

Zhuoyuan Zhang *Editor*

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Preface I

Over 60 years have passed from the founding of the People's Republic of China in 1949 to the present. And this period can be roughly divided into two stages. One is the stage of establishing of socialist system and exploring socialist construction from 1949 to 1978, namely the stage before reform and opening up. The other is the stage of building socialism with Chinese characteristics from 1979 to the present, namely the stage of reform and opening up. Because the establishment of a new socioeconomic system liberated productivity, national economy has seen rapid recovery and development. When the stage of the recovery of national economy ended in China in 1952, its gross domestic product amounted to 67.9 billion RMB. In 2010, its gross domestic product rose to 39.8 trillion RMB, showing an increase of 92.7 times, calculated at constant price, and an average annual growth rate of 8.1%. During this period, the average annual growth rate was 6.1% from 1952 to 1978 and 9.9% from 1979 to 2010. The proportion of Chinese economy to the total of the world's economy rose from less than 1% before the founding of the People's Republic of China to 1.8% in 1978 and then to 9.5% in 2010. The international status of Chinese economy rises conspicuously. China has already become the second largest economy on the globe. In 2010, China's per capita GDP exceeded US\$4,000, calculated at the exchange rate of RMB to US dollar in 2009. China has become an above-middle power. Now China is comprehensively building a well-off society. Its goals include completing building a well-off society of higher level that benefits more than a billion population by 2020 and completing building a wealthy, powerful, democratic, civilized and harmonious socialist modernized country at the centennial anniversary of the founding of the People's Republic of China.

The study on economics in The People's Republic of China has been carried out with one piece of important progress after another achieved on the basis of the above practice in economic and social construction. The study on economics in The People's Republic of China can also be divided into two major stages, namely the ones before and after the reform and opening up. Before the reform and opening up, China practiced the traditional socialist economic system and traditional theory of socialist economy dominated in the area of economics. However, some scholars proposed a number of novel and original views and challenged the theory of socialist economy. For example, they contributed far-reaching and insightful views and opinions on the

questions of the relationship between planning and market, the role of the law of value, the separation of ownership and management right, the principle of material interests, and the production price. This indicated that there were theoretical innovations in the circle of economics in China before the reform and opening up. After the reform and opening up, the Chinese circle of economics truly welcomed the spring of thriving academic schools and theoretical innovations. Guided by Marxism and by the ideological line of the Communist Party of China of liberating the thought and seeking truth from facts, Chinese economists connected theory with practice, exploring bravely and innovating courageously, achieved a series of research results that contained rich theoretical value and practical meaning, and gradually formed the system of theories of socialist economy with Chinese characteristics. The important ones among these theories include the theories on socialist market economy, the primary stage of socialism, opening up to the outside world, socialist basic economic system, combination of distribution according to performance and distribution according to other factors of production, Chinese-styled economic growth, transforming economic development mode, and progressive reform. One important characteristic of economic research in this period was to fully absorb useful research results in modern economics and, particularly, scientific summarization of the general regularities of market economy and the experiences of developed countries on regulating and managing the operation of market economy. Many applied economics mushroomed and developed.

A prosperous time helps to produce masterpieces. This book aims to systematically sort out the progress and research results in the study of economics in China during over 60 years of the People's Republic of China. It presents the miraculous achievements that attract the world's attention, made during the economic construction and takeoff after its foundation, and the flourishing picture of the study of economics in China in which many academic schools thrive. Despite our hard work, there will be some inaccuracies and incompleteness in this book caused by our limited abilities. So we will be work on improving it if it is possible.

This book is a collective treatise. The whole book, designed by Zhang Zhuoyuan, contains 33 chapters divided into a general discussion and 5 other parts. Each chapter is composed independently by an author according to a uniform structure and style. Zhang Zhuoyuan reviewed and finalized the draft of the entire book. The authors of the chapters are as follows:

Zhang Zhuoyuan: General Discussion and Chaps. 1–3, 7, 8, 11, 13–18, and 28.

Wan Jun: Chaps. 4, 5, and 10.

Zhang Wenmin: Chaps. 6 and 23.

Zhang Lin: Chap. 9.

Chang Xiuze: Chap. 12.

Cheng Jinzhui: Chap. 19.

Chen Xiaowei: Chap. 20.

Gao Peiyong, Yang Zhiyong: Chap. 21.

Zhang Lei: Chap. 22.

Zheng Bingwen, Gao Qingbo, Yu Huan: Chap. 24.

Li Xiaoxi, He Kui, Wu Ming: Chap. 25.
Mao Tianqi: Chap. 26.
Wang Hongmiao, Zhang Ping: Chap. 27.
Hu Jiayong: Chap. 29.
Wu Li: Chap. 30.
Huang Fanzhang: Chap. 31.

The contents in *Sixty Years of Chinese Economics (1949–2009)* (Zhang Zhuoyuan ed., Beijing: China Social Sciences Press, 2009), written by the authors to this book, are fully absorbed into the book in the process of its composition. Four chapters in it are modified on the basis of related chapters in that book. At present, there are not many books that describe by specific topics the research results made in over 60 years in China. The chapters here are mainly arranged in a chronicle order so that it meets the requirements better as a treatise of intellectual history. Some chapters in this book are particularly devoted to discussing in a temporal order the First National Symposium on the Theories of Economics in 1959, the Second National Symposium on the Theories of Economics in 1979, the establishment of the theory on commodity economy in 1984, the Bashan Tourist Ship Conference in 1985, the Moganshan Conference in 1985, the Mid- and Long-Term Reform Planning Meeting in 1987, and the establishment of the theory of socialist market economy in 1992. This is also a feature of this book. Some chapters in the book are also particularly devoted to discussing the composition of textbooks on Sinicized Marxist political economy and the important progress in the study of Chinese economic history after the beginning of the twenty-first century.

I would like to extend my heartfelt thanks to the advocacy, support, and encouragement from Zhao Jianying, president and chief editor of the China Social Sciences Press, and Lu Xiaosheng, professor of editorship, and also the vigorous support and help from many collaborators over a long period of time in the writing and publishing of this book. I would also like to thank my assistant Dr. Cheng Jinzhui for the large amount of work in organizing, contacting and proofreading that he did for me.

Several years of hard work finally fructifies. And there's much to savor when I look back. In addition, I would like to take the chance here to welcome all my readers to offer me their suggestions.

Beijing, China

Zhuoyuan Zhang

Preface II: Six Areas of Major Progress in the Study of Economics During Over Sixty Years of the People's Republic of China

62 years have passed since the founding of the People's Republic of China from 1949 to 2011. Under the leadership of the Communist Party of China (CPC), the Chinese people overthrew the dark rule of the "Three Big Mountains" of imperialism, feudalism, and bureaucratic capitalism, founded the People's Republic of China in which the people became the master of the country, and gradually moved onto the broad road to socialism. After over 60 years of development, China's national social and economic landscape experienced tremendous changes. It is now recognized as the country that has achieved the fastest economic development in the whole world and that has created the "China Miracle". In 2010, China became the second largest economy in the world. And calculated at the current exchange rate, China's per capita GDP amounted to over US\$5,000 in 2011. China is now speeding up and pushing forward industrialization and urbanization and comprehensively building a well-off society. It is expected that, in about 40 years' future or by the centennial anniversary of its foundation, the country will basically realize modernization and become one of the moderately developed countries in the world.

In this great historical transformation, economics also sees unprecedented development and prosperity in China. On the one hand, The People's Republic of China carried out large-scale economic construction and accumulated large amounts of experiences in this respect, which provided rich soil and nutrition for the research work of economists. On the other hand, the Communist Party of China practiced the policies of respecting knowledge and talents and of "letting a hundred flowers blossom and a hundred schools of thought contend." This provided the broadest arena for Chinese economists to exert their talents. Driven by practical needs and encouraged by good environment, economics exhibits a flourishing scene in China in which many schools blossom in competition and, at the same time, it also serves the great practice of the country in the construction of socialist modernization.

In the following, the author summarizes the six areas of major progress in economics in China and, mainly, in theoretical economics during over 60 years from the foundation of the PRC based on his own research and observation and of his personal participation in the discussion on the hotspot issues in economics in over 50 years.

I. Under the guidance of the basic principles in Marxist economics, China endeavored to explore its own road to the construction of socialism. It established the theory of the primary stage of socialism in the process of reform and opening up, started and shaped the sole correct road to socialism with Chinese characteristics

The success of revolution in China and the foundation of the PRC were both achieved under the guidance of the Mao Zedong Thought, in which the fundamental principles in Marxism were combined with the specific practice in Chinese revolution. Similarly, the issues on how to take the road of socialist development and how to carry out socialist economic construction, which the nation encountered after the foundation of the PRC, could be successfully resolved only through exploring in a good way the combination of the fundamental principles in Marxist economics with the practical situation of the construction efforts in China. Both the leaders of the state and the Communist Party of China and the extensive community of workers on the theory of economics and on practical economic tasks are clearly aware of the above point and persist in following it.

In the process of socialist construction in China, some explorations succeeded and some failed. The practice in socialist construction in over 60 years stands as the test standard to success or failure. After earnestly summarizing the experiences in success and the lessons from failure, the Chinese people finally find a road to build socialism with Chinese characteristics that conform to both objective principles and actual situation in China and develop the theory of socialism with Chinese characteristics which includes a system of economic theories.

First, there were failures in exploration. These included the People's Commune Movement, the initiative of being "large in size and collective in nature," which started in 1958, and the initiative of "equalitarianism and indiscriminate transfer of resources" that negated commodity production and exchange at equal values, the criticism on putting profit in command and distribution according to performance and the campaign of cutting the tail of capitalism from 1958 to 1960 and during the period of 1966 to 1976, and also the repeated replacement of the central role of economic construction with class struggle during the first three decades after the foundation of the PRC.

But there were more successes in exploration. In 1956, Mao Zedong published *On Ten Major Relationships* as an important result of his exploration in the road of China's socialist construction. In 1959, Mao Zedong proposed that the law of value was a "great school" after he summarized the lessons from the mistake of "equalitarianism and indiscriminate transfer of resources." In the 1950s, Chen Yun, Sun Yefang, Gu Zhun, Yu Guangyuan, and Zhuo Jiong achieved far-reaching and insightful understandings on commodity production, law of value, and regulatory role of the market under socialist system. In the 1960s, the Chinese circle of economics held heated discussion and made an exploration into rate and proportion, economic calculation and effects, profit rate on funds, and production price. After the start of the reform and opening up, Deng Xiaoping proposed the guiding policies of taking economic construction as central task and implementing reform and opening up

and also some great conceptions including that China's socialism was still in the primary stage, that a socialist country could also have market economy, that the criterion of productivity should be the "Three Favorables" criteria of whether it was favorable to developing the productivity of socialist society, to enhancing the comprehensive national strength of the socialist country, and to improving the living standard of the people, that development was of overriding importance, and that China should follow a "Three Steps" development strategy. The third-generation central leading group of the Communist Party of China proposed that the goal of China's economic reform was to build socialist market economic system, that development was the primary task of the Party in governing and rejuvenating the nation, that taking public ownership as the dominant ownership and achieving the joint development of multiple ownership economies was the socialist basic economic system in China, and that China should concentrate forces and resources to comprehensively building a well-off society in the first 20 years of the twenty-first century. The CPC Central Committee with Hu Jintao as general secretary proposed the scientific outlook of development of people-orientedness, comprehensive coordination and sustainability and building a socialist harmonious society in China. During this period, China's circle of economics carried out one after another heated discussion and argumentation on the questions of development stages of socialism, relationship between planning and market, socialist commodity economy and market economy, economic system and radical transformation of growth mode, inflation, three issues of agriculture, the countryside and farmers, and rural migrant workers, income distribution relation, necessity and importance of developing individual and private economies, foreign investment utilization and investment in foreign countries, specific roads to industrialization and urbanization, coordinated and sustained development of economy, macroscopic economic regulation and choice of macroscopic economic policy, and relationship between reform, development, and stability. They proposed a series of valuable opinions and suggestions and provided theoretical demonstration and intellectual support to the scientific decision-making of the Communist Party of China and the state. A series of innovation results on the Sinicization of Marxist economics were achieved through the successful explorations in the above, which contributed to the prosperity and development of economic sciences in China.

Then why did some explorations succeed while others failed? In the author's opinion, over 60 years of practice in socialist construction shows that the radical cause lies in whether an exploration starts with the national situation in China and meets the actual demand of China. And the most fundamental national situation in China after the founding of the People's Republic of China is that China's socialism is still in the primary stage, namely a stage of underdevelopment. Many failures in exploration in the past were resulted from the problem that people did not start with the fact that China was still in the primary stage of socialism and acted inconsistently with objective reality. In the end, they failed to achieve their goals because they wanted to expedite their mission. They hit hard against the wall of reality and had to turn back. However, all successes in exploration started with the fact that China was still in the primary stage of socialism and with the national situation in China. And

in such successes, people employed the basic laws in Marxist economics to resolve real problems with a down-to-earth attitude.

Here is one simplest example. From the foundation of the PRC to the end of 1976, China had the problem of rash advance regardless of current development stage in the area of ownership relations. There were repeated movements aiming at being “large in size and collective in nature” in the city and the countryside. Non-public ownership economies were seen as forces alien to socialism and rejected. Once these economies emerged, they were purged as remnants of capitalism. But in fact, China’s productivity development was far from reaching the stage of comprehensively realizing socialist public ownership system. Because Chinese economy was rather backward, many kinds of work in the city and the countryside were completed through manual labor. The multilevel nature of productivity development in China determined the diversity of ownership structure. Therefore, while developing public ownership economy, the Chinese economy also needed to allow the coexistence and development of the economies with various kinds of ownerships, including individual economy and private economy. Thus China could mobilize forces in various areas and get out of the conditions of poverty and backwardness as quickly as possible. Marx once said, “A social order never perishes before all the productive forces for which it is broadly sufficient have been developed, and new superior relations of production never replace older ones before the material conditions for their existence have matured within the womb of the old society. Mankind thus inevitably sets itself only such tasks as it can solve, since closer examination will always show that the task itself arises only when the material conditions for its solution are already present or at least in the process of formation.”¹ So after reform and opening up started in 1979, China first allowed and encouraged the development of non-public ownership economies, such as individual economy, private economy, and foreign-funded economy. At the Fifteenth National Congress of the Communist Party of China held in 1997, it was further determined that taking public ownership as the dominant one and achieving the joint development of multiple ownership economies would be the basic economic system for the primary stage of socialism. Non-public ownership economies such as individual economy and private economy were the organic components of socialist market economy. In this way, the obstructions to productivity, caused by the practices in disregard of proper development stage in ownership structure in certain period in the past, were gradually eliminated, which greatly liberated social productivity and powerfully promote the development of production and the improvement of the living standard of the people. By 2008, individual and private economies recruited 137 million people in employment. The reports published by the National Bureau of Statistics in China indicated that the percentage of the employed population who worked in urban non-public ownership organizations rose from 0.2% in 1978 to 75.7% in 2007. Since 1990s, individually- and private-operated enterprises in China showed a net average annual increase of 4.2 million new jobs, accounting for

¹Marx, Preface to A Contribution to the Critique of Political Economy (1857–58), p. 3 of 4. https://msuweb.montclair.edu/~furr/gned/marx_pref2contrib.pdf.

58.7% of the annually increased jobs in the city.² Non-public ownership enterprises, such as individually- and privately-operated enterprises as well as foreign-funded enterprises, have already become the main channel of job increase in China and has an important and irreplaceable role.

The theory on the primary stage of socialism was formed and won extensive common understanding. In this process, Deng Xiaoping played a crucial role. In April 1980, Deng Xiaoping said, “We should fully study the question of how to do socialist construction. Now we are summarizing the experiences in the thirty years of the foundation of our state. In summary, first, we should never depart from reality, go beyond proper stage and adopt some left-deviation measures. We will never succeed in building socialism in that way. In the past we suffered loss because of left-deviation. Second, no matter what you do, it must be favorable to developing productivity.”³ Guided by this thought, the Sixth Plenary Session of the Eleventh CPC Central Committee held in June 1981, proposed for the first time that “our socialist system is still in a primary stage.” In August 1987, Deng Xiaoping said again, “We need to expound what stage China’s socialism is in. Namely, it is in the primary stage and it is the primary stage of socialism. Socialism itself is the primary stage of communism. And China is in the primary stage of socialism, namely an underdeveloped stage. Everything needs to start with this reality and planning needs to be made on the basis of this reality.”⁴ In the famous South Tour Speech in 1992, Deng Xiaoping said, “Our socialism has just been built for several decades. It is still in the primary stage. There needs to be a very long historical stage for consolidating and developing socialist system. It needs the relentless efforts and struggle of several generations, a dozen of generations or even several dozens of generations. We should never treat the task lightly.”⁵

Chinese circle of economics made its own contribution in forming and disseminating the theory on the primary stage of socialism. In 1979, Su Shaozhi and Feng Lanrui published the first article that frankly admitted that China did not complete building socialism and that China “is still in a society of the socialism at an underdeveloped stage or a transitional stage of socialism.”⁶ Yu Guangyuan, a famous economist in China, wrote a treatise *On the Economy of the Primary Stage of Socialism*⁷ in the 1980s, which systematically discussed the theory on the primary stage of socialism and the economy in such a stage. In 1997, the expert demonstration committee organized by the Institute of Economics of the Chinese Academy of Social Sciences selected this book as one of the “Ten Works on Economics That Have Influenced the Economics Construction of The People’s Republic of China”. Yu Guangyuan recalled in 2008 that, “when I participated in the drafting of the *Resolution of the CPC Central Committee on Several Historical Issues of the Party from*

²See *Beijing Daily*, November 4, 2008.

³Deng (1994)

⁴Deng (1993b).

⁵Deng (1993d).

⁶Su and Feng (1979).

⁷Yu (1998).

the Foundation of the State in 1981, I advocated that the judgement that our country was still in the ‘primary stage of socialism’ be written into the document so that we could have deeper understanding of the wrong turns that we had taken. Some comrades disagreed to my view and there were arguments. However, the concept of the ‘primary stage of socialism’ was still written into the document in the end.”⁸

The establishment of the theory on the primary stage of socialism allow people to have an accurate understanding of the most basic national situation of China. And because of this, the Communist Party of China, starting from the basic principle in Marxism that people should first develop social productivity in socialism, eventually opened up a road of socialism with Chinese characteristics in reform and opening up. As a result, the Communist Party of China gives great vigor and vitality to socialism and Marxism on the land of China, brings more benefits to the people, and makes the Chinese nation catch up with the trend of the advancement of the time in big steps and welcome the brilliant prospects of its great rejuvenation. Therefore, it can be said that the theory on the primary stage of socialism is the most important and influential innovation result of the Sinicization of Marxism.

II. The relationship between planning and market was the No. 1 hotspot in the research and discussion of the circle of economics in China and its prominent result was the establishment of socialist market economy

The question of the relationship between planning and market under the socialist system is the question that has caused the most heated discussion and the largest controversy in the Chinese circle of economics and on which Chinese economists have published the largest number of articles and achieved the most prominent research results from the foundation of the PRC. It has been the first hotspot that the circle of economics has discussed for over 50 years after Xue Muqiao, an elder generation economist in China, published the article *Planned Economy and the Law of Value* on *People’s Daily* on October 28, 1956.

The following reasons can explain why it is known as the first hotspot:

- (1) After the foundation of the PRC, the first and second National Symposiums on the Theories of Economics were held, respectively, in 1959 and 1979. The theme of both meetings was the question of commodity production and the role of the law of value under socialist system. In essence, it was the question of the relationship between planning and market.
- (2) After the foundation of the PRC, different schools were formed among Chinese economists. These schools were first distinguished from each other according to their different views on commodity production and the law of value. For example, Sun Yefang belonged to the wide school of the law of value, Yu Guangyuan and Zhuo Jiong to the wide school of commodity production, Luo Gengmo to the narrow school of commodity and value, and so on.
- (3) After the beginning of the reform and opening up, Chinese economists have had the most and sharpest arguments on whether people support or oppose market

⁸Yu (2008).

orientation or marketization reform. It can be said that such debate has continued until the present.

- (4) The most prominent research result of the Chinese circle of economics since the founding of the People's Republic of China is the formation of the theory on socialist market economy. This theory is the main theoretical pillar of China's reform and opening up. It is also the main contribution of Chinese economists to the treasure house of Marxist economics.

The discussion of Chinese economists on the relationship between planning and market after the foundation of the PRC, including that on the question of commodity production and the law of value under socialist system, can be divided into the two major stages of before and after the reform and opening up.

The stage before the reform and opening up could be summarized as a period of exploration. It mainly lasted from 1956 to 1964. In this period, the Chinese circle of economics was very active. Many influential economists frequently challenged mainstream traditional theory of economics and proposed far-reaching and insightful views and positions. At the time, social environment often fell into the problem of taking class struggle as the guiding principle. Politics caused great disturbance and damage to academic research. Some economists were criticized and wronged out of no proper grounds. These seriously affected theoretical exploration and truthful views and insights were suppressed. Despite such a difficult situation, some economists still made the following contributions that could never be denied.

In 1956, Sun Yefang proposed the distinctive proposition that planning and statistical work should be established on the basis of the law of value.⁹

In 1957, Gu Zhun believed that it could be conceived that the law of value be allowed to spontaneously regulate the production and operation activities of enterprises in socialist economy. Namely, production could be regulated through the spontaneous rise and fall of price.¹⁰

In 1959, Yu Guangyuan believed that all products that became part of exchange were commodities, as long as the exchange needed to be made through comparing the socially necessary labor contained in the products and according to the principles of equal labor and equal labor exchange. The several kinds of exchange relations present in socialist economy were all commodity exchange relations.¹¹

In 1962, Zhuo Jiong, namely Yu Fengcun, proposed that commodity economy was determined by social division of work. As long as there was social division of work, there would be commodity economy. Commodity economy did not conflict with socialism. Rather, it could become a powerful instrument in building socialism.¹²

In 1963, Sun Yefang proposed that, of all kinds of economic laws and principles, the law of value was the primary one. The amount of profits was the most comprehensive indicator of the technological standard and the quality of operation and

⁹Sun (1956).

¹⁰Gu (1957).

¹¹Yu (1959).

¹²Yu (1962).

management of an enterprise. Average social profit rate on funds was the standard that each enterprise had to reach. Those that achieved profits higher than average social profit rate on funds are superior enterprises. Those that failed to reach the standard were inferior enterprises.¹³

It needs to be pointed out that leaders of the state and the Communist Party of China also proposed some views and policy ideas of positive meaning in this period. For example, Chen Yun proposed in 1956 that there needed to be market regulation in socialist economy as a supplementary factor.¹⁴ In 1959, Mao Zedong stated that the law of value “is a great school. Only through utilizing it can we teach our cadres in tens of millions and our people in hundreds of millions and can we build socialism and communism. Otherwise, nothing is possible.”¹⁵

But this good situation did not last long. In the period of 1966 to 1976, all explorations of the circle of economics on the relationship between planning and market in the past were said to be anti-Party, anti-socialist, and anti-Marxist big poisons and condemned unceasingly in speech and in writing. In addition, the left-deviated theories on economy developed. For example, when talking about socialist system at the beginning of 1975, Mao Zedong said, “All in all, China belongs to a socialist country. It was something like a capitalist country before liberation. Now we are still implementing eight-grade wage system, distribution according to performance, and exchange through money. These are not much different from the old society. The difference is that ownership system has been changed.” “Our country now implements commodity system. Wage system has inequality. There is the eight-grade wage system etc. This situation can only be limited under the dictatorship of the proletariat. So if Lin Biao and his men seized power, it would be easy for them to run capitalist system.”¹⁶ The book *Socialist Political Economics*, published in 1975 by the Shanghai People’s Publishing House, which was rather popular in the later stage of 1970s, formulated a series of views and policy positions more lopsided than traditional socialist economy theory. In summary, there was a great regression in the theories on economy.

After 1976, people started to take some actions and criticized the left-deviated theoretical system. Particularly, the circle of economics showed exceptionally active thinking, guided by the ideological line of the Communist Party of China that advocated liberating the thought and seeking truth from facts, after the reform and opening began in 1979. The study and discussion on the relationship between planning and market developed fervently and a large group of valuable research results emerged in this area. And the majority of the Chinese economists identified themselves with the establishment of the theory on socialist market economy.

¹³Sun (1998).

¹⁴Chen (1986).

¹⁵See Party Literature Research Office of the Central Committee of the Communist Party of China (2003).

¹⁶See *People’s Daily*, Feb. 22, 1975.

The establishment of the theory on socialist market economy was not completed at one go after the reform and opening up started. Rather, it was achieved gradually. Generally speaking, the first step was to advocate the introduction of market mechanism into economic activities. The second step was to establish the theory on socialist commodity economy. And the third step was to establish socialist market economy.

As the first step, people advocated introducing market mechanism into economic activities and respecting the role of the law of value at the beginning of the reform and opening up. The symbolic measures in these areas are as follows:

In December 1978, the Third Plenary Session of the Eleventh CPC Central Committee, which was of great historical meaning, started the new period of reform and opening up. The meeting negated the wrong theory and practice of “taking class struggle as the guiding principle” and made the historic decision of turning the center of the work of the state and the Communist Party of China to economic construction and implementing reform and opening up. It was pointed out in the communiqué of the meeting that “a serious weakness of the economic management system of our country at present is over-concentration of power. Such power should be boldly delegated to lower levels under good leadership so that local authorities and industrial and agricultural enterprises could have the right and power of operation and management with more freedom under the guidance of the centralized planning of the state.” “People should resolutely practice the principle of handling matters according to economic laws and respect the role of the law of value. They should pay more attention to combining ideological and political work with economic means and fully mobilize the production initiative of cadres and workers.” In order to vigorously restore and speed up developing agricultural production, the meeting suggested that the State Council made the decision that the state monopoly grain purchasing price be raised by 20% when summer grain crops started to be sold on the market in 1979. And the part of state-purchased grain that exceeded the quota in state monopoly purchase would be given another 50% price rise on the basis of the above. The purchasing prices of agricultural and sideline products, such as cotton, oil crops, sugar crops, livestock products, aquatic products, and forest products, would also be raised to certain extent correspondingly on the basis of specific situation.

From the end of 1970s to the beginning of 1980s, China implemented the measure of fixing farming output quota by household in the extensive regions of the countryside. Such measure respected the autonomy of the farmers in production and operation and also their role as independent commodity producer. State control was lifted on the prices of small commodities and part of agricultural and sideline products. The state also allowed the existence and development of individual economy. China utilized foreign investment and established special economic zones. The autonomy of enterprises in production and operation was also expanded, and so forth. These measures of reforming and opening up quickly made national economy active. The extensive community of cadres and the mass all personally experienced the miraculous action of market mechanism.

The circle of economics also acted quickly. Guided by the ideological line of the Communist Party of China that advocated liberating the thought and seeking

truth from facts, the Second National Symposium on the Theories of Economics was held in Wuxi, Jiangsu in April 1979. The theme is to discuss the role of the law of value under socialist system. Over 300 scholars took part in the symposium. The most prestigious economists Xue Muqiao and Sun Yefang attended this meeting and made speeches. The symposium received over 100 contributed papers and proposed many theoretical views with far-reaching influence, including that it was affirmed that socialist economy was commodity economy, that it was affirmed that market had a regulatory role in socialist economy,¹⁷ that the law of value played a regulatory role in socialist economy and competition was its inherent mechanism,¹⁸ and that enterprise was independent or relatively independent commodity producer and operator, and it was advocated that the autonomy of an enterprise be gradually expanded. In January 1980, Jiang Yiwei further proposed the famous enterprise standard theory.¹⁹ Reform needed to be made on the current irrational price system and management system to gradually narrow the “scissors difference” between the prices of industrial and agricultural products.²⁰

In summary, introducing market mechanism and competition mechanism in economic activities, expanding the regulatory role of market, and handling matters according to the law of value was the main tone of the Second National Symposium on the Theories of Economics in 1979.

As the second step, people established the theory of socialist commodity economy, which was regarded as the decisive move toward the theory of socialist market economy.

Early at the end of 1970s and at the beginning of 1980s, a group of scholars in China’s circle of economics wrote articles to advocate that socialist economy was also a kind of commodity economy and the law of value played a regulatory role in social economic activities. However, some economists took the opposite stand, and there was very intense argument. For example, in 1982, Yuan Mu and other four people who participated in the drafting the report of the Twelfth CPC National Congress wrote a letter to Hu Qiaomu who was in charge of the work about ideology in the party. The letter criticized the position that stressed the regulatory role of market and the belief that socialist economy was commodity economy, which took a dominant place in the circle of economic theories in China in the latest several years. It said, “Although there are commodity production and exchange in China, we could never summarize our economy as commodity economy. If we make such summarization, we are saying that the relation of common possession and joint labor among the people under socialism is the relationship of exchange of equivalents between commodities. We will affirm that what controls our economic activities is

¹⁷See Reference Room of the Institute of Economics of the Chinese Academy of Social Sciences et al. (1980).

¹⁸See Sun et al. (1979).

¹⁹See Jiang (1980).

²⁰See Reference Room of the Institute of Economics of the Chinese Academy of Social Sciences et al. (1979).

mainly the law of value rather than the basic economic principles and planned development principles of socialism. Thus we will definitely blur the boundary between socialist economy, which has planned development, and capitalist economy, which is in anarchy, and also the substantive difference between socialist economy and capitalist economy.”²¹ In August 1982, Hu Qiaomu approved and transmitted this letter. For about 1 year after that, many papers which criticized the idea that socialist economy was commodity economy emerged in the arena of theoretical discussion in China and the papers which advocated that socialist economy was also a kind of commodity economy were nowhere to be found. However, the voice of truth could never be suppressed. The practice in economic system reform totally broke the theoretical boxes made artificially in the above. After 1983, the theory of socialist commodity economy reappeared on the arena of theoretical discussion in China with stronger background in reality and more reasonable theoretical demonstration and attracted the attention of thousands. In October 1984, the Third Plenary Session of the Twelfth CPC Central Committee summarized the argument in the circles of economy and economic theories in China over many years. It affirmed in the form of a resolution of the party that China’s socialist economy was a planned commodity economy on the basis of public ownership. This brought the study and discussion of Chinese economists into a brand new stage.

As the third step, people established the theory of socialist market economy. After establishing the theory of socialist commodity economy, economists did not stop but continue their exploration. In the second half of 1980s, economists further proposed that China’s economic reform should be specifically defined as a market-oriented reform or a marketization reform. Its contents included that enterprise should become the main entity in market competition, that the goal of market reform should be to establish market price system and to establish and develop a market system that included both commodity market and factor market, that macroscopic economic management should transform from direct management to indirect management as main part, and that China should implement opening up to the outside world in an all-round way and participate in international market competition. In 1986, some articles believed that the main line in the target model of macroscopic economic management was that the state-controlled market, namely that the country mainly regulate supply and demand through economic means and market parameters and realize the “leading power” over the market, and market-led enterprise or that “the state regulates and controls market and market leads enterprise.”²² In 1987 and 1991, Wu Jinglian et al. specifically proposed, “Planned commodity economy system is in fact a market economic system with macroscopic management.” The goal of reform was to establish socialist market economic system. These scholars also made detailed discussion on the framework of this new system.²³

In the spring of 1992, Deng Xiaoping, the chief designer of China’s reform and opening up, further expounded his view on the question of the relationship between

²¹Peng et al. (2008).

²²Li (1986).

²³Wu Jinglian’s Research Group (1988), Wu and Liu (1991).

planning and market in his South Tour Speech. He said, “Whether there is more planning or market is not the essential distinction between socialism and capitalism. Planned economy is not equal to socialist economy. There is planning in capitalism. Market economy is not equal to capitalism. There is market in socialism. Planning and market are both economic means.” In September the same year, the report of the Fourteenth CPC National Congress determined that the objective model of China’s economic system reform was to establish a socialist market economic system so that market could play a fundamental role in resource allocation. This symbolized that the understanding of the theory of economic reform reached a brand new stage. After that, the theory of socialist market economy experienced increasing consolidation and development as the reform advanced and China’s experience in reform became richer and richer.

It needs to be pointed out that the establishment of the theory of socialist market economy was never an easy journey. After the political turmoil in 1989, some economists expressed their doubt or negation on market-oriented reform and advocated the turning from “market orientation” to “planning orientation.” The most extreme view was that “market economy means to abolish public ownership. It means to negate the leadership of the communist party, negate socialist system and engage in capitalism.” And “marketization” meant “liberalization” and “capitalist peaceful evolution.”²⁴ Because most economists adhered to “market-oriented” reform and also because Deng Xiaoping delivered several speeches in 1990 and 1991, in which he specifically pointed out that people should not consider that planned economy was socialism and market economy was capitalism and that both planning and market were economic means that could serve socialism, this theoretical debate soon quieted down.

As China’s economic reform deepened, the theory of socialist market economy also deepened. In 1993, the Third Plenary Session of the Fourteenth CPC Central Committee adopted the *Decision on Several Issues in Building Socialist Market Economic System* and determined the basic framework of the socialist market economic system. The Fifteenth CPC National Congress proposed the task of strategically adjusting the overall arrangement of national economy and required that people should run state-owned economy well in general. And it was specifically stated that non-public ownership economy, such as individual economy and private economy, were organic components of socialist market economy. The Sixteenth CPC National Congress proposed the task of building the state-owned property management system, in which central and local governments, respectively, performed the functions and duties of investor on behalf of the state and enjoyed the rights and interests of the owner so as to achieve the unification of right, obligation and responsibility and the combination of the management of property, personnel, and matters. The Third Plenary Session of the Sixteenth CPC Central Committee pointed out the task of improving socialist market economic system and proposed the ideas that shareholding system was the main form for realizing public ownership system and that modern property right system should be established in China. The Seventeenth

²⁴See Wu and Zhang (1999).

CPC National Congress proposed the tasks of speeding up building state-owned capital operation budget system, of improving the price formation mechanism for production factors and resources that reflected supply and demand relation on the market, resources scarcity and environmental damage costs, of building social insurance system with full coverage, and of deepening the reforms in government, fiscal matters and taxation, finance, and the countryside.

During the same period, economists made heated discussion on the issues in the theory of socialist market economy and published a large amount of papers and treatises so that the theory of socialist market economy gradually won public support. The Chinese circle of economics carried out in-depth research on the theories of modern enterprise system, corporate governance, foreign investment utilization, capital market, market price, public finance, financial innovation, social insurance, relationship between efficiency and fairness, market economy under the rule of law, combination between public ownership system and market economy, income distribution, the “Three issues of agriculture, the countryside and farmers,” and so on. Among them, some research results are foresighted.

Because of the theoretical innovation of the theory of socialist market economy and the powerful promotion of the Communist Party of China, China’s marketization reform deepened gradually. Important cases in this reform included the following: the reform of tax distribution system in 1994, the reforms of corporation system and shareholding system of state-owned enterprises since 1990s, the rapid development of individual and private economies after 1992, the reform of collective enterprises carried out in the end of the twentieth century, centering round clearly defining property right, the accession of China to the WTO in 2001, the reform of state-owned property management system since 2002, the transformation of the fiscal system into public finance and the requirement on gradually achieving the equalization of basic public service since 2003, the reform of the shareholder structure of listed companies, the successive entire-company listing on the stock market of China Construction Bank, Bank of China, Industrial and Commercial Bank of China, and Agricultural Bank of China, the reform of Renminbi exchange rate formation mechanism, and the reform of the tax systems for enterprise and personnel income taxes since 2005, the comprehensive reform in rural areas that started at the end of the twentieth century, and the construction of social insurance system with full coverage as its goal in the recent 2 years, and so on.

People should be clearly aware that China’s socialist market economic system is still rather incomplete until now, and there are many tasks that need to be completed in tackling and cracking difficulties in reform. The important ones of these tasks include at least the following: The separation of administration from state-owned enterprise and property management has not been achieved in a good way. The environment for the equal competition of various ownership economies has not been formed in a good way. State-owned property management system needs to be improved and completed. Reform has just started in monopolized industries in China. Administrative means have been used more often in macroscopic regulation. The relations in income distribution are far from being well-organized and rationalized. Social insurance system is rather weak. The preventive measures against systematic financial risks need to

be improved and completed urgently. The standard and quality of opening up to the outside world need to be improved. The legal system for market economy is far from being complete and so on. In the future, people need to strengthen reform and work hard to achieve building a complete socialist market economic system by 2020.

It can be expected that, as the efforts to tackle and crack difficulties in reform deepen and unfold and as socialist market economic system gradually become complete, the theory of socialist market economy will see constant enrichment and development. It will form a complete theoretical system, become one of the most important components in the theoretical system of socialism with Chinese characteristics, and contribute to the realization of the epochal development of the principles of Marxist economics.

The following several understandings can be obtained when people look back at the study and exploration of China's circle of economics on the relationship between planning and market and the reform of economic system since the foundation of the PRC:

First, the question of the relationship between planning and market is the kernel question in the theory of socialist economy. The radical defect in traditional theory of socialist economy lies in that advocating planning or market, either of which is in fact a means of economic regulation, is said to be the basic sign that draws the line between socialist and capitalist economic systems and that planning is taken as socialism while market as capitalism. Such understanding completely disagrees with the practices of economic development in various countries in the world. After the World War II, many developed capitalist countries also formulated various kinds of economic development plans to regulate the operation of macroscopic economy. Because of derogating and expelling the role of market, the countries that practiced traditional socialist planned economic system stifled the vitality and vigor of their economy so that they lost in the peaceful economic race. Reality makes more and more economists become aware that, only by resorting to the market, can a socialist country revive its economic activities completely fettered in mandatory plans. Only by bringing into play the fundamental role of the market in resources allocation can it improve its economic efficiency. Of course, market is not omnipotent. It is necessary to have a "visible hand," such as the macroscopic regulation of the government, to correct the defects of the market to ensure the healthy operation of the economy.

