  - Elimination of landowners and Japan- and nationalist-sympathizers (1-5 million killed)
  - Long-standing local tensions b/w peasants and landlords unleashed
  - 40% of China's cultivated land changed hands
- 1952 – CCP started Soviet-style economic policy
  - 1953-57: First Five-Year plan
  - Expropriated private enterprises
  - Organized farmers into cooperatives
  - Prohibited trade in farm products by private traders

---

---

---

---

---

---

---

---

### Economic/Social instability

- 1957-58 – “Hundred Flowers Movement”

百花齊放, 百家爭鳴 (*bài huā qí fàng, bǎi jiā zhēng míng*, “Let a hundred flowers bloom: let a hundred schools of thought contend.”)

  - Initially, it looked like political liberalization
  - In fact, it was not.
- 1958-61 – The Great Leap Forward Movement
  - Mao's mobilization efforts for rapid industrialization
  - Farmers organized into “communes”
  - People worked hard to meet unreasonable output targets
  - It only led to economic disaster and coincided with bad weather
  - 10-25 million died of famine due to great reduction in food production
  - Weakened Mao's political position in CCP

---

---

---

---

---

---

---

---

### Economic/Social instability

- 1962-65 – relative stable period
  - Unreasonable output targets abolished
  - Farmers allowed to cultivate for their own production
- 1966-76 – The Great Cultural Revolution (文化大革命)
  - Initiate by Mao who wanted to regain his political power
  - Mao mobilized students to attack the party's “capitalist road”
  - The “Red Guards” were destroying every aspect of the establishment or whatever is considered to be “anti-revolutionary,” i.e., “rightists”, “capitalists”, sympathizers of old tradition, elderly people, intellectuals, etc.
  - Most of the production facilities and the education system ceased to function
  - Millions sent to labor camps and “reeducation facilities”
  - Millions (20-30) killed

---

---

---

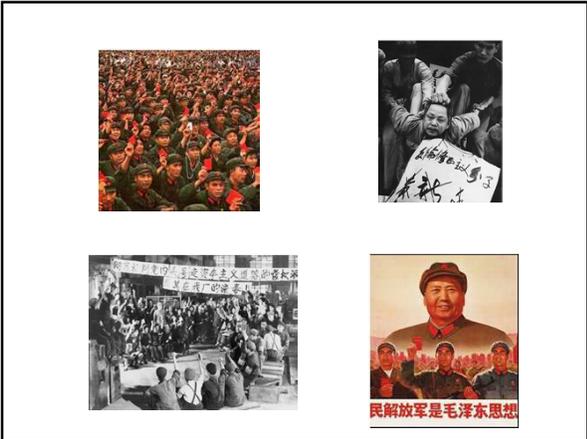
---

---

---

---

---




---

---

---

---

---

---

---

---

**General observations – pre-1978**

- Centrally planned system guided by five-year plans
- State ownership of land and industrial enterprises
- Products priced and distributed by state
- Close political and economic relationship with USSR and other communist countries. About 50% of trade was conducted with USSR.
- Ideological breakup with USSR in 1960 – increasing trade with US and Japan.

---

---

---

---

---

---

---

---

**After all, ...**

- The post-1949 period is full of a series of battles between Mao/his followers (leftist Maoists) and more pragmatists (e.g., Deng Xiao Ping)
- Broadly speaking, when pragmatists took control, the economy experienced higher growth
- But higher growth led to criticism as being too capitalistic and eventually to emergence of political campaigns
- Chow and Kwan (1996) estimate the size of the damage caused by the two biggest political campaigns in China, the Great Leap and the Cultural Revolution, and argue that the size of the Chinese economy as of 1992 could have been 2.7 times larger than it is if these two political campaigns had not occurred.

---

---

---

---

---

---

---

---

### All started in 1978

- Chinese government decided to liberalize its economic system in 1978
- But why in 1978?
  - 
  - 
  - 
  -
- Deng Xiao Ping (邓小平) remerged as the party leader

---

---

---

---

---

---

---

---

### Liberalization efforts since 1978

#### Key Elements of Reform

- Reorganization of production units, in both manufacturing and agriculture
  - More autonomy given to economic agents
  - Introduction of market incentives
- Emphasis on export-oriented policy
- Gradual/Incremental approach through experimentation
- **Dual-track approach in which a market track was established in parallel with the pre-existing planning tracks, with the former gradually increasing in importance over time**

---

---

---

---

---

---

---

---

### Liberalization Efforts

Started with the agri. sector Why?