Second, the scientific nature of the socialist political economics relies to a large extent on whether people can scientifically expound the relationship between socialism and commodity economy and market economy so that socialism and market economy can adapt to and combine with each other. Thus, the construction of socialist economy with Chinese characteristics is to develop socialist market economy. Today, scientific and technological progress is picking up speed in the world and the trend of economic globalization is unstoppable. Only through rapidly developing socialist market economy can the Chinese people rejuvenate the nation and realize industrialization, urbanization, and modernization. China can effectively participate in international market competition, and the Chinese nation becomes a member of the world family of nations. Then people can prove the establishment and maturity of

the theory of socialist market economy with China's brilliant economic achievement and construct the great structure of socialist political economics.

Third, transition economics or transitional economics, as an important component of socialist political economics, takes discussing the transitional process from planning dominant economic system to socialist market economic system and its principles as its main content. China is a large country with 1.3 billion people. Up to the present, only the experiences and regularities of China's economic system transition have the most typical meaning. Revealing the regularities of China's economic system transition will add new chapters to modern economic science and in turn enrich and develop modern economic science.

Fourth, the theory of socialist market economy is a brand new theoretical system. This theory needs the practice in the development of socialist market economy to provide material and nutrition for it. It also needs economists to make arduous exploration and theoretical summarization. It needs these scholars to display their courage of upholding a theory and their spirit to surmount the peaks in science. The process of understanding the truth is complex and full of twists and turns. Sometimes, truth is in the hands of the few. There needs to be a process for the truth to be understood by the majority. To truly implement the "Two Principles" policy of letting a hundred flowers blossom and a hundred schools of thought contend in academic research in China is the heartfelt expectation of Chinese economists. And this is also the important guarantee to prevent the tragedies of killing the truth and suppressing the people who stood up for the truth from recurring.

III. Important breakthroughs are achieved in ownership system theory and distribution theory: Affirming public ownership system as the dominant part, joint development and equal competition of the economies of various ownership systems, and shareholding system as the main form to realize public ownership system and combining distribution according to performance and distribution according to production factors

Over 60 years since the foundation of the PRC, while exploring the worldly difficult question of the relationship between planning and market, the circle of economics in China carried out in-depth study and discussion on ownership system theory and distribution theory and achieved important breakthroughs and progress.

The study on ownership system theory can be divided into the following three points in discussion.

(I) About Ownership System Theory

1. The study on the issue of the socialist transformation of agriculture, handicraft industry and private capitalist industry and commerce in the 1950s.

From 1953 to 1956, China carried out large-scale socialist transformation on individual agriculture and handicraft industry and private capitalist industry and commerce, which were based on private ownership system of production means. The book *Socialist Transformation of the National Economy of China*, written jointly by Xue Muqiao, Su Xing, and Lin Zili and published by the People's Publishing House

in 1959, was a representative research result in this area. At the time, the circle of economics emphatically formulated that China's socialist transformation took the unique road of starting from the national situation in China, which mainly included guiding individual agriculture and handicraft to take the road of cooperative transformation and adopting the policy of peaceful redemption with private capitalist industry and commerce. In this way, great triumph was achieved within a short period of several years. After 1976, some economists and personages in other circles believed that there were some defects and mistakes in the socialist transformation in the 1950s. With respect to this situation, the *Resolution of the CPC Central Committee on Several Historical Issues of the Party since the Founding of the People's Republic of China*, adopted at the Sixteenth Plenary Session of the Eleventh CPC Central Committee held in June 1961, stated that "There are defects and deviations in this work. After the summer of 1955, the cooperative transformation of agriculture and the transformation of handicraft industry and individual commerce showed too rash requirements, too rough work, too fast change and too simplistic and monotonous form so that some problems were left unsolved over a long period of time. After the transformation of capitalist industry and commerce was basically completed in 1956, the use and handling of some of the former industrial and commercial workers was rather improper. But on the whole, it was indeed a great historic victory as such complex, difficult and profound social transformation was relatively smoothly completed in a large country with hundreds of millions of people, which promoted the development of agriculture and the entire national economy."

2. From the basic completion of socialist transformation in the 1950s to the time before the reform and opening up

From the basic completion of socialist transformation to the time before 1976, the mainstream view in the arena of economic discussion was still the doctrine of Stalin. Namely, it was believed that socialist public ownership was the only economic basis of a socialist society. Socialist public ownership included whole people ownership and collective ownership. Whole people ownership was the superior form while collective ownership was the inferior form. As social productivity developed, collective ownership should transform into whole people ownership and form all-round ownership of the whole people.

Some views of innovative value were proposed in this period.

(1). Sun Yefang proposed in 1961 that the right of ownership of production means could be separated from its rights of possession, use, and dominion. He believed that, under the ownership of the whole people, "the issue of operation and management right should take the place of ownership system and become the first of the three aspects in production relation studied in socialist political economics." "The central question in financial and economic management system is the right and obligation of enterprises as independent accounting unit and their relationship with the state,

namely the question of the operation and management right of enterprises.”²⁵ Su Shaozhi also held similar views.²⁶

(2). Luo Gengmo proposed in 1959 the distinctive view that there was “minor whole people ownership” in “major whole people ownership.” He believed that, “in socialist stage, the production means and products under the ownership of the whole people also contains the relation of local whole people ownership in certain scope and to certain extent. Namely there are relations of ‘minor whole people ownership’ in ‘major whole people ownership’.” “In the final analysis, such crossing relation between major and minor whole people ownerships was caused by the situation that the development standard of productivity was not high enough and the communist consciousness of the people was also not high enough. These two facts make it necessary for the state, which represents the whole people, to utilize proper material interests to promote its local economic organizations and the economic organizations of various departments as well as grassroots enterprises and institutions to work hard to manage production well. This is just like the fact that the state must properly utilize the principle of ‘distribution according to performance’ to drive the people to work hard.”²⁷

(3). In 1957, Luo Gengmo proposed the view that collective ownership was “public inside and private outside.” He said, “Although collective ownership economy was socialist economy, it was the public ownership of groups of people but not ownership of the whole people. I believe that it can even be said that such collective public ownership economy of groups of people is ‘public inside and private outside’. Namely, it is public ownership in the inside but it contains more ‘remnants of private ownership’ to the state than the enterprises and individuals in the whole people ownership economy to the state.”²⁸

3. 30 years after the start of the reform and opening up

After the reform and opening up started, there have been a series of important breakthroughs in the theory of ownership system in the circle of economics in China.

First, in the area of ownership structure, it was believed that, under the condition that China’s productivity development standard was still low and it was in the primary stage of socialism, people had to allow the existence and development of non-public ownership economies, such as individual economy and private economy. In 1997, the Fifteenth CPC National Congress further established the system that took public ownership as the dominant part and included the joint development of the economies of various ownership systems as the basic economic system of the current stage.

Early in 1979, China’s prestigious economist Xue Muqiao boldly made the important suggestion of developing various economic components and broadening the channels of employment in response to the actual situation that there were more than

²⁵Sun (1979).

²⁶See Su (1962).

²⁷Luo (1959).

²⁸Luo (1957).

20 million urban personnel waiting for employment nationwide at the time, which affected social stability. He specifically proposed that, “at present, there might be more benefit than harm to leave a bit of the tail of individual economy and capitalism.” “We could not eradicate capitalism for now. There is nothing to fear if there is a bit of it.”²⁹ He was the economist who advocated the development of various economic components the earliest after China started reform and opening up.

One conspicuous merit of China’s economic system reform is that, while people pushed forward reform in public ownership system, individual and private economies outside regular systems experienced rapid development. These sectors became new growth points in national economy and important channels for offering jobs to people. Thus China’s economy was quickly activated. By 2011, there were over nine million private enterprises in China and the number of privately or individually-owned businesses exceeded 36 million. The fixed assets investment of non-public ownership economy exceeded 50% of the national total. The non-public ownership economy accounted for over half of the GDP and contributed 60% of China’s export trade volume. It provided over 80% urban jobs and over 90% new jobs.³⁰

The practice in over 30 years of reform and opening up proved that permitting the development of non-public ownership economies, such as individual and private economies, affirming that non-public ownership economies, such as individual and private economies, were organic components of socialist market economy, and establishing socialist basic economic system greatly liberated social productivity and powerfully promoted the sustained and rapid development of Chinese economy. In 2007, the report of the Seventeenth CPC National Congress further proposed that people should adhere to and improve the basic economic system with public ownership system as the dominant part and joint development of the economies under various ownership systems. They should adhere to the equal protection of property rights and form a new situation in which the economies under various ownership systems could realize equal competition and mutual promotion. This pointed out the direction for further improving the structure of ownership system in the future.

Second, it was proposed that the form of realization of public ownership system could be diversified and it was believed that shareholding system was the effective form of realization for people to combine public ownership system, which included state ownership system, with market economy.

Early at the beginning of 1980s, some economists proposed that, as the reform advanced, public ownership system would not be limited to the two forms of whole people ownership and collective ownership. “At present, many forms emerged in socialist public ownership system.” “We should re-study the theory on socialist ownership system of production means on the basis of the changes in actual economic life rather than mechanically applying available theories on the complex situations in actual life.”³¹

²⁹See *Xue Muqiao’s Memoir*, Tianjin People’s Publishing House, 1996.

³⁰See *China Daily*, Dec. 3, 2011.

³¹He (1984).

Some economists also proposed the concept of the diversity of socialist ownership system. They pointed out that, in an underdeveloped socialist society, public ownership system was not “one size that fits all” or uniform in all cases. Rather, it was a complex structure with diversity. It was a system of possession relations in multiple levels and tiers, which took whole people ownership system as dominant one, consisted of collective ownership, joint ownership and other forms of public ownership system, and showed a scale of degrees of socialization from high to low. The complexity of such public ownership system matches the imbalance and multi-level of productivity. People should examine the combination, interlacing and mutual permeation of various possession relations in the movement of socialist commercial reproduction and then further analyze and reveal the very rich specific forms of socialist public ownership system.³²

From the middle of 1980s, China started to develop shareholding system economy in its socioeconomic life. This was a kind of mixed ownership economy. In this economy, large amounts of shareholding system economy controlled by public ownership components should be regarded as a form of public ownership. Economists did not have much controversy in this respect. At the end of 1980s and, particularly, in the 1990s, various kinds of shareholding cooperative system economies emerged in different places in China. It is generally believed that the economies under shareholding cooperative system possessed public ownership properties in different degrees. Among them, the shareholding cooperative system, which mainly contained the conjunction between capital and the labor of workers, was a new form of public ownership.

In 1987, the State Commission for Restructuring the Economic System entrusted the Chinese Academy of Social Sciences, the Party School of the CPC Central Committee, and the Peking University to study and propose the reports on mid-term reform planning (1988–1995). Almost all these reports made the suggestion on the transformation from the current contract system into shareholding system. It was pointed out that, because contract system did not radically change the congenital weaknesses in traditional property right system of state-owned enterprises, enterprise reform had to develop toward the direction of restructuring property right relations, namely of shareholding system.³³

The report of the Fifteenth CPC National Congress made important breakthrough in the search for the form of realization of public ownership system. The report proposed that the form of realization of public ownership system could and should be diversified. All operation modes and organization forms that reflected the principles of socialized production could be utilized with confidence. People should endeavor to search the form of realization of public ownership system that could greatly promote the development of productivity. Shareholding system was a capital organization form of modern enterprises that was favorable to the separation of the

³²Liu (1986).

³³See Department of Comprehensive Planning of the State Commission for Restructuring the Economic System (1988).

rights of ownership and operation and to improving the operation efficiency of enterprise and capital. Capitalism could make use of it; socialism could also make use of it. So people could not say in a general way that shareholding system belonged to public or private ownership. The key resided in which party had the controlling stake in hands. A company controlled by the state or the collective through shareholding possessed obvious public ownership nature. Such a situation was favorable to expand the scope of domination of public capital and strengthen the role of public ownership as the dominant part. This statement in the report of the Fifteenth CPC National Congress had important guiding meaning. After the conclusion of the Fifteenth CPC National Congress, some articles listed the new forms of realization of public ownership other than state-owned and collective ownerships since the reform and opening up: shareholding cooperative system, mass organization ownership, lease, entrusted operation, local mass organization ownership, company limited by share controlled by public ownership, and ownership systems of town, township, village, and villager's group.³⁴

In 2003, the *Decision of the Third Plenary Session of the Sixteenth CPC Central Committee* further proposed the assertion that shareholding system was the main form of realization of public ownership system. It was pointed out that people "should adapt to the trend of the constant development of economic marketization and further strengthen the vigor of public ownership economy. They should largely develop mixed ownership economy with the participation of state-owned capital, collective capital and non-public capital. They should realize the diversification of the main parties of investment and make shareholding system the main form of realization of public ownership system." Some economists believed that the diversification of the forms of realizations had been achieved in public ownership system and shareholding system became the main form of realization of public ownership system. This indicated that China found the correct approach to combine public ownership system with market economy and that the theory of socialist market economy had more complete and solid argumentation basis.

Finally, large- and medium-sized state-owned enterprises should take the road of corporation reform and shareholding system reform.

In the first 30 years after the foundation of the PRC, state-owned enterprises dominated nationwide except for the countryside after the socialist transformation was basically completed. Urban collective enterprises were in fact local state-owned enterprises. These state-owned enterprises were not market entities and corporate legal entities in the true sense that possessed independent economic interests. They were attachments to their superior competent administrative departments like beads on abacus. They produced and operated in accordance with the mandatory plans of the state and all or almost all their profits were submitted to superior authorities. The wages of their workers were subject to uniform provisions of their competent departments. These enterprises were operated with egalitarianism like feeding on a giant rice pot, and their workers were given life-long fixed positions like having an iron rice bowl that would never break. Both the enterprises and their workers were

³⁴Wei (1997).

treated indiscriminately regardless of the quantity and quality of their work. Such practice seriously confined the initiative and creativity of the enterprises and their workers. The enterprise showed little vigor and poor economic performance.

After China started implementing reform and opening up at the end of 1978, the reform of state-owned enterprises began with expanding the autonomy of enterprises. It was pointed out in the communiqué of the Third Plenary Session of the Eleventh CPC Central Committee that “one serious shortcoming of the economic management system of China at present is too much concentration of power. The power should be delegated to lower levels boldly under leadership so that local enterprises and industrial and agricultural enterprises have more operation management autonomy under the guidance of the centralized state plans.” Around this period, the circle of economics made theoretical demonstrations that state-owned enterprises should be independent commodity producers and operators and main entities of economic interests under socialist system. Jiang Yiwei proposed the famous “enterprise standard theory.”³⁵ Some economists proposed the theory of “separation of the two rights of ownership and management right” and the theory of “contract system.” As market-oriented reform deepened, people found that delegating power and transferring interests without restraining mechanisms might result in short-term action and drain of state-owned assets. Some economists wrote articles of the opinion that the contract system implemented during the period in the late 1980s and early 1990s could not solve the problems of mixing up the functions of government and enterprise. It could not allow different enterprises to compete equally and caused the short-term action of enterprises. These economists advocated that large- and medium-sized state-owned enterprises should establish modern enterprise system to replace contract system.³⁶ Some of them proposed to carry out the shareholding system transformation of large- and medium-sized state-owned enterprises.³⁷ In 1992, the Fourteenth CPC National Congress determined that the socialist market economic system should be the objective model of China’s economic system reform. In November 1993, the Third Plenary Session of the Fourteenth CPC Central Committee made the *Decision on Several Issues on Building Socialist Market Economic System*. It was specifically proposed that the direction of the reform of state-owned reform was to establish modern enterprise system. It was also pointed out that the characteristics of modern enterprise system included clearly-defined property rights, clearly-determined rights and obligations, separation of government function from enterprise management, and scientific management. From then on, China’s state-owned enterprise reform entered the state of system innovation. At the beginning of the twenty-first century, important progress was achieved in the reform of China’s state-owned enterprises. Large- and medium-sized state-owned enterprises initially established modern enterprise system, initially adapted themselves to market economy, and gradually improved their competitiveness. A large number of medium- and small-sized state-owned enterprises were opened and invigorated in various forms. State-owned economy

³⁵See Jiang (1980).

³⁶See Wu (1993).

³⁷See Li (1987).

continued to play a dominant role in national economy. State-owned and state-controlled enterprises became market entities with considerable competitiveness in socialist market economy.

Centering round the corporation reform and shareholding system reform of state-owned enterprises, Chinese economists made in-depth studies on the theories of shareholding system, modern company, corporate governance, state-owned assets management, agency by agreement, modern property right, mixed economy, monopoly and competition, and equal competition of market entity.³⁸ A series of innovation results in enterprise theory achieved in the study powerfully promoted the deepening of state-owned enterprise reform and the improvement of the governance standard of state-owned enterprises.

(II) About Distribution Theory

The distribution theory can also be discussed in the two parts respectively about the first 30 years after the founding of the People's Republic of China and the rest over 30 years.

1. Study and Discussion on the Issue of Distribution according to Performance in the 30 Years after the Founding of the People's Republic of China

The question of distribution according to performance is also a hotspot in the research and discussion of China's circle of economics. The first theme of the First National Symposium on the Theories of Economics in 1959 was the question of commodity production and the law of value under socialist system. Another theme was the question of distribution according to performance and piece rate wage. The then prevailing view affirmed distribution according to performance and piece rate wage, affirmed the role of the principle of material interests in socialist society, and corrected the influence of the article published by Zhang Chunqiao in 1958³⁹ that negated the principle of distribution according to performance in socialism. From that moment to the time before 1966, the circle of economics proposed some valuable views in their discussion.

First, Shen Zhiyuan proposed in 1962 the opinion that distribution according to performance possessed relative stability and that distribution according to performance and the principle of material interests did not contradict with "having politics in command." He pointed out that, in the historical stage of socialism, "the system of distribution according to performance will definitely experience a process of constant improvement, consolidation and development." "If people partially stress on having politics in command and overlook the material interests of the mass, the initiative of the mass will be affected.... To correctly implement the principle of 'distribution according to performance' and adhere to the socialist distribution system is in itself an important aspect of having politics in command. Otherwise, if people do not take the principle of 'distribution according to performance' as an important one and

³⁸See Zhang and Zheng (2008), Liu (2008), Lü and Jin (2008).

³⁹Zhang (1958).

take the material interests of the mass seriously, the principle of 'having politics in command' will end up in nothing."⁴⁰

Second, Wang Xuewen proposed the view that partial private ownership of labor determined the necessity to implement distribution according to performance. He said, "in socialist whole people ownership system, there are factors of partial individual ownership of labor, namely the labor whose object is in product. The existence of such ownership is determined by the development standard of labor productivity, the Three Major Differences, namely the differences between workers and farmers, between the city and the countryside, and between physical and mental labor, left from the old society, and the existence of the remnants of capitalist rights. Now that there are such factors of partial individual ownership of labor, the society needs to exchange the labor owned individually with consumer goods owned by the whole people so as to admit such ownership owned individually."⁴¹

Third, Gu Zhun et al. proposed the view that labor remuneration was connected with the operating results of an enterprise. Gu Zhun believed, "Establish very close connection between the material reward of workers with the degree of occurrence of profit and loss of an enterprise" and "practice economic calculation system. And then it is possible to regulate the reward of workers through utilizing price and wage rate."⁴² In 1962, Shi Xiulin proposed that "bonuses should be accrued and paid on the basis of the comprehensive operating effect of an enterprise."⁴³

Fourth, Li Yun proposed that piece rate wage was a good form of distribution according to performance. He said, "Compared with time rate wage, piece rate wage has the characteristic that it represents the principle of distribution according to performance in a direct, simple and clear way so that the mass can understand it." "Piece rate wage can represent the principle of equal pay for equal work the best." "The principle of distribution according to performance means that distribution needs to be based on the result of labor, so no one can blame that piece rate wage shows too much distribution according to performance."⁴⁴

Fifth, Wu Jiawei proposed that people needed to thoroughly implement the principle of material interests in order to practice the principle of distribution according to performance. He said, "It is one of the basic characteristics of the principle of distribution according to performance that workers care about the development of social production from the perspective of material interests. The role of the principle of distribution according to performance in socialist economy directly determined the principle of material interests." "The better and the more sufficient this principle is employed, the larger and the more conspicuous the superiority of socialist society is actualized. In order to create conditions to eliminate the principle of material interests at the advanced stage of communism, people must fully utilize and vigorously

⁴⁰Shen (1962).

⁴¹Wang (1959).

⁴²Gu (1957).

⁴³Shi (1962).

⁴⁴Li (1959).

develop the principle of material interests at the inferior stage of communism, namely the period of socialist construction.”⁴⁵

Finally, China’s circle of economics started its efforts to put wrongs to rights in theory with the question of distribution according to performance. During the time of more than 1 year from April 1977 to November 1978, China’s circle of economics held four discussion meetings on the theory of distribution according to performance, presided over and promoted by Yu Guangyuan. Among these, the scholars carried out academic discussion on the questions of the nature, object, and form of distribution according to performance.

2. Discussion on the Questions of Distribution according to Performance and Distribution according to Production Factors after the Start of Reform and Opening Up

After reform and opening up started in 1979, the greatest breakthrough in distribution theory was that it was proposed that, in addition to practice distribution according to performance, people also needed to implement distribution according to production factors in socialist society. Prof. Gu Shutang and Prof. Cai Jiming were the scholars who proposed distribution according to production factors the earliest. In 1988, the two professors proposed the view of combining distribution according to performance with distribution according to production factors.⁴⁶ At the time, some economists disapproved of their view and there was very heated discussion on it. Soon after, with the establishment of the objective model of the reform of socialist market economic system, distribution according to production factors was gradually affirmed by the documents of the Communist Party of China. In 1997, the report of the Fifteenth CPC National Congress proposed that “people should adhere to the system of taking distribution according to performance as the main part and allowing the coexistence of multiple distribution modes. They should combine distribution according to performance with distribution according to production factors. And they should adhere to the principle of prioritizing efficiency with due consideration to fairness.” In 2002, the report of the Sixteenth CPC National Congress proposed that people should “establish the principle that production factors such as labor, capital, technology and management participate in distribution according to distribution. They should improve the distribution system of taking distribution according to performance as the main part and allowing the coexistence of multiple distribution modes.” In 2007, the report of the Seventeenth CPC National Congress further reaffirmed the above policy. And it pointed out that people should “adhere to and improve the distribution system of taking distribution according to performance as the main part and allowing the coexistence of multiple distribution modes. They should improve and complete the system in which production factors such as labor, capital, technology and management participate in distribution according to contribution. People should address well the relationship between efficiency and fairness in primary distribution and redistribution and pay more attention to fairness in redistribution.”

⁴⁵Wu (1959).

⁴⁶See Gu and Cai (1988), also published in *Economist*, Issue 2, 1989.

Will it violate the labor theory of value when production factors participate in distribution according to contribution? This is a question that Chinese economists have paid much attention to. Early in 1998, some economists pointed out that distribution according to production factors did not violate the labor theory of value. The labor theory of value means that the value of commodity is created by man's living labor. It concerns the production area. But distribution according to production factors decides how to distribute the value created in the process of production. It concerns the distribution area and does not involve how value has been created at all. Jean Baptiste Say's theory on production factors' participation in distribution was based on the fact that production factors created value. But the theory here on production factors' participation in distribution does not involve such fact but concerns the role of production factors in the formation of wealth.⁴⁷

The question of the relationship between efficiency and fairness is the second hotspot in the discussion on the issue of distribution.

In 1993, it was proposed in the *Decision of the Third Plenary Session of the Fourteenth CPC Central Committee* that the principle of prioritizing efficiency with due consideration to fairness should be implemented. Before this, young economists Zhou Weimin and Lu Zhongyuan already proposed such idea in 1986,⁴⁸ but it did not cause a trend in discussion. In 1993, the Decision of the CPC Central Committee of the Communist Party recognized the principle of prioritizing efficiency with due consideration to fairness. After that, various important documents of the Communist Party of China all reaffirmed the principle of prioritizing efficiency with due consideration to fairness until the *Decision of the Third Plenary Session of the Sixteenth CPC Central Committee* in 2003. It can be said that, during these 12 years, the main outlook of the circle of economics in China was to recognize the principle of prioritizing efficiency with due consideration to fairness. It means to make the cake better first and then consider how to reasonably distribute this bigger cake. Upon the beginning of the new century, because the gap in resident income distribution grew larger in China and the Gini coefficient already exceeded the alarm line of 0.4, some people in the circle of economics gradually proposed that people should abandon the principle of prioritizing efficiency with due consideration to fairness and change to attaching equal weight to efficiency and fairness. Starting from the Decision of the Fourth Plenary Session of the Sixteenth CPC Central Committee in 2004, the documents of the Communist Party of China stopped mentioning the principle of prioritizing efficiency with due consideration to fairness. However, there were still two different views among economists. One believed that people should continue adhering to the principle of prioritizing efficiency with due consideration to fairness⁴⁹ and the other believed that people should abandon the principle of prioritizing efficiency with due consideration to fairness and change to attaching equal weight to efficiency and fairness.⁵⁰

⁴⁷Huang (1998).

⁴⁸Zhou and Lu (1986).

⁴⁹Xiao (2003).

⁵⁰Yu (1997, Liu (2003).

In the author's opinion, it was correct and necessary to propose and implement the principle of prioritizing efficiency with due consideration to fairness in the early period of reform and opening up so as to break equalitarianism in distribution and quickly make the cake of national economy bigger. Upon the beginning of the new century, because the problem became more and more prominent that the gap in resident income distribution enlarged terribly, more attention needs to be paid to fairness in the policy on resident income distribution so as to contain the tendency of the over-enlargement of income gap. People should find a right moment to abandon the principle of prioritizing efficiency with due consideration to fairness and turn to implementing the principle of considering both efficiency and fairness and attaching roughly identical weight to them so as to facilitate the realization of the goal of common prosperity of the whole people.⁵¹ Of course, it was necessary to continue to make in-depth discussion on this issue.

In addition to the above two questions, economists also studied and discussed the question of the gap in resident income after China started reform and opening up and, in particular, the question of Gini coefficient, the question whether Kuznets curve in inverted U-shape applied to China, and the question of the theory of social insurance. Some treatises were published on these questions, such as *The Issue of Resident Income Distribution in China*, edited by Wang Chunzheng and published in 1995 by the China Planning Publishing House, *Resident Income Distribution in China Restudied—Income Distribution in the Process of Economic Reform and Development*, written by Zhao Renwei et al. and published in 1999 by China Financial and Economic Publishing House, and *Re-Discussion on Income Distribution in Reform and Development—Did Social Polarization Occur in China?*, written by Chen Zongsheng et al. and published in 2002 by Economic Science Press.

VI. Explorations were made in the development of national economy from being closed and semi-closed to opening up, the promotion of reform and development with opening up, and the combination of “introducing to China” and “Going Global” and the theory on opening up to the outside world that conforms to economic globalization was gradually formed

Before the reform and opening up started in 1979, there were very few studies on the issues about foreign economy in the circle of economics in China, and it was almost a blank space. At the time, the scholars generally repeated the “theory of two parallel world markets,” proposed in the book *Socialist Economic Issues in the Soviet Union* published by Stalin in 1952, namely one capitalist world market and one socialist world market. Stalin believed that, in the socialist world market, various socialist countries could rely on mutual cooperation to realize economic development and “do not need import commodities from capitalist countries.” Although China did not follow the Stalin's dogmatic ideas in real practice, China's foreign trade and, particularly, trade and other foreign economic relations with capitalist countries were rather underdeveloped and in a semi-closed status at the time.

⁵¹See Zhang (2001).

After the reform and opening up started in 1979, there were two major measures implemented the earliest in economic work and practice for opening up to the outside world. In July 1979, the central authorities approved that the two provinces of Guangdong and Fujian implemented special policies and flexible measures in foreign economic activities. On July 15, 1979, the CPC Central Committee and the State Council decided to try operating special zones in Shenzhen, Zhuhai, Shantou, and Xiamen. On May 16, 1980 special zone was renamed as “special economic zone.” In 1988, the Hainan Special Economic Zone was established. The development of special economic zones mainly aimed at attracting foreign investments. The products manufactured in them were mainly exported. A management system different from the inland areas were implemented. For example, enterprise income tax was 15%. The special economic zones also had large management autonomy. As the windows of opening up to the outside world, special economic zones played a demonstrative, radiating, and leading role. After that, China developed and implemented all-round opening up to the outside world from the east to the west and from processing with supplied material to opening manufacturing industry and to gradually opening service industry.

Two monumental events need to be explained in particular in the process of China’s expanding its opening up to the outside world. One is China’s accession to the World Trade Organization (WTO) in November 2001. This represented an important move of China to conform to the trend of economic globalization. It was of milestone meaning. The accession to the WTO indicated that China’s reform and opening up entered a brand new stage and China boldly entered the arena of international market competition. In the process of negotiations on the accession to the WTO, many people were greatly worried that the accession might affect China’s national economic safety, and many industries in China would suffer huge impact so that it might result in more problems than benefits. However, the experience after the accession to the WTO in many years indicated that the accession brought more benefits than problems to China. Many things worried about in the past did not emerge at all. China benefited from economic globalization. After its accession to the WTO, the growth rates of China’s economic aggregate, foreign trade, foreign investment utilization, and foreign exchange reserves all picked up. Moreover, opening-up promoted reform. The accession to the WTO resulted in the abolition and modification of a large group of laws, regulations, rules, and policies that contradicted with general principles of market economy. Many industries and enterprises made efforts to improve independent innovation ability and enhance their competitiveness in the international market. In 2010, China’s total goods import and export amounted to US\$2,974 billion, showing an increase of 16.8%, i.e., 143 times in comparison with 1978. The percentages of the total of import and that of export of China to the world’s goods import and export rose to 10.4% and 9.1%, respectively. In 2011, China’s total goods import and export further rose to US\$3.6 trillion. In 2011, China was the No.1 export country and No. 2 import country in the world’s goods trade for 3 consecutive years.

The another monumental event was the shift of focus in China from 2005 from “introducing into the inside” to “Going Global” so as to better utilize the two markets

and two kinds of resources in- and outside China and optimize resources allocation. In 2005, China's foreign dependency on main mineral products rose from 5% in 1990 to around 50%. Resources "bottleneck" became a prominent constraint. At the same time, there were excessive production capacities for many products. It became necessary to find the way out in the international market. So people paid more attention to "Going Global" to invest in foreign countries and to search for resources and markets. By 2010, Chinese enterprises made direct foreign investment amounting to US\$220 billion accumulatively. In 2010, such investment reached US\$59 billion. The operating amount of foreign project contracting and labor service cooperation reached US\$335.2 billion. By June 2011, China's foreign exchange reserves amounted to US\$3.2 trillion and ranked the first place in the world. There were completely sufficient conditions for China to "go to the outside world" in a better way and expand investment in foreign countries.

In the early period of opening up to the outside world, various circles in the society kept arguing about it. Deng Xiaoping gave clear and definite exposition on the importance and far-reaching meaning of opening up to the outside world. In 1984, Deng Xiaoping said, "We propose opening up to the outside world while we formulate the policy of invigorating domestic economy. Upon summarizing historical experiences, we find that one important reason why China has been in a condition of stagnation and backwardness is autarchy. Experiences have proven that no one will succeed if he makes construction behind closed doors. China's development will not succeed without the world."⁵² He also said, "We have opening up in three aspects. One aspect is to open up to developed western countries. The foreign investment that China absorbs, the technologies that China introduces and other things mainly come from these countries. Another aspect is to open up to the Soviet Union and the countries in Eastern Europe. This is an area Still another aspect is to open up to the developing countries in the Third World. These countries have their own features and strengths. There are many things to do in this area."⁵³ With respect to the argument on whether it was worthy to introduce foreign investment, Deng Xiaoping proposed in 1992 the famous principle of "Three Favorables", namely being favorable to developing the productivity of socialist society, to enhancing the comprehensive national strength of the socialist country, and to improving the living standard of the people. He said, "Some people believe that one bit more foreign investment brings one bit more capitalism. When there are more overseas-funded enterprises, there are more things of capitalism and that means that we have developed capitalism. These people do not even have common sense. According to current laws, regulations and policies, overseas-funded enterprises in China allow foreign investors to earn money at present. But the state takes taxes back, workers earn wages, and we can also learn technology and management, get information and open market. Therefore, overseas-invested enterprises are under the control of the whole of the political and economic

⁵²Deng (1993a).

⁵³Deng (1993e).

conditions in China. They form beneficial supplementation to socialist economy and, in the end, favorable to socialism.”⁵⁴

Stimulated by the successful practice of China’s opening up to the outside world and encouraged by a series of policies proposed by Deng Xiaoping that advocate opening up to the outside world, the circle of economics in China positively carried out the study on the theory of opening up to the outside world and obtained an abundant series of research results.

In the early 1980s, the circle of economics in China first made exploration on the applicability of David Ricardo’s Comparative Cost Doctrine in foreign trade. In the 1980s, the inaugural issue of *Social Sciences in China* published as its first article *International Industrial Specialization and China’s Foreign Economic Relations*, a paper written by Yuan Wenqi et al.⁵⁵ The paper made theoretical demonstration that developing foreign trade, including developing foreign trade with capitalist countries, could obtain comparative interests, which could play a positive role in a country’s economic development. Some other scholars supported or held views similar to the above.⁵⁶

In the late 1990s, the circle of economics in China further turned from the study on comparative advantage to the study of competitive advantage. Some articles believed that comparative advantage, which was purely determined by endowment of resources, might not become competitive advantage in international trade. If people determined a country’s international trade structure merely on the basis of its endowment of resources and sought to take labor-intensive products as its export orientation, it would fall into the “comparative advantage trap.” In the long run, such a strategy was unfavorable to the healthy development of the national economy in a developing country and also to the adjustment and upgrading of industrial structure in it. Only when comparative advantage was finally transformed into competitive advantage could a country truly form its export competitiveness. In order to adapt to the needs in the flourishing of knowledge economy and high and new technology industry, it was a necessary choice that China’s foreign trade development strategy turned from comparative advantage orientation to competitive advantage orientation.⁵⁷ During this period, Wang Jian proposed the theory of “great international circulation,” which had larger influence. He believed that advanced heavy industry and backward agriculture coexisted in Chinese economy. The strategies of prioritizing the development of agriculture and light industry internally and of introducing foreign investment and developing manufacturing industry for export externally both could not drive Chinese economy to develop fast in a long period. In order to resolve this structural contradiction, people need to take the road of great international circulation. Namely, China should obtain the funds and technologies needed for the development of heavy industry through developing the exporting of labor-intensive product and

⁵⁴Deng (1993c).

⁵⁵Yuan et al. (1980).

⁵⁶See Ji (1981), Chen (1981).

⁵⁷See Hong (1997), Wang (2000).

getting foreign exchange. Then it should turn back to support the development of agriculture with the funds accumulated after heavy industry has been developed. It should connect the circulating relation between heavy industry and agriculture through the transformation mechanism of the international market. Thus China could achieve the goal of eliminating its deviation of “dualistic structure.”⁵⁸ This view played an important driving role for China to develop foreign-oriented economy.

Here are some facts related to the theories on foreign investment. One remarkable achievement in China’s opening up to the outside world was that it attracted large amounts of foreign investment to accelerate its economic growth and provide more jobs to labor force. By the end of 2010, China accumulatively approved the establishment of 710,000 foreign-invested enterprises and actually used nearly US\$1.1 trillion foreign direct investment. In 2010, the actually-used foreign direct investment amounted to US\$105.7 billion and newly-approved foreign-invested enterprises reached 27,000. By 2010, China retained the first place among developing countries in attracting foreign direct investment for 18 consecutive years. Such large scale of foreign investment introduction aroused the interest of economists in academic research.

The positive role of introducing foreign investment can be summarized into the following points on the basis of large amounts of literature: First, it was believed that foreign investment played a positive role in promoting the increase of employment. Second, it was believed that transnational companies brought obvious technology spillover effect, which greatly accelerated the upgrading of industrial structure in China. Third, no solid evidence indicated that foreign direct investment “squeezed out” domestic investment that had created economic benefits. Foreign direct investment and domestic capital jointly became the engines that drove China’s economic growth. Fourth, novel business modes and management modes were brought in together with foreign investment. “In general, foreign direct investment made positive contribution to China’s economic development.”⁵⁹

Some treatises connected the use of foreign investment with the trend of economic globalization and believed that China’s opening up to the outside world entered a new stage upon the beginning of the twenty-first century. China needed to “consider comprehensively the balances of interests between itself as a host country of foreign investment and the home country of foreign investment, between the flow of goods and the flow of production factors, and between protecting domestic market and promoting other countries to open up their markets. China should participate in multilateral negotiation in a more positive and active attitude and balance the interests of various parties by means of multilateral rules” and thus “merge into global economy in a more balanced and reasonable manner.”⁶⁰

How to address well the relationship between introducing foreign investment and protecting national economic safety was also a question that economists paid attention to. The kernel of this question was to protect national industry. Some articles

⁵⁸See Jian (1988).

⁵⁹See World Bank (2007).

⁶⁰See Jiang (2006).

pointed out that, in the protection of domestic market, people needed to depend on entrepreneurs rather than administrative power in the end. More importantly, the way to protect national industry had to rely on methods that conformed to international practice rather than on administrative measures. People should make national industry an organic component of socialist market economy rather than the specially protected one. People should provide proper support and protection from an open perspective and a positive attitude rather than implementing the protection of national industry from a negative and closed-door attitude.⁶¹

Some articles proposed that, examined from theoretical paradigm, using foreign investment mainly concerned a whole set of trade-fund theories in development economics, such as dual gap theory, transnational corporation theory, infant industry protection theory, industry transfer theory, etc. These theories provided theoretical research paradigms for studying the entering of foreign investment into China and its possible influence and also furnished certain basis for formulating relevant policies.⁶²

With respect to the question of the exchange rate of Renminbi, the circle of economics had the common understanding that people should adopt a way of gradually lifting control. They should first lift the control over the items in current account and take a prudent attitude toward lifting the control of capital account. In July 2005, the People's Bank of China published an announcement that China started to implement a floating exchange rate system that took market supply and demand as basis, carried out regulation with reference to a basket of currencies, and imposed proper management. From then on, Renminbi started to appreciate gradually. This could be seen from the exchange rate of Renminbi to US dollar. In the past, US\$1 was exchanged for RMB8.27 yuan. By the end of 2008, the exchange rate was US\$1 to RMB6.83 yuan. Renminbi appreciated by 21%. By the end of 2008, China's foreign exchange reserve reached US\$1,946 billion, ranking the first place in the world. This figure continued to grow in the years after. In recent years, the circle of economics in China carried out heated discussion on how to preserve or increase of the value of China's huge foreign exchange reserve and to bring into play the role of foreign exchange reserve in a better way. And many valuable opinions were proposed in the discussion.

Opening up to the outside world is a fundamental national policy for China to realize socialist modernization. Some articles made the following summarization on the theory of opening up to the outside world. People discarded closed and semi-closed development modes and turned economic development from domestically-oriented economy to export-oriented economy. They followed a "progressive road" in the process of exploring opening up. Namely, they started implementing progressive opening up in the manner of spatial expansion through developing economic special zones. They established open economic system, promoted system reform and improvement with opening up, promoted the regulation of government action, and constructed the new administrative management system of economy. They made full

⁶¹See Wang et al. (1996).

⁶²See Zhang (2008).

use of the two kinds of international and domestic resources and markets to positively introduce foreign investment, vigorously develop import and export trade, and included investment in foreign countries as part of the initiative of “Going Global”. Driven by the theory on opening up to the outside world, China openly promoted domestically-oriented strategy characterized by import substitution in the 1980s. At the Third Plenary Session of the Fourteenth CPC Central Committee in 1993, it was proposed that people should deepen the reform of foreign economic system, including the reform of the foreign trade system and that related to foreign investment, foreign-funded enterprises, foreign exchange, foreign-related taxation and laws, regulations, and rules. This proposal promoted the comprehensive development of export-oriented economy. After it expanded opening up to the outside world in 1994, China started to implement “outward-looking” or export-oriented strategy and achieved enormous economic benefits from it. Such strategic transition brought Chinese economy and system into a new stage. From then on, “China Miracle” attracted more and more attention in the world.

These articles also pointed out that China’s experience in reform and opening up indicated that breaking old system and forming new system needed the driving of opening up. Without the driving of opening up, it was difficult to break old system. Because opening up gave rewards to new system in the manner of “increment,” it became a continuous force for breaking old system. The purpose of system reform was to achieve development and to establish a new economic system that had high efficiency and could stand firm in the world in competition. So, China needed an open system rather than a closed one. It needed to absorb and draw from advanced civilizations of the mankind and compete with other nations. Thus it would develop into a modernized and advanced country. This was the only road to the great rejuvenation of the Chinese nation. In opening up to the outside world, a country would encounter a kind of “unequal competition” unfavorable to developing country, present on the international market, including commodity market and financial market. There would be external impact that caused risks, such as the East Asia Financial Crisis in 1997 and the International Financial Crisis in 2008. So, it was an important strategy for the opening up of a major country to centering round its own appeal in the issue of opening up. Such strategy could lower the risks brought about by internationalization.⁶³

V. More and more importance was attached to economic growth and development theory. After the reform and opening up started, research efforts were focused on studying the questions of what kind of development to achieve and how to develop under the guidance of the principle that development is of overriding importance and on studying the regularities in China’s industrialization, urbanization, and modernization

To realize socialism, people need to first develop productivity. This is the axiom of Deng Xiaoping. The Chinese people carried out new democratic revolution and socialist revolution and implemented reform and opening up for the purpose of

⁶³Ibid.

liberating and developing social productivity, getting China out of poverty and backwardness, and constantly raising the living standard of the people. Therefore, soon after the founding of the People's Republic of China, the CPC Central Committee proposed to carry out large-scale socialist construction and gradually achieve the task of the modernization of agriculture, industry, science and technology, and national defense in China. The Chinese people needed not only have the courage to destroy an old world but also have the wisdom to build a brave new world. Thus, it was natural that China's circle of economics studied the question of economic growth and development extensively.

Generally speaking, great achievement was made in the first 30 years of socialist construction during over 60 years from the founding of the People's Republic of China. The average annual GDP growth rate from 1953 to 1978 reached 6.1%.⁶⁴ This result laid the initial foundation for socialist industrialization in China. But such development was still not fast enough to meet people's expectation. There are two reasons for such problem. One was that China's development was often disturbed by the idea of taking class struggle as the guiding principle so that China deviated from the line of taking economic construction as the central task and lost some development opportunities. The other was that there were the problems of disregarding national situation, going beyond its proper development stage, and advancing blindly and rashly. In particular, the 3 years from 1958 to 1960 caused disastrous consequences to China's national economy.

In order to study the lessons from 1958 to 1960, the circle of economics in Beijing held a number of discussion meetings from the beginning of 1960s, jointly presided over by Xue Muqiao, Yu Guangyuan, and Sun Yefang, which was about the questions of speed and proportion, socialist reproduction, relationships between agriculture and light and heavy industries, and economic accounting and economic effect. Economists outside Beijing also published many articles on these questions. Large amounts of research and discussion articles in these areas were also published in *Economic Research Journal*, *People's Daily*, and *Guangming Daily* around this period.

With respect to the question of the relationship between speed and proportion, Xue Muqiao and Yang Jianbai et al. said, "It is not that, when raising the speed of development, people need not consider objective possibility of such raise or the proportional relations between various sectors in national economy. Speed must be built on the basis of objective possibility. And people must retain the basic proportional relations between various sectors in national economy. Only in this way can they guarantee the development of national economy at a high speed."⁶⁵ High-speed development had to take being according to relevant proportions as "the necessary condition" or "as its premises." Only "when development is achieved according to relevant proportions can it realize comprehensive and lasting high speed."⁶⁶ Liu Guoguang said that the speed and proportions in economic development could have

⁶⁴See *Economic Daily*, Oct. 30, 2008.

⁶⁵See Xue (1959).

⁶⁶See Yang (1962, 1959).

various kinds of combinations in a certain period. “People should choose the best plan among various possible combinations of speed and proportion so that national economy can not only develop at a high speed and according to relevant proportions in the current planning period but also create good conditions for further development in subsequent periods.” “It is particularly important to correctly understand and master the quantitative relations between speed and proportion. Namely what proportion will result in what speed and what speed will definitely require what proportion.”⁶⁷

From 1959 to 1960, people required positive balance and “leap-forward balance” disregarding objective reality. With respect to this problem, some treatises pointed out that positive balance “should be that balance generated from the high unity between objective possibility and subject initiative. Within the limits of objective possibility, people can improve objective economic conditions and make them adapt to each other through their subject power of agency.”⁶⁸ “People should start with the actual situation when addressing the proportional relations between various sectors in national economy. This is positive balance rather than negative balance. If people depart from objective possibility and partially emphasize needs, then it becomes impossible for them to organize new balance and, on the contrary, they will aggravate imbalance.”⁶⁹

Whether to leave some leeway in planning work to prevent proportional imbalance was one issue in the discussion at the time. Some articles proposed that “leaving some leeway is a positive policy.” “‘Gap’ is the opposite of leaving some leeway. We need to leave some leeway but we should not leave ‘gaps’.” “Plans must be formulated with a positive attitude.” “But it must also be practical and reliable. We should never put unreliable ‘potential’ into a plan without proper grounds.” “Leaving some leeway is not negative but positive. It is not optional but essential.”⁷⁰

With regard to the lessons in the 1950s, some treatises also discussed the question of the starting point or intention of the comprehensive balance of national economy. For example, some treatises specifically advocated that comprehensive balance should be carried out in the order of agriculture, light industry, and heavy industry. The scholars said that “to achieve comprehensive balance according to the order of agriculture, light industry and heavy industry means to arrange all the plans for the reproduction in heavy industry and of national economy and achieve the comprehensive balance of the entire national economy through following the objective requirements that agriculture is the basis for the development of national economy while industry is the leading sector in the development of national economy, taking agriculture as the starting point and also as the center, centering round agricultural reproduction, and giving due consideration to industry production.”⁷¹ Some

⁶⁷ See Liu (1962).

⁶⁸ See Guo et al. (1959).

⁶⁹ See Xu (1964).

⁷⁰ See Li (1964).

⁷¹ See Yang (1962).

proposed that, “under socialist system, the purpose of production and the contradictory characteristics between social production and social demand stipulate that comprehensive balance must be achieved with satisfying social demand as the starting point.” “When regulating the contradiction between social production and social demand with comprehensive balance, people need to both see the social demand in the long run and, starting with the current actual standard, pragmatically stipulate the reasonable quantitative boundaries to satisfy social demand to the maximum.”⁷²

Socialist reproduction was a hotspot question in the discussion in the 1960s. In addition to the discussion on general questions like the relationship between the two major departments in social production, a question of stronger realistic nature was the question about the restrictive role of the production of consumption means in social reproduction. Some economists believed that people had to see the restrictive role of the second department in the expanded reproduction while affirming the leading and decisive role of the first department in expanded reproduction. This was because expanded reproduction needed not only more machinery, equipment, and raw materials but also more food and other daily supplies.⁷³ Some articles further believed that it was not accurate enough to just define the role of consumption means as a restrictive one. “Because such definition makes people feel that the production of consumption means is only in a passive position or even only plays a curbing role in socialist expanded reproduction. In fact, not only the production of consumption means but also the production of production means have a restrictive role. Also, both the production of production means and the production of consumption means have a promotive role.”⁷⁴

The idea of “calculating political effects but not economic ones,” disregarded practical costs, paid no attention to economic effects, and caused serious loss and astounding waste. With respect to this problem, the circle of economics carried out, in particular, the discussion on the question of economic accounting and economic effect in socialism and proposed many valuable ideas.

With respect to the content of economic accounting, some article proposed that the economic accounting that an enterprise carried out should include not only cost accounting but also fund accounting. It was believed that the economic accounting of a socialist enterprise should include the two aspects of cost accounting and fund accounting. This is because, in the process of production, an enterprise needed to “not only consume certain amount of labor but also occupy certain amount of funds.” “Viewed from the angle of the society, lowering the funds that must be occupied for producing certain product means the effect of fund use is raised. People can produce more and better products with the same amount of funds and thus improve the economic effect of the labor of the entire society.”⁷⁵ Some articles proposed that socialist economic accounting included the accounting in production and in construction. It was believed that “the economic accounting in socialist society included

⁷²See Wen and Feng (1963).

⁷³See Shi (1961).

⁷⁴See Zeng (1963).

⁷⁵See He et al. (1962).

economic accounting in production, mainly the accounting of the fruits of labor and production cost, and economic accounting in construction, mainly the accounting of investment effect. The former ensures that the current production capacities can be utilized reasonably to achieve the maximal economic effect. The latter ensures that people can use as little as possible consumption of living labor and materialized labor to create as much as possible new production capacities.”⁷⁶

Was there the most comprehensive or central index in economic accounting? If there was, what was this index? This was a hotspot in the discussion at the time and it was rather foresighted. Early in 1957, Sun Yefang mentioned in the article *A Discussion Starting from “Gross Output Value”* that the so-called central index should be a central link in enterprise management which could drive other indexes when people take control of it. Profit showed the performance of an enterprise’s operation in the most focal manner. The best advantage of using this index was that it reflected the actual situation in production and it could promote enterprise management. The achievement of target in this index would not obstruct but would definitely drive the achievements of target in other indexes.⁷⁷ Shen Jingnong had similar views. He believed that there could be only one central or commanding index rather than two or more. Otherwise, there would be nothing meaningful in being central. The central index in a system of economic accounting was the index of profit.⁷⁸

Differently, some people held that cost and profit be the main indexes to evaluate the economic effect of an enterprise and attach equal weight to them. Product cost was the most important component of the labor consumption of product. To a certain extent, the value of product cost directly reflected the value of labor consumption in the production of product. It was a comprehensive index of the technological and economic activities of an enterprise. Profit index reflected both the factor of the value of cost and the influence of other indexes on economic effects that other indexes could not reflect. Both were comprehensive indexes and should be given equal weight.⁷⁹

After the beginning of the reform and opening up, the discussion on economic growth in the circle of economics entered a brand new stage. In 1992, the study and discussion on the issue of economic growth and development became the No. 1 hotspot in the study and discussion of the circle economics after Deng Xiaoping proposed the strategic thought that development is of overriding importance. In 2003, how to realize the scientific development of economy, which included implementing people-oriented, comprehensively-coordinated and sustained development, transforming the mode of economic growth and development, building resource-saving and environment-friendly society, and improving the ability of independent innovation and building innovative country, became the focus of the circles of academic study and politics after the CPC Central Committee proposed the outlook of scientific development. At the end of the twentieth century, China initially established socialist

⁷⁶See Xue (1961).

⁷⁷See Sun (1957).

⁷⁸See Shen (1962).

⁷⁹See Yang and Li (1962).

market economic system and market started to play its fundamental role in resources allocation. The issue of reform did not seem to be as prominent and urgent as before. Because of this, some economists believed that China's "reform economics" gradually evolved into "development economics" after the country entered the new century. These themes of academic study and discussion shifted their positions in the whole picture.⁸⁰ Such judgment had certain ground.

First, the discussions on the issue of economic growth and development are gathered here from the documents of the Communist Party of China.

At the end of 1978, the Third Plenary Session of the Eleventh CPC Central Committee determined that the work of the party would center round economic construction. After that, it was proposed in the report of the Twelfth CPC National Congress in 1982 that, "in the twenty years from 1981 to the end of the present century, the general goal of struggle in China's economic construction is to work hard to quadruple the annual gross output value of agriculture and industry in all China under the premises of constantly increasing economic effects, namely to grow from RMB710 billion yuan in 1980 to RMB2.8 trillion yuan in 2000."

In 1987, it was further proposed in the report of the Thirteenth CPC National Congress that, "after the Third Plenary Session of the Eleventh CPC Central Committee, the strategic arrangement of China's economic construction has been divided roughly into three steps. In the first step, China would realize the doubling of the GDP figure in 1980 and resolve the issue of people's subsistence. This task has been basically completed. In the second step, China will double the GDP figure again and raise the people's living standard to the level of a well-off society at the end of the present century. In the third step, China's per capita GDP will reach the standard of a moderately-developed country by the middle of the next century. The people will live a relatively affluent life and China will basically complete its modernization."

In 1995, it was proposed in the *Suggestion of the CPC Central Committee on the "Ninth Five Year Plan"* that people "should practice two fundamental transformations with global meaning. One is the transformation from traditional planned economic system to socialist market economic system. The other is the transformation of economic growth mode from extensive type to intensive type to promote the sustained, rapid and healthy development of national economy and all-round social progress."

In 2000, it was proposed in the *Suggestion of the CPC Central Committee on the "Tenth Five Year Plan"* that, "in the formulation of the 'Tenth Five Year Plan'," people should "take development as the theme, structural adjustment as the main line, reform and opening up and scientific and technological progress as driving power, and raising the living standard of the people as fundamental starting point."

In 2002, the report of the Sixteenth CPC National Congress proposed the task of comprehensively building a well-off society and taking the road of new-type industrialization in the first 20 years of the new century. It was pointed out that "we need to concentrate our power in the first twenty years of the present century to comprehensively build a well-off society of higher level that benefits more than a dozen billion

⁸⁰See Huang (2008).

population so that there are more developed economy, more complete democracy, more progress in science and technology, more thriving culture, more harmonious society, and more well-off livelihood of the people in China.” “On the basis of optimizing structure and improve effects and through hard work, GDP will quadruple from 2000 to 2020 and China’s comprehensive national strength and international competitiveness will see obvious improvement. China will basically realize industrialization and finish building a complete socialist market economic system and a more vigorous and open economic system.” “People should adhere to the principle of taking economic construction as central task and resolve the issues encountered in advancement with the method of development.” It was also pointed out that “people should persist in driving industrialization with informatization and promote informatization with industrialization and created a new-type road of industrialization that has higher scientific and technological content, better economic effect, lower resource consumption, less environmental pollution, and full exertion of the advantages in human resources.”

In 2003, the decision of the Third Plenary Session of the Sixteenth CPC Central Committee proposed scientific outlook of development. It was also proposed in the decision that people should “adhere to people-orientedness, establish a comprehensive, coordinated and sustained outlook of development, and promote the comprehensive development of economy, society and people.”

In 2005, the *Suggestion of the CPC Central Committee on the “Eleventh Five Year Plan”* proposed that people should “take resources preservation as a basic national policy. They should develop circular economy, protect ecological environment, speed up building resources-saving and environment-friendly society, and promote the mutual coordination between economic development and population, resources and environment.”

In 2007, the report of the Seventeenth CPC National Congress proposed that “the first essence of the scientific outlook of development is development. Its kernel is people-orientedness. Its basic requirements are comprehensiveness, coordination and sustainability. Its fundamental approach is overall planning and all-round consideration.” The report of the Seventeenth CPC National Congress also made new and higher requirements on comprehensively building a well-off society, which mainly included “to achieve important progress in the transformation of the modes of development and to quadruple per capita GDP from 2000 to 2020 on the basis of optimizing structure, improving effect, reducing consumption and protecting environment.”

During the same period, the circle of economics also made extensive and positive study on the questions on economic growth and development.

The first question studied was about the strategy of economic development. From February 1981, some scholars of theoretical economic studies in Beijing held a strategic discussion meeting every 2 months. Altogether 49 meetings were held until March 1989. These meetings exerted important influence on the formation of the strategies of “three steps” and “quadrupling” in China. After the report of the Twelfth CPC National Congress proposed the task of “quadrupling” in 1982, prestigious Chinese economist Sun Yefang wrote an article entitled *There Are Not Only Political*

*But Also Technical Guarantee for Achieving the Quadrupling Goal in Twenty Years—Also a Discussion on That ‘Low Speed for Large Base Number’ Is Not a Principle,*⁸¹ which won full recognition from the leaders of central authorities. On November 23, 1982, the then State Council premier Zhao Ziyang visited Sun Yefang at the Beijing Hospital and said, “I read your article published on newspaper a few days ago. Your opinion on the quadrupling goal was great and your criticism on the view of ‘low speed for large base number’ was forceful. When the central authorities held meetings to discuss five-year plans, Comrade Chen Yun mentioned your opinion in particular and Comrade Hu Yaobang also valued your article very much.”⁸²

The second question studied was how to take the new-type road of industrialization. The question that caused the greatest argument in the circle of economics in China then was whether China’s industrialization entered the inevitable stage of heavy industrialization upon the beginning of the new century. The research group on the topic of “the Study of New-Type Road of Industrialization” of the Development Research Center of the State Council held an affirmative view on the question. They believed that “various countries in the world have basically developed along the track from agriculture, to light industry, to heavy industry, to high and new technology industry, and to service industry.” “Only when a country has experienced the stage of heavy industrialization can it become an industrial power and become part of the first group in economic development in the world.” “It is already an established fact that China’s economy has entered a new round of rapid growth. Its main characteristic is that China officially entered the ‘stage of heavy industrialization’.

If China seizes the opportunity of heavy industrialization, Chinese economy will definitely retain 20 years of high growth.” “The Chinese economy at present is not overheating in general or locally and it is not normal development without any new characteristic. In fact, China’s industrialization has entered a historical stage with the great re-development of heavy industry as its main characteristic.”⁸³ Wu Jinglian disapproved of such opinion and wrote a number of articles in an opinion different from the above. He pointed out that the above view was a conclusion obtained from the “Law of Hoffman”. In 1931, Walther G. Hoffman concluded that the production of capital goods grew faster than consumer goods in the process of industrialization after summarizing the empirical data on the changes of the internal structure of industry in the industrialization process of over 20 countries. But this conclusion was made at the time when the third industry or service industry was not regarded as a fundamental industry. When the leaders of industrialized countries entered the late

⁸¹ *People’s Daily*, Nov. 19, 1982.

⁸² “Care in the Heart”, *People’s Daily*, Dec. 6, 1982.

⁸³ See Research Group on the Topic of “the Study of New-Type Road of Industrialization” of the Development Research Center of the State Council, “China’s Industrialization Entered a New Stage”, *Economic Daily*, Dec. 1, 2003; “The Development of Our Province Cannot Get Around the Stage of Heavy Industrialization”, *Nanfang Daily*, Sep. 11, 2003; “Heavy Industrialization: Main Driving Power of China’s High-Speed Economic Growth”, Xinhua News Agency, Beijing, Nov. 29, 2003; “Second Industrialization: Industrialization Process of China’s Private Enterprises”, *Business Monthly*, March 2, 2004; “An Analysis on the Investment in Four Key Industries in China”, *Economic Daily*, June 16, 2004.

stage of industrialization, the prediction in the Hoffman theorem that the industry of capital goods or heavy industry would dominate in national economy did not come true because service industry showed the fastest growth then. Simon Smith Kuznets, Nobel Prize laureate in economics, named the economic growth in this stage as modern economic growth. His basic conclusion was that, different from the situation that economic growth in earlier stages mainly relied on resources or, in particular, capital investment, modern economic growth had the conspicuous characteristic that its high output growth only had a limited and small portion that could be attributed to investment. The majority of such high output growth should be ascribed to the high growth rate of productivity. On such basis, Wu Jinglian believed that China had to thoroughly transform its economic growth mode and take a new-type industrialization road. Only when it set building resource-saving and environment-friendly economy as its guiding policy in the future could China realize faster and sustained growth. In the middle and late stages of industrialization, the demand on durable consumer goods such as housing, automobile, and household appliance would grow and the demand on heavy industrial products would also grow rapidly, but this did not mean that the demand on heavy industrial products would exceed the demand in service industry.⁸⁴

Chen Jiagui and Huang Qunhui, scholars in the Chinese Academy of Social Sciences, proposed representative opinions on the issue of China's industrialization. They believed that, after over 20 years of rapid industrialization process, China transformed from a major country of agricultural economy to that of industrial economy. This meant that China's economic modernization process entered a new stage in which realizing the transformation from a major country of industrial economy to a powerful country of industrial economy and promoting industrial modernization process became the core task. The new stage of the modernization process required the selection of new strategy. In the strategy on technological progress, people should pay more attention to the independent innovation of strategic technology and the increase of the investment in the area of basic scientific research. In the strategy on economic growth, people should practically promote the transformation of economic growth mode and persist in taking the road of new-type industrialization in the development of heavy industrialization. In the strategy of industrial development, the three major industries should have new strategic mission and development positioning. In the strategy on economic system reform, people should resolutely continue deepening marketization reform.⁸⁵

The third question studied was about transforming economic growth mode. After China started implementing reform and opening up in 1979, Chinese economy achieved an annual GDP growth rate of 9.8% from 1978 to 2008, exceeding the world's average growth rate of 3% in the same period by over twice. It was known as the "China Miracle" in the world. During this period, Chinese economy encountered a series of problems of unsustainability in its rapid development. So China proposed the task of transforming the mode of economic growth and development.

⁸⁴See Wu (2005).

⁸⁵Chen and Huang (2005).

In the 1990s, China mainly relied on the investment of production factors such as capital and resources and paid less attention to improving efficiency. Because of the defects of such extensional expansion, China proposed the task of transforming from extensive growth mode to intensive growth mode. At the beginning of the new century, China proposed the task for transforming from the extensive growth mode with the problems of high investment, high consumption, high emission, and low efficiency to the resource-saving growth mode with the features of low investment, low consumption, low emission, and high efficiency in consideration that too large costs had been paid in resources and environment so that it was impossible to retain high-speed economic growth like that. Obviously, such transformation entailed greatly diverse contents and requirements. In 2007, when explicating that one of the keys to promote the development of national economy in a good and fast way is to speed up the transformation of the mode of economic development, the report of the Seventeenth CPC National Congress further proposed that people should realize three transformations. Namely, they should promote the transformation of the mode of economic growth from mainly relying on the driving of investment and export to relying on the driving of consumption, investment, and export, from mainly relying on the leading and driving of the secondary industry to relying on the synergic leading and driving of the primary, secondary, and tertiary industries, and from mainly relying on increasing the consumption of material resources to mainly relying on scientific and technological progress, improvement of workers' quality, and management innovation. The impact of the international financial crisis in 2008 on Chinese economy indicated that it was more urgent and important for China to transform the mode of economic growth and development. Only when people vigorously transform the mode of economic growth and development and achieve actual effect in it can Chinese economy realizes sustainable faster growth. This view has won extensive recognition in the circle of economics. Some economists pointed out that transforming the mode of economic growth and development and realizing the optimization and upgrading of industrial structure is a difficult task that takes long time. People need to make long-term consideration and hard work and achieve the combination between such efforts and the deepening of reform. Sometimes, this task may contradict with retaining economic growth in the short term. So it is difficult to fulfill. People must take realizing scientific development and good and fast development as a starting point and precisely and practically implement the requirements on the three transformations proposed in the report of the Seventeenth CPC National Congress. Only in this way can they promote the sustained, balanced, and faster growth of Chinese economy.⁸⁶

The fourth question studied was about modern economic growth. As Chinese economy kept development, many empirical research results were published, various economic growth theories were introduced, including the theories of "structural model," "comparative advantage," and "learning by doing," and the research paradigm of modern economic growth started to become popular. In 1994, Lin

⁸⁶See Fang (2009), Zhang (2009c).

Yifu, Cai Fang, and Li Zhou published a treatise entitled *China Miracle: Development Strategy and Economic Reform*⁸⁷ and proposed the development mode of comparative advantage. Later, other paradigms emerged successively such as “low-price competition mode” and “low-price industrialization growth mode.” These new research paradigms emphasized the endogeneity and sustainability of economic growth and possessed important theoretical value and realistic meaning.⁸⁸ In particular, it is worth mentioning that the research groups on the topics of “economic growth frontiers” and “China’s economic growth and macroscopic stability” of the Institute of Economics of the Chinese Academy of Social Sciences consecutively published ten articles on *Economic Research Journal* from 2003. They believed that there were some regularities in the route along which a country developed from poverty to affluence. If the vertical axis represented per capita GDP, the horizontal axis represented time, the curve between them the curve of output, then such curve would be roughly in an S-shape. Such S-shaped growth curve can be further broken down into several stages corresponding to relevant economic theories such as the “Malthusian Equilibrium” related to poverty trap, the “theory of industrial revolution” related to economic catch-up, the “theory of economic growth under Kaldor typical facts” related to neo-classical theory, and “new economic bifurcation” related to new growth theory. At the same time, a stage of middle-income trap was defined in response to the fact that some countries failed in economic catch-up.⁸⁹

The fifth question studied was about urbanization. There was always argument on whether or not China should focus on developing large cities or it should realize urbanization by relying on developing medium-sized and small cities and small towns. In 2007, the Seventeenth CPC National Congress summarized practical experience and specifically proposed that China should take the road of urbanization with Chinese characteristics. It was pointed out that people “should take the road of urbanization with Chinese characteristics. They should follow the principles of making centralized planning for the city and the countryside, setting up rational layout, saving lands, providing complete function mix, and driving the development of small cities with that of large ones. They should promote the coordinated development of large-, medium- and small-sized cities and small towns. They should take enhancing comprehensive carrying ability as the focus, relying and basing on megacities, forming urban agglomerations with radiating function, and cultivate new growth poles.” Some economists made systematic exposition on how to adhere to the road of urbanization with Chinese characteristics. They proposed that people should turn from excessively pursuing the expansion of quantity to paying more attention to the improvement of quality and gradually enhance the standard of urbanization. On the one hand, they should continue to positively push forward urbanization and promote the transfer of surplus rural labor and population into the city and improve the supportive capacity of various production factors to the development of cities and

⁸⁷Lin et al. (1994).

⁸⁸See Liu et al. (2008a).

⁸⁹See Liu et al. (2008b).

towns. On the other hand, people should reasonably control the size of a city, optimize and adjust urban structure, make efforts to improve the quality of construction and development of the city, and bring into play in a sustained and stable manner the promotive role of urbanization in economic and social development.⁹⁰

The sixth question studied was about economic growth and economic stability. Before the reform and opening up, Chinese economy retained general stability except that extremely serious disproportions and rocketing black market prices appeared during the period 1958–1960. The main indication of such a situation was that commodity price was basically stable and inflation was concealed. After the reform and opening up started in 1979, Chinese economy quickly took off and economic growth also accelerated. The average annual GDP growth from 1978 to 2008 reached 9.8%, which was 3.7% higher than the average annual GDP growth from 1953 to 1978 of 6.1%. During this period, there was the problem of rushing for quick results. Some people held that economic growth should be as fast as possible and that inflation should be used as a means to support hyper-speed growth of the economy. Due to the influence of such rush for quick results, economic overheating and inflation occurred in different degrees in 1985, 1988, 1993–1994, 2007–2008, and from July 2010 to 2011. The CPC and the Chinese government had to implement tight macroscopic policies to control and regulate inflation and restore coordination and stability in macroscopic economy. During this process, some economists persistently objected the use of inflation as a means to support short-term high-speed economic growth. They believed that such practice was unfavorable to both the stable growth of economy and the deepening of reform. When China tried to “make a breakthrough” in price reform in 1988, Xue Muqiao and other economists held that people should not “make a breakthrough” under the situation of inflation and it would not be successful. Facts proved that they were right. In the fourth quarter of 1988, China was forced to stop “making a breakthrough” and turned to implement policies to control and regulate inflation.

In 1987, a research group in the Chinese Academy of Social Sciences also proposed the guide line of “making progress while maintaining stability”⁹¹ in reform and development and held that people should promote reform and development on the basis of stabilizing economy. They had to control and regulate inflation when they tried to stabilize economy. In later period, although economists still have disagreements and different understandings on inflation, most of them held that two-digit rise of commodity price should be avoided as much as possible. It was believed that, ideally, annual CPI rise should be controlled at around 4% and such a range belongs to the situation that commodity price was basically stable.

The realization of stable economic development requires that people find the point of equilibrium between economic growth and commodity price rise. If people want to control the rise of commodity price within two digits so that it could stay around 4%, China’s economic growth could not be too high. On the basis of China’s national situation, such growth should be no higher than two digits. In particular, it should not

⁹⁰See Ning (2005).

⁹¹See Research Group of the Chinese Academy of Social Sciences (1988).

be in two digits for 2 consecutive years or more. Otherwise, macroscopic economy would definitely lose its balance. From 2003 to 2007, China's economic growth reached two digits for 5 consecutive years. Such a situation not only caused inflation in 2007 and 2008 but also resulted in excessive costs in resources and environment and the imbalance between consumption and investment, between internal and external demand, and between secondary and tertiary industries. From the fourth quarter in 2008, Chinese economy took a sharp turn. Although such a situation had a close relation to international financial crisis, it also resulted from the adjustment forced to be made due to economic imbalance.⁹²

The seventh question studied was the countermeasures and experiences in successful responding to the impact of the international financial crisis in 2008 so that China became the first country that got out of the crisis on the globe. In 2008, the most serious economic crisis since 1929 broke out on the globe. On September 15 that year, the Lehman Brothers Inc., one of the five investment banks in the USA, filed for bankruptcy and triggered the global financial crisis. Around that moment, major developed countries in the world all fell into economic recession. During the six quarters from the first quarter of 2008 to the second quarter in 2009, there were five quarters that showed dropping GDP chain relative ratios in the USA. In the third quarter of 2009, GDP grew by 2.2% and, in the fourth quarter, by 5.7%. This financial and economic crisis caused the global economy in 2009 to shrink by about 2% and the trade volume between different countries by about 10%. In April 2010, the International Monetary Fund held that financial crisis caused banks in the world to write down US\$2.3 trillion in book value. Now the banks have written off US\$1.5 trillion, and there was still US\$800 billion to be written off. The international financial and economic crisis caused serious impact to Chinese economy. Such impact became further explicit from the fourth quarter of 2008. The GDP growth in the quarter dropped to 6.8%. It further dropped to 6.1% in the first quarter of 2009 and fell into a historical low. The main reason for this was the downslide of export. In 2009, China's good export was US\$1201.7 billion, dropping by 16%. Its import was worth US\$1005.6 billion, dropping by 11.2%. The trade surplus was US\$196.1 billion, showing a decrease of US\$102 billion in comparison with the last year.

Confronted with the impact of global financial and economic crisis, the government adopted a series of measures in response, including implementing an investment incentive plan of RMB4 trillion yuan, which quickly made Chinese economy become stable and turn around and better. Chinese circle of economics made research and discussion centering round this issue. They published a large number of articles and made proposals and suggestions to the country. In 2009, Chinese economy realized a growth rate of 9.2% with the efforts of various circles and achieved the most brilliant performance among all major economies in the world. In 2010, China's GDP growth further reached 10.4%, indicating that economy was a bit overheating.

Why could China still retain positive growth and did not fall into negative growth or recession (when an economy has negative growth for two consecutive quarters, it is called recession) and became the first country to get out of the crisis? According

⁹²See Zhang (2009b).

to the analysis of economists, the reasons could be summarized into the following several points:

First, China's financial system was relatively healthy and complete. Many hidden problems were eliminated after major state-owned banks stripped off non-performing assets, replenished their capital, and were traded on the stock market through overall listing successively in 1998. In this crisis, China's financial institutions, particularly several major banks, did not purchase many toxic assets. The Industrial and Commercial Bank of China, the Bank of China, and the China Construction Bank purchased assets worth tens of millions of dollars at the most and did not suffer much loss. Major banks in developed countries purchased billions or tens of billions of dollars of toxic assets. There are nearly US\$1 trillion of bad assets that are waiting to be written off until now. Their task in bettering their balance sheet was still arduous in a long time. This shows how serious this financial crisis has been. But major Chinese financial institutions have not been trapped deep in it. They did not sustain substantial damage, and their credit relations still ran as normal.

Second, central authorities timely adjusted macroscopic economic policies. In November 2008, the authorities proposed the idea of "retaining growth and expanding internal demand" and implemented proactive fiscal policy and moderately loose monetary policy. On November 5, 2008, the State Council promulgated ten measures on expanding internal demand and promoting growth and proposed a plan to stimulate economy in which RMB4 trillion yuan investment be made in China by the end of 2010. And the central fiscal authorities would invest RMB1.18 trillion yuan in such plan. In 2008, the central fiscal authorities allocated RMB120 billion yuan and, in 2009, the authorities allocated RMB500 billion yuan in several sums to invest in infrastructure construction and people's livelihood project and to boost internal demand. Driven by the investments from central authorities, various local authorities all strengthened their investment activities. Rough estimation showed that investments from various provincial and municipal authorities nationwide reached RMB25 trillion yuan. These measures greatly increased the growth rate of fixed assets investment in 2009. The growth rate of fixed assets investment nationwide reached 30.1%. This was the main driving power of economic growth in 2009.

Third, the government promulgated a series of policies to reduce taxes, promote the increase of residents' income, and stimulate consumption. These policies included increasing the subsidies to farmers growing grain, to purchase of farming machinery and automobile, and to household appliance to the countryside, transforming value-added tax, lowering vehicle purchase tax of small-displacement vehicle, lowering real estate tax and stamp duty on stock transactions, increasing medical subsidies, raising the standard of subsistence allowances, increasing the supply of low-rent housing and price-limited housing, increasing post-disaster reconstruction fund, and so on. All these directly stimulated and drove consumption demand. The total retail sales of consumer goods in the whole year of 2009 reached RMB12,534.3 billion yuan, showing an increase of 15.5% in comparison with last year. The actual growth was 16.9% or over 2% more than the figure 14.8% in 2008.

From the second half of 2009, global economy recovered slowly under the strong stimulation policies implemented by various countries. However, the crisis had not

completely passed and there were uncertainties in economic recovery. At the end of 2009, some European countries such as Greece, Portugal, Ireland, Spain and Italy also faced the threat of sovereign debt crisis after the Dubai World debt crisis occurred. Under such a circumstance, Chinese economy could no longer be driven into high growth mainly in reliance on export and investment like the time before 2008. China's resource and environment carrying ability did not allow such practice, either. It became even more urgent to adjust economic structure and transform the mode of economic development. It became the only choice to achieve the sustainability of growth to shift from the priority of "fast" to the priority of "good."

The eighth question studied was that Chinese economy needed transformation: from excessively pursuing quantitative expansion to stressing on quality and benefits. After the beginning of the new century, China's economic growth accelerated. Chinese economy retained a growth rate of 10% and more for 5 consecutive years from 2003 to 2007. After China was hit by the international financial crisis in 2008, the country still achieved growth rates of 9.6% and 9.2% in 2008 and 2009 because the government implemented a package plan including strong investment stimulation. In 2010, China's per capita GDP reached a bit over US\$4,000 after converted into USD according to the exchange rate at the end of that year, and China became the second largest economy in the world. Because of rapid economic growth, China's output of many major industrial and agricultural products ranked the first place in the world. This indicated that Chinese economy achieved brilliant performance in scale and quantitative expansion that attracted the attention of the whole world. China has become a major economic and industrial country in the real sense.

However, people need to see that many problems related to bad coordination were accumulated because Chinese economy basically followed extensive and expansive mode to achieve high-speed growth. These problems constrained the stable, efficient, and sustained growth of Chinese economy. The problems included the imbalance between savings and consumption or between investment and consumption. In this problem, the percentage of final consumption to GDP lowered to less than 50% in China. And the proportion of residents' consumption to GDP lowered to 33.8% in 2010. Another problem was the imbalance between internal and external demand. China depended on external demand excessively and had too high export dependency. This figure reached 36% in 2007, one time higher than 18% in 1998. And internal demand was seriously inadequate. Still another problem was that too much cost in resources and environment was paid for economic development. There was the imbalance between economic growth and the carrying capacity of resources and environment. Resources and environment became important bottlenecks in economic development. One more problem was the imbalance in development between different regions and between the city and the countryside. The gap in residents' income was too large, and the situation was not turned around with good efforts. In particular, the standard of income and consumption of farmers was too low. In 2010, China's urban resident per capita consumption expenditure was 13,471 RMB, while rural resident per capital consumption expenditure was 4,382 RMB, less than 1/3 of the former. This indicated that the fruits of economic development failed to bring benefits to the people in the whole country in a good way. In the several imbalances mentioned

above, the critical ones are that between investment and consumption or between savings and consumption. Because of high investment growth, excessive production capacity, and weak domestic consumption, the economy had to find its way out through expanding external demand so that export dependency kept rising. Very high investment growth plus extensive expansion would definitely cause China to pay too large costs in resources and environment. Such very high investment growth was caused by the pursuit to fast GDP growth. As a result, fiscal budget paid too little in public service expenditure. The financial resources used to support the development of underdeveloped regions, and the increase of the income of low-income groups was severely inadequate. Thus people could not do well in narrowing the economic and income gaps between different regions and between the city and the countryside and in effectively turning around the situation that there was too large gap in residents' income.