- The **“Household Production Responsibility System”** was very successful

Then moved to the industrial sector

- **Liberalization in the State-Owned Enterprises (SOEs)**
- Started with six pilot enterprises in Sichuan (四川) Province that are allowed to retain part of the profits
- Gradually, the implementation of this rule were expanded to other parts of the country (80% of SOEs in 1981)

---

---

---

---

---

---

---

---

### Liberalization in the State-Owned Enterprises (SOEs; 国有企业)

- The reform was formalized as a national policy in 1984 and involved
  - Allowance of profit retention
  - Autonomy over decisions on production planning, sales of output, procurements, relationship with other firms
  - Introduction of market mechanism for the determination of the prices including those for intermediate goods and labor (i.e., wages based on productivity levels)
  - Experiments with new products and capital investment
  - Streamlining of administrative system and reducing the government's involvement in economic activities
  - Encouragement of foreign trade and foreign direct investment
- 1987 – The "Contract Responsibility System" was adopted
  - SOEs became an independent entity
  - SOEs' activities are now based on contracts
  - Output targets → fixed tax

---

---

---

---

---

---

---

---

---

---

### The Non-state sectors: TVEs

- The agricultural reform led to creation of excess labor force and agricultural surpluses, leading to a creation of commodity markets which became a precursor of the non-state sector economy
- Local government officials and politicians at the town or village levels helped community people to set up firms which later came to be known as town and village enterprises (TVEs: 乡镇企业)
  - Local governments assisted financing of the firms through credibility
  - Government officials provided skills and knowledge
  - Local governments expected an increase in tax revenues
  - Local governments were concerned about rising unemployment; The dismantling of communes and productivity improvement in the agricultural sector yielded excess labor force.
- The regulations governing the registration and supervision of non-state enterprises were progressively liberalized beginning in 1984 and resulted in rapid industrialization
- Emergence of the TVEs led rural inhabitants to leave agriculture over a relatively brief time-span

---

---

---

---

---

---

---

---

---

---

### Price reform and the banking system reform

- Under the central planning system, there were chronic problems with misallocation of resources
- Production didn't respond to market signals; there were always shortage of goods or over-accumulation of inventories
- In the 1984 reform, CCP decided to implement a gradual reform of the price system
  - the two-tier price system: The state enterprise could purchase the assigned amount of input and sell quota of outputs at the administered prices as before, but could purchase additional inputs and sell above-quota outputs at market prices. → essentially a tax and subsidy system
- Gradually, the administered prices were gradually adjusted to market prices, and these two kinds of prices merged into one by the 1990s

---

---

---

---

---

---

---

---

---

---

### Price reform and the banking system reform

- In 1983, the People's Bank of China became the central bank.
- Specialized banks (Industrial and Commercial Bank of China, Agricultural Bank of China, and People's Construction Bank of China) were created and given autonomy in providing credit
- In 1993, CCP decided to give more independence to the People's Bank of China and to transform specialized banks into commercial banks.
- However, Chinese banks were once ridden with a large volume of non-performing loans from the late 1990s to the early 2000s (max. 20% of total loans)
- China has agreed to open the financial sector to foreign institutions, but it is still weak and underdeveloped