The breakout of international financial crisis in 2008 and its impact made China's imbalance problems and extensive expansion problems more prominent. It became extremely urgent to transform the mode of economic development. Transforming the mode of economic development means economic transformation. Namely, economic development was transformed from the type of pursuing quantitative expansion to the type of paying attention to the quality and benefits of growth so that the economy could truly take the tracks of stable, coordinated, efficient, and sustained development and of scientific development.

Economic transformation could not be finished overnight. No substantial progress could be achieved without hard work in about a decade. But from now on, China needs to set the focus of work on pushing forward economic transformation.

Some economists believed that there were three most important measures for smoothly pushing forward economic transformation.

First, people should properly slow down economic growth. The root cause that Chinese economy encountered problems in its operation was the pursuit of unrealistic high-speed growth. According to the study of some economists, China's potential growth rate at present stage ranged between 7.5% and 9%. So its economic growth should better be controlled around 8% in the decade in the future. People should not seek to achieve growth rate in two digits but should focus their work on improving the quality and benefits of economic growth. With growth rate staying around 8%, people should speed up developing the tertiary industry and medium- and small-sized enterprises and, if China's economic structure tends to become rational, the industry and these enterprises will provide more jobs to China's labor force than in the past. Chinese economy hit the bottom in the first quarter of 2009. The GDP growth in that quarter showed a year-on-year growth of 6.1%. After that, it gradually turned better and resumed the status of high-speed growth in the third quarter that year. The GDP growth in that quarter reached 8.9%, and the GDP growth in the year was 9.2%. In the first quarter of 2010, it reached a high of 11.9%. China's fiscal revenue also showed fast increase. Now it appears that people should give proper control over the growth rate of Chinese economy from 2010 so as to shift the focus of work from pursuing quantitative and scale expansion to improving the quality and benefits of the operation of economy. If people continue to blindly pursue the high-speed growth

of GDP so that economic growth rate reached two digits once again, it will be very hard to achieve the transformation.

Second, people should endeavor to adjust structure and transform the mode of economic development. People should earnestly and practically implement the three transformations proposed at the Seventeenth CPC National Congress in 2007. Namely, in promoting economic growth, people should transform from mainly relying on the driving of investment and export to relying on the coordinated driving of consumption, investment and export, from mainly relying on the leading and driving of the secondary industry to relying on the synergic leading and driving of the primary, secondary and tertiary industries, and from mainly relying on increasing the consumption of material resources to mainly relying on scientific and technological progress, improvement of workers' quality, and management innovation. It was a very arduous task to transform the mode of economic growth and development. People should make efforts to improve the ability of independent innovation and to save energy, lower consumption and reduce emission. They should take time in their efforts and should not rush. It was even possible that no obvious effects be achieved in the present term of the government. Because of this, some government departments always showed little interest on this task, which was a big problem. The adjustment of structure involved even wider areas. In addition to industrial structure, economic structure also included regional structure, urban and rural structure, income distribution structure, internal and external demand structure, and also the issue of whether there was harmony between man and nature. In this aspect, the tasks of optimizing and upgrading industrial structure, vigorously developing the tertiary industry, and saving energy and reducing emission were consistent with the task of transforming the mode of economic development. The most important tasks in the adjustment of structure at present included the following: People should adjust the structure of investment and consumption and vigorously increase the proportion of residents' consumption in GDP. They should adjust the income distribution structure and work hard to contain the abnormal situation that there was too large gap in residents' income. People should vigorously promote energy conservation, consumption lowering and emission reduction and endeavor to build resource-saving and environment-friendly society. They should speed up urbanization process and the process of turning farmers into urban residents, which was the most effective choice in expanding domestic demand in the future, and so on. In particular, it needed to be pointed out that there were contradictions sometimes between adjusting structure and transforming the mode of economic development and pursuing high-speed GDP growth. It could be the task that became the issue the most difficult to handle well in economic work in the future how to give proper consideration to both optimizing structure and transforming development and economic growth. It seemed that it would be more favorable to optimizing economic structure and transforming the mode of economic development to retain the stable growth of the economy and not to blindly pursuing unsustainable high-speed growth. It should also be seen that adjusting economic structure and transforming the mode of economic development need long-term relentless efforts. The Central Economic Working Conference held in the winter of 2009 set transforming the mode of economic development as the

strategic priority in the economic work in 2010. This was a good start. People hoped that this could be truly and practically implemented and carried on in the future so that substantial progress could be achieved after around a decade of step-by-step hard work.

Third, people should deepen reform and improve and perfect socialist market economic system. There were many approaches to adjust economic structure and transform the mode of economic development. For example, people should promote scientific and technological innovation, enhance the ability of independent innovation, and greatly increase the investment in research and development. People should improve and perfect laws, regulations and rules, and complete the environment of the rule of the law. People should improve, support, and encourage various policies favorable to the transformation of the mode of economic development and stop implementing all policies of retro-regulation. People should improve and complete various technological standards and formulate necessary access standards. People should deepen reform and promote the transition of economic and social development into the track of scientific development, and so on. And the most important approach was to deepen reform and improve socialist market economic system. First, people should deepen government reform. They should realize the transformation from the government that oriented toward economic construction and pursued GDP growth to a service-oriented government. They should practically perform the functions of the government in economic regulation, market supervision, social management, and public service. They should practically change the current situation that the government got involved in economy too deeply. Second, people should implement price reform. They should seize the favorable opportunity brought about by stable commodity price at present and speed up price reform of resource products so that such price could truly reflect supply and demand relationship on the market, resource scarcity, and environmental damage costs. They should bring into play the role of price lever in promoting resources conservation and environmental protection and push forward the optimization of resources allocation and the optimization and upgrading of industrial structure. Third, people should implement fiscal and taxation reform and transform government finance into public finance as quickly as possible. In order to expand consumption and improve the people's livelihood, they had to transform government finance from the finance that oriented toward economic construction to public finance and gradually realize the equalization of basic public service. With respect to the strong speculation trend on China's real estate market, people should impose property tax as quickly as possible to contain the excessive development and speculation demand of real estate. The imposition of property tax was proposed in 2003. But many years have passed the implementation of such measure still face a great deal of obstruction. Now it is the time to implement pilot projects and then promote the measure gradually. Fourth, people should implement financial reform. People should learn lessons from the international financial crisis and take all possible measures to prevent systematic financial risks, including building residents' deposit insurance system as quickly as possible. The financial industry should serve real economy in a better way and promote the optimization of resource allocation. People should develop medium- and small-sized banks and

provide better service to medium- and small-sized enterprises. They should continue to improve and develop capital market and insurance market. Fifth, people should deepen the reform in monopolized industries. They should loosen the market access in service industry and introduce competition mechanism. Such measure could play an important role in accelerating the development of finance, telecommunications, railway, public utilities, and undertakings in culture, education, medicine and health, in optimizing industrial structure and raising the proportion of the tertiary industry, and increasing the jobs in service industry. In the present stage, people need to make great efforts to create more jobs. And the creation of more jobs mainly relies on developing the tertiary industry. Thus people had to overcome various system obstructions and break various glass-door-like invisible obstacles. They should open up market in all areas where the market could be opened and, particularly, in the service sector and introduce competition mechanism. Sixth, people should push forward various reforms helpful to improving the income standard of people who earned medium and low income and to expanding consumption. These reforms included the following. People should largely raise the amount of subsidies provided by fiscal budget to rural cooperative medical service. As the first step, the standard was raised from 100 RMB per capita per year to 200 RMB. And it would continue to be raised in the future. They should lower the tax rate of personal income tax. They should continue to promote the initiative that household appliances, other electronic products, agricultural machinery, automobiles entered rural market in a large scale and at low prices. They should raise the standard of subsistence allowances, find stable fund sources for low-rent housing and other affordable housing, build unemployment aid system for migrant rural workers, and so on.

China's economic reform entered the stage of tackling and cracking difficult issues. Some reforms were subject to the obstruction and opposition of vested interest groups so that it was hard for these reforms to advance. So people had to formulate mid- and long-term plan. There had to be the powerful top-down push from the CPC and the government so that reform could deepen. At present, the economy faced a severe situation. But this was helpful for people to work hard to find a way out for reform and give the reform larger impetus. The important thing was to seize this favorable opportunity and to launch necessary reform at a proper moment. Then people could positively support the reform with proper macroscopic economic policy so as to gradually bring national economy onto the track of balanced and sustained development and to realize the goal of comprehensively completing building a well-off society by 2020.⁹³

It needed to be pointed out that some economists already wrote treatises on the topic of China's economic transformation and these books attracted extensive attention. Here, the author recommends in particular a book edited by Chi Fulin, entitled *The Second Transformation—At the Crossroads of Transforming Development Mode*.⁹⁴

⁹³See Zhang (2009a).

⁹⁴Chi (2010).

VI. Important reformations were achieved in the methodology of economics: people attached importance to innovation, closely related to reality, fully absorbed useful research results in modern economics; they paid more attention to empirical study and quantitative analysis and courageously proposed various kinds of countermeasures and suggestions; and various selection and awarding activities were carried out step by step for promoting the prosperity of the economic science

During over 60 years from the founding of the People's Republic of China, important reformations emerged in the methodology of economics as the study in economics gradually deepened. Important ones among them are as follows:

(I). More attention was paid to theoretical innovation and innovation results kept emerging in the sinicization of Marxist economics

During the period from the founding of the People's Republic of China to the time before the reform and opening up, many treatises on economics showed the limitations of dogmatism. The authors were enthusiastic in interpreting classical works, or listing patterns and principles, or only making simple policy propaganda. They lack independent thinking, felt unwilling to create new and original things, and exhibited weak innovation spirit. Because it was hard to draw a clear line between politics and academic research in the circle of economics, new views were often given a terrible political label and criticized as soon as they emerged. Such practice stifled the innovation spirit of the people and suppressed the voice of truth. As a result, the policy of letting a hundred flowers blossom and a hundred schools of thought contend could not be implemented well at all. The mass criticism on the population theory of Ma Yinchu and the theory of value of Sun Yefang was the most prominent cases in such a situation.

After the reform and opening up started, economists opened up their eyes and gradually got out of the confines of traditional socialist economic theories under the guidance of the ideological lines of the CPC on liberating the thought and seeking truth from facts. Going deep into real life, exploring courageously, and innovating boldly, they achieved one valuable research result after another and constantly and deeply develop the theory on the sinicization of Marxist economics. Theories on the primary stage of socialism, socialist market economy, socialist basic economic system, the combination between distribution according to labor and distribution according to production factors, opening up to the outside world, and Chinese-styled economic growth and development were all the most important research results in the sinicization of Marxist economics. These theories were important components of the theoretical system of socialism with Chinese characteristics. In the latest 30 years, the leaders of the CPC and the state in China encouraged theoretical innovation and earnestly practiced what they advocated, exhibiting excellent political wisdom. The combination between their efforts and the bold exploration and fruitful work of economists made a series of innovation results in the sinicization of Marxist economics the mainstream in the arena of economic discussion in China.

People should also courageously innovate important views in Marxism. The discussion on the labor theory of value at the beginning of the twenty-first century

exemplified such a point. In October 2000, the Fifth Plenary Session of the Fifteenth CPC Central Committee proposed in the *Suggestion on the "Tenth Five Year Plan"* that, "as productivity develops, scientific and technological work and operation and management played a more and more important role in social production as an important form of labor. Under new historical conditions, people need to deepen their understanding on labor and the labor theory of value." After the meeting, the circle of economics carried out in-depth discussion on the labor theory of value. According to the author's personal experience, the mainstream view was roughly that the assertion of Marx that only living labor created value was correct and it was not outdated until the present. Although some economists believed that materialized labor also created value, such a view did not win much recognition. Moreover, people should see that, as socialist productivity developed, the tertiary industry was on the rise and its status and role in national economy gradually grew. As a matter of fact, the added value of the tertiary industry in developed countries accounted for over 60% or 70% of their GDP. So people should recognize that large amounts of service labor, including the labor in business, passenger transportation, communications, consultation, and financial service, should also be the labor that creates value. This also indicates that the economic theory in Marxism needs to be developed as social economic practice develops.

From 2004, the CPC Central Committee directly led the compilation of *An Introduction to Marxist Political Economics*, a key textbook in the Project of the Study and Construction of Marxist Theories which was published by the People's Publishing House and the Higher Education Press in May 2011. The chief experts in the textbook compilation group included Liu Shucheng, Wu Shuqing, Ji Baocheng, Li Xingshan, Zhang Yu, and Hu Jiayong. The task of this book was to systematically formulate the innovation results of the sinicization of Marxist economics.

(II) Theoretical study was closely linked to the reality under the socialist construction

The progress in the field of China's economic theoretical study over 60 years since the founding of the People's Republic of China was that the theoretical study of economics gradually stepped outside the hall of science and extensively participated in and closely connected itself with the reality in the socialist construction in China. China was a major developing country with backward economy in which 80% of the population was in the countryside. When carrying out socialist modernization construction in such a country, people needed to catch up in the areas of industrialization, urbanization, marketization, socialization, and internationalization. They also needed to help the extensive public community to get rid of poverty and advance toward common prosperity and realize the great rejuvenation of the Chinese nation. Such an undertaking was great pioneering work unprecedented in history. On the one hand, such great practice urgently needed the theoretical study in economics to support and provide various options and to explore the road that conformed to objective economic principles for China's socialist modernization construction. On the other hand, the rich practice in socialist construction provided unprecedented precious materials and experiences for the theoretical study in economics. In particular, the transition or transitional economics which could be used to study the process

in which China turned from traditional planned economic system to socialist market economic system became an important research topic that economists in the whole world had interest in studying. Chinese economists bravely shouldered their important duty and explored in various aspects. They carried out theoretical summarization on large amounts of practical experiences to look for objective regularities and thus continuously enriched the treasure house of the economic science.

One prominent indication that the theoretical study in economics was closely connected with reality was that, after the reform and opening up began, many economists became think tankers in the decision-making of the CPC and the government. Some economists participated in the drafting of important documents of the CPC and the government and some economists worked as advisors to local governments, departments, and enterprises. Economists were regarded as “lucky children of the time” by the people. Driven by the enormous demand in social practice, various applied economics saw rapid development and formed a prosperous picture. Great development was achieved in the disciplines of finance, public finance, management of national economy, international trade, regional economics, labor economics, population, resources and environmental economics, sustained development economics, statistics, quantitative and technological economics, national defense economics, and marketing. There were a great abundance of treatises and an increasing multitude of scholars in these areas. Various disciplines in economic management, including rural economy and management, business administration, which included accountancy, business management, tourism management, and technological economy and management, and public administration, which included educational economy and management, social insurance, and land resources management, all became hotspots in research and study and attracted more and more people who aspired to study and learn economics.

(III) Useful research results in modern economics were fully absorbed

In general, modern economics refers to western economics and includes microscopic economics, macroscopic economics, development economics, econometrics, and some other applied economics. These disciplines take mature capitalist market economy as the object of study. On the one hand, western economics took capitalist private ownership as natural and eternal, which was incompatible with Marxism. On the other hand, western economic study made careful research on the regularities of the operation of market economy and summarized principles and concepts from them. And these were useful for people to understand and master the regularities of the activities in market economy. So they were not to be negated lightly. For example, Keynesian theories on regulating the relationship between total social supply and demand with fiscal policy and on lowering unemployment rate had important referential value for China to implement the regulation and control of macroscopic economy. The idea that people could regulate the activities in market economy and conduct market supervision in the form of legislation in western economics was also applicable in China’s market economy. There were also a series of innovative financial theories in western economics that were valuable enough for China to draw from. Some other western theories were also used to analyze the issues in Chinese

economy such as theory of industrial organization, theory of dualistic economic structure, unbalanced development theory, institutional efficiency theory, theory of cost-benefit analysis, modern company theory, theory of the firm, and sustained development theory. Some concepts in western economics, such as scarcity, opportunity cost, marginal utility, equilibrium price, GDP and GNP, production function, propensity to consume, and Gini coefficient, became indispensable instruments for Chinese economists to analyze economic activities. Of course, people should never jump from one extreme to the other. Before the reform and opening up, Chinese people almost completely negated western economics. The fruits of modern civilization contained in western economics were also negated. Now there was a different trend of completely affirming western economics so that it appeared that western economics could explain and resolve all the issues in Chinese economic development. This was very one-sided understanding. Closeness and rigidity would not work, neither would be changing road and flying a different flag. The right attitude was to take the innovation results in the sinicization of Marxism as the guide, fully absorb the useful research results in modern economics, earnestly study the regularities in the movement of China's socialist market economy, promote the smooth development of China's socialist modernization construction, and promote the prosperity and development of economics in China.

In order to learn and borrow from western economics, a large number of masterpieces in western economics were published in China after the reform and opening up started. In the past, the works of Adam Smith, David Ricardo, John Maynard Keynes, and Alfred Marshall were translated and published in China. In addition, *Economics* written by Paul A. Samuelson was translated and published by China Development Press and other publishers. *The New Palgrave: A Dictionary of Economics* was translated and published by Economic Science Press. Upon the start of the twenty-first century, *Macroeconomics* by Rudiger Dornbusch and *International Economics: Theory and Policy* by Paul R. Krugman were translated and published by China Renmin University Press in 2002. *The World Economy: A Millennial Perspective* by Angus Maddison was translated and published by Peking University Press in 2003. *Economics* by Joseph E. Stiglitz was translated and published by China Renmin University Press in 2005. *Principles of Economics* by N. Gregory Mankiw was translated and published by Peking University Press in 2006, and so on.⁹⁵

(IV). More importance was attached to empirical study and quantitative analysis

Before 1966, Chinese economic treatises only contained rough normative analysis in general, and there were few investigation reports. After the reform and opening up started, empirical research started to become popular. Economic research needs both normative and empirical analyses. Many treatises written by the Chinese circle of economics in the past were studied from concepts to concepts or interpretations to policies. Such a situation was unfavorable to exploring the objective regularities in socialist construction. It affected the creative thinking of economic research. Empirical analysis mainly contains objective and truthful description of economic

⁹⁵See Huang (2008).

movement and process. It analyzes the mechanism in them and does not make value judgment or preach on how people must do something or what they are required to do. Empirical analysis and, in particular, case analysis in it are similar to what Chairman Mao Zedong has advocated by comparing analyzing a typical case to “dissecting a sparrow.” Such an approach is helpful for starting economic study from specific typical cases and gathering materials and information so as to find inherent and intrinsic connections. Then through comparing a number of cases, people could find some common things that emerge repeatedly. Thus the study of economic theories will not deviate from reality and violate the principles of understanding things. During a certain period of time, many doctorate dissertations in economics contained empirical analysis and achieved gratifying research results. Case studies could be found not only in the treatises with empirical analysis but also in treatises particularly devoted to case study. Such a situation exerted good influence on promoting the study of economic theory.

The study of economic theory always entails statistical data and quantitative analysis. An article that only develops from concepts to concepts without any data can hardly be called a paper on economic science or even an academic paper. Before 1966, Chinese circle of economics paid more attention to the study on production relations and its reformation. Under the influence of the idea of taking class struggle as central task, economic study showed very strong influence of ideology and people paid inadequate attention to quantitative analysis. After the start of the reform and opening up, the circle of economics not only paid attention to the study of the issues on production relations and economic system but also attached more and more importance to the study of the issues on economic development and specific policies. Such study required sufficient data in the analysis of an issue and the demonstration of a scholar’s opinion, countermeasure, and suggestion. Under such a circumstance, more and more articles were written to carry out quantitative analysis on the operation of economy or to analyze economic issues with mathematical models. The data on certain indexes like import and export dependency, energy consumption coefficient, electricity consumption coefficient, Engel’s coefficient, investment rate, savings rate, consumption rate, contribution rates of investment, consumption and export, urbanization rate, CPI and PPI and population aging rate, and so on were almost indispensable in an article on economics. This was a good phenomenon that could help to break the stereotype that economics was not a precise science.

(V). Various countermeasures and suggestions were proposed courageously

Economics is a science that helps to govern the society and benefit the people. During the period of socialist construction, how to carry out socialist modernization construction in a fast and good way is a research topic that economists mainly focus on and work hard to study. In order to better serve the modernization of the state, economists all spontaneously provided operable suggestions for countermeasures and policies on the basis of their own research results. The CPC and the Chinese government also encouraged economists to provide intellectual support to the formulation and implementation of policies. Socialist market economy was a competitive economy.

Various regions and enterprises were all in a competition environment. Local government and enterprises often required economists to provide advice and suggestions on how to improve the competitiveness of the region or the enterprise and speed up its development. Therefore, people could often see that economists carried out various kinds of consultation activities and official and semi-official economic consultation institutions mushroomed. Such a situation gave a broad space for economists to boldly propose various kinds of countermeasures and suggestions.

Not only local authorities and enterprises but also central government needed economists to provide advice and suggestions. Socialist market economy was the economy with government regulation and macroscopic regulation and control. Economists are needed to provide good suggestions and countermeasures on how to implement proper macroscopic economic policies, including fiscal policy and monetary policy, on the basis of the changes in economic situation and ensure the stable and healthy operation of macroscopic economy and how to formulate practical and feasible mid- and long-term development plans. People greatly valued various kinds of analytical and predictive reports on economic situation. There were also various kinds of economic reform plans for the government and decision-making departments to choose from. After the beginning of the twenty-first century, economic consultation activities were not limited to domestic consultation institutions and organizations. Some international organizations, such as the World Bank, the International Monetary Fund, the UN agencies, and offices of transnational companies in China, continually participated in such activity. For example, when China's was formulating its eleventh five year plan in 2005, the World Bank voluntarily provided a system report entitled *Policies on China's Eleventh Five Year Plan (December 2004)* (translated from a Chinese version). Similarly, UN resident agencies in China proposed *Promoting the Development of Chinese Society—the Admonitions of UN Resident Agencies in China on China's Eleventh Five Year Plan (July 2005)* (translated from a Chinese version). These documents provided many foreign experiences and data that China could learn from. It appears now that the participation of international organization was greatly beneficial for Chinese economists to study the issues in Chinese economy better with the world's perspective.

(VI). Various kinds of selections and awarding activities were carried out step by step to promote the prosperity of economic science in China

First, the Chinese Academy of Sciences selected 61 commissioners of the academic division of philosophy and social sciences in 1955. Among them, 14 were from the research direction of economics, who were Tao Menghe, Di Chaobai, Guo Dali, Huang Songling, Luo Gengmo, Ma Yinchu, Qian Jiaju, Qian Junrui, Shen Zhiyuan, Wang Xuewen, Wang Yanan, Xu Dixin, Xue Muqiao, and Yu Guangyuan. The title was the supreme academic honorary title in China. In 2006, the Chinese Academy of Social Sciences selected 13 commissioners of the academic division of economics, who were Liu Guoguang, Liu Shucheng, Lü Zheng, Yu Yongding, Zhang Zhuoyuan, Zhang Xiaoshan, Li Yang, Li Jingwen, Yang Shengming, Wang Tongsan, Chen Jiagui, Zhou Shulian and Tian Xueyuan, and 20 honorary commissioners of the academic division of economics, who were Yu Guangyuan, Yu Zuyao,

Wang Guichen, Wang Gengjin, Zhu Shaowen, He Naiwei, He Zhenyi, Wu Chengming, Wu Jiajun, Zhang Shouyi, Li Cong, Wang Haibo, Wang Jingyu, Gu Yuanyang, Chen Baosen, Chen Dongsheng, Zhao Renwei, Luo Gengmo, Gao Dichen, and Dai Yuanchen. According to the provisions in the documents of the Chinese Academy of Social Sciences, commissioner and honorary commissioner of an academic division of the Chinese Academy of Social Sciences were “the highest academic title of the Chinese Academy of Social Sciences and a life-time honor.”

Second, a book entitled *104 Economists Who Influenced the 60 Years of Economic Construction of The People’s Republic of China* was published in 2009 in celebration of the 60th anniversary of the founding of the People’s Republic of China by the Guangdong Economy Publishing House, edited by Wu Taichang, Zhang Zhuoyuan, Wu Jinglian, Li Yining, and Liu Wei, after the discussion and confirmation of a discussion and compilation committee, which consisted of 19 economists such as Huang Da, Lin Zhaomu, and Zhou Shulian, on the 104 economists who influenced the 60 years of economic construction of The People’s Republic of China. The book, published in eight volumes, collected three or four representative papers of each economist in addition to giving a brief introduction on his academic contribution. Here is a list of these 104 economists:

Volume 1: Cai Fang, Chen Daisun, Chen Jiagui, Chen Qingtai, Chen Xiwen, Chen Zhenhan, Chi Fulin, Di Chaobai, Dong Fureng, Du Runsheng, Fan Gang, Fang Weizhong, Gao Hongye, and Gao Shangquan.

Volume 2: Gu Shutang, Gu Zhun, Gui Shiyong, Guo Shuqing, He Liancheng, He Wei, Hong Yinxing, Hu Jichuang, Huang Da, Huang Fanzhang, Ji Congwei, and Jia Kang.

Volume 3: Jiang Xiaojuan, Jiang Xuemo, Jiang Yiwei, Jin Bei, Li Chengrui, Li Jiange, Li Jiangfan, Li Jingwen, Li Shi, Li Xiaoxi, Li Yang, and Li Yining.

Volume 4: Lin Gang, Lin Ling, Lin Yifu, Lin Zhaomu, Liu He, Liu Shibai, Liu Shijin, Liu Shucheng, Liu Wei, Liu Zunyi, Lü Zheng, Luo Gengmo, and Ma Hong.

Volume 5: Ma Yinchu, Pang Jinju, Qian Yingyi, Shen Zhiyuan, Shi Jinchuan, Song Tao, Song Zexing, Su Xing, Sun Shangqing, Sun Yefang, Tang Congtai, Tao Dayong, and Wang Jingyu.

Volume 6: Wang Jiye, Wang Jian, Wang Jue, Wang Luolin, Wang Mengkui, Wang Xuewen, Wang Yanan, Wang Yiming, Wei Xinghua, Wei Jie, Wei Liqun, Wu Baosan, Wu Chengming, and Wu Jinglian.

Volume 7: Wu Shuqing, Wu Xiaoling, Xiao Zhuoji, Xie Ping, Xu Dixin, Xu Yi, Xue Muqiao, Yan Zhongping, Yang Jianbai, Yi Gang, Yu Guangyuan, Yu Yongding, and Yuan Zhigang.

Volume 8: Zeng Muye, Zhang Jun, Zhang Peigang, Zhang Weiyang, Zhang Zhuoyuan, Zhao Haikuan, Zhao Renwei, Zhong Yangsheng, Zhou Qiren, Zhou Shulian, Zhou Xiaochuan, Zhuo Jiong, and Zou Zhizhuang.

Third, in order to review and summarize the development course and contribution of economics in China during nearly half a century since the founding of the People’s Republic of China, the Institute of Economics of the Chinese Academy of Social Sciences and the Guangdong Economy Publishing House jointly launched and implemented the discussion and selection of the “Ten Works of Economics That

Influenced the Economic Construction of The People's Republic of China" in 1997 and 1998. Finally, the ten works were selected after voting, and then these works were reprinted and published as a series by the Guangdong Economy Publishing House in September 1998. These works were as follows: *Papers on the Theory of Socialist Economy* written by Sun Yefang, *New Population Theory* by Ma Yinchu, *A Study on the Issues of Socialist Economy in China* by Xue Muqiao, *The Economy in the Primary Stage of Socialism in China* by Yu Guangyuan, *An Original Discussion on Chinese Economy* by Wang Yanan, *On Socialist Commodity Economy* by Zhuo Jiong, *On the Models of Enterprise in Socialism* by Jiang Yiwei, *A Study on the Models of China's Economic System Reform* by Liu Guoguang, *Chinese Economy in Imbalance* by Li Yining, and *On Competitive Market Mechanism* by Wu Jinglian and Liu Ruiji.

Fourth, various awarding activities were carried out. The most influential one was the Sun Yefang Award of Economic Science. In June 1983, the Sun Yefang Economic Science Award Foundation, later renamed as the Sun Yefang Economic Science Foundation, was established under the initiation of Bo Yibo, Yao Yilin, Song Ping, Gu Mu, Zhang Jinfu, Rong Yiren, Xue Muqiao, Wang Daohan, Xu Dixin, Yu Guangyuan, and Xu Xuehan for the purpose of commemorating the important contribution of eminent Chinese economist Sun Yefang to Marxist economic science, encouraging and promoting new scholars, and making China's undertaking in economic science thrive. An award selection was made every 2 years from 1984. Altogether 14 selections were made by 2010. 47 treatises and 164 papers were selected. Around RMB2 million yuan prize was given out. At present, a group of backbone researchers in the area of economic study and teaching are all winners of the awards of treatise or paper of the Sun Yefang Economic Science Award. A group of scholarly officials in economic area were also honored with the Sun Yefang Economic Science Award.

Besides, the China Economics Award, jointly established by the CSM Fund of the China Society of Macroeconomics and the China Society of Economic Reform in 2004, was also very influential. Four laureates of the China Economics Excellent Contribution Award were selected, who were Xue Muqiao, Ma Hong, Liu Guoguang, and Wu Jinglian. Each was awarded a prize of RMB300,000 yuan. But because of various reasons, the selection of this award did not continue.

In addition, there are a number of awards named after some Chinese economists that have a certain influence in the Chinese society, such as the Xue Muqiao Price Award, the Jiang Yiwei Enterprise Reform and Development Award, the Xu Yi Financial Science Award, and the Dong Fureng Economic Theory Innovation Award.

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Part I
The Peroid of 1949–1965

Chapter 1

The Spreading of Stalin's Issues on the Socialist Economy in the Soviet Union in China in the 1950s and the Discussion on the Issue of Basic Economic Principles During the Transitional Period Triggered by Such Spreading



Zhuoyuan Zhang

1 The Spreading of Stalin's Issues on the Socialist Economy in the Soviet Union and the Textbook on Political Economics of the Soviet Union in China

In 1952, Stalin published the book *Issues on the Socialist Economy in the Soviet Union* and, soon after, the *Textbook on Political Economics* of the Soviet Union was compiled on the basis of Stalin's book and then published. These two books were quickly translated into Chinese and published. It was then the early period of The People's Republic of China after its foundation. People did not have any definite ideas about how to build socialism. The two books published caused great attention in various circles and, particularly, the circle of economics in China. The Chinese people studied them devouringly and the ideas in these books quickly became mainstream theoretical views.

Stalin proposed the following views with very large influence in the book *Issues on the Socialist Economy in the Soviet Union*.

First, socialist economic principles had objectivity. People could understand them and use them to benefit the society. But they could not create, change or eliminate them.

Second, there were whole people ownership system and collective ownership system in the socialist society in the Soviet Union at the current stage. And there would definitely be commodity production and circulation under such a condition.

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Third, the law of value still existed and played its role under the socialist system. It played a regulatory role in the area of commodity circulation and it only played a role of influence in the area of production rather than a regulatory role because the means of production had gotten out of the scope of action of the law of value.

Fourth, because of the existence of two opposite camps, a unified and all-inclusive world market crumbled. There were two parallel and mutually opposite world markets.

Fifth, the fundamental economic principle (or law, the same as below) was to guarantee the satisfaction of the often increasing material and cultural needs in the entire society to the maximum with the method to constantly increase and improve socialist production on the basis of high technology.

Sixth, the fundamental principles in Marxist reproduction theory were effective to the capitalist social formation. Moreover, any socialist society would not work if it did not apply these principles in planning its national economy.

And so on.

The several principles above can be said to be the basic points in traditional socialist economic theory and the theoretical explanations to traditional socialist economic system. The complete domination of public ownership system, the expulsion of market, the limitation of commodity production and exchange, the derogation of the role of the law of value, almost no incentive mechanism, and self-closeness became the main characteristics of traditional socialist economic system and theory. At the time only the Soviet Union had the experience in socialist construction in the world. And because the World War II ended only not long before, Stalin enjoyed great personal prestige and personality cult on him prevailed. As a result, many people regarded Stalin's *Issues on the Socialist Economy in the Soviet Union* as scientific summarization to the experience of the Soviet Union in socialist construction. They saw it as a classic in Marxism and believed it firmly.

In the great trend of studying in Stalin's *Issues on the Socialist Economy in the Soviet Union* in the 1950s, the circle of economics in China became very interested in the basic economic principles of socialism in the book. The first reason to this was that it was very necessary to make discussion and exploration on how basic economic principles of socialism should play their role under such condition that China was still in the period of New Democratism in which various economic sectors coexisted. The second reason was that people felt that basic economic principles were something new. Before this, they only knew that Engels discussed in *Anti-Dühring* that the law of value was the basic principle of commodity production. They never saw any other statement made by the authors of the classical works on basic economic principles of socialism. So from 1953, the circle of economics in China started to discuss the issue of the basic economic principles in China during the transitional period. This issue included the question how the basic economic principles of socialism should play its role in China during the transitional period. And it became the No. 1 hotspot topic and the focus of attention in the circle of economics at the time because there were different opinions on it so that a debate occurred.

2 Three Different Main Views

The discussion on the issue of the basic economic principles during the transitional period in the circle of economics in China in the 1950s was triggered by an article entitled *Several Economic Laws and Principles in China during New Democratism*, written by Wang Xuewen, an old generation economist, on the magazine *New Construction* in October 1953. In 1954, Su Xing published an article entitled *On the Issue of the Role of Basic Economic Laws and Principles of Socialism in China during the Transitional Period* in the fourth issue of the magazine *Study*. He proposed opinions different from those in Wang Xuewen's article. Then more and more influential economists participated in this debate which lasted for about three years. A large number of articles were published in newspapers and magazines to discuss this issue. During this period, *Economic Research Journal* started publication in April 1955. From the beginning of its publication, the magazine published articles discussing this area in succession. The first article in its inaugural issue was written by Luo Gengmo, the then vice director of the State Development Planning Commission, and entitled *On the Issue of Basic Economic Laws and Principles in China during the Transitional Period*.

There were three different main views in such discussion.

The first type of view was represented by Wang Xuewen. He believed that, now that there were several (or, in fact, five) economic sectors in China during the transitional period, each economic sector should have the main economic laws and principles that determined the main processes and aspects that governed such economic sector. He made specific analysis on the main economic laws and principles of various economies, namely state-operated economy, cooperative economy, individual economy, capitalist economy, and state capitalist economy, and gave representations to these laws and principles. His representation included both the production purpose of an economic sector and the means adopted to achieve such purpose. For example, the main law and principle of individual economy was "to adopt methods that can initially improve production technology to endeavor to develop and improve production so as to supply and meet the increasing material and cultural needs of themselves and the market." The main law and principle of capitalist economy was "to adopt the methods of exploiting proletariat, peasant and handicraft worker and other methods on the basis of advanced technology to develop capitalist production and ensure the maximal profit." The main law and principle of state-operated economy was "to adopt the method of constantly increasing and improving production of socialist nature on the basis of advanced technology to ensure satisfying the often increasing material and cultural needs in the society to the maximum."¹ He also believed that basic economic law and principle was an independent epochal socioeconomic law and principle and, as China still did not have an independent social formation at present, its current economic conditions could not form a single basic economic law and principle.²

¹See Wang (1953).

²See Wang (1954).

The second type was represented by Luo Gengmo. He believed that the basic economic principles of socialism were the basic economic principles of the entire Chinese society during the transitional period. His main view was like this: “At present, our country is still in the transitional period. Its society is still a transitional society. It is not an ‘independent and epochal’ society or a socialist society that has already been formed. It basically contains three types of economies: state-operated economy, namely socialist economy, capitalist economy and individual economy. Each of these three economies has its own basic economic principles. (Comrade Wang Xuewen called it ‘main economic principle’.) Because state-operated economy is the most powerful among these three economies, which does not refer to its proportion in national economy, it takes the dominant or leading position. So the basic economic principles of socialism are, (rather than ‘will become’ or ‘has already become’), the basic economic principles in the transitional society in China.”³ Such view proposed by Luo Gengmo won the support of some economists.

At the time, famous economists Wang Sihua, Xu Dixin, Wang Ya’nan and Qian Jiaju all had such view. For example, Wang Sihua said, “During the transitional period, socialism controls the key branches of economy. Thus as socialist elements constantly increase and develop, the basic economic laws and principles, which determine new production purposes, gradually expand its range of action in national economy and exert increasing influence on the development of the entire national economy. Therefore, what determines all the main aspects and processes in the development of the entire social production in China during the transitional period is the basic economic laws and principles of socialism. However, because the presence of small commodity economy and capitalist economy, the law of value and the law of surplus value still have their place of action at present. So the range of action of the basic economic laws and principles of socialism is still subject to certain limitation.”⁴

The third type of view was represented by Su Xing and Wu He. They believed that, now that there were both capitalist and socialist production modes during the transitional period, the basic economic principles of socialism and capitalism both functioned in China during the transitional period. Su Xing said, “During the transitional period, China does not have an independent social formation. So now there cannot be a single basic economic law and principle that determines all main aspects and processes of all social productions. However, because there is socialist economy which takes the leading position during the transitional period, the basic economic laws and principles of socialism have already become the laws and principles that play a dominant role in the entire national economy.” “Meanwhile, because of the presence of capitalist economy, there are still the basic economic laws and principles of capitalism in China, which include the law of surplus value, one that fits the concept of the basic economic laws and principles of capitalism the best. But the scope of action of this law has been increasingly confined. And as economic conditions change, it will gradually lose its effect and leave the stage.”⁵ Moreover, Xu He said,

³See Luo (1955).

⁴See Wang (1955)

⁵See Su (1955).