---

---

---

---

---

---

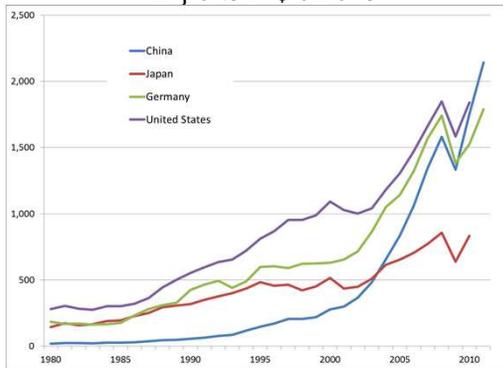
---

---

---

---

### Big Exporters: 1970 – 2011 Exports in \$ billions




---

---

---

---

---

---

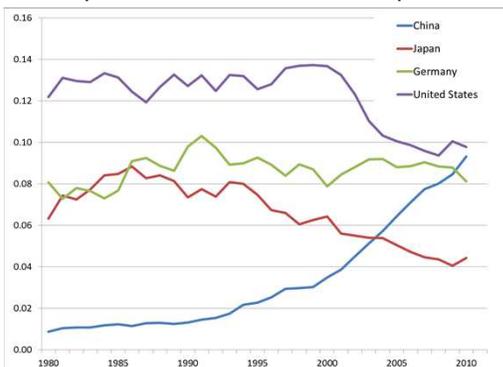
---

---

---

---

### Big Exporters: 1970 – 2011 Exports as shares of world exports




---

---

---

---

---

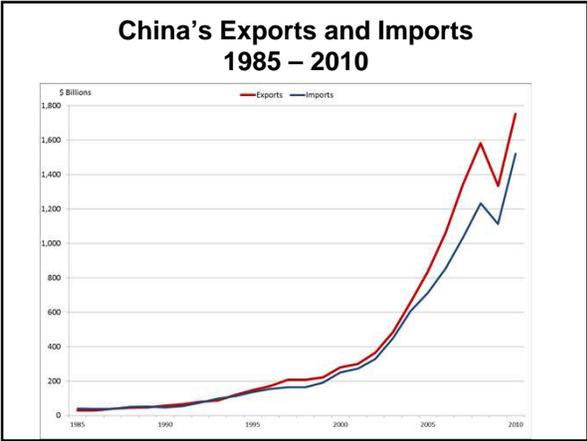
---

---

---

---

---




---

---

---

---

---

---

---

---

---

---

### Outward-Oriented Strategy (開放政策)

**In the pre-1979 period**

- CCP wanted to achieve self-sufficiency (like any other LDC such as India)
- Imports were under the control of the central government
- So were exports, i.e., strict license system
- And, so was Foreign exchange, i.e., strict license system existed and permission was given only to import essentials → The government monopolized FOREX
- Multiple exchange regime → cheaper exchange rate for exporters and strong rate for importers → de facto subsidy system

---

---

---

---

---

---

---

---

---

---

### Outward-Oriented Strategy (開放政策)

**Trade promotion policy inaugurated in 1979**

- Exports were decentralized: except for necessities (natural resources and cereal), the licensing authorities were first given to local governments and later abolished
- Trading companies were created and cooperated with manufacturing/industrial enterprises  
貿易公司, 商社
- Special treatment of exporting firms through favorable licensing of FOREX
- The multiple exchange rate system was formalized (exch rates weren't unified till 1994)

---

---

---

---

---

---

---

---

---

---

**Special Economic Zones (SEZs) : 经济特区**

- In 1980, four southern coastal cities – Shantou (汕头), Shenzhen (深圳), Xiamen (厦门), and Zuhai (珠海)– were designated as the **Special Economic Zones (SEZs)**, which were provided certain discretionary powers over taxation and autonomy over production
- In addition, SOEs operating in the SEZs were exempted from most elements of the central plan, such as labor regulations and the tax code
- Foreign investors were welcomed to set up factories independently or jointly with Chinese enterprises
- No import duties were levied on materials processed for exports

---

---

---

---

---

---

---

---



---

---

---

---

---

---

---

---

**Special Economic Zones (SEZs): 经济特区**

- With the phenomenal initial growth of the SEZs, the privileges they were granted spread quickly to other areas, including to Hainan which became the fifth SEZ in 1988.
- Purported to absorb excess labor
- Purported to absorb foreign capital and technology
- Modeled after successful SEZs in Taiwan
- Leaders were hoping trickle-down effects on inland

---

---

---

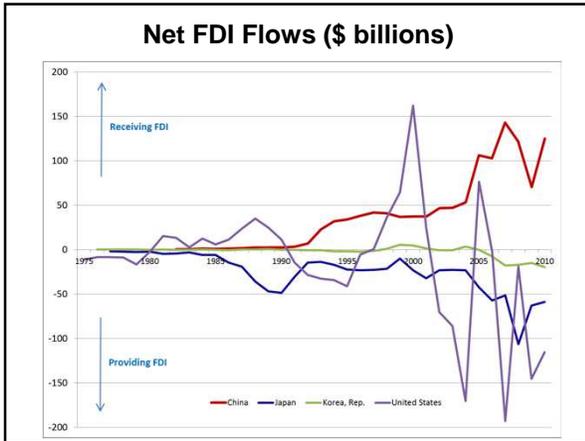
---

---

---

---

---




---

---

---

---

---

---

---

---

---

---

---

---

### Accession to the WTO in 2001

- By the mid-1990s, Chinese leaders were convinced that freer trade is beneficial to China
- Benefits accession to WTO could bring to China
  - 
  - 
  - 
  -
- Benefits accession to WTO could bring to foreign firms
  - 
  - 
  -

---

---

---

---

---

---

---

---

---

---

---

---

### Political economy reasons behind the accession to the WTO

- Chinese leaders start facing diminish returns in liberalization efforts as well as persistent opposition from the bureaucracy
- They wanted to use foreign pressure to enhance the transformation of the economy and the establishment of legal institutions
- Foreign firms, esp. those who don't or cannot enter the Chinese market, felt that Chinese underdeveloped market conditions bring out unfair competitions (lack of laws on labor conditions, environmental protection, intellectual property, etc.)
- Other developing/emerging market countries had ambivalent feelings toward China's accession to the WTO
  - They wanted China to follow the international rules in int'l trade
  - But they didn't want the presence of Chinese trade to be larger

---

---

---

---

---

---

---

---

---

---

---

---