“China still does not have an independent social form at present.” “There are only two types of economic sectors that have formed independent social forms among five of them, namely socialist economic sector and capitalist economic sector.” Therefore, the basic economic laws and principles of socialism and capitalism coexisted in China during the transitional period.⁶

Lin Lifu held a view similar to them. He believed that “There are only three types of basic economic laws and principles that respectively determine the five types of economic sectors in China at present, namely socialism, private capitalism, small commodity production, state capitalism and cooperative economic sector. These are the basic laws and principles of socialism, capitalism and small commodity production. Because the production modes of state capitalism and semi-socialist cooperative are both transitional social forms of production that do not have their own inherent, independent and special basic economic laws and principles, they can only be governed respectively by the basic economic laws and principles of socialism, capitalism and small commodity production.”⁷

3 Several Comments

First, the discussion on the issue of the basic economic principles during the transitional period in the Chinese circle of economics in the beginning and middle of the 1950s was the first discussion of the circle of economics in China on hotspot issues in economy after the founding of the People's Republic of China. And clearly different views were formed in the discussion and scholars argued with each other, directly identifying their opponents by name. A situation in which many academic schools contended with each other was formed initially. This event created a good opening for the academic discussion in the circle of economics in China. For example, after Wang Xuewen, one old generation economist, published his article, Su Xing, a young teacher in the China Renmin University, published an article to propose different views. Then the scholars took turns in argumentation. Wang Xuewen wrote an article to defend his view. And Xu He, another young teacher in the China Renmin University, wrote an article to support Su Xing's opinion. After that, many famous economists in China joined the debate and wrote articles to propose their own views. A wave of heated discussion was soon formed. Although their opinions were different, the scholars carried out the discussion in an even-tempered, good-humored, equal and reasonable manner. Thus, a good atmosphere was established and a group of promising young economists emerged.

Second, the discussion was closely related to the national situation in China. In this discussion, all the articles involved started from the transitional period in which China developed from New Democratism to socialism and also from the situation that there were five economic sectors in China, namely state-operated economy, private

⁶Xu (1954).

⁷Lin (1955).

capitalist economy, individual economy, semi-socialist cooperative economy, and state capitalist economy and that state-operated economy played a dominant role. These articles discussed the issue on the basic economic principles in China during the transitional period on the basis of the basic principles of Marxism. The authors did not show any bad tendency to take ready answers from the writers of classics or to copy and apply mechanically the statements available from the writers of classics.

Third, the idea that showed the eagerness to transform to socialism also emerged in the discussion. In the beginning and middle of the 1950s, China was in the development stage of New Democracy or in the stage of the transition from New Democracy to socialism, in which five economic sectors coexisted. In the early period of The People's Republic of China after its foundation, people conceived that such a stage might last more than a decade. But soon ideas and practices that showed eagerness to complete transition emerged. This reflected that the view that advocated that the basic economic principles of socialism was the basic economic principles in China during transitional period prevailed in the discussion on the basic economic principles during the transitional period. Such a view won the support of more influential economists and became the mainstream. Now it appears that China's transition was made in a pace too fast with too many rash requirements, which caused many sequelae. If the time of transition could have been longer and socialist transformation could have been completed at a steadier pace, it could have brought more benefits to the development of socialist economy in China.

Fourth, the discussion laid initial foundation for further discussions on relevant issues in the future. Basic economic principles mainly provided answers to the question on the purpose of social production. The discussion provided many valuable insights and materials for other discussions in the future, such as the study and discussion on the basic economic principles of socialism in the 1960s, and the discussion on how to realize people-oriented development after the beginning of the 21st century. To certain extent, it can be said that the several discussions later were the continuation, deepening and development of the discussion on the basic economic principles in China during the transitional period in the beginning and middle of the 1950s.

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Chapter 2

Exploration and Argument on the Relationship Between Planning and Market and the Issues of Commodity and Value in the 1950s



Zhouyuan Zhang

1 The Raising of the Questions

The issue on the relationship between planning and market in socialist economy, which contains the issues on commodity production under socialist system and the law of value, is the question in economic theory with which Chinese economists have had the most discussion, made the most intense argumentation, and produced the most remarkable research results since the founding of the People's Republic of China. From the 1950s when far-sighted and insightful economists in China courageously broke through traditional socialist economic theories and proposed novel and original innovative opinions to the time after 1990s when the theory on socialist market economy was gradually established, relevant exploration and discussion lasted for over 50 years and formed a process full of twists and turns in which people approached the truth step by step. After China started to implement reform and opening up at the end of 1978, the theory on socialist market economy gradually became the common understanding of the circle of economics and other social circles in China, driven by the great trend of reform and the rapid takeoff of national economy. The theory on socialist market economy is the main theoretical pillar of China's reform and opening up. It is an important component of the theoretical system of socialism with Chinese characteristics and also the important contribution of the Chinese circle of economics to the treasure house of economic science.

When looking back at the study and discussion on the issue of the relationship between planning and market during over 60 years, people will notice that the development of the study on this issue underwent several stages. And these stages all conformed to the development of China's undertakings in socialist construction, to the constant exploration for better economic system and development road on the basis of gradual accumulation of practical experiences, and to the improvement

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of economic policies. The origin of theory is in practice, but theory has enormous reaction on practice. Various theoretical views published in the process of the discussion on the issue of the relationship between planning and market exerted important influence on China's practice in socialist construction. When viewed from such influence, such reaction was basically positive. But there still were some wrong views that played a negative role.

In the discussion, many papers and treatises closely related to the reality in China's socialist construction under the guidance of Marxism. The authors of these works carried out investigation and research on the questions that people faced in reality, drew from foreign experiences and lessons, and gradually made comprehensive and deepened analysis on the substance of economic phenomena and processes. In this way, they made conclusions that relatively conformed to objective reality. And their conclusions exerted positive influence on the practice in socialist economy and made contribution to the construction and development of the part on socialism in political economics.

However, some works with wrong views were also published. These works started with book worship and disregarded lively economic practice or they followed certain wrong ideological trends and misinterpreted economic practice. They exerted negative influence on practice. The main part or a large amount of the wrong opinions on the issues on the relationship between planning and market and on commodity and value were such left-deviated views that negated to different extents the necessity of commodity production under socialist system, the role of market, and the role of the law of value.

Stalin's book *Issues on the Socialist Economy in the Soviet Union* reflected to a large extent the experience of the Soviet Union in socialist economic construction during over 30 years. It has certain meaning in the intellectual history of political economics. Stalin recognized the objectivity of economic principles, the necessity of commodity production and exchange in socialist economy, the fact that the law of value was a "very good school of practice", and so on. But at the same time, such book also contains some assertions that are incorrect or inconsistent with reality. For example, it claims that the means of production exchanged inside the whole people ownership system are in fact not commodity and that the law of value only plays the role of influence and not of regulation in socialist production. And it expels market mechanism. These ideas confined the thought of the people and restrained the reform in economic management system over a long period of time. The Chinese circle of economics advanced step by step in the exploration on the issue of the relationship between planning and market in socialist economy. As a result, the theory on socialist market economy was established. These achievements were obtained through breaking the boxes in traditional socialist economic theories represented by the book *Issues on the Socialist Economy in the Soviet Union*.

In the following, the author intends to make a brief review on the study and discussion of the circle of economics in China on the relationship between planning and market and on commodity and value in the 1950s.

2 The First Wave of Heated Discussion Arising in 1956 and 1957

The first great wave of the discussion on the issues of the relationship between planning and market and of commodity and value under socialist system in the Chinese circle of economics occurred in 1956 and 1957 around the time when the Three Major Transformations were basically completed. At the time, the economic relations in the entire society were undergoing important changes and socialist economy gradually became the sole economic basis of the entire society. What was popular in the first few years in the 1950s was the theory that used the coexistence of multiple economic sectors to interpret the existence of commodity production and exchange. This theory faced the challenge from the economic life in reality. And economists were confronted with important theoretical research questions that needed to be studied and solved, such as whether commodity production and exchange were compatible with socialist productive relationship, what was the relationship between commodity production and socialist public ownership and distribution according to performance, and what were the changes and characteristics in the role of the law of value, the essential law of commodity production. Thus heated discussion on these questions arose. At the time, discussion was made centering round the objective necessity for the existence of socialist commodity production and the issue on the relationship between planned economy and the law of value. On October 28, 1956, Xue Muqiao published an article entitled *Planned Economy and the Law of Value* in *People's Daily*, which lifted the curtain on the discussion.

At the time, what dominated was the views in Stalin's book *Issues on the Socialist Economy of the Soviet Union*. Namely, it was believed that the coexistence of two types of socialist public ownership was the reason what socialist commodity production existed. With the establishment of socialist public ownership, the principle of the planned and proportionate development of national economy became the regulator of production. The means of production even got out of the "range of the action of the law of value".¹ This was the so-called "substitution theory". As the scope of planned management expanded, the range of action of market and the law of value would be further limited. This was the so-called "limitation theory". In addition, some believed that, when the action of the principle of planned development grew strong, the action of the law of value would become weak and, when the action of the law of value grew strong, the action of the principle of planned development would become weak. This was the so-called "opposite growth theory". The popularity of these views was compatible with the practice of China in following the Soviet Union in establishing economic system.

During the same period, there were some articles that broke the boxes of traditional socialist economic theories and clearly proposed some opinions that were proved correct in practice later.

¹Joseph (1962).

The first of such opinions was proposed by Sun Yefang in 1956, who believed that planning should be placed on the basis of the law of value. Sun Yefang held that the basic content and role of the law of value, namely to promote the development of social productivity through determining value with the amount of average socially necessary labor and to regulate social production or distribute social productivity, existed in both socialist and communist societies. In the commodity economy under private ownership system, the law of value played its role and expressed itself through commodity circulation and market competition. So it had destructiveness. In planned economy, people should spontaneously master it through calculation. He emphasized that China's plans to develop socialist economy had to be based on the law of value. Thus, Sun Yefang raised the role of the law of value in socialist economy to an unprecedented height and opened up a broad horizon for people to understand this question.²

The second of such opinions was proposed by Gu Zhun in 1957. In a paper that he published, he proposed that socialist economy was the contradictory unity between planned economy and economic accounting. The law of value regulated social production through economic accounting. The practice of such regulation at its maximal limit was "to form very close connection between the material reward of workers and the degree of profit and loss of an enterprise and to make price the main instrument to regulate production. Because an enterprise will spontaneously pursue productions that can bring more profitable prices and prices will have spontaneous rise and fall, such rise and fall will actually regulate production. Meanwhile, the entire society will have a unified economic plan. But this plan includes 'some forecasts rather than being the integration of particular plans'. So it has more elasticity and tends to stipulate on some important economic indexes and reduce its specific stipulations on the economic activities of enterprises."³ This means to advocate fully utilizing the regulatory role of the law of value on socialist economy. It is the essential element of socialist market economy to regulate production through the spontaneous rise and fall of price. In this sense, it can be said that Gu Zhun was the first person who advocated the theory on socialist market economy in China.

The third of such opinions was proposed in some articles that started with the view that there were the principles and relations of material interests in socialist society. These articles discussed the reasons why there were commodity relations inside socialist society and, in particular, whole people ownership system and thus affirmed that the means of production exchanged inside the whole people ownership system were also commodities.⁴

The fourth of such opinions was proposed by Chen Yun who advocated the idea of utilizing market regulation in socialist planned economy. In his speech at the Eighth CPC National Congress, he said, "As to the aspect of production planning, the main part of the industrial and agricultural products nationwide is produced according to plans. But at the same time, part of the products has been produced freely on the basis

²See Sun (1956).

³See Gu (1957).

⁴See Nan and Suo (1957).

of market change and within the scope allowed by state plans. Planned production is the main part of industrial and agricultural production and free production is the supplementation to planned production on the basis of market change and within the scope allowed by state plans. Therefore, the market in our country will definitely not be a free market of capitalism but a unified market of socialism. In a unified market of socialism, state market is its main body but it is attached with a free market under the leadership of the state acting within certain scope. Such free market becomes supplementation to state market under the leadership of the state. So it is a component of the socialist unified market.”⁵

3 Several Comments

In the introduction above, the readers might be delighted to see that, when China’s socialist planned economic system was just established, some economists already proposed that people should handle well the relationship between planned economy and the law of value and correctly address the role of commodity production and market. This indicates that some economists found very quickly at very early time the defects of planned economic system characterized by high concentration. For example, because of the joint state-private ownership in enterprises, factories wanted to produce more and faster. If there was a diverse product line, they needed to change machinery and raw material more often and production would become smaller and slower. Some factories always tried to save the trouble and only produced popular goods with dependable quality regardless of the needs of consumers. Then the problems of lowering commodity quality and reducing diversity occurred. The root cause of such problems was the unified purchase and sale system in the planned economy in which products of superior quality were not sold at better prices and thus the law of value was violated. As a result, there were some among both economists and CPC and state leaders who became aware of the necessity to respect the law of value and utilize market regulation to improve economic management.

Second, the issues on the relationship between planning and market, the relationship between planned economy and the law of value, and the value of commodity in socialist economy are the crucial questions in the theory and practice of socialist economy. The circle of economics in China identified these crucial issues in the very beginning and carried out study and exploration on it. Many foresighted opinions were proposed. This indicated that Chinese economists were insightful, well-trained and praiseworthy. Of course, traditional socialist economic theory was still the mainstream at the time. Some original thoughts of the economists were influenced by it. But the roles of “prophet” of some economists were not to be obliterated.

⁵ *Collected Works of Chen Yun*, Vol. 3, People’s Publishing House, 1995, p. 13.

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Chapter 3

The First Symposium on the Theories of Economics of the People's Republic of China in April 1959



Zhouyuan Zhang

1 The Reflection on the Negation of Commodity Production and “Equalitarianism and Indiscriminate Transfer of Resources” in the People's Commune Movement in 1959 and 1960

In the People's Commune Movement in 1958, the “communism fad” characterized by “equalitarianism and indiscriminate transfer of resources”, which negated commodity production and the law of value, swept the countryside in China. In the industrial area, people propagandized the “great campaign of smelting steel” without proper calculation on labor and cost, only considering the effects in politics regardless of economic effects. Under such a situation, a group of documents and papers that preached the strange and preposterous arguments and theories emerged within a few months. The prominent ones were the idea of Chen Boda that negated commodity production and exchange¹ and the article *Breaking and Removing the Thought of Bourgeois Rights*² published by Zhang Chunqiao, negating distribution according to performance.

At the end of 1958, the Sixth Plenary Session of the Eighth CPC Central Committee timely criticized the view that negated commodity production and the law of value. It was specifically pointed out that “To continue developing commodity production and to continue to retain the principle of distribution according to performance are two important principle issues in the development of socialist economy. People must unify the understanding of the entire Party. Some people sought to ‘enter communism’ too early and, at the same time, sought to abolish commodity

¹See Su (2007).

²*People's Daily*, Oct. 13, 1958.

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production and exchange too early and negate the positive role of commodity, value, currency and price too early. Such idea is harmful to the development of socialist construction and thus is incorrect.”

In March 1959, Mao Zedong pointed out, targeting the “communism fad” characterized by “equalitarianism and indiscriminate transfer of resources”, that, only through calculation, could people practice the law of value which existed objectively. “This law is a great school. Only through utilizing it can we teach our cadres in millions and our people in hundred millions and can we build socialism and communism. Otherwise, nothing is possible.” This assertion proposed by Mao Zedong represented an important turning point in the study on the issues of commodity and value in socialism in the circle of economics in China.

From then on the study on the issues of commodity and value in the circle of economics quickly turned from criticizing the “communism fad” to the discussion on the issues about the historical status and role of commodity production in socialism and why the law of value was a great school.

2 The First Symposium on the Theories of Economics of the People’s Republic of China Held in Shanghai in April 1959

It was under the circumstance mentioned above that the Institute of Economics of the Chinese Academy of Sciences, namely the present Institute of Economics of the Chinese Academy of Social Sciences, and the Institute of Economics of the Shanghai Academy of Social Sciences initiated the largest symposium on the theories of economics since the founding of the People’s Republic of China, which was held in Shanghai and lasted for twenty days from April 3 to 22 in 1959. 245 economists attended the symposium and 77 papers and investigation reports were submitted, which mainly discussed the issue on the roles of commodity production and the law of value in socialism. This meeting was of unprecedented scale and tremendous influence. It raised the great wave of discussion on the issues above.

On June 1, 1959, the *People’s Daily* published a news report on the First Symposium on the Theories of Economics of The People’s Republic of China in 1959, entitled *Letting One Hundred Schools of Thought Contend to Achieve Joint Improvement*. It reads as follows:

“*People’s Daily News*: The Institute of Economics of the Chinese Academy of Sciences and the Institute of Economics of the Chinese Academy of Social Sciences recently held a symposium on the theories of economics in Shanghai, discussing the issues of commodity production, the law of value and piece rate wage under socialist system. Altogether 245 people attended the meeting, including the workers on economics theories from the research organs of economic science in various provinces and municipalities and from the departments and schools of economics in higher education institutions and workers on economy and on economic theories from

state economic departments and competent departments in various CPC committees. 54 papers and 23 investigation reports were contributed to the symposium.”

“The symposium focused on discussing three questions related to the commodity production and the law of value under socialist system, namely the self-sufficient and commodity productions of the people’s commune, the three types of exchange relations under socialist system, and the role of the law of value under socialist system. (See the seventh page in today’s newspaper for the main content of the discussion.)”

“In the past, the circle of economics of our country discussed over a long period of time on the issues of commodity production and the law of value under socialist system. In addition, some preparations were made before the symposium. The comrades who were to attend the meeting carried out study and research on the issues to be discussed at the meeting beforehand. They made surveys and investigations in state-operated enterprises and the people’s communes in the countryside and submitted investigation reports. They compiled and printed related materials and wrote papers on the basis of them. And they also made discussions in various regions and organizations.”

“The comrades who attended the meeting believed that certain achievements were made both in theory and in the study of style at this symposium. The main reason to this was because the meeting implemented the policies of combining theory with practice and of letting one hundred schools of thought contend. The issues discussed in this meeting, such as commodity production, the law of value and piece rate wage under socialist system, were all important questions in the economic life in reality currently in China. They were also important questions in the part on socialism in political economics. It is of great importance to carry out academic discussion and exploration on these issues for correctly handling contradictions among the people in the area of economic relations and mobilizing the initiative of the people in the city and the countryside in building socialism, for consolidating people’s communes in China and further improving and developing the production relations inside people’s communes, and for further improving the standard of the work in the planning and management of national economy. It also plays a positive role in summarizing in theory the experiences of socialist construction in China and improving our theoretical standard.”

“The comrades who attended the meeting believed that this symposium showed very active atmosphere in free discussion. Various academic opinions were fully expressed. People made great efforts to convince their opponents with scientific demonstration and carried out debates in a delightful mood. Through discussion and debate, they took each other’s strengths to make up for their own shortcomings. They either revised or strengthened their own arguments. All of them achieved improvement in different degrees.”

The economists who attended this symposium and make speech at the meeting included Xue Muqiao, Sun Yefang, Yu Guangyuan, Wang Xuewen, Luo Gengmo, Wang Sihua, Huang Yifeng, Wang Yanan, Yong Wenyuan, Jiang Xuemo, Fan Hong, Gu Shutang, Yao Nai, Yang Jianbai, Guan Mengjue, Zhu Jiannong, Song Zexing, Qi Qisheng and Deng Kesheng.

After the symposium, the Institute of Economics of the Chinese Academy of Sciences edited the book *A Compilation of the Papers and Materials on the Symposium in April 1959 on the Issues of Commodity Production and the Law of Value under Socialist System* (1959 Edition). It was published by the Science Press in a length of 1.27 million Chinese characters.

3 Some Important Common Understandings Achieved at the Symposium

Through this symposium, people achieved agreements on the following several questions.³

First, China was a country with much undeveloped commodity production. China had too little commodity economy rather than too much. Its commodity economy was not only inferior than developed capitalist countries but also more backward even than India. China's rural population, which accounted for 80% of its population nationwide, led a semi-self-sufficient life. As social productivity developed in China, division of work became more and more detailed and production showed an increasing degree of specialization and socialization. In the end, such development would manifest itself as the development of commodity economy. The development of commodity production in the present stage was first a major issue in which the working class united with five hundred million peasants in China to build socialism. As far as a people's commune is concerned, various units inside it also needed to develop commodity production and exchange while it developed commodity production to carry out exchange with the state and other communes.⁴

Second, commodity production existed from the late primitive commune period to socialist society. But the social nature of commodity, namely the relationship between people which was embodied by commodity, and the status and role of commodity production in the economic life in the society were different in different periods. In his paper submitted to the symposium, Yu Guangyuan said, "What is the characteristic of commodity exchange as a mode of exchange? In a word, it means that two parties in equal status compare in exchange the socially necessary labor crystallized in the value in use to be exchanged and practice the principle of exchanging an amount of labor with an identical amount of labor. Any exchange carried out in such a mode is commodity exchange. And the products that entered such a type of exchange are commodities."⁵ He also pointed out specifically that the exchanges between the two types of public ownership systems under socialist system, between state-operated enterprises, and between the society and an individual were all commodity relations.

Third, people should all admit and respect the role of the law of value and adhere to the principle of exchange at equal values. In particular, when handling the economic

³See Sun et al. (1979).

⁴See Xu (1959).

⁵See Yu (1959).

relations with collective ownership system, people had to oppose “equalitarianism and indiscriminate transfer of resources”, practice exchange at equal values, and do pricing and accounting between the state and communes and between various levels inside a commune. Besides, they should recognize that the law of value played a regulatory role in collective ownership economy. When directing the production in collective economy and arranging the tasks in sale by state quota, they need consider such regulatory role.⁶

Fourth, the law of value was a great school indeed. The reasons were as follows: First, people could learn from it how to correctly handle contradictions among the people from economic relations. Second, people could learn economic management. In the exchange relations between the state and commune, between communes, and inside a commune, people practiced exchange at equal values for the purpose of retaining and encouraging the initiative of economic production in collective ownership system. In the exchange relations between the state and employees, people practiced exchange at equal values for the purpose of correctly implementing the principle of distribution according to performance. In the exchange relations between state-operated enterprises, people practiced exchange at equal values for the purpose of ensuring that the labor consumed in production could be rewarded, of carrying out reproduction, and of strictly implementing economic accounting system.

Fifth, people had to make full use of the function of the law of value and let it serve for socialist planned economy. The law of value could be utilized by the state as one of the bases for formulating national economic plans. It could be utilized to influence the quantities of some products in production and sale and to function as supplementary means for carrying out regulation through state planning and achieving the balance between supply and demand. It could be utilized to organize economic accounting and improve the effect of economic activities. And it could be utilized as the instrument for the distribution and re-distribution of national income, and so on.⁷ Some economists further stated that the true role of the law of value was exhibited in its positive functions of improving labor productivity and promoting production. The main issue that we faced today was not how to prevent its negative and destructive effect but how to bring into playing its positive effect in promoting production as much as possible.⁸

Sixth, the law of value and the principle of developing national economy in a planned and proportionate way were not mutually repelling, restrictive or destructive. When organizing economic activities, including formulating plans, the state should fully consider the roles of both the principle of planned development and the law of value. This was because these two principles acted simultaneously in real life. As long as there were economic conditions on which certain economic principle depended to exist, such principle would act. It would not stop acting because of the existence of other economic principles. The state might stipulate the prices of various commodities according to the principle of developing national economy in a planned and proportionate manner. But when determining the planned prices of

⁶See Zheng (1959).

⁷See Xue (1959).

⁸See Wang (1959).

various kinds of products, the state still could not stop estimating and utilizing the action of the law of value. Similarly, the state needed to determine the proportions between various departments in national economy on the basis of the principle of developing national economy in a planned and proportionate manner. But this did not mean that, when carrying out regulation through state planning on the production and circulation of commodities, the state could stop considering the law of value. If the law of value was regarded as being in a subordinate status, such practice would result in the failure to correctly estimate and utilize the action of the law of value in practical work.⁹

Seventh, now that the law of value was an objective economic principle, there were no positive or negative roles in the law of value itself. It can only be said that, on what condition the action of the law of value was favorable to people or on what condition it was unfavorable. Moreover, the law of value itself did not have the distinction between spontaneous action and conscious action. A principle was objective so that it acted on a spontaneous basis permanently. The only difference was whether people could recognize it and whether there were conditions to utilize it to achieve a predetermined goal.

It should be said that the views above were all obtained from the study on the lessons in the economic construction work in 1958. These were spiritual wealth obtained at enormous price and therefore very precious. In the practice later, these views were proved to have both theoretical and practical values. They not only further enriched Marxist economic theory but also played an important instructive role in China's socialist construction. Besides, it should also be pointed out that opinions different from the mainstream views above were also fully expressed at the symposium so that a situation of letting a hundred schools of thought content was formed.

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⁹See Institute of Economics of the Chinese Academy of Sciences ed., *A Compilation of the Papers and Materials on the Symposium in April, 1959 on the Issues of Commodity Production and the Law of Value under Socialist System*, Science Press, 1959, pp. 9–10.

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Part II
The Peroid of 1966–1976

Chapter 4

The Economic Views of Sun Yefang and Others Were Taken as “Revisionism” and Condemned in “Mass Criticism”



Jun Wan

1 Sun Yefang Was Labeled the “Greatest Revisionist in the Chinese Circle of Economics” and Criticized Harshly

The decade from 1966 to 1976 was a period full of bitter and painful memories in the history of The People’s Republic of China. It not only caused tremendous damage to economic construction and social development but also resulted in a standstill period of the study in economics. *The Resolution of the Sixth Plenary Session of the Eleventh of the CPC Central Committee on Several Historical Issues of the Party from the Foundation of the State* pointed out that the mistake that occurred in the period of 1966 to 1976 was a “serious global left-deviation mistake over a long period of time”. During that time, the thought trend of left deviation became extremely inundant and many absurd theoretical views were faddish. Some famous economists were ruthlessly criticized as being wrong in the realm of principle or guideline. Many economic research institutions were dissolved and researchers were transferred to lower levels for tempering through labor. The development of economics fell into a low point.

Soon after the founding of the People’s Republic of China, the country quickly completed its transition from new democratic revolution to socialist revolution. Socialist system was basically established in China. After socialist transformation was basically complete, China’s economic construction showed rapid development for a moment. The Eighth CPC National Congress believed that, with the establishment of socialist system, the main contradiction in China was not the contradiction between working class and bourgeois any more but the contradiction between the quickly-developing economic and cultural needs of the people and the situation that current economic and cultural conditions could not meet the people’s needs.

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The main task of the people nationwide was to concentrate forces and resources to develop social productivity, to realize the industrialization of the country, and to gradually meet the increasing and growing material and cultural needs of the people. Although class struggle still existed and people still needed to strengthen the people's democratic dictatorship, the essential task already became to protect and develop productivity under new productive relations.

However, because the CPC did not have sufficient experience in leading socialist undertakings, subjectivist deviation occurred in its understanding on China's national condition and its analysis on the situation in and outside China so that left-deviated thoughts constantly arose and the correct line determined in the Eighth CPC National Congress was quickly abandoned. The CPC supreme leader proposed the theory of continuing revolution under the dictatorship of the proletariat. It was believed that class, class contradiction and class struggle still existed in the entire socialist stage. The main contradiction in Chinese society was still the contradiction between proletariat and bourgeois. The class struggle between proletariat and bourgeois and the struggle between the two roads of socialism and capitalism would always be present. The danger of the restoration of capitalism would also always exist and become the source of the revisionism that emerged in the CPC. According to this theory, proletariat had to continue its revolution after the establishment of socialist system. The socialist revolution in the economic front alone was not sufficient for this and it was not so solid. There had to be the thorough socialist revolution in the political and ideological fronts. Under the guidance of such wrong theory, various left-deviated thought trends prevailed and grew even stronger. Many things that did not possess the inherent properties of socialism or that were applicable only to particular historical conditions were taken as "socialist principles" and adhered to. Many things that were favorable to the development of productivity and the commercialization, socialization and modernization of production were taken as "capitalist factors" and opposed. Extreme left-deviated ideology mistook rigidly following dogmatism as maintaining the purity of Marxism and the expansion and absolutism of class struggle as defending socialist system. From 1966 to 1976, extreme left-deviated thought and line reached its pinnacle.

Before 1966, some economists in the China already started to notice the bad influence of dogmatism and the thought trend of left deviation to China's economic construction and the study in economics. And they criticized traditional economic theories and systems from different perspectives. The representative one among these economists was Sun Yefang, the then director of the Institute of Economics of the Chinese Academy of Sciences. Sun Yefang was not only a pioneer in the Chinese circle of economics who advocated economic system reform the earliest but also a scholar who explored the system of socialist economic theory the earliest and the most deeply. In the late 1950s and early 1960s, he published a series of articles and research reports such as "Place Planning and Statistical Work on the Basis of the Law of Value", "Starting from Gross Output Value", "People Must Learn Some Philosophy to Understand Economics", "On Value" and "Profit Indexes in the Management System of Socialist Planned Economy". With huge courage to upholding his own theory, he challenged traditional highly-centralized economic management system

and the system of economic theories and proposed reform plans with clear targets and a system of socialist economic theories with unique features.

Sun Yefang's views in theory posed serious challenge to traditional socialist economic theories. In a background that thought trends of left deviation prevailed at the time, his view was naturally criticized harshly. From October, 1964, the work team of the "Four Clean-Ups" of cleaning up politics, economy, thought and organization entered and started to work in the Institute of Economics. Sun Yefang was labeled the "biggest revisionist in the Chinese circle of economics". He was removed from office and transferred to the countryside for labor reform.¹ After 1976 started, Sun Yefang was criticized nationwide as the "leading figure of the anti-party, anti-socialist, anti-Mao Zedong Thought black line in the circle of economics". In the famous editorial published in the beginning of 1966, it was pointed out with Sun's name clearly identified that, "in the circle of economics, Sun Yefang proposed a full set of revisionist fallacy. They opposed letting the Mao Zedong Thought and politics take command and advocated letting profit and money take command. They sought to change socialist productive relation and turn socialist enterprises into capitalist enterprises." After that, the criticism and prosecution on Sun Yefang kept upgrading. He was arrested and imprisoned in April 1968 and held in the Qingcheng Prison for seven long years.² Under the slogan of "opposing capitalist academic authorities", a group of famous economists were criticized and prosecuted.

2 The Wrong Criticism of Sun Yefang's Theoretical Views

The criticism of Sun Yefang's theoretical views concentrated on the following aspects:

I. It Was Believed that Sun Yefang's View that People Should Respect the Law of Value in Socialist Economy Was "Sabotaging Planned Economy"

Sun Yefang broke through the set patterns of traditional theory in political economics and believed that value and the law of value was inherent to socialist economy. "Of all kinds of economic laws and principles, the law of value was the primary one." He advocated that planning and statistical work should be established on the basis of the law of value. He believed that, in socialist economy, it was the manifestation of the important role of the law of value to promote the development of socialist social productivity through understanding and calculating the amount of average socially necessary labor. Therefore, the law of value should not be repelled. Rather, more importance should be attached to it.

However, critics insisted on expelling market mechanism and the law of value in socialist economy and harshly scoured Sun Yefang's view of valuing and stressing

¹Deng and Sun (2006).

²Mao (1998).

on the law of value. “His reactionary economics started with ‘things with commonality’ between capitalism and socialism.... The so-called ‘things with commonality’ that Sun Yefang found out, racking his brains, were value and the law of value. On such basis he built his ‘system of political economics’ with ‘letting profit take command’ as the kernel.”³ In the eyes of his critics, the operation of national economy was mainly dominated by the principle of developing in a planned and proportionate manner in socialist economy. Although the law of value had certain influence, it did not play a regulatory role in production and it was not the most fundamental economic law as its role was strictly limited. They believed that “to place planning on the basis of the law of value and to take the general line of socialist construction as the basis are two radically opposite lines of construction.” Sun Yefang required that socialist planned economy should be built on the basis of the law of value. It meant to raise the law of value to a status of dominating everything and let it play the “role of regulator” spontaneously and blindly. Thus capitalist economy would run rampant so that the entire society would fall into competition and anarchy and into the swamp of capitalist “liberalization” and that socialist planned economy would end up in annihilation. Now that the negative role of the law of value was so obvious, “we resolutely oppose taking the law of value as the basis for regulating production and for formulating plans. There is one common feature when modern revisionists try to restore capitalism in economy. Namely, they will do their best to exaggerate the role of the law of value in theory and preach using the law of value to regulate and dominate the entire social production. Thus economic construction will be led from the socialist track of letting proletarian politics take command to the capitalist track of ‘letting profit take command’.”⁴

II. Sun Yefang’s Thought on Enterprise Reform Was Criticized as “Turning the Unified Socialist Whole People Ownership System into One After Another Independent Kingdom”

With respect to the problem that highly centralized management system imposed too much and too rigid control over enterprises so that they lacked vitality, Sun Yefang proposed the conception of reforming financial management system. He suggested that people could handle well the relationship between the centralized leadership of the state and the independent operation of enterprises through reasonably dividing the “big right” of the state and the “small right” of the enterprises. He advocated that the amount of capital value be used as the standard to divide the authority of state and that of the enterprises. The matters within the scope of expanded reproduction should belong to the “big right” of the state while the matters within the scope of simple reproduction should belong to the “small right” that the enterprises should take care of themselves. In this way, people could achieve the effect to controlling but avoiding rigidity and activating but preventing chaos.

³The Writing Group of the Jilin Provincial Revolutionary Committee, “The Class Struggle in Socialist Construction and the Area of Economics—Criticizing Sun Yefang’s Revisionist Economic Theory”, *The Red Flag*, Issue 2, 1970.

⁴Ibid.

However, in the eyes of his critics, Sun Yefang's reform suggestion on dividing "big right" and "small right" opposed the centralized and unified leadership of the CPC and the state on national economy. It "wants enterprises to detach themselves from the centralized and unified leadership of the state and declare independence and autonomy." Sun Yefang wanted the state to manage enterprises "by the single index of profit". This radically changed the socialist relationship in which an enterprise was subordinate to the proletariat country into an ice-cold capitalist relationship of pecuniary exchange. The whole of the socialist whole people ownership system was dismantled and fell into pieces immediately. Enterprises became independent kingdoms. Competition and production anarchy would run rampant. Socialist planned economy would turn into the free economy of capitalism. If these critics thought that Sun Yefang's reform suggestion was to engage in the restoration of capitalism, what kind of relationship between government and enterprise was an ideal model in their mind? "Thousands of enterprises under the socialist whole people ownership system have but one owner. It is the state of proletariat dictatorship under the leadership of the CPC. Only this country can represent the radical interests of the working class and the extensive community of working people. It decides on major matters and policies of an enterprise, on its development direction, on the production and distribution of its products, and on the disposal of its assets. The state implements democratic centralism on an enterprise. It takes big right in its own hands only and decentralizes small rights. It practices centralized leadership and leveled management. This is the requirement in consolidating whole people ownership system and proletariat dictatorship." "Each enterprise should establish the idea of considering every matter inside the whole picture of the nation. People should bear the global situation in the mind, look far ahead and aim high, understand critical matters, and care for overall situation.... 'They should do well in unifying understanding, policy, planning, command and action'. They should comprehensively complete and over-fulfill the plans of the state and build socialism in a greater, faster, better and more economical manner."⁵ Such enterprise management system, which seemed to conform to orthodox views, was exactly what, as Sun Yefang believed, needed to be reformed, the highly centralized traditional system that mixed up the functions of government and enterprise.

III. Sun Yefang's View on Profit Was Criticized as "Letting Profit Take Command"

Traditional political economics always took profit as an economic category of capitalism. This view made scholars in theoretical study feared to talk about the issue of profit when studying the issues in socialist economy. And enterprises dared not to talk too much about profit in their practice in operation and management. At the time, the practice of only making calculations in politics but not in economy once became prevailing. Because people did not consider cost accounting, great waste was

⁵The Writing Group of the Jilin Provincial Revolutionary Committee, "The Class Struggle in Socialist Construction and the Area of Economics—Criticizing Sun Yefang's Revisionist Economic Theory", *The Red Flag*, Issue 2, 1970.

caused in practical economic work. Sun Yefang believed that the amount of profits was the most comprehensive indicator of the technological standard and the quality of operation and management of an enterprise. The index of profit was the “most central link” in the entire system of planning indexes. “People will be able to promote all other links when they get close control over this one.” He proposed that it was the supreme principle of socialist economic activity to achieve the maximal effect with the minimal consumption. He often compared the entire national economy to an ox and the index of profit to the “nose of the ox”. He believed that, when people get hold of the ox’s nose, namely the index of profit, the ox of national economy would naturally follow their steps. He further proposed that the profit rate on funds was the comprehensive index to evaluate the effect of the economic activities of an enterprise. Average social profit rate on funds was the standard that each enterprise had to reach. Those that achieved profits higher than average social profit rate on funds are superior enterprises. Those that failed to reach the standard were inferior enterprises. From 1966 to 1976, these views of Sun Yefang was accused as preaching “letting profit take command” and harshly criticized by left-deviated theorists.

In the eyes of his critics, Sun Yefang valued and stressed on profit and this meant to see and operate an enterprise completely from the perspective of a capitalist. They believed that socialist enterprises should not pursue economic benefits and profit level but devoted themselves to retaining political purity. “The proletariat should first see politics when examining the quality of an enterprise. Namely, they should see whether the enterprise holds high the great red flag of the Mao Zedong Thought, whether the power of leadership was held in the hands of true Marxists, and whether people earnestly implement the line, guideline and policy of Chairman Mao on proletariat revolution. They should see whether an enterprise handles well the ideological revolution of man and cultivate and build a revolutionized industrial force and whether the enterprise completes the production tasks assigned by the CPC and the state in a comprehensive way and in a greater, faster, better and more economical manner, bearing the global situation in mind and starting from their own duties, so as to make contribution to socialism.” “We do not rely on ‘letting profit take command’ or ‘giving material incentives’ but on ‘letting proletariat politics take command’.” “From Liberman to Sun Yefang, those people all preach ‘using economic methods to management economy’ and practice ‘letting profit take command’. This is actually to let bourgeois politics take command and to disintegrate socialist economic basis with bourgeois politics. This is a completely reactionary revisionist line for the restoration of capitalism.” “The critical mistake of ‘letting profit take command’ lies in opposing letting proletariat politics take command and restoring capitalism. This is what we firmly oppose.”⁶ The opinion of his critics in fact confused the relationship between politics and economics. From 1966 to 1976, such wrong outlook that only focused on political lines and disregarded operation conditions

⁶The Writing Group of the Jilin Provincial Revolutionary Committee, “The Class Struggle in Socialist Construction and the Area of Economics—Criticizing Sun Yefang’s Revisionist Economic Theory”, *The Red Flag*, Issue 2, 1970.

seriously disturbed the normal operation of enterprises and eventually resulted in a major downslide of national economy.

IV. Sun Yefang's Criticism on Voluntarism and the Theory of Natural Economy Was Attacked as "Negating Letting Politics Take Command"

Before 1966, the theoretical system of socialist political economics was greatly popular in China. A highly concentrated economic management system was built on such basis. In fact, both were basically transplanted from the Soviet Union. Soviet theory on political economics was filled with voluntarism and theory of natural economy and exerted negative influence on the formulation of policies and theoretical study in China. Sun Yefang opposed the bad tendency that people did not use objective economic principles to explain economic phenomena and issues in theoretical study but used reasons in politics and ideology to replace objective economic principles. "It was not only an idealist view but also the way of thinking of the sluggard in economics to talk about politics while detaching from economy, to replace objective principles with mass line and letting politics take command, to replace explanation in economics with explanation in politics."⁷ Sun Yefang made forceful criticism on the view that saw socialist economy as a big factory and all enterprises as one after another workshops that only had technical division of work without social division of work and that believed that there was only the transfer and allocation of products between enterprises without exchange at equal values. He believed that such a view had no essential difference from the situation in a primitive society in which the chieftain controlled in a centralized manner all areas of production, distribution and consumption. With far-reaching insight and profound analysis and at the height of methodology, Sun Yefang criticized "voluntarism" and "theory of natural economy". He advocated that people should eliminate voluntarism and metaphysical views in political economics and adhere to dialectical materialism.

Sun Yefang's criticism on voluntarism and theory of natural economy hit the crucial weakness of traditional theory and left-deviated thoughts from the perspective of methodology. His critics found it hard to refute him. The only thing they could do was to accuse Sun Yefang of opposing letting politics take command and to claim that he stigmatized letting politics take command as "voluntarism" and the "way of thinking of sluggard" and that he outrageously opposed the general line of the party, and people's commune. His critics not only refused to admit the non-scientific and harmful nature of voluntarism but also wielded it as their magical wand once again and further brought it to the extreme. They believed that, in socialist economy, the central link that could drive everything was only to let proletariat politics take command. "These were to radically opposite lines in economics construction to let politics take the command of economy or to 'use economic methods to manage economy' and to adhere to letting proletariat politics take command or to practicing 'letting profit take command'. Chairman Mao leads us to carry out socialist construction and he always takes proletariat politics as the top priority. He uses politics to

⁷Sun Yefang, "People Must Learn Some Philosophy to Understand Economics", *Selected Works of Sun Yefang*, Shanxi People's Publishing House, 1984, p. 163.

take command of economy and stresses on revolution to promote production. This is a Marxist and Leninist line to consolidate and strengthen proletariat dictatorship.” Critics also believed that, as long as “people highlight proletariat politics, implement mass movement to creatively studying and applying Mao Zedong Thought, and realize the ideological revolutionization of man, they will be able to adhere to correct political direction and fully mobilize powerful revolutionary vigor in work. Thus the socialist initiative and creativity contained in the mass would erupt like a volcano and powerfully promote the development of production.” Historical lessons proved that such thinking that extremely exaggerated the role of the will and ignored objective economic principles caused enormous harm to socialist practice.

3 Several Comments

First, the study in economics needs academic criticism, but such criticism should be made within academic study. The criticism with strong political colors from 1966 to 1976, characterized by putting labels on people and making personal attack like wielding a stick, could only suppress normal academic argumentation. Scientific research has already proven that scientific criticism is the tremendous driving power for scientific progress. In the process of scientific research, serious and careful scientific criticism can help researchers to identify the elements of truth in research results and locate and discard the elements of mistake in them. Thus it can promote scientific research to constantly advance and make progress. In the area of economics, academic criticism also plays an important role in the development of the discipline. But such academic criticism should only target views rather than researchers. There should be academic argumentation in which people are convinced through reasoning rather than political criticism with strong utilitarian colors. Otherwise, criticism will do no good to extending the width and depth of academic research. On the contrary, it will twist and mislead the direction of academic research, confine the thinking of the scholars and bring academic research into standstill or even regression. The situation in the study of economics in the late period of Stalin’s reign in the Soviet Union and from 1966 to 1976 in China fully proved this point.

Second, an excellent economist not only needed to possess good attainment in economics and the ability to analyze a question but also the courage to challenge traditional outlook and adhere to the truth. Sun Yefang was an example in this respect. When traditional political economics, which came from the Soviet Union, dominated economic study, he could incisively perceive the deep-level contradictions and problems contained in that seemingly profound theoretical system and made comprehensive challenge on the views, system and methodology in traditional theory. Then on the basis of his own understanding on the specific national situation in China, he proposed a series of truthful and insightful theoretical views and reform suggestions. And on such basis, he initially formed his own independent system of socialist economic theory. However, his theoretical views were put under all-round assault and ruthless criticism from 1966 to 1976 and he himself was imprisoned because of

his work. Yet he would not change his views easily to follow political trends. After he was released from prison, he immediately declared, “First, I will not change my ambition. Second, I will not change my job. And third, I will not change my view.” This fully exhibited the sublime style of a scholar with serious academic attitude who pursues and adheres to truth and deserves to be an example for later generations.

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Chapter 5

Extreme Left-Deviated Thought Trend Ran Rampant



Jun Wan

1 The Distortion and Criticism of Basic Economic Views in Marxism in Extreme Left-Deviated Theory

From 1966 to 1976, extreme left-deviated thought trend prevailed. Some people criticized basic economic views in Marxism and even negated traditional socialist economic views and the research results in economic study of The People's Republic of China since its foundation. Under the pretext of defending Marxism, they garbled quotes from the works of classical writers of Marxism, took particular statements and made infinite exaggeration. They distorted and altered Marxist political economics, cooked up a large amount of fallacies that were completely opposite to Marxism, and caused serious ideological chaos in the society.

I. The Reaction of Productive Relations and Superstructure on Productivity and Economic Base Was Exaggerated to the Extreme

Classical writers of Marxism believed that the development of the economic forms of society was a natural historical process. The change of the economic forms of society depended on the paradoxical movement between productivity and productive relation and between economic base and superstructure. Productivity was the most active and revolutionary factor. The constant change of productivity required that productive relation adapted itself with it. When productive relation adapted itself with the development of productivity, it could promote the development of productivity. Otherwise, it would obstruct such development. The relationship between economic base and superstructure was the same. Productive relation and superstructure would exert reaction on productivity and economic base. But essentially, productivity determined productive relation, economic base determined superstructure, and social existence determined social consciousness.

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After the founding of the People's Republic of China, the above views of classical writers on the law of social development were generally accepted as Marxism spread in China. However, left-deviated theorists acted in opposition to it from 1966 to 1976. They proposed, "Should people adhere to letting proletariat politics take command and drive mechanization with revolutionization? Or should they oppose letting proletariat politics take command, engage in 'placing technology in the first place' and 'providing material incentives', only want mechanization and discard revolutionization, and thus let bourgeois politics dominate? These are two radically opposite lines between Marxism and Leninism and revisionism."¹ They negated the importance of developing productivity and wantonly criticized the "theory of the unique importance of productivity". Zhang Chunqiao once said, anyone who said that the transition to communism even needed material basis was obsessed with materials. These people despised of the role of science and technology in promoting the development of productivity. They believed that science and technology were "never a determinant factor of productivity. It was more wrong to draw from it the absurd conclusion that 'productivity is science' or that 'productivity is science in the first place'."² But they enjoyed greatly talking about things of superstructure such as "politics" and "lines". They talked at length that, "under the condition of socialism, proletariat politics takes command. The socialist initiative of man is fully mobilized. Thus people will definitely promote the rapid progress in production. The theory of the unique importance of productivity excludes class struggle and refuses to engage in the socialist revolution on superstructure and productive relation. It takes the development of production as the sole decisive thing. This is the substance of the issue."³ They also made some eccentric talks, such as "If production goes up but the line is incorrect, people should be criticized. As long as the line is correct, people should be commended even if production does not rise." These people exaggerated the reaction of productive relation and superstructure to the extreme. Yao Wenyuan once said, "Because of advanced thought and advanced leadership of the party, the society can achieve leap-forward and go beyond different stages." They even proposed that, "in the entire historical stage of socialism, productive relation always played a primary and decisive role to productivity and superstructure does the same to economic base." Such views obviously violated the basic principles in Marxism and the principle of historical development.⁴

II. The Outlook of Material Interests Was Negated and the Purpose of Socialist Production Distorted

In early the 1950s, Stalin proposed the fundamental economic principle of socialism in his book *Issues on the Socialist Economy in the Soviet Union*. Namely, people should "guarantee the satisfaction of the often increasing material and cultural needs in the entire society to the maximum with the method to constantly increase and

¹Quan (1971).

²Zheng (1976).

³Cheng (1976).

⁴See Xiang (1979).

improve socialist production on the basis of high technology.”⁵ Such statement told people that the purpose of production in socialism was to satisfy the often increasing material and cultural needs in the entire society to the maximum and that the means to achieve such a purpose was to constantly increase and improve socialist production on the basis of high technology. The fundamental economic principle of socialism proposed by Stalin triggered heated discussion in the circle of economics in China. The scholars who participated in the discussion published their own views on whether the content in Stalin’s discussion was correct and accurate and whether his representation was complete and precise. But all of them did not have large disagreement on the view that the purpose of socialist production was to satisfy the increasingly growing material and cultural needs of the mass.

From 1966 to 1976 the study on the fundamental economic principle of socialism in the Chinese circle of economics was disrupted. Extreme left-deviated theorists wantonly distorted the purpose of socialist production. In their eyes, material interests only played a negative role in the process of social and economic development. “Modern revisionist work so hard to stealthily replace socialist production purpose with capitalist welfarism that they could deceive the people with the mirage of good food, good clothing and good housing and thus the people would forget class struggle, revolution, elimination of classes, and the fundamental goal of realizing communism.”⁶ They preached that the mass should practice religious-styled asceticism. “To only plant trees with enjoying the shade is the sublime ideological conception of a communist.”⁷ They exaggerated spiritual encouragement as the most important incentive mechanism and believed that, in socialist economy, the central link that drove everything could only be letting proletariat politics take command. Only when people stressed on proletariat politics, let Mao Zedong Thought take command, and promoted the ideological revolution of man could they guarantee the socialist development direction of an enterprise and mobilize the revolutionary initiative and creativity to the maximum. “In our socialist country, people do not rely on letting profit take command or giving material incentives in the development of production. We rely on the line of proletariat revolution of Chairman Mao, on letting proletariat politics take command, on taking class struggle as central task, and on carrying out powerful political and ideological work.”⁸ A conclusion drawn on the basis of such left-deviated theoretical view was that “people turn into revisionists when they get rich”. That is to say, the people could not achieve common prosperity under socialist system. Otherwise, they would turn into revisionists. This was obviously very absurd. If the pursuit of material interests was not the purpose of socialist production, then what was the purpose of socialist production. The answer was revolution. Then what was the purpose of revolution. None of those extreme left-deviated theorists gave an answer to this question. Left-deviated theories not only misinterpreted the purpose of socialist production but also distorted to means to achieve production purpose. If the

⁵Joseph (1961, p. 31).

⁶*Socialist Political Economics*, Shanghai People’s Publishing House, 1976, p. 118.

⁷Quoted from Xue (1979, p. 61).

⁸Zhong (1976).

pursuit of material interests was not the driving force in socialist production, then how could people develop socialist production. Left-deviated theory believed that revolution was the driving force of the development of production. “In socialist society people could promote the constant development of socialist production only when they take class struggle as the central task, adhere to the continuation of revolution under proletariat dictatorship, deeply carry out proletariat revolution in the fronts of politics, ideology and economics..., and mobilize all positive factors. Otherwise, if people do not focus on revolution but only work hard on production and technology, they will not only fail to improve production but also depart from socialist direction. Then capitalism will restore. Therefore, ‘revolution is the locomotive of history’ and revolution is the driving power of the development of production.”⁹

III. Commodity Production and the Law of Value in Socialist Economy Was Negated

After the founding of the People’s Republic of China and, in particular, after socialist system was basically established, there were always many discussions on the issues of commodity production and the law of value in socialist economy. There was a great wave of such discussion in late the 1950s. And there was some discussion in the early 1960s. In Marx and Engels’ conception, socialist society came from advanced capitalism. There was no commodity production and exchange or currency in it. However, in reality, socialist revolution was the breakthrough first achieved in underdeveloped capitalist countries. So the socialist countries at the time generally had the issue of low productivity standard and it was unrealistic to abolish commodity production. In his book *Issues on the Socialist Economy in the Soviet Union*, Stalin admitted that there was still commodity production in socialist economy. And he attributed the existence of commodity production to the co-existence of the two kinds of socialist ownership systems of whole people ownership system and collective ownership system. The economic connection between these two kinds of ownership systems could only be realized through the connection of commodity and the exchange in transaction. As long as these two basic production components existed under socialist system, people could not abolish commodity and money relations. Stalin further believed that, if there was still commodity production in socialist economy, then the law of value also existed and played its role. But the role of the law of value was strictly limited within certain scope and could not play the role of a regulator of production. The principle of developing national economy in a planned and proportionate manner was the principle that determined the operation of socialist economy. After the introduction of Stalin’s work into China, the Chinese academic circle carried out in-depth discussion centering round such issues like the reason to the generation of commodity production under socialist system, the scope of commodity production, the difference and similarity between socialist and capitalist commodity production, whether to utilize or limit commodity and money relations, the status and role of the law of value in socialist economy, and the relationship between the law of value and planned

⁹Compilation Group of *Speeches on Political Economics (The Part on Socialism)*, *Speeches on Political Economics (The Part on Socialism)*, People’s Publishing House, 1976, p. 73.

economy. Although there were still some disagreement on some specific issues, the academic circle generally believed that the existence of commodity production under socialist conditions possessed objective necessity and, therefore, people had to admit and respect the role of the law of value.

However, extreme left-deviated theorists made a big fuss centering round commodity production and the law of value from 1966 to 1976. They intentionally confused the essential difference between the commodity production under the two kinds of social systems of socialism and capitalism. “Now that both are called commodity production and exchange through money, they cannot be so much different in substance.”¹⁰ So in socialist society, commodity system was still the soil to produce capitalism and bourgeoisie. “After the public ownership system of the means of production was established in a socialist country, there are not only the conditions to produce new bourgeoisie in politics and ideology but also the soil to produce them in economy. This mainly refers to commodity system, exchange through money, distribution according to performance, and so on.”¹¹ Because of this, people should limit commodity production and exchange. “People can only impose limitations under proletariat dictatorship on such things that showed not much difference with those in old society.” “To limit commodity system means to limit capitalist legal right in commodity economy, to limit the spontaneous action of the law of value, and limit the capitalist tendency in commodity economy.”¹² “If people do not impose such limitation, capitalism and bourgeoisie will quickly develop.”¹³

With respect to the treatment of the law of value, extreme left-deviated theories always regarded it as an “alien force” in socialist economy. “The so-called law of value is, in essence, an alien force. Its movement will always get rid of the conscious and planned control of man, more or less.”¹⁴ In the eyes of extreme left-deviated theory, the law of value was not the regulator of social production in socialist economy and its spontaneity was already strictly limited. Nonetheless, it was the economic law for commodity production, after all. So it fully reflected the capitalist legal right in commodity system. As long as the law of value existed, it was inevitable that it would play a negative role and bring harm with it. This would not only cause polarization in income distribution but also “cause some state-operated enterprises and collective economic units to partially pursue output value and profit regardless of the needs of the state and the people. This will sabotage the plans of national economy and change the nature of public ownership system. It will cause the spontaneous capitalist tendency in petty production to run rampant. Landlord bourgeoisie who have been overthrown and new-born bourgeoisie will take the advantage of commodity system and the law of value to sabotage socialist plans... and make commodity system the

¹⁰“Old Power Is the Social Basis of the Restoration of Capitalism----Reading Notes about *Left-Wing Communism: An Infantile Disorder*”, *Wen Hui Bao*, March 13, 1975.

¹¹ Wu (1975).

¹² Zheng (1975).

¹³ Zhang (1975).

¹⁴ Quoted from Zhang (1979, p. 159).

instrument for them to restore capitalism.”¹⁵ So people had to impose limitations on the law of value.

IV. Distribution according to Performance Was Negated

Marxist political economics believed that distribution according to performance was the objective principle in the area of the distribution of personal consumer goods. Although socialist society has basically achieved the common possession of the means of production by the workers, as the standard of productivity of the socialist society has not reached the extent of the overwhelming abundance of social wealth, people still cannot implement distribution according to needs on the basis of the needs of each social member in the area of the distribution of consumer goods. They can only carry out distribution on the basis of the amount of labor contribution of social members.

However, from 1966 to 1976 extreme left-deviated theorists wantonly denigrated that distribution according to performance was “an element of capitalism” and did everything to preach equalitarianism. According to the statements of Marx, Lenin and other Marxist classical writers, socialist society came from capitalist society, so it bore some traces of old system in some respects. In the principle of distribution according to performance, such issue was mainly exhibited as the general practice of applying the principle of exchanging labor by equal amount. Namely, One form of labor in certain amount could be exchanged with another form of labor in the same amount. Although such exchange was equal in form, it would bring de facto inequality because it tacitly approved that different types of work abilities were natural privilege. Extreme left-deviated theory made a great fuss on such a point. They distorted the statements of classical workers and negated the socialist nature of distribution according to performance. “Socialism turns the means of production into public property. It abolishes capitalist legal right in this area. But in the aspects of distribution and exchange, capitalist legal right still exists. The ‘equal right’, embodied by distribution according to performance and exchange through money, is ‘still capitalist legal right according to relevant principles’. Capitalist legal right is a hotbed in socialist society that can generate bourgeoisie and revisionism. People must impose limitations on it under proletariat dictatorship.”¹⁶ On the one hand, extreme left-deviated theorists talked at length that distribution according to performance would definitely bring about the consequence of polarization in income distribution. On the other hand, they did everything to preach equalitarianism. They regarded distribution according to performance and more pay for more work as “providing material incentives” or “seeing money as omnipotent”. They believed that “the initiative mobilized with ‘material incentives’ can only be the initiative to achieve fame and profit in bourgeois individualism and to develop capitalism. If people mobilize such initiative, they will corrupt the thought and soul of the working people, nourish reactionary economism, disintegrate the economic basis of socialism, and cause the restoration

¹⁵Compilation Group of *Speeches on Political Economics (The Part on Socialism)*, *Speeches on Political Economics (The Part on Socialism)*, People’s Publishing House, 1976, pp. 156–157.

¹⁶Cheng (1975).

of capitalism.”¹⁷ Therefore, these people opposed the implementation of the piece rate wage system which connected labor with reward in a closer and more direct manner. They believed that the capitalist legal right reflected by such system seemed more prominent and that it could easily help to generate individualist thought that only narrowly care about personal gains and losses. They sang highly of the practice from the beginning of 1958 in which the majority of the enterprises changed piece rate wage into time rate wage and various types of bonuses into integrated bonus and then to additional wage. They believed that it “reflects that, as objective conditions change, the ideological and political awareness of the workers are improved so that they impose limitations on capitalist legal right present in the area of distribution.”¹⁸ They failed to realize that such practice was exactly a measure of equalitarianism with which people were treated as the same regardless of the quantity and quality of their work results. It resulted in overall superfluous staffing and low efficiency in enterprises at the time and seriously impeded economic development.

2 Several Comments

First, extreme left-deviated thought trends caused huge damage to China’s socialist revolution and construction and triggered great chaos in ideological and theoretical front. Extreme left-deviated thoughts often disguised themselves as pure Marxism. Their believers often took advantage of several partially quoted and misinterpreted statements of Marxist classical writers to preach a series of specious outlooks and to mislead the practice in socialism. After the conclusion of the transformation into socialist ownership systems of the means of production, followers of extreme left-deviated thought trends did their best to preach the transformation of productive relations that went beyond proper historical stage. From 1966 to 1976, extreme left-deviated thought trends appeared in the disguise of orthodox Marxism. Their followers wantonly preached the reaction of productive relations and superstructure respectively on productivity and economic base. They did everything to exaggerate the role of subjective will, negate commodity economy and the law of value, and ignore or even restrain the basic needs of the mass for material interests. The wrong policies caused by the wrong outlook in extreme left-deviation seriously jeopardized the progress of productivity, obstructed the continuous development of national economy, and resulted in the failure to improve the living standard of the people over a long period of time. After 1977, the hated extreme left-deviated thoughts were eradicated from various areas. Comrade Deng Xiaoping pointed out seriously that China had to oppose both left- and right-deviation. But at present, people should

¹⁷Compilation Group of *Speeches on Political Economics (The Part on Socialism)*, *Speeches on Political Economics (The Part on Socialism)*, People’s Publishing House, 1976, p. 211.

¹⁸Compilation Group of *Speeches on Political Economics (The Part on Socialism)*, *Speeches on Political Economics (The Part on Socialism)*, People’s Publishing House, 1976, p. 207.

mainly pay attention to opposing left-deviation. It appears now that such a view still has its significance in reality.

Second, theoretical economics is absolutely not economics of annotations. In the study of economic theories, people should not just quote classical works or find some statements from the works of masters in the past to judge reality or the truthfulness of other theories. Only practice is the sole criterion of testing truth. Economics is a discipline for governing the state and benefiting the world. This determines that economics should take root in reality and pay attention to reality. People need to apply existing theories to explain the phenomena in the operation of economy in reality, to analyze existing problems and predict future directions. They should also make use of fresh facts and cases in economic life in reality to deepen theoretical study, to enrich the connotations of these theories, and to correct the defects of existing theories. Thus they can promote the constant development of the theories on socialist economy.

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Part III
The Peroid of 1977–1991

Chapter 6

The Action in Economics Started with the Issue on Distribution According to Performance in 1977 and 1978



Wenmin Zhang

1 Situation on the Study and Exploration About Distribution According to Performance in China Before 1966

In 1949 China completed the New Democratic Revolution. Before 1956, there were basically five coexisting economic sectors, namely state-operated economy, cooperative economy, private capitalist economy, individual economy and state capitalist economy. Viewed from distribution relations, there were three forms of distribution, namely distribution according to performance, self-sufficiency and distribution according production factors. Besides, ration system was practiced in CPC and governmental organs and the military for a period of time. The five economic sectors had different proportions in gross national product and different population coverage ratios. Among them, the dominant one was individual economy, the second largest ones were state-operated economy and cooperative economy, and the third largest was capitalist economy. Viewed from this angle, the dominant distribution form was distribution according to production factors and the second important ones were distribution according to performance and according to ration system. In 1953, Mao Zedong proposed the CPC's general line for the transition period. Namely, "within a certain long period of time, China will basically realize the industrialization of the country and the socialist transformation of agriculture, handicraft industry and capitalist industry and commerce." In 1955, *Textbook on Political Economics*, edited by the Institute of Economics of the Soviet Academy of Sciences, was published and circulated in China. This signified that Soviet socialist economic theories were disseminated systematically in China. Thus, performance according to performance and the distribution issues in real life started to attract the attention of the circle of theoretical study. In 1956, the "Three Major Transformations" mentioned above

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was completed. Now, because capitalists only received fixed interests in some joint state-private ownership enterprises and stopped participating in the production and operation of enterprises, these enterprises had almost no difference from those under public ownership system. Thus, in the area of ownership relations, a situation was formed nationwide that two public ownership systems of whole people ownership system and collective ownership system became the dominant ones. As the ration system in CPC and governmental organs and the military was changed into wage system and labor point system was implemented in cooperatives in the countryside, distribution according to performance became the main distribution form at the time in the area of distribution relations and it also became the basis of China's distribution theory. One of the issues discussed at the First National Symposium of the Theories on Economics in 1959 was the issue on distribution according to performance and piece rate wage. From the 1950s to late 1970s, distribution according to performance became a kernel issue in discussion in the area of distribution. And in such discussion, the issues on the basis of existence of distribution according to performance, on the principle of materials interests, and on capitalist legal right became the key questions.

I. The Question on What Was the Basis of Existence of Distribution according to Performance

After the theory on distribution according to performance was introduced into China, the main task in the first place was how to understand its theoretical connotation. What was worth mentioning was the question what was the basis of existence of distribution according to performance.

In this large scale discussion, the most important progress was proposed the question what were the determinant conditions of distribution according to performance? There were four types of views in the discussion:

First, it was believed that the practice of distribution according to performance was determined by the socialist public ownership of the means of production. Such a view indicated that, because exploitation was eliminated under the circumstance of socialist public ownership, it was a necessary choice to practice distribution according to performance. But it did not answer the question why people did not practice the principles of distribution according to needs and of equal distribution under the circumstance of public ownership.

Second, it was believed that distribution according to performance was determined by the ownership system of the means of production and the standard of productivity. But such a view still could not answer the question why people only practiced distribution according to performance rather than the principle of equalitarian distribution.

Third, it was believed that distribution according to performance was determined by multiple factors, namely by socialist public ownership system, standard of the development of productivity, the Three Major Differences, namely, those between workers and farmers, between the city and the countryside and between physical and mental labor, and ideological consciousness. Generally speaking, such a view was

comprehensive. But it still did not answer the question what was the basis of distribution according to performance in recognizing the difference between individual labor. If people did not answer this question, they would not be able to explain the issues such as why people would care about the losses and gains in personal interests and why they should abolish equalitarianism.

Fourth, it was believed that distribution according to performance was determined by individual ownership of labor. Ai Siqi believed that, under the condition of socialism, “the labor of individual is, as a matter of fact, still admitted as being owned privately although there is no private ownership of the means of production. It was because of such privately-owned right that it becomes possible for people to require corresponding reward in the society”.¹ Wang Xuewen said, “in socialist whole people ownership system, there are factors of partial individual ownership of labor, namely the labor whose object is in product. The existence of such ownership is determined by the development standard of labor productivity, the Three Major Differences, namely the differences between workers and farmers, between the city and the countryside, and between physical and mental labor, where were passed down from the old society, and the existence of the remnants of capitalist rights. Now that there are such factors of partial individual ownership of labor, the society needs to exchange the labor owned individually with consumer goods owned by the whole people so as to admit such ownership owned individually.”² Yu Wu believed that “the direct basis of the principle of distribution according to performance was no other things but the personally private ownership of labor.” He also believed that public ownership system and standard of productivity “are only some necessary conditions for practicing distribution according to performance but not its direct basis.” “The principle of distribution according to performance itself indicates that ‘laboring’ (involving the quantity and quality of the labor expended) is the direct basis for the principle of distributing the means of consumption. It also indicates that socialist society recognizes the strength of labor is a ‘natural privilege’ to its possessor. It means that socialist society admits that there is a kind of ownership relation between a worker and his own labor. Namely it admits that labor is privately owned by the worker from whom it comes from. This means that there is the personal privately ownership of labor in socialist society as a productive relation. And such productive relation is the direct basis of the principle of distribution according to labor.”³ Taking the personal private ownership of labor as the direct basis of distribution according to performance is the most important progress in the discussion on the issue of distribution according to labor in the 1950s. The reasons are as follows:

First, such view correctly understood and developed the Marxist theory of distribution according to performance. As Karl Marx proposed in *Critique of the Gotha*

¹Ai (1958).

²Wang (1959).

³Yu (1962).

Program, “Any distribution whatever of the means of consumption is only a consequence of the distribution of the conditions of production themselves”.⁴ At the time, people’s understanding on this statement often emphasized on the distribution (or possession) of the means of production and excluded the worker, which was included in production conditions. So such understanding was partial. And it exhibited as mechanically emphasizing that there were different modes of distribution corresponding to different modes of production. In such a view, it was believed that there was only one type of distribution mode, namely distribution according to performance, after the socialist public ownership of the means of production was realized. Thus it further negated the forms of distribution which were determined according to the principles of economic operation.

Second, after the view that the private ownership of labor determined distribution according to performance, it was, in fact, natural to admit that worker was an indispensable condition in production process. Then, it further provided theoretical basis for further clarifying in the future that both worker and means of production were factors of production and proposing after the reform and opening up the view of combining distribution according to performance to distribution according to production factors.

Third, the theory on the determination of distribution with the private ownership of labor was a powerful weapon to overcome equalitarianism. In traditional distribution theory, it was believed that, under the condition of socialism, the function of distribution was to guarantee supply. To set the positioning of socialist distribution as guaranteeing supply was an outlook that came from the intention to realize the so-called requirement of socialist basic principles with natural economy. Because the idea of supply was emphasized, the thought trend to abolish wage system and restore ration system emerged in 1958 and the phenomena of replacing distribution according to performance with equalitarianism appeared and lasted for many years. The theory of the private ownership of labor was to set the positioning of distribution as the realization of ownership right. It means to define the positioning of distribution relation from the angle of combining the mode of economic operation with the characteristics of socialism. Therefore, it could overcome equalitarianism in substance.

Fourth, such view resolved the issue that labor was commodity under the condition of socialism. In traditional socialist political economics, it was a capitalist category to regard labor as commodity. Under the condition of socialism, worker was the owner of the means of production and thus the commodity of labor could exist no more. The theory on the private ownership of labor resolved the contradiction that worker was the owner of the means of production while labor was commodity under the condition of socialism so that the theory on labor as commodity could become true. As a result, the theory not only explained the direct reason of the existence of distribution according to labor in distribution theory but also could help to open up

⁴*Selections of Karl Marx and Friedrich Engels* Vol.3, People’s Publishing House, 1972, p. 13. <http://libcom.org/library/critique-of-the-gotha-program-karl-marx>.

labor market in reality, to realize the reasonable flow of labor, and to promote the development of socialist market economy.

II. The Discussion on the Principle of Material Interests

In this stage, the issue how to implement the principle of distribution according to performance and overcome equalitarianism did not cause large scale discussion. However, the issue of distribution in real life, such as the issue of the material interests of an individual, attracted the attention of the circle of theoretical study. At the time, national economy saw quick recovery and development on the one hand while, on the other hand, the tendency appeared that people did not “pay attention to adequately improve the living standard of the people on the basis of improving labor productivity and to the current interests and personal interests of the mass”.⁵ At the same time, some people had dissatisfaction in the area of distribution. Under such a background people carried out discussion on the principle of material interests in socialism and mainly discussed the relationship between taking care of the personal interests of the working people and developing production. In the discussion, people basically affirmed the necessity to take care of the material interests of the employees of an enterprise under the condition of socialism. Yu Guangyuan said, “This is because it is the requirement of socialist economic laws and principles to constantly improve the personal material interests of the working people, because, out of various reasons, we need to rely on not only a small number of vanguards of the working class but also the extensive community of the laboring mass, who have grown up in the old society and have the remnants of the thinking of the old society in their mind, to build socialism, and because, under socialist system, production has not yet developed into such an extent that people can practice the principle of ‘from each according to his ability, to each according to his need’.”⁶ Besides, some people proposed that the reasons of practicing the principle of material interests laid in the following: (1) The working people experienced in life the benefits to themselves in developing production. (2) Working was still a means to make a living rather than the primary need. (3) Private ownership, individual economy and bourgeois ideology still existed. (4) There was still difference between different types of labor. and (5) Such practice was chosen to encourage working people to generally improve their level of education and technology.⁷ Such affirmation on the principle of material interests indicated that, on the issue of spiritual and material relations, the circle of economics in China basically emphasized on the primacy of matter. So without the principle of material interests as guarantee, the initiative of people in work would not last long. Besides, such principle of material interests was also the premise to implement the principle of distribution according to performance. And it conformed to the principles of Marxism. Early in 1957, Gu Zhun connected

⁵“The Resolution of the Eighth National Congress of the Communist Party of China on the Political Report”, *Documents of the Eighth National Congress of the Communist Party of China*, People’s Publishing House, 1956, pp. 84–85.

⁶Yu (1954).

⁷See “A Summarization of the Papers Contributed on the Issue of Combining the Personal Interests of Working People with Social Public Interests”, *Study*, Issue 10, 1955.

the material interests of the working people with enterprise operation results and proposed the view that people should “establish very close connection between the material reward of workers with the profit and loss of an enterprise”.⁸ This indicates that people demonstrated the relationship between the principle of material interests and production over twenty years before reform and opening up. But from the end of the 1950s to the end of 1970s, extreme left-deviated thought trend emphasized that the principle of material interests was something revisionist and opposed it and thus caused tremendous harm to economic life.

III. The Debate on the Issues of Distribution according to Performance and Capitalist Legal Right

In 1958, the Second Plenary Session of the Eighth CPC Central Committee adopted the “general line of exerting the best effort, striving for the best, and building socialism in a greater, faster, better and more economical manner”. At the time, China rashly launched the “People’s Commune” movement under the guidance of this general line and caused enormous damage to national economy. In addition, ration system was implemented in the countryside, mainly characterized by cancelling the labor point system and providing free meals. And bonuses and piece rate wages for employees working in the city were also cancelled. Moreover, Zhang Chunqiao published the article *Breaking and Eliminating the Thought of Capitalist Legal Right* in the sixth issue of *Liberation* in Shanghai in September 1958. On October 13, the *People’s Daily* reprinted the article with “Editor’s Note” added to it. The article proposed that “the kernel of capitalist legal right is hierarchy system”. The function of “graded wage” and “piece rate wage system” was to advocating that “money can move god”. But it did “not stimulate the initiative in production but that to compete for fame in the imperial court and for profit on the market”. “In fact, it wants to replace proletariat equal relations with the rites and laws in capitalist hierarchy system.” It was also believed that changing ration system into wage and salary system “is for the bourgeoisie to protect unequal capitalist legal right and to attack proletariat revolutionary tradition.” It was proposed that people should “thoroughly break and eliminate capitalist legal right”, cancel wage system and restore ration system.⁹ This was the first initiative to create the theoretical basis for extreme left-deviation thought trend in the area of distribution. It caused enormous ideological chaos. Under such a circumstance, the first great discussion on distribution according to performance was carried out in China. The main content of the discussion included the following: what distribution according to performance was, the issue of the objective necessity of distribution according to performance, what capitalist legal right was, the relationship between distribution according to performance and capitalist legal right, and so on.

Among the works of Marxism, the first one that proposed capitalist legal right was *Marx’s Critique of Gotha Program*. Why did Marx say that there was capitalist legal right in distribution according to performance. (Before 1960s, people generally

⁸Gu (1957).

⁹Zhang (1958).

used the term “capitalist legal right” or in Chinese *Zi Chan Jie Ji Fa Quan*. Then after 1960s, many people thought that the word “legal right” was ambiguous and might cause theoretical confusion. And the contents in *Critique of Gotha Program* and *State and Revolution* discussed relationship of right rather than law. So “capitalist legal right” was not equivalent to “bourgeois right” or in Chinese *Zi Chan Jie Ji Fa Quan* Li, which should be a better translation of the term.¹⁰) Marx wrote about the idea to oppose the mistake that Ferdinand Lassalle stuffed into the program of the workers’ party such ideas that the income of labor “belongs to all members of the society according to equal right”, that “the income of labor should be distributed fairly”, and that “all social and political inequalities should be eliminated”. Marx pointed out that the concepts such as “fairness” and “equality” were social and historical categories. Various classes had very different outlooks on them. There were no such ambiguous ideas about “fairness” and “equality” in general like the “equal right of all social members”. Marx also pointed out that the distribution according to performance to be realized in socialist society was not so fair but both equal and unequal. He understood the equal right present in distribution according to performance as a social and historical category and pointed out that “But as far as the distribution of the latter among the individual producers is concerned, the same principle prevails as in the exchange of commodity equivalents: a given amount of labor in one form is exchanged for an equal amount of labor in another form. Hence, ‘equal right’ here is still in principle— ‘bourgeois right’... ”¹¹ So the bourgeois right in distribution according to performance was the bourgeois right that did not reflect but opposed the interests of bourgeoisie. Early in 1957, Zhong Jin, namely Yu Guangyuan, made a correct answer about how to understand the relationship between distribution according to performance and capitalist legal right. He said, “The establishment of socialist system has eliminated exploitation. This is the basis for true equality in the society. But ‘distribution according to performance’ is still capitalist legal right. It can be said to be a phenomenon of social inequality in comparison with ‘each according to his need’.”¹² Zhang Chunqiao talked about the nonsense that “the kernel of capitalist legal right is hierarchy system” and that “it wants to replace proletariat equal relations with the rites and laws in capitalist hierarchy system.”¹³ In order to denigrate distribution according to performance, Zhang Chunqiao inadequately equalized distribution according to performance to “hierarchy system”. Such misattribution was completely groundless. The so-called hierarchy system referred to the class relation existed in slave society and feudal society, in which there were orders and distinctions between superiors and inferiors and between gentle and simple. The clearly-defined hierarchy formed an unsurpassable privilege system. By means of such system, slave

¹⁰See *A Collection of the Minutes of the Four Sessions of the Discussion Meeting on Distribution according to Performance in 1977 and 1978*, China Financial and Economic Publishing House, 1979, p. 36. Here the terms of “capitalist legal right” or in Chinese “*Zi Chan Jie Ji Fa Quan*” and “bourgeois right” or in Chinese “*Zi Chan Jie Ji Fa Quan* Li” are regarded as identical.

¹¹“*Critique of Gotha Program*” *Selections of Karl Marx and Friedrich Engels*, Vol.3, People’s Publishing House, 1972, p. 11. <http://libcom.org/library/critique-of-the-gotha-program-karl-marx>.

¹²Zhong (1957).

¹³Zhang (1958).

owners and feudal lords made extra-economic exploitation on slave and serf. It was extremely unequal both in form and in reality. It was quite different from bourgeois right. Bourgeois right was equal on the surface but unequal in essence while hierarchy system was completely unequal. Bourgeois right referred to the private ownership right or ownership title of bourgeoisie on means of production and surplus value. Hierarchy system contained not only the ownership title to the means of production but also complete possession or semi-possession of the physical person of slave or serf.¹⁴ Under socialist system, bourgeois right only existed in commodity exchange and distribution according to performance as the traces of old society because of the establishment of socialist public ownership system. Zhang Chunqiao's nonsense that distribution according to performance meant hierarchy system showed that he did not have even a bit of commonsense in historical materialism. His idea was to influence public opinion for the purpose of cancelling distribution according to performance.

In this great discussion, some people advocated Zhang Chunqiao's view in confusion and believed that people should "admit, limit and gradually eliminate" distribution according to performance and "should not beautify, develop and expand it".¹⁵ But such view was never the mainstream. In fact, some economists like Shen Zhiyuan believed that, similar to socialist mode of production, distribution according to performance "possessed relative stability". Some people excessively stressed the transitional nature of distribution according to performance and, particularly, the "defect" that it possessed the nature of legal right. Thus, "it seems that they talk the matter into a situation that the scope of action of the principle of distribution according to performance gradually shrinks and the scope of action of the principle of distribution according to need gradually expands from the first day of the existence of socialism." This was very arguable. In fact, in the historical stage of socialism, "distribution according to performance will definitely experience a process of constant improvement, consolidation and development".¹⁶ This indicated that the circle of economics in China did not approve of Zhang Chunqiao's view. In particular, it was pointed out in the *Resolution on Several Issues on the People's Commune*, adopted at the Sixth Plenary Session of the Eighth CPC Central Committee in December 1958 that "negating the principle of distribution according to performance will hamper the initiative of the people in labor. Thus it was unfavorable to increasing social products and to promoting the realization of communism".¹⁷ The resolution timely corrected the view of negating distribution according to performance and cancelling wage system and practicing ration system. It unified people's understanding on objective necessity to practicing distribution according to performance under socialist conditions.

¹⁴Qi (1978).

¹⁵See "How to Understand the Principle of 'Compensating according to Performance' in Distribution", *Wen Hui Bao*, November 18, 1958.

¹⁶Shen (1962).

¹⁷*Documents of the Sixth Plenary Session of the Eighth Central Committee of the Communist Party of China*, People's Publishing House, 1958, p. 14.

2 The Review on the Discussion of the Issue on Distribution According to Performance Round the Third Plenary Session of the Eleventh CPC Central Committee

I. The Reflection on the Meaning of Distribution according to Performance

After 1976, they explored how to completely and accurately understand the theory of distribution according to performance. The reflection on distribution according to performance thus occurred.

In the exploration on the theory of distribution according to performance in this period, what was distribution according to performance was still an important issue because the distribution according to performance described in the books showed great difference from that in practice after some time in the practice of building socialism in China.

First, what was the word “performance” referred to in distribution according to performance. When examined from the natural forms of labor as “performance” meant performance of labor, such forms included potential form, flowing form and condensed or materialized form. When examined from the nature of labor, such forms included socially necessary labor, individual labor and average social labor. But what on earth was labor? There was common view about it.

Second, “working according to one’s ability” was the premise of distribution according to performance. However, under the condition of socialism, people still cannot achieve the status of working according to their ability. Whether the premise should be “working according to one’s ability” or labor was still an unsolved question.

Third, it was believed according to traditional outlook that distribution according to performance only applied to working people who participated in productive labor. Yu Guangyuan said, “Distribution according to performance means that the society only distributes personal means of consumption to people who engage in productive labor for the society. Distributing personal means of consumption to people who do not engage in productive labor does not belong to the area of distribution according to performance.” Because “labor remuneration is the personal means of consumption distributed to a worker-in-production according to the principle of distribution according to performance after the state or collective has made deductions to the amount of labor that he has provided.” The salary of non-workers-in-production belongs to the deduction part in gross social product. “Their salaries do not belong to labor remuneration” and thus “not to distribution according to performance”.¹⁸ However, some people believed that distribution according to performance applied to both worker-in-production and non-worker-in-production. This was because of the following: First, distribution according to performance was both the product and the actualization of socialist public ownership system. The socialist public ownership system of the means of production referred to the common possession of the means of production by all working people in the society, including those in the spheres of both material and non-material production. Second, the labor of the working people

¹⁸Yu (1978), p. 37, p. 60.

in various sectors in the sphere of non-material production was the indispensable condition for the normal operation of social production although these people did not produce material products. The reason why working people in non-material production could participate in the distribution of personal means of consumption was because they participated in the work of the society. Thus distribution according to performance would definitely play its role in their distribution relation. Third, workers-in-production and non-workers-in-production obtained personal consumption fund from different approaches. The former obtained it from the primary distribution of national income while the latter from re-distribution. The approach to obtain consumption fund and the principle that people had to follow in the distribution of personal means of consumption were two completely different issues. Each working individual who worked for the society took the labor that he or she contributed personally as the rule to distribute the means of consumption.¹⁹

Fourth, the distribution according to performance practiced was only in name and, in essence, it was equalitarian distribution. In the economy of whole people ownership system, people implemented the eight-grade wage system while, in collective economy, the labor point system. Both systems were known as part of distribution according to performance. However, people would find after careful analysis that the so-called eight-grade wage system was a unified national standard. The average grade difference of grade one to eight wages was 17.8%. The difference between the wage of a grade one worker and that of a grade eight worker was 3.15 times. This could not reflect the differences of the contribution in labor and remuneration nationwide. Moreover, it was more unlikely to summarize the labor point system in collective economy with the term of distribution according to performance. In many regions, the per day remuneration of a strong laborer could only pay the expenses for the reproduction of the labor force of the laborer himself. Under such low productivity, people could only implement equal distribution for survival. Thus, the theory of distribution according to performance was inconsistent with the life in reality so that the theory lost its basis of existence. People started trying to re-understand what were socialism and distribution according to performance.

In view of the situation above, some people proposed that China implemented for many years the distribution according to performance not exactly what was described in the book but the practice of giving labor income without unified rule of labor.²⁰

II. Rural Household Contracted Responsibility System Broke the Monotonous Form of Distribution according to Performance

During the period of late 1970s and early 1980s, the production and operation form of household contracted responsibility system emerged in the countryside in China, in which the method of distribution that people “fully submit the quota of the state, leave enough for the collective, and take the rest for themselves”. The emergence of this novel thing broke the so-called distribution according to performance implemented since 1956, the main characteristic of which was the evaluation and recording of

¹⁹Huang (1978).

²⁰Zhang (1987).

labor point. And a new form appeared in which production factors participated in distribution. Because the form negated the modes of production and distribution in the past, such as those figuratively named as “Da Hu Long” (working in big groups and shouting aloud a lot with little accomplished) and “Da Guo Fan” (practicing equalitarian distribution like that everyone eats from a big rice pot), it mobilized people’s initiative in production and labor, marked the first victory of the reform and opening, and became a good start for realizing the distribution mode of “taking distribution according to performance as the main form and allowing the coexistence of various forms of distribution”.

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Chapter 7

The Issue of the Role of the Law of Value as the Central Theme at the Second National Symposium on the Theories of Economics in 1979



Zhouyuan Zhang

1 Background: People Introduced Market Mechanism and Respected the Role of the Law of Value in Economic Activities in the Early Period of Reform and Opening up

After October, 1976, the Chinese circle of economics welcomed the spring of theoretical study. From 1977, people started to take some actions, cleaned up the wrong ideology, and criticized their series of left-deviated theories and policy positions. As the work of the CPC shifted to the track of taking economic construction as the center and as people advanced in reform and opening up, the circle of economics showed active thinking after 1978. The scholars constantly broke through the boxes of traditional economic theories and boldly absorbed the scientific research results in modern economics. They worked hard to explore the essence of socialist economy and search for the objective regularities in reform and opening up and in modernization construction. In particular, a series of important research results were achieved in the area of the issue on the relationship between planning and market. This played a positive promotive role to China's economic reform and development.

In December 1978, the convening of the Third Plenary Session of the Eleventh CPC Central Committee, which was of great historical meaning, started the new period of reform and opening up. The meeting negated the wrong theory and practice of "taking class struggle as the central task" and made the historic decision of turning the center of the work of the state and the Communist Party of China to carrying out economic construction and implementing reform and opening up. It was pointed out in the communiqué of the meeting that "a serious weakness of the economic management system of our country at present is over-concentration of power. Such power should be boldly delegated to lower levels under good leadership so that local authorities and industrial and agricultural enterprises could have the right and

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power of operation and management with more freedom under the guidance of the centralized planning of the state.” “People should resolutely practice the principle of handling matters according to economic laws and respect the role of the law of value. They should pay more attention to combining ideological and political work with economic means and fully mobilize the production initiative of cadres and workers.”¹ In order to vigorously restore and speed up developing agricultural production, the meeting suggested that the State Council made the decision that the state monopoly grain purchasing price be raised by 20% when summer grain crops started to be sold on the market in 1979. And the part of state-purchased grain that exceeded the quota in state monopoly purchase would be given another 50% price rise on the basis of the above. The purchasing prices of agricultural and sideline products, such as cotton, oil crops, sugar crops, livestock products, aquatic products, and forest products, would also be raised to a certain extent correspondingly on the basis of specific situation.

It needs to point out that, on the eve of the opening of the Third Plenary Session of the Eleventh CPC Central Committee, the *People's Daily* published on October 6, 1978 an important article written by Hu Qiaomu, entitled *Handle Matters according to Economic Principles and Speed Up Realizing the Four Modernizations*. It is said in the article that, “in order to speed up realizing the Four Modernizations of the modernizations of industry, agriculture, national defense and science and technology, we must handle matters according to economic principles and greatly improve the standard of economic management. There are many economic laws and principles. Here, the author only want to express some views about the three issues of the principle of developing in a planned and proportionate manner, the law of value and the unity of the interests of state, enterprise and individual.” When discussing that people should observe the law of value in economic work, the article said, “under the condition of socialism, commodity production and circulation will continue to exist over a long period of time. In China, it is necessary to develop them into a much greater size. The law of value still plays an indispensable role in economic life. When formulating and implementing plans, we must utilize the law of value and reflect the requirement of the law of value. We must require all enterprises, including those in national defense industry, to strictly practice time saving. They should constantly endeavor to achieve the optimal proportions in the consumption of labor and of materials, namely that of the so-called ‘materialized labor’ and in economic effect. They should strictly implement economic accounting, work hard to reduce the cost of unit product, and endeavor to improve labor productivity and profit rate on funds. Otherwise, they will cause great loss and confusion to socialist undertakings.” “At present, people should consider properly expanding the authority of the enterprises so as to urge the leaders and the mass in the enterprises to spontaneously concern themselves with the results of the enterprises’ economic activities.” In fact, this important article written by Hu Qiaomu made some preparation in the ideological theory for the convening of the Third Plenary Session of the Eleventh CPC Central Committee. The role of the law of value attracted the attention to the people once again.

¹*Communiqué of the Third Plenary Session of the Eleventh Central Committee of the Communist Party of China*, People’s Publishing House, 1978, p. 7.

People started to achieve breakthrough in theory. And In particular, market mechanism was introduction into practical economic life and effect was quickly seen. These greatly stimulated the initiative of Chinese economists in studying the issues like relationship between planning and market, commodity production, and role of the law of value. After preparation for some time, the Institute of Economics of the Chinese Academy of Social Sciences, the Institute of Economics of the National Development Planning Commission, the Jiangsu Provincial Institute of Philosophy and Social Sciences jointly initiated and sponsored the Second National Symposium on the Theories of Economics. It was held in Wuxi, Jiangsu from April 16 to 29, 1979. This meeting played a pioneering role in launching the marketization reform in China.

Sufficient preparation was made for this symposium. At the opening ceremony of the symposium, Sun Shangqing, the secretary general of the meeting, made the speech *About the Preparation and Proceeding of the Symposium on the Issue of the Role of the Law of Value*. He said, "in over half a year, the circle of economics and competent departments in charge of economy in China successively held several dozens of symposia in different sizes. For example, provinces and municipalities like Sichuan, Fujian and Jin already have convened such meetings. Hubei has one in process. Jilin province wants to hold the second one on the law of value. During the same period, more colloquia were held. Not only the extensive community of workers and teachers of economic theories but also many comrades who worked in competent departments in charge of economy attended these symposia and colloquia. Because of thought liberation and heated discussion, various opinions were exchanged extensively. Many questions that were inspiring or worthy of in-depth research were proposed. Many comrades made a great amount of economic investigation and made some beneficial exploration on China's socialist economic construction and relevant experiences and lessons. They submitted a large number of academic papers and economic research materials. The symposium received over 100 papers and materials. Such work made necessary academic preparation for this symposium."

"During the preparation of the symposium, it has been decided upon the consultation with various parties that the symposium will focus on the discussion of the following three issues: The first one is the relationship between planning and market in socialist economy. The second one is the law of value and the expansion of the authority of enterprise. And the third one is price."

"The symposium will be convened according to the following principles: 1. Upon the exchange of opinions among the initiating organizations of the symposium, it is agreed that the symposium is an academic meeting. People should always follow the policies of linking theory with practice and letting one hundred schools of thought contend. They should implement the spirit of the communiqué of the Third Plenary Session of the Eleventh CPC Central Committee. They should liberate thought, discuss freely, and inspire each other so as to promote the study in economics to serve the Four Modernizations in a better way. 2. We convene this symposium to carry forward the excellent tradition of the CPC. We advocate seeking truth from facts, speaking out freely, and discussing in modesty. We advocate the scientific atti-

tude in presenting the facts and reasoning things out and oppose abusively attaching political labels. And 3. People should combine meeting sessions in large, medium and small sizes. And small sessions will be the dominant form.”²

2 The Report on the Symposium on the Issue of the Role of the Law of Value

First, the author wants to show the report on the Second National Symposium on the Theories of Economics, submitted by the sponsors to competent leading departments, so that the readers may get a rough understanding on the results of the meeting.

The full text of the report on the symposium on the issue of the role of the law of value is as follows:

Central Financial and Economic Committee, the party leadership group of the National Development Planning Commission, and the party leadership group of the Chinese Academy of Social Sciences:

For the purposes of implementing the spirit of the Third Plenary Session of the Eleventh CPC Central Committee, promoting the study on the issues in the theories of the reform of economic management system, and benefiting socialist modernization construction, the Institute of Economics of the Chinese Academy of Social Sciences, the Institute of Economics of the National Development Planning Commission, and the Jiangsu Provincial Institute of Philosophy and Social Sciences jointly initiated the symposium on the issue of the role of the law of value in socialist economy, which was held in Wuxi, Jiangsu from April 16 to 29, 1979. Over 380 representatives and renowned economists from economic theory research organs, competent department leading in economic business, departments of economics in universities and financial and economic colleges and universities, and the publicity departments in the government of some provinces, autonomous regions and municipalities directly under the central government. The meeting received over 100 contributed papers and materials. Comrade Xue Muqiao, advisor of the National Development Planning Commission and director of the Institute of Economics subordinate to the commission, and Comrade Sun Yefang, advisor of the Chinese Academy of Social Sciences and of the Institute of Economics subordinate to the academy, both delivered speeches at the opening and closing ceremonies of the symposium. They also made academic reports at the symposium respectively. In his speech, Comrade Xue Muqiao particularly emphasized that the symposiums should vigorously implement the policies of linking theory with practice and letting one hundred schools of thought contend.

²See Reference Room of the Institute of Economics of the Chinese Academy of Social Sciences ed., *The Relationship between Planning and Market in Socialist Economy* Vol. 2, China Social Sciences Press, 1980, pp. 770–772.

The task of the symposium was to explore the direction of the reform of economic management system in China and relevant theoretical issues on the basis of summarizing our own experiences. Because people thoroughly implemented the policies of linking theory with practice and letting one hundred schools of thought contend, the comrades who attended the meeting all felt that the symposium was productive, inspiring and helpful. Many comrades said that the practice of letting workers on theory and in practical work discuss questions together could not only increase the depth of the discussion but also could do good to the lack of practical richness in study that troubled workers on theory and to the inadequate understanding of theory in work that troubled workers in practical work. The discussion at the symposium focused on the following three issues:

I. The Issue of the Relationship Between Planning and Market in Socialist Economy

In order to reform economic management system on the basis of the reality in socialist economy, people needed to clearly figure out the basic features of socialist economy.

There were three different opinions on such an issue.

One opinion emphasized that socialist economy was planned economy in essence. The comrades from the development planning commissions in Guangdong and Yunnan believed that many problems that existed at present, such as that the plans imposed too detailed and rigid centralized control and became irrelevant to reality, were not caused by socialist planned economy itself. They were the defects in work. If people wanted to resolve these issues, they needed to carefully summarize the experiences in planning work and reform planning management system rather than weakening planned economy. The faster development of national economy achieved during the restoration period, the First Five Year Plan, and the adjustment period in the 1960s was mainly the result from the practice that people paid more attention to the role of the principle of development in a planned manner and strengthened planning work. The comrades who had such an opinion stressed on planned regulation and planned management and believed that only such practice conformed to the essence of socialist economy. Some comrades said that it was faster and more flexible to utilize planned regulation to identify and resolve issues related to some important proportional relations than to utilize market regulation. Market mechanism only played its role at places where the plans could not impose their control.

Another opinion was the belief that socialist economy was both planned economy and commodity economy on the basis of public ownership system. So people should implement the combination of planned regulation and market regulation. Planned regulation showed that the society could consciously arrange social production in a proportionate manner while market regulation realized the proportionate development of social production through market mechanism. The comrades from the Institute of Economics of the Chinese Academy of Social Sciences, the Institute of Economics of the National Development Planning Commission and the Shanghai Municipal Development Planning Commission said that the several devastations of the economy in our country from the founding of the People's Republic of China were all the result of the violation of both the principle of development in a planned

manner and the law of value. Viewed from practice, some countries that excessively emphasized the leadership of unified and centralized planning and paid little attention to utilizing market regulation encountered problems that showed certain negative commonalities, such as imbalance of important proportions, fewer product types, poor product quality, large consumption in production, low efficiency and economic growth slowdown. This indicated that the situation was not completely caused by the problems in planning work but by the defects in economic management system. People should respect the role of the law of value and fully utilize market mechanism under the guidance of planned regulation in the future. And they also had to let the plans meet the requirements of objective principles, such as those of the law of value.

Some scholars in theoretical study emphasized the commodity feature in socialist economy. The comrades from the Central Institute of Fiscal Matters and Finance said that our economy was commodity economy in essence. The economic characteristic of the society in our country was commodity economy rather than planned economy. Planning was the form while commodity economy was the basis. The comrades who had such an opinion also negated that planned development was an objective principle in socialist economy.

How should people combine planned regulation with market regulation?

In one kind of opinion, it was believed that, in the entire national economy, the production and circulation of main products were regulated through planning while the production and circulation of secondary or sporadic products through market. An investigation report of the Beijing College of Commerce stated that planned regulation was implemented on the materials in unified purchase and purchase by state quotas while market regulation was implemented on the materials in three categories of supplies. There was nothing about the combination of planned economy and market economy in the areas managed by direct planning. Production was regulated through the market only in the areas that could not be managed by direct planning.

In another opinion, it was believed that planned regulation and market regulation were mutually permeating. The comrades in the Institute of Economics in Chinese Academy of Social Sciences and the Jiangsu Provincial Institute of Philosophy and Social Sciences believed that planned regulation could not be implemented without market mechanism while market regulation could not be implemented without the guidance of planning. These two measures were of the relationship that there was a bit of me in you and a bit of you in me. Market mechanism should be utilized to a proper extent with respect to the products transferred according to state direct planning so that these products could better conform to the needs of their users. The production and sale of large amounts of goods for everyday consumption were organized in a planned manner. But such activities did not repel that people fully employed the role of the law of value and market mechanism. Only in this way could people make planning conform to reality. The products exchanged in rural fair trade seemed to be managed through market regulation completely. But it was in fact guided by state agricultural product purchase plans and influenced by planned prices.

A few comrades believed that planned regulation and market regulation were the same thing. The comrades from the Beijing College of Economics believed that planned economy and commodity economy under socialist condition were the same

thing. There was no such issue of the combination of the two at all. Planned regulation and value regulation were the same. Planned regulation was value regulation in a planned manner.

The relationship between planned regulation and market regulation was in substance the issue of how to understand the relationship between the principle of developing in a planned and proportionate manner and the role of the law of value. Some comrades believed that the law of value was the primary principle. It should be said that the law of value was the fundamental basis for formulating plans and also the direct starting point and end result of planning work rather than a tool in planning work. Some comrades did not agree to this opinion. They believed that, under the condition of socialism, the role of the law of value was subordinate to basic economic principles and the principle of developing in a planned and proportionate manner. Naturally, planning had to show the respect to the law of value and reflect the requirement of such law. Some other comrades believed that the principle of developing in a planned and proportionate manner and the law of value played a regulatory role jointly. These two principles did not have completely opposite and mutually repulsive roles but have both unity and contradiction. The unity of them was seen in the fact that they functioned in the same direction. Namely, they jointly and complementarily regulated the proportionate distribution of social labor from different sides in accordance with the requirements of basic economic principles. Contradiction was mainly seen from the contrasts that one of them focused on regulating from the angle of the society while the other from the local angle and that one focused on long-term interests while the other reflected immediate interests. Because of such differences, the two regulation ways had their own strengths and weaknesses and thus it was necessary to combine them together to achieve joint regulation.

Was the formulation of the combination of planned economy and market economy scientific?

Most comrades held that people should not use the formulation of combining planned economy with market economy but of combining planned regulation with market regulation. The main reasons were as follows:

1. The circle of economics generally equalized capitalist economy with market economy. Thus, if we did not specify what the “market economy” as we called it actually meant, it might cause the misunderstanding that we wanted to combine socialist planned economy with capitalism.
2. It could easily cause the misunderstanding that socialist economy was partly planned economy and partly market economy. It seemed to be telling about the combination of two pieces of things without inherent connection. Some comrades said that some other comrades who engaged in practical work understood the combination of planned economy with market economy as the combination of planned economy with rural fair trade. This had something to do with the ambiguity of the meaning of “market economy”.
3. Socialist planned economy inherently included not only productive relation in the narrow sense and distribution relation but also exchange and market relation. It was unreasonable to say combining planned economy with market economy just like saying “combining the body of a person with his blood circulation system”.

But some comrades believed that people could use the formulation of combining planned economy with market economy because market economy was another name of commodity economy. Now that socialist economy was still commodity economy, there was socialist market economy. Some other comrades believed that a considerable amount of market economy already existed in real life. For example, market economy and semi-market economy already accounted for about a quarter of the gross industrial product in the Jiangsu province.

The discussion on the issue of the law of value mainly studied the theoretical foundation for the reform of economic management system. And thus it involved the issue whether the means of production exchanged inside the whole people ownership system was commodity. With respect to this issue, many comrades demonstrated that the means of production was still commodity from analyzing the characteristics of the relations inside the whole people ownership system.

Some said, when state-operated enterprises exchanged the means of production, people could not say that no transfer of ownership right occurred at all. This was because the means of production under whole people ownership was possessed permanently, used, operated and managed by different enterprises. And ownership right was separated to a certain extent from the rights of possession, use and operation and management. Such ownership right was also connected with the economic interests of different enterprises. Ownership right would come down to economic interests in the end. Now that the purchase and sale of the means of production between enterprises were connected with their respective economic interests, the purchase and sale of the means of production resulted in fact the transfer of ownership right to a certain extent. Thus such type of means of production was still commodity.

Some said that the “whole people” in the socialist whole people ownership system still divided into different individuals and collectives with different interests. It was different from the “whole people” in the advanced stage of communism in which the essential difference in labor was eliminated, distribution according to needs was practice, and thus there was no contradiction in economic interests between individuals and collectives. Thus, the whole people ownership in socialism was “incomplete whole people ownership system”. When these entities exchanged their own products between each other, people had to use the principle of exchange at equal values to regulate the economic interests between them. So the products were still commodity.

Some said that socialist whole people ownership system was a public ownership system with whole people ownership system as the dominant part, which included the collective ownership system of part of the production units, or the whole people ownership system that included local ownership system and enterprise ownership as its components. Such form of ownership system would definitely exist in underdeveloped socialism. It determined that the products produced inside the whole people ownership system were commodity and the exchange between them was commodity exchange.

In addition, some said that there were two reasons why the means of production was commodity: One was the difference in labor. At present, labor was still the means to make a living. Its compensation needed to be realized through the exchange at equal values in enterprises. The other was underdeveloped productivity.

II. The Issue on Expanding the Authority of Enterprises

In the discussion, people believed that there were two approaches to resolve the issue of where to start in the reform of economic management system in China's situation: One was to start with directly reforming various management systems and the other was to start with expanding enterprise authority. Many comrades said that people should start with expanding the authority of enterprises and then reform various management systems correspondingly. In this way, various economic management departments could easily achieve common understanding and avoid passing the buck to each other, sticking to their respective argument, and thus not being able to take action. This approach also agreed more to the reality or the objective situation that China was in the period of adjusting its economy at present and it was not appropriate to implement major change or transformation in economic management system. Of course, various economic management departments should not just watch and wait. They should implement any reform that they felt certain about according to the guiding thought of the central authorities on the reform of economic management system. Some necessary reforms would benefit the adjustment of national economy and promote reform in adjustment.

Then how powerful should the authority of enterprises or companies be? Some comrades believed that enterprise should be given all functions and authorities that a relatively independent commodity producer had to possess so as to manage well in a centralized manner manpower, fund and materials and also supply, production and sale.

Some believed that enterprises should not be given the power to increase employees and sell important products.

Comrades from the Institute of Industrial Economics of the Chinese Academy of Social Sciences believed that there were three methods to expand the authority of enterprises: The first one was to expand authority under the principle of keeping the current basic system intact. For example, an enterprise could only give official approval to a matter involving a value of RMB50 yuan originally. Now it could be expanded to the approval to a matter involving a value of RMB200 yuan. Bonus was only related to the total of wages originally. Now it could be expanded to relating it to the amount of profit. Although the authority of enterprises in a certain aspect was expanded, it did not involve the basic relations in the original system. The second one was to change the supply without compensation to that with compensation in the supply of fixed assets and working fund from the state to enterprises. Thus the relation of enterprises to the state started to change. It also resulted in the expansion of the relations in commodity economy. The third one was that enterprises had autonomy in both the supply of raw materials and the sale of products. When this area was opened up, market economy in fact took up the dominant position.

At the symposium, a comrade from the Sichuan Provincial Academy of Social Sciences introduced the situation and experience in the pilot projects of expanding the authority of enterprises carried out in Sichuan province. He explained vividly with examples the remarkable effect achieved in expanding the authority of enterprises.

Initial experience was achieved through experimentation in combining the expansion of the authority of enterprises with the reform of economic management system.³

III. The Issue of the Theoretical Foundation of the Planned Prices in Socialism

The discussion was about how to determine the part of profit in planned prices. There were three kinds of opinions in general: namely determining it according to average profit rate on wages, average profit rate on fund, or average cost-profit ratio. Some comrades proposed after discussion that these three ideas both had their own strengths and defects. At present, it was difficult to tell which one was the best. So people could take one of them as the dominant one, and refer to and absorb the strengths of other ideas, and thus further study the opinions on improving planned prices. Some explorations were also made with respect to how to calculate the amount of occupied funds of each type of product so as to determine the amount of profit of each product determined according to profit rate on fund and how to further reduce the price scissors differential of industrial and agricultural products and also on the policies to stabilize the prices of commodities.

At this symposium, people liberated their thinking, developed and exchanged various kinds of opinions, and also proposed some questions worthy of further exploration. Compared with the discussion meeting on the theories of economics held in Shanghai in 1959, the symposium was held in different historical background for the discussion of relevant issues. At the time, the discussion meeting was held mainly to criticize and correct the mistake of Chen Boda in instigating the abolition of commodity production, negating the law of value, and trying hard to promote the “communism fad”. The meeting focused on the issue of the commodity production between two kinds of public ownership system and the role of the law of value. This symposium was mainly to explore the issue of the theoretical foundation of the reform of economic management system. It focused on discussing commodity production and the role of the law of value inside the whole people ownership system. At the symposium, people showed more liberated thinking because of the encouragement of the spirit of the Third Plenary Session of the Eleventh CPC Central Committee. But back in the time of the former meeting, there were many forbidden areas in theory and more boxes and rules. At this symposium, people not only summarized China’s own experience in socialist construction in nearly thirty years but also referred to positive and negative experiences in foreign countries so that their view became broader. However, because of limited time, the study and exploration on relevant issues were not in-depth enough. Besides, there was more academic exploration but the study on practical issues was still inadequate. People still needed to strengthen their investigation and study on how to further implement the policy on combining theory with reality and find the economic management system suitable to the actual situation in China.

Because the Central Working Conference did not conclude yet when the symposium was held, the spirit of the conference was not communicated to the people

³See The Institute of Economics of the National Development Planning Commission ed., *Planned Economy Study*, Issue 1, and *Bulletin of the Chinese Academy of Social Sciences*, Issue 33, 1979.

here. So they did not have the opportunity to carry out discussion on the issue of the adjustment of national economy.

It is hereby reported.

Institute of Economics of the Chinese Academy of Social Sciences
Institute of Economics of the National Development Planning Commission
Jiangsu Provincial Institute of Philosophy and Social Sciences
May 31, 1979.

3 Some Representative Views

The last section introduces the general situation of the symposium. Specifically speaking, prominent progress was achieved in the following aspects with respect to the issues of commodity and value in socialism around the time of this symposium.

First, with respect to the issue of how to understand socialist economy, some comrades proposed that socialist economy was both, and first of all, planned economy and commodity economy based on public ownership system. The existence of commodity economy could not be explained with the fact that there were two forms of existence of socialist public ownership system in the present stage. Rather, it was determined by the fact that there was economic interest relationship between the people in the socialist society, including between various collectives of producers, under the premise that their radical interests were consistent. Therefore, socialist enterprises, either enterprises under the whole people ownership system or enterprises under the collective ownership system, were both production units under public ownership system and relatively independent commodity producers.⁴ Some articles even specifically defined socialist economy as planned commodity economy.⁵ These views were very important to studying some important economic issues in socialism.

Second, the means of production exchanged inside the whole people ownership system was in essence commodity. Early in the 1950s, Zhong Jin, namely Yu Guangyuan, and other comrades proposed that the means of production exchanged between the enterprises under the whole people ownership system was also commodity.⁶ This was a profound insight. But at the time, most works on economics in China held the opposite view, namely the belief that this part of social products were not commodity. China's material management system then was also designed according to the formula that these means of production was not commodity. However, the practice in over twenty years proved that such understanding and material management system did not conform to the inherent nature of socialist economy and its development requirements. The situation that people did not recognize the means of production as commodity and implemented planned transfer and allotment system on it caused the problem of low economic effect and the issue that materials

⁴See Sun et al. (1979b), Li et al. (1979).

⁵See Xie and Hu (1979).

⁶See Zhong (1958).

showed serious overstock on the one hand and serious deficiency on the other hand. People should recognize in theory that the means of production was also commodity. And in practice, they should gradually create and establish conditions to transfer step by step the circulation of the means of production onto the track of commerce. They should regulate and retain the balance of supply and demand with various economic levers and urge the enterprises that manufactured these products to increase the types of product, improve quality, reduce consumption and better technical service.

Many comrades demonstrated that the means of production was still commodity from analyzing the characteristics of international relations of the whole people ownership system.

Some said, when state-operated enterprises exchanged the means of production, people could not say that no transfer of ownership right occurred at all. This was because the means of production under whole people ownership was possessed permanently, used, operated and managed by different enterprises. And ownership right was separated to a certain extent from the right of possession, use and operation and management. Such ownership right was also connected with the economic interests of different enterprises. Ownership right would come down to economic interests in the end. Now that the purchase and sale of the means of production between enterprises were connected with their respective economic interests, the purchase and sale of the means of production resulted in fact the transfer of ownership right to a certain extent. Thus such type of means of production was still commodity.

Some said that the “whole people” in the socialist whole people ownership system still divided into different individuals and collectives with different interests. It was different from the “whole people” in the advanced stage of communism in which the essential difference in labor was eliminated, distribution according to needs was practice, and thus there was no contradiction in economic interests between individuals and collectives. Thus, the whole people ownership in socialism was “incomplete whole people ownership system”. When these entities exchanged their own products between each other, people had to use the principle of exchange at equal values to regulate the economic interests between them. So the products were still commodity.⁷

Some said that socialist whole people ownership system was a public ownership system with whole people ownership system as the dominant part, which included the collective ownership system of part of the production units, or the whole people ownership system that included local ownership system and enterprise ownership as its components. Such form of ownership system would definitely exist in underdeveloped socialism. It determined that the products produced inside the whole people ownership system were commodity and the exchange between them was commodity exchange.

It was obvious progress to turn from studying the relations between different ownership systems in the past to studying the relations inside the whole people ownership system in the discussion on the objective necessity of the existence of commodity production.

⁷See He (1979), Liu et al. (1979).

Third, the law of value still played a regulatory role in socialist production. In the past, people generally negated that the law of value played a regulatory role in socialist production and put the principle of developing in a planned manner in opposition to the law of value. In the period before the discussion, many articles were written to emphasize that both the principle of developing in a planned manner and the law of value contained the requirement to distribute social labor proportionately, which was the common basis for the two principles to play their regulatory role in socialist economy which included both production and circulation. The several devastations of the economy in our country from the founding of the People's Republic of China were all the result of the violation of both the principle of development in a planned manner and the law of value. Viewed from practice, some countries that excessively emphasized the leadership of unified and centralized planning and paid little attention to utilizing market regulation encountered problems that showed certain negative commonalities, such as imbalance of important proportions, fewer product types, poor product quality, large consumption in production, low efficiency and economic growth slowdown. This indicated that the situation was not completely caused by the problems in planning work but there were defects in economic management system. In the future, people should, first of all, respect the regulatory role of the law of value and fully utilize market mechanism in economic management while respecting the principle of planned development. They should unify and combine the regulatory roles of the principle of planned development and the law of value both in theory and in practical work. Thus, they could break through the theory on the mutual exclusion of planning and market in socialist economy in theoretical study.⁸

Sun Yefang further believed that, of all kinds of economic laws and principles, the law of value was the primary one. He said, "As far as the entire social production is concerned, what plays the determinant role is, after all, the law of value in the sense of saving time." "The law of value is the main basis of the planning work."⁹ Soon after, Sun Yefang also proposed that people should take "value" as the baseline to construct the new system of socialist political economics.¹⁰

Fourth, people should practice the combination of planned regulation and market regulation in socialist economy. Now that socialist economy was planned economy and the principle of planned development and the law of value jointly played the regulatory role, people should follow the policy of combining planned regulation and market regulation. Planned regulation showed that the society could consciously arrange social production in a proportionate manner while market regulation realized the proportionate development of social production through market mechanism. Besides, planned regulation and market regulation were mutually permeating. Planned regulation could not be implemented without market mechanism while market regulation could not be implemented without the guidance of planning. These

⁸Reference Room of the Institute of Economics of the Chinese Academy of Social Sciences et al. *The Materials on the Issue of the Role of the Law of Value*, China Social Sciences Press, 1979, pp. 103–104.

⁹Sun (1978).

¹⁰Sun (1959).

two measures were of the relationship that there was a bit of me in you and a bit of you in me.

Some comrades pointed out that what should dominate in the relationship between planning and market was a question that should be answered through deeply studying the essence of socialist economy and considered in relation to what kind of model China's reform would follow. If people stressed on concentration, then it was naturally that planned regulation should dominated and the relations of commodity and money and the law of value should be utilized under such premise. Otherwise, people should employ more extensively the regulatory role of market mechanism and the law of value. People should decide prudently on which approach would be chosen and made thorough study on it. Many comrades believed that neither too much concentration nor too much decentralization would work. We should start with China's own situation and create the road of Chinese style.¹¹

Fifth, enterprises or companies should be given all functions and authorities that relatively independent commodity producers had to possess so that enterprises could have certain autonomy in manpower, fund and materials and also supply, production and sale. Thus, people could form close connection between the result of operation of an enterprise and the material interests of its employees so that the employees would care about improving the operation and management of their enterprise because of material interests and thus the enterprise would have internal economic dynamics. In the beginning of 1980, Jiang Yiwei further proposed the famous enterprise standard theory and pointed out that an enterprise was an entity with independent economic interests and an independent commodity producer and operator.¹²

Sixth, necessary competition should be allowed and carried out. Competition was an objective principle in commodity production and exchange. It was also an important mechanism to strengthen and improve planned economy. The difference between competition and contest mainly laid in the situation that the enterprises that stayed behind without any shame over a long period of time so that their products had very high cost or were needed by the society no more would be eliminated. To allow and carry out competition to a certain extent under the guidance of planning in socialist economy could form an external compulsory force to urge enterprises and economic sectors to work hard to advance.

Seventh, some articles further proposed and explored the issues in socialist market. It was believed that socialist economy was planned market economy. People should bring into full play the regulatory role of the law of value and also the role of market mechanism. These assertions were very far-reaching.¹³

¹¹ Secretariat of the Symposium, "The Situation of the Discussion at the Symposium on the Issue of the Role of the Law of Value and the Questions Proposed", in Reference Room of the Institute of Economics of the Chinese Academy of Social Sciences et al. ed., *The Relationship between Planning and Market in Socialist Economy* Vol. 2, China Social Sciences Press, 1980, p. 776.

¹² Jiang (1980).

¹³ See Yu Zuyao, "A Tentative Discussion on Socialist Market Economy", Gu Jirui, "Several Issues on Socialist Market Economy", in Reference Room of the Institute of Economics of the Chinese Academy of Social Sciences et al. ed., *The Relationship between Planning and Market in Socialist Economy*, Vol. 1, China Social Sciences Press, 1980.

Eighth, in order to adapt to the reform of economic management system, people need to gradually implement pricing according to production price. The theory on production price was proposed early at the end of the 1950s but very few people approved it. Now more people advocated set prices according to production price. Compared with the situation before 1966, their arguments showed the following developments: (1) To demonstrate that pricing according to production price was the standard to correctly evaluate the result of labor from the fact that socialist society needed to make working people and their collectives to care about the results of their labor because of material interests. (2) To explain that products should be priced according to production prices from the aspects of the reform of economic management system, including implementing fund tax, gradually implementing loan system in infrastructure investment, and gradually implementing the system of getting working fund exclusively from bank loans. And (3) To demonstrate the objective necessity of pricing according to production price from the fact that competition needed to be practiced to a certain extent in socialist economy, including the comparison of investment effect and economic effect between different sectors.¹⁴

Some articles proposed that people should reform the current irrational price system and price management system and gradually narrow the “scissors differential” between the prices of industrial and agricultural prices. Raising the purchase prices of agricultural products and lowering the sale prices of the means of agricultural production were measures to narrow the “scissors differential” between the prices of industrial and agricultural prices. But the most fundamental one was to rely on the improvement of the labor productivities in industry and agriculture.¹⁵

The discussions in the symposium indicated that the study on the issues of commodity and value under socialist system needed to start with reality rather than books. When the study started with reality, the theory would become lively and active and play a positive role in practice. When it started with books, theoretical study would become stale and dying and depart far away from practice. A group of treaties emerged in the discussion, which could applied Marxism and Leninism to the practice of socialist construction in China, summarized new theories from it, and broke the boxes of outdated principles and conclusions. It was because people took such an attitude of seeking facts from truth that theoretical study showed creative spirit and played a positive role in developing socialist economy.

¹⁴See He et al. (1979); Zhang Weida, “Production Price and Economic System Reform”, Liu Sihua, “The Discussion on Production Price and the Lessons in It in the Development History of the Theories of Economics in China”, Xiao Zhuoji, “On the Role of Average Profit Rate in Socialist Economy”, in Reference Room of the Institute of Economics of the Chinese Academy of Social Sciences et al. ed., *The Issue of Price Formation under Socialist System*, Chinese Social Sciences Press, 1980.

¹⁵See Hu Changnuan, “Talking about the Issues of Scissors Differential and General Price Level”, Lu Nan, “The Issue of Price Comparison and Scissors Differential of Industrial and Agricultural Products”, in Reference Room of the Institute of Economics of the Chinese Academy of Social Sciences, *The Issue of Price Formation under Socialist System*, Chinese Social Sciences Press, 1980.

The discussion in the symposium indicated that, in such a country like China where capitalism was very undeveloped and petty production took the absolute dominant position in the past, there could often be various misunderstandings and difficulties when people developed commodity production and brought into play the role of the law of value after the victory of the revolution. Some people saw the relations of commodity and money from the angle of petty production and adopted an attitude of expulsion and opposition. This often encouraged the outlook of natural economy and also the attitude of taking left-deviation rather than right-deviation when dealing with commodity economy. This situation was unfavorable for developing commodity production and exchange and utilizing the law of value to serve socialism.

The discussion in the symposium also indicated that the process of understanding truth was complicated and full of twists and turns. Sometimes, the truth was in the hands of the few. And there needed to be a process for the majority to understand the truth. People should truly implement the “Double Hundreds” policy of letting a hundred flowers blossom and a hundred schools of thought contend and strictly separate political issues from academic issues. Only in this way can they avoid the recurrence of the tragedies of stifling the truth and attacking the people who adhered to the truth.

In the beginning of 1960s, people proposed in China’s arena of theoretical discussion the position that practice was the sole standard to test whether economic theories, policies, plans and measures were correct. However, some rules and boxes still tightly confined the mind of the people at the time so that this issue could not attract sufficient attention of the people and let them see its importance. Only after China learned the painful lesson of two rises and two drops of national economy did people deeply feel the extreme importance of testing economic theory and policy with practice.

After the Third Plenary Session of the Eleventh CPC Central Committee, the central authorities called for workers in theoretical study to study and resolve the new issues proposed in the process of the transfer of the CPC work priority and the realization of the Four Modernizations. Such calling was made at the time when conditions were ripe for completing this task. People believed that, as long as they adhered to the policies of linking theory to practice, seeking truth from facts, and letting one hundred schools of thought contend, they could complete the task in a good way, constantly push the study on the theoretical issues of the commodity and value under socialism to deeper levels, and thus promote socialist modernization construction. Besides, the practice in the study of economic theories told us that the scientific nature of socialist political economics depended to a very large extent on whether people could scientifically formulate the issues of commodity and value in socialism. Therefore, any new progress in the study on the issues of commodity and value would forcefully promote the establishment and improvement of the scientific system of socialist political economics.

Like the exploration on any scientific question, the study on the issues of commodity and value under socialist system was a process of constantly approaching the truth. People could only advance step by step on the road of climbing the peaks of science and it was unlikely for them to complete their mission at one go.

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Chapter 8

Scholars Working on Economic Theories Participated in a Large Scale in Economic Investigation and Survey Activities in the Early Period of the Reform and Opening Up



Zhouyuan Zhang

1 Background of the Investigation and Survey Activities

In order to resolve the imbalance in major proportions in national economy from 1966 to 1976, the Finance and Economy Committee of the State Council decided to form four investigation groups to carry out in-depth investigation and survey on Chinese economy in June, 1979 soon after the reform and opening up started. The purpose of such decision was to better implement the eight-character policies of adjustment (*Tiao Zheng*), reform (*Gai Ge*), rectification (*Zheng Dun*) and improvement (*Ti Gao*) and to push forward socialist modernization construction in China. These investigation groups were as follows: the investigation group of economic management system led by Zhang Jinfu, the investigation group of economic structure led by Ma Hong and Sun Shangqing, the investigation group of technology introduction and enterprise modernization led by Gu Mu, and the investigation group of theory and methodology led by Yu Guangyuan. The members of these groups included both workers in practical economic work and a large number of workers on economic theories and teaching of economics. For example, the group of economic structure took in over 200 scholars in economics who engaged in theoretical study and teaching.

The investigations lasted for a longer period of time. It was not several months or half a year but several years. For example, the research team of the reform of economic management system submitted in December 1979 the first general plan on economic reform in China entitled *Initial Opinions on the General Conception of Economic System Reform*. In May 1980, the State Council formed the Economic System Reform Office to take over the work of the investigation group. Later, it formed the Economic System Reform Committee to continue the investigation work carried out before.

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In the following, the author intends to focus on introducing the activities of the investigation groups of economic structure and economic management system.

2 Activities of the Investigation Group of Economic Structure

From June 1979, the investigation group of economic structure lead by Ma Hong and Sun Shangqing organized over 400 economic experts who engaged in practical work and over 200 economic scholars who engaged in theoretical research in the group. And they gathered over 100 people together to form the comprehensive investigation team of economic structure to carry out investigation work for ten months in more than ten provinces and municipalities. The economists who took part in the investigation at the time included Liu Zhongyi, Wu Jinglian, Zhou Shulian, Yang Jianbai, Chen Jiyuan, Cai Zhongjie, Yang Shengming, Zhang Shuguang, Zhang Zehou, Zhang Zhuoyuan, Rong Wenzuo, Hu Zhaoliang, Yu Zuyao, Chen Xikang, Wang Haibo, Li Yue, Chen Shengchang, Wei Jianing, Mao Tianqi, Xue Yongying, Dai Yuanchen, Yun Xiliang and Ren Weizhong.

Fruitful results were achieved in the investigation. All these results were reported to the CPC Central Committee and the State Council to provide reliable basis for decision making in the efforts to implement adjustment of economic structure at the time. Part of the research results of the investigation group were included in the book *The Study on the Issue of Economic Structure in China* edited by Ma Hong and Sun Shangqing and published by the People's Publishing House in 1981. The book was the first work in economic study published in China that contained a large amount of practical materials and systematic data and caused great social influence in China and abroad.

On such basis, Sun Shangqing organized in 1983 experts and scholars to carry out further study and propose countermeasures and suggestions on a number of particularly important issues in China's economic structure at the time, including strategic goal of economic development, industrial structure, technology structure, structure of science and education, employment structure, enterprise size and organizational structure, regional structure, structure of accumulation, investment structure, consumption structure, and international exchange and ownership structure. Their research work was collected in a book entitled *On the Countermeasures in Economic Structure*, compiled by the scholars with Sun Shangqing as chief editor and Zhang Zhuoyuan, Cai Zhongjie and Chen Jiyuan as vice chief editor and published by China Social Sciences Press in 1984. The book included pioneering research work on important issues in China's economic structure. It was honored the First Sun Yefang Award for the Works in Economic Science in 1984.

In the middle of 1980s, Ma Hong and Sun Shangqing continued to organize a group of economists to study the issue of economic structure and wrote the *Collections on China's Socialist Economic Structure*. Among these publications, *A Collection*

of the Readings on China's Socialist Economic Law was written by the scholars with Ma Hong and Sun Shangqing as chief editors and Zhou Shulian and Zhang Zhuoyuan as vice chief editors and published by the Shanxi People's Publishing House and the China Social Sciences Press at the end of 1980s. The majority of the authors participated in the work of the investigation group of economic structure under the Finance and Economy Committee of the State Council from the summer of 1979 to the spring of 1980 and thus had good experience in studying the issues on China's economic structure. The collection had various features in theoretical study, practical application, referential value and knowledge dissemination combined together. It possessed inherent connection to the two books of *The Study on the Issue of Economic Structure in China* edited by Ma Hong and Sun Shangqing and *On the Countermeasures in Economic Structure* edited by Sun Shangqing. It represented the continuation, deepening and development of the study on China's economic structure contained in the first two works. The collection included 19 books as follows: *An Introduction to China's Economic Structure*, *The Study on the Structure of Industrial Sectors in China*, *The Study on China's Agricultural Structure*, *The Study on the Structures of the Light and Textile Industries in China*, *The Study on the Structure of Communications and Transportation in China*, *The Study on the Energy Structure in China*, *The Study on the Structure of Steel and Iron Industry in China*, *The Study on the Structure of Construction Material Industry in China*, *The Study on the Structure of Chemical Industry in China*, *The Study on the Financial Structure in China*, *The Study on the Circulation Structure in China*, *The Study on the Price Structure in China*, *The Study on the Consumption Structure in China*, *The Study on the Population Structure in China*, *The Study on the Education Structure in China*, *The Study on the Employment Structure in China*, *The Study on the Structure of Ownership Systems in China*, *The Study on the Regional Structure in China*, and *The Study on the Enterprise Organizational and Management Structure in China*.

In particular, it was worth mentioning that the structural issues present at the time and the suggestions on improving China's economic structure, proposed by the investigation group of economic structure after investigation work about thirty years ago, were not only practical, profound and reasonable at the time but also of realistic meaning in many areas until today. After the investigation work, people listed the following main issues present in economic structure at the time: (1) Agriculture lagged behind industry seriously and obstructed the rapid development of national economy. (2) Light industry was backward and it could not satisfy the needs of the people in the city and the countryside to improve living standard. (3) Heavy industry showed one-sided development, disconnected from agriculture and light industry, and also internal disproportions. (4) Communications and transportation were backward. Postal service and telecommunication was a weak link in national economy. (5) Business and service industry did not match the development of national economy. (6) Foreign trade did not match the requirements in modernization. (7) Infrastructure construction was of too large scale and too wide range. (8) The "bone" and "meat" in economy was disproportionate, meaning that the investment concerning the livelihood of the people showed lower proportions. "In the issues in the above, the most important was the disproportions between agriculture, light industry and heavy

industry. The proportions between agriculture, light industry and heavy industry were in essence the relationship between the two major sectors of the means of production and the means of consumption. At present, the radical issue in China's economic structure was that it did not create the balance between the production of the means of production and that of the means of consumption. In particular, the production of the means of consumption lagged behind that of the means of production. We should take resolving the relationship between these two major departments as the starting point in resolving a series of issues on economic structure."¹

With respect to the issues present at the time, the investigation group proposed ten suggestions for accelerating the adjustment of economic structure:

(1) To comprehensively develop agriculture and lay a solid foundation for the development of national economy. (2) To speed up the development of light industry and improve the livelihood of the people. (3) To adjust the structure of heavy industry and bring into full play the role of machine industry in technical transformation. (4) To vigorously develop energy industry and establish long-term and stable energy policies. (5) To gradually implement the transformation of construction units into enterprises and the commercialization of buildings. (6) To appropriately lower the rate of accumulation and reasonably adjust investment structure. (7) To adjust the structure of imported and exported goods. (8) To carry out well the division of economic regions and exert the economic advantages of various regions. (9) To set transportation as priority, which was an important condition in the rationalization of economic structure. And (10) To reform management system and promote the rationalization of economic structure.

The report of the investigation group of economic structure exerted important influence on the decision making of the central authorities on economy. In September 1982, Hu Yaobang specifically proposed in the *Report at the Twelfth CPC National Congress* that people "should concentrate main forces and resources to carry out adjustment in various aspects in economic structure" during the Sixth Five Year Plan from 1981 to 1985. It was said in the report that "during the Sixth Five Year Plan from 1981 to 1985, people should continue to relentlessly implement and carry out the policies of adjustment, reform, rectification and improvement. They should practice strict economy and oppose waste and shift the entire economic work onto the track of taking the increase of economic benefits as the center. They should concentrate main forces and resources to carry out adjustment on various aspects in economic structure. They should implement the rectification, restructure and merger of existing enterprises and conduct the technological transformation of enterprises with clear priorities. Besides, they should consolidate and improve the progress of the initial reform already implemented in economic management system and speed up formulating the general plan and implementation steps of the reform. During the Seventh Five Year Plan from 1986 to 1990, they should extensively implement technological transformation of enterprises, gradually carry out the reform of economic system, and continue to complete the rationalization of the organizational structure of enterprises and various aspects of economic structure."

¹See Ma and Sun (1981), p. 7.

Under the guidance of the correct policies of the CPC and the government, important progress was achieved in the adjustment of economic structure in China in the early period of the reform and opening up. Agriculture saw quick restoration and development, light industry also experienced accelerated development, and the proportions between agriculture, light industry and heavy industry became coordinated and balanced again. During the Sixth Five Year Plan from 1981 to 1985, gross agricultural product showed an average annual growth of 11.7% while the average annual growth in the 26 years before 1978 (1953–1978) was only 3.2%. The gross product of light industry showed an average annual growth of 12% while the average annual growth in the 26 years before 1978 was only 9.1%. The growth of heavy industry slowed down to a certain extent in comparison with the past. Thus the structure of agriculture, light industry and heavy industry was improved. In 1978, the proportions of agriculture, light industry and heavy industry in the gross industrial and agricultural product were 27.8:31.4:41.1. In 1985 such proportions were adjusted to 34.3:30.7:35. During the Sixth Five Year Plan from 1981 to 1985, main agricultural product showed large growth. In comparison with the Fifth Five Year Plan from 1976 to 1980, average annual product of food grew from 305 million tons to 370 million tons, that of cotton from 2.24 million tons to 4.32 million tons, and that of pork, beef and mutton from 9.37 million tons to 14.62 million tons. Such progress brought great improvement of the market supply of agricultural and sideline products and remarkable bettering of the livelihood of the people so that the reform and opening up won the support and advocacy of the extensive public community in China from the beginning. In addition, improvements were also achieved in other economic structures.

As it is shown in the above, the research results, countermeasures and suggestions from the investigation on economic structure in the early period of the reform and opening up were correct and played a good promotive role to the practice of economic development.

3 Activities and Research Results of the Investigation Group of Economic Management System

The research team of economic system reform was headed by Zhang Jinfu, the then vice director of the Finance and Economy Committee of the State Council. In December 1979, the research team submitted the first general plan on economic system reform in China entitled *Initial Opinions on the General Conception of Economic System Reform*. The conception proposed was that people should organize the activities of the entire national economy according to the requirement of socialized production. People should mainly adopt economic measures, manage economy through economic organizations, practice the combination of planned regulation and market regulation, and expand the autonomy of enterprises under the guidance of state plans. Then with the above as the premise, they should divide the functions and

powers of central and local authorities on the basis of the characteristics of various economies and undertakings. What was suitable for central authorities to manage should be given to central authorities in management while what was suitable for local authorities to manage to local authorities. The main aspects in reform included the following: People should break the boundaries between departments, regions and military and civil undertakings, free themselves from the restrictions of the differences in ownership forms, and organize various specialized and joint companies in various forms according to the inherent connections in economy and specialized cooperation, which was taken as principles. Enterprises should manage their own manpower, fund and materials and also production, supply and sale and then practice independent accounting and assume sole responsibility of their profit and loss. The state mainly direct, control and coordinate the economic activities of the enterprises through various economic legislation and means and necessary administrative means retained. The planning of the state mainly focuses on middle- and long-term plans. Annual plans should be formulated in a bottom-up manner with the planning of the enterprises as the basis, guided by state-controlled figures. It can be seen that such general plan highlighted the expansion of the autonomy of enterprises and proposed that people should positively push forward the horizontal integration of economy and change the situation that instructions given in the vertical direction took up the dominant position in the traditional system of planned economy.

In May 1980, the State Council formed the Economic System Reform Office and continued to carry out investigation work on economic system. And it proposed in the same year *Initial Opinions on Economic System Reform*. It was proposed in the *Opinions* that “the principles and directions of China’s economic system reform” included the following: People should consciously apply economic principles and break the restrictions of the boxes in administrative measures and the thought of natural economy according to the requirements of developing commodity economy and promoting socialized production and under the condition of retaining the dominance of the public ownership system of the means of production. They should change the highly-centralized state decision making system into the decision-making system that combined the state, economic units and individuals among the working people. They should change monotonous planned regulation into bringing into full play the regulatory role of the market under the guidance of the plans. They should change the management of economy mainly in reliance to CPC and governmental organs and administrative measures to the management of economy mainly in reliance to economic organizations, economic measures and economic laws and regulations. And they should mobilize the initiative of various parties, reasonably organize various economic activities, achieve the maximal economic effect with the minimal labor consumption, and speed up socialist modernization construction. It can be seen that the *Opinions* in 1980 made a step further than the “general conception” in the year past and clearly proposed that reform meant to build an economic system adapted to commodity economy.

Then in February 1982 the State Commission for Restructuring the Economic System drew up the *General Plan on Economic System Reform*. The document presented the “objectives of the economic system reform at the present stage” as

follows: People should build a planned economic system adapted to the development of commodity production in which socialist public ownership took up absolute dominant positions and various economic components coexisted. With such a system, they should mobilize the initiative of various parties, promote the coordinated development of socialist economy, and improve social and economic benefits to the maximum. This new economic system was a socialist economic system that took public ownership economy as the dominant part and other economic components as supplementation, in which major powers were centralized and minor powers decentralized, in which planned economy dominated and market regulation supplemented, in which people moved freely in and out of an enterprise and practiced distribution according to performance, and in which scientific division of work was practiced between the CPC, the government and enterprises and economic and administrative means formed close cooperation. *The General Plan* summarized outlining ideas in eleven aspects about the specific content of the reform as follows:

(1) People should build an ownership structure with state-operated economy as the leading sector, public ownership economy as the dominant party, and other economic components as supplementation, in which various economic components coexisted. Relevant measures included that the scope of state-operated economy should be narrowed properly, that service industry should mainly be operated by collectives and individuals, that rural economic units should develop collective economy syndicates in different forms according to the principle of voluntariness and mutual benefits and properly develop the Chinese-foreign joint ventures and joint venture economy in various forms.

(2) People should build economic responsibility system in various forms and break the system of egalitarianism in enterprises according to the principle of the combination of responsibility, right and profit.

(3) People should organize various economic activities and realize the rationalization of enterprise organizations and economic organizations according to internal connections of economy, including breaking the boundaries of regions, departments, military and civil undertakings and ownership system, forming economic unions in various forms and implementing enterprise-styled management inside these unions, and establishing various kinds of industrial centers and trade centers and corresponding financial, intelligence, forecasting and consultation economic organizations.

(4) People should establish open and unified commodity circulation market with multiple channels and less intermediate links and with state-operated commerce as the main part.

(5) People should improve and enhance planned management and establish scientific and effective planning system.

(6) People should bring into full play the role of economic levers according to the requirement of economic principles, including building scientific price, taxation, fiscal and financial systems.

(7) People should build employment and compensation system in which people could move freely in and out of an enterprise, in which they could be promoted and demoted, and in which people were paid more when they worked more, less when

they worked less and with nothing when they did not work and changed the situation that each person was given a secure job like an iron rice bowl.

(8) People should strengthen the legislation, law enforcement and supervision related to economy. It was proposed that people should formulate economic laws and regulations, such as civil law, factory law, shop law, corporate law, foreign trade law, taxation law, price law, planning law, law on statistical matters, accounting law, law on fiscal matters, banking law, labor law, market law, investment law, metrological law, standard law, patent law, land law, grassland law, aquatic resources law, and mining resources law, and form economic courts.

(9) People should implement well the reasonable division of work between central and local authorities under the centralized leadership of the central authorities and according to the principle of “centralized leadership and graded management”.

(10) People should improve the leadership and management system inside the enterprises according to the principles of the collective leadership of the CPC committee, the democratic management of the employees, and the administrative commanding of the factory director. And it was also proposed that factory director was the legal representative of an enterprise.

(11) People should complete and improve economic management organization system according to the principle of the reasonable division of work between the CPC and the government. It can be seen that a noticeable characteristic of the General Plan was that it was specifically proposed that people should reasonably adjust ownership structure and build an ownership structure in which public ownership system was the dominant part and various economic components coexisted.

It needs to be pointed out that, in addition to the leaders and experts of the fiscal and economic departments, a group of economists, such as Xue Muqiao, Ma Hong, Gao Shangquan and Yang Qixian, also joined the investigation group of the reform of economic management system in the early period of the reform and opening up.

The results of the investigation activities directly pushed forward reform and opening up and development in economy. Expanding the autonomy of enterprises, developing non-public-ownership economy and rural household contracted responsibility system, establishing special economic zones, utilizing foreign investment, developing rural fair trade, and lifting the limitations on the prices of small commodities all gradually spread out in China so that the entire national economy started to become active.

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Chapter 9

The Reform to Establish the Rural Household Contracted Responsibility System in the 1980s Was the Important Breakthrough in Traditional Socialist Economic Theory



Lin Zhang

The reform of China's economic system started at the end of 1970s. Breakthrough was first achieved in the reform of rural economic system. This was the most important characteristic of China's economic system reform and also an important reason that such reform could achieve remarkable success within a period of time not very long.

1 Background

From the late the 1950s, one wave after another of the “climaxes of the People's Commune Movement” rose in the countryside in China, pushed by the constantly fermenting left-deviation thought trend. With a bit more than three years, the movement of forming “advanced commune” of complete socialist nature was completed. And then with a bit more than two years, the initiative of forming the people's commune, which was the preparation for the “transition into communism”, was accomplished nationwide. The people's commune represented a system with the characteristics of “being large in size and collective in nature” and “combining government and commune into one”. It was established on the basis of self-sufficient and semi-self-sufficient natural economy. It was a syndicate that bore the colors of strong administrative nature, equalitarianism, military communism, and utopianism that went beyond the proper development stage of society. It was born with great defects. The people's commune stressed on “collectivization” in labor organization, “equalization” in income distribution, and “planning” in agricultural production. Compounded by the troubles caused by the “communism fad” and the “boast and

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brag fad”, the movement of people’s commune resulted in the devastation of agricultural productivity in China. The initiative of the peasants in work was greatly damaged and the peasants themselves still lived in extreme poverty for a long period of time. From the end of 1970s to the beginning of 1980s, millions of Chinese peasants in the mass bravely broke the cage of the rigid system in the highly centralized operation of the people’s commune. They implemented the household contracted responsibility system (or “household contracting system” for short) which took “fixing farming output quotas by household” and “contracted fixed tax payment and quota fulfillment by household” as the main forms of operation and the collective ownership of land and other means of production as the basis. The reform was a fundamental transformation of epochal meaning in China’s rural economic system.

Household contracting system was of various forms. Its basic content was that the collective divided the land that it owned to its members evenly according to the proportions of population and labor forces and contracted to peasants by household for operation. The collective and the peasant households signed contracts. The peasants took full responsibility in farming and harvesting and paid public reserve fund, public welfare fund and other retentions to the collective and agricultural tax and tax grain to the state according to fixed quota proportions. Such system emerged in the countryside in China early in 1956 and was welcomed by the extensive community of the peasants and rural grassroots cadres. But the government criticized and banned it under the accusations of “individual farming fad”, “taking capitalist road”, and “revisionist line”. Nonetheless, such operation form never died out completely after several rises and falls. It still existed in some places publicly or secretly. After the Third Plenary Session of the Eleventh CPC Central Committee held at the end of 1978, the system, created independently and implemented spontaneously by the peasants, quickly spread all over the countryside in China as a major reform and became the dominant form in the operation of rural economy in early 1980s under the ideological guideline of the CPC Central Committee of “seeking truth from facts and liberating the thought”.

2 People Gradually Reached Consensus in Understanding

When the reform of the household contracting system just began, people did not have consensus on it in understanding. Some people still did not free themselves from the confines of left-deviated theories, thoughts and outlooks. As a result, they still had different questions and doubts on the implementation of the household contracting system. For example, some people believed that the system did not adhere to public ownership and distribution according to performance. The collective economy at the level of production team actually already became “empty shell” and “existed in name only”. The public ownership “based on production team” was shaken and disintegrated. So the system in fact represented the retrogression to “individual farming”. It was a special form of small-scale peasant economy that only retained the look of collective economy. Such a view was once rather popular the moment when the

system was just implemented. Later, fewer people took such view but it never died out. There were still a large number of people who held such a view. Some of them were peasants and grassroots rural cadres. Some peasants called the distribution of contracted land as the “Second Land Reform” which meant that “land returned to home”. Some rural cadres complained that “thirty years of hard work was reset to the situation before liberation overnight”. These were both the reflection of such a view.¹ Some other people believed that the household contracting system was good but it was of “dubious ownership attribute” and “skewed direction”. So it might not last long and would turn back to old tracks some day so that a “Second Collectivization” might occur.²

The doubts on the nature of the household contracting system in the society were also reflected in the circle of economic theories. In early 1980s, a group of articles that discussed the household contracting system were published successively on some major newspapers and magazines nationwide. The main points in these articles were focused on the question of whether household contracting system changed the nature of collective economy. Most articles regarded household contracting system as the “change of labor organization form” or the “change of operation and management form” or even only the “change of the form of production responsibility system” and so on within the framework of collective economy and cooperative economy. And these ideas were taken as the basis of the assertion that the system “did not change the nature of collective economy”.³ It should be pointed out that a few particular articles analyzed that the implementation of the household contracting system “delegated all of the actual powers of operation and management and product distribution in production and the rights of possession, use and disposal of the means of production to peasant household”. It was also proposed in them the issue of the “realization of public ownership”. However, the authors believed that it was exactly these powers and rights that indicated the household contracting system was “no more complete in the nature of collective economy” and that it was “the way-out and direction of Chinese agriculture” “to adhere to the form of collective economy based on production team”.⁴ Some scholars in theoretical work proposed various doubts on whether the household contracting system would influence the modernization process of agriculture. For example, some people believed that the system intensified the peasants’ psychology of dependency and attachment to the land and they would take contracted lands as privately owned lands. Besides, the land was divided into small pieces. This hindered both the mechanization of agriculture and the concentration of land to develop operations in a properly large scale. Household contracting system also resulted in the allocation of all the accumulations of the collective economy over many years. As collective economy was weakened, it would be extremely difficult to raise the funds needed for the modernization of agriculture. After the abolition of the old people’s commune system, the degree of organization of the peasant

¹See Liu (1980), Yin (1980).

²See Lin (1983b).

³See Guo (1982).

⁴See Ma (1981).

community was greatly reduced. The peasant households that operated in extreme decentralization found it hard to adapt themselves to the development and change in market economy and even harder to improve themselves to certain height according to the needs of the market so as to adapt to modernization. Therefore, some scholars in theoretical work believed that household contracting system was a product that came out of the failure of collectivization on the basis of traditional agriculture. The system represented both the correction of the mistakes in collectivization in the past and the efforts made to retain and save the direction of collectivization and its results. The system was born under such special social and historical background as the above. This determined that it would not exist forever. And because it was suitable to the agriculture in China at present, which was in the traditional stage, but not to modern agriculture, it would declare the completion of its own historical mission some day as China's agriculture developed more and more toward the direction of modernization.⁵

In the beginning of 1982, the *Minutes of National Rural Work Meeting*, transmitted by the CPC Central Committee, pointed out in response to the worries of the cadres and the mass about the nature and prospects of the household contracting system that various forms of the household contracting system, including "fixing farming output quotas by household" and "contracted fixed tax payment and quota fulfillment by household", belonged to the forms of cooperative economy in socialism.⁶ Then the report of the Twelfth CPC National Congress held in September 1982 further affirmed the creative practices of the peasant mass in rural reform. It pointed out that "various forms of production responsibility system established in the countryside in the recent several years further liberated productivity. People must persist in implementing them over a long period of time. They can only gradually improve them on the basis of summarizing the experience of the mass in practice. They shall not make rash changes in violation of the will and intention of the mass. They should never turn back onto old paths."⁷ In the beginning of 1983, the CPC Central Committee transmitted *Several Issues on Current Rural Economic Policies*, a document put into trial application as a draft, which laid down policy provisions on the new situations and issues that emerged in the countryside after the household contracting system was put into practice.⁸ All these documents played a very important role in removing the worries of the cadres and the mass on the household contracting system and promoting its healthy development and consolidation.

After a few years of practice, household contracting system saw increasing development, consolidation and improvement and its superiority was brought into full play. Agricultural production developed and thrived, the income of the peasants saw large increase, and the situation in the countryside was greatly improved. In front of such reality, the doubts of the people on household contracting system were basically eliminated. However, how to deeply analyze the status, role and future of the

⁵See Lin (1983b), Zhao (1983), Yuan (1996).

⁶"The Minutes of National Rural Work Meeting", *People's Daily*, April 6, 1982.

⁷Hu (1982).

⁸"Several Issues on Current Rural Economic Policies", *People's Daily*, January 2, 1983.

system in the entire rural economic system reform from a theoretical perspective and how to examine the practical and theoretical meaning of the system from a macroscopic angle of China's market-oriented reform was an important research topic that urgently needed to be dealt with in the circle of economic theory in China.

3 The Theoretical Meaning of the Reform of Rural Household Contracted Responsibility System

In 1983 three articles about household contracting system were published in *Economic Research Journal*, a renowned periodical of economic theories in China. These were the attempts of scholars in theoretical research to explore the practice of reform in household contracting system in the countryside from novel angles. These three articles included "Implementing Contracted Fixed Tax Payment and Quota Fulfillment by Household is the Prelude of China's Economic System Reform" written by Yu Zuyao and published in the thirteenth issue, "Contracted Fixed Tax Payment and Quota Fulfillment by Household is the Reform to Realize Advancement in Productive Relations" written by Li Jiapeng and published in the eleventh issue, and "The Rise of New-Type Household Economy in the Countryside in China" written by Tang Mingxi and published in the twelfth issue. A common characteristic of these three articles was that authors of these articles all believed that the implementation of household contracting system was not just the "change of labor organization form" or the "change of operation and management form" or the "change of the form of production responsibility system" but was a profound change in socialist productive relation and an important breakthrough in traditional theory of socialist economy. With the discussion in these three articles taken into consideration, such change or breakthrough could be summarized into that in the following several aspects.

First, in the area of the ownership system of the means of production, the original people's commune system was established according to the basic modes in traditional socialist economic theory, in which land and other main means of production were possessed and used commonly. Under household contracting system, the productive relation between peasant household and land and other main means of production were established according to the basic modes in socialist commodity economy. Its theoretical basis was the formulation that ownership system could be further divided into the four parts or four forms of the rights of ownership, disposal, possession and use. The household contracting system was in fact established according to a new public ownership system in which land and other main means of production were still owned by the "collective" composed of peasant households and disposed of by such "collective" but given to peasant households to hold in actual possession and use and thus the four rights were separated from each other. It was a creative invention of Chinese peasants in the practice of cooperative economy over a long period of time. Its essence was to establish a new mode to combine producer and the means of production. Under the system of people's commune, the members of the

commune realized the indirect combination of producer and the means of production in the scope of the society in general under the premise of publicly-owned land and the integration of the four rights into one. Differently, peasant households under household contracting system realized the direct combination of producer and the means of production within the scope of household in the process of production under the premise of publicly-owned land and the separation of the four rights. In the transformation from indirect combination to direct combination, peasant households also changed from providing individual laboring members to production team, the basic economic unit under the system of people's commune, to functioning as a basic economic unit in an independent level in socialist commodity economy that possessed the nature of economic entity. Naturally, in some places where collective economy had stronger economic strength, when implementing household contracting system, the collective still retained the rights of use and disposal on some means of production such as large machinery and equipment and large water resources facilities and implemented centralized operation on them. Thus a mode was formed featuring "combining centralization and separation and carrying out two-leveled operation". But land was still contracted to peasant household as the basic means of production in agriculture and, therefore, the level of the operation in peasant household still became the main level in operation.

Second, very large change occurred to the relation between the collective and peasant household because of the separation of the ownership rights of the means of production. Under the system of people's commune, production team was the basic production unit in the countryside. It took the responsibility of organizing the specific process of agricultural production and operation under the administrative intervention of the organs of the people's commune at various levels and the governments of the state at various levels. The relationship between production team and peasant household was the relation between the organizer and operator of production and the worker established in the form of administrative subordination. Under the household contracting system, the relationship between the collective and peasant household became the equal contractual relationship in commodity nature between the owner and disposer of the means of production and the possessor, user and operator of the means of production. Through contracting, the two parties involved not only confirmed their mutually independent statuses and independent interests but also combined the four already separated rights of ownership together again according to the principle of economic interests. On the one hand, the collective collected public reserve fund, public welfare fund and other retentions from the fruits of operation of peasant household on the strength of the ownership right to land. It also imposed restrictions on the use of land and other main means of production. For example, they should not be bought, sold, mortgaged, pawned and used for building houses to live in. The collective could also make necessary adjustment to the division of land and re-distribute the right to use under proper circumstances on the strength of its right of disposal to land. On the other hand, peasant household engaged in independent production and operation on the basis of the demand on the market, in reference to the planning of the state and the collective, and on the strength of the exclusive rights of possession and use to land obtained within the term of the

contract. Thus peasant household turned from working people who were originally attached to collective economy into relatively independent operator in commodity production that possessed large autonomy in operation.

Third, radical change also occurred correspondingly to the form of distribution of labor products because of the separation of the four rights of ownership, the change of the status of peasant household, and the formation of operation autonomy. Such change was first seen in form. Under the system of people's commune, the members of the commune obtained their labor products in two parts obviously separated from each other. The basic part was labor remuneration calculated in "labor points" and distributed by the collective, including "grain ration" paid in kind and cash paid after conversion. The other part was the income from a small amount of private plots and sideline economy that directly belonged to themselves. Under household contracting system, peasant households obtained their labor products according to the principle of "fully submitting the quota of the state, leaving enough for the collective, and taking the rest for themselves". Such basic form of distribution was seen in the situation that peasant household took a part from all their labor earnings to submit to the state and the collective and saved the rest from themselves. Thus the form of distribution changed from the original "distributing from the publicly owned" to "turning over by household".

Such change was secondly seen in the specific contents of distribution. Because peasant household economy possessed the identities of independent "production unit" and "operation level", a new form of distribution according to performance emerged characterized by "accounting by household and remuneration related to production". Namely, materialized labor in condensed form was taken as the basis to calculate remuneration. Such practice stressed on economic effect and effective labor. Thus it conformed better to the characteristics in agricultural production, reflected more accurately the actual contribution of the working people, and embodied more fully the principle of distribution according to performance. In addition, the part "for themselves" under household contracting system was greater than the amount purely calculated on the basis of distribution according to performance. It included the compensations of the peasants for the value of the products of their necessary labor, for the value of the funds and labor that the peasants invested for simple reproduction, and for the part of additional investment that the peasants made for extended reproduction. Therefore, although labor was the main source of the part "for themselves", the tools, technologies, equipment and funds that each household possessed also became important factors that influenced the income of the peasants. This contained the factor of "distribution according to funds" in commodity production. During the term of the contract, the part of "fully submitting the quota of the state and leaving enough for the collective" was of fixed amount while the part "for themselves" was of variable amount. Such practice encouraged land contractors to add investment and improve labor productivity so as to achieve higher extra income.

Through the separation between the rights of ownership and disposal and the rights of use and possession, household contracting system made peasant family a relatively independent level of operation. This resolved the issue of “right”. Through contracting, peasant household became commodity producer and operator that possessed operation autonomy. This resolved the issue of “responsibility”. Through implementing the distribution form of directly linking labor with labor results, people truly realized the effect of “getting more payment when working more and less when working less and more returns when investing more and less when investing less”. This resolved the issue of “interests”. It was such direct and close combination of right, responsibility and interests in household economy that fully stimulated the initiative of the peasants in increasing production and income. It was not exaggeration at all to say that the implementation of household contracting system allowed the productivity of agriculture in China to have another liberation. Moreover, with the implementation of household contracting system, rural commodity production saw significant development and a new-type household economy, established on the basis of commodity production, gradually rose. Such new-type household economy took retaining and developing traditional household economic base as starting point. It developed commodity production, used advanced tools and technology, gradually practiced the division of work and business separation, and then gradually expanded the scale of production. It developed from the form of being “small but comprehensive” in business areas, to that of being “small but diversified”, and then to being “small but specialized”. Household economy gradually became commercialized, specialized and then corporatized. Factors of production socialization constantly permeated into traditional agricultural system so that the process in which people consciously and subjectively promoted construction was organically integrated with natural and objective historical development process. Such a situation greatly accelerated the historical process of the modernization of agriculture in China. So it can be said that the birth and growth of such new-type household economy would not only bring great vitality to the development of rural economy in China but also definitely play a huge promotive role to the completion of agricultural modernization with Chinese characteristics.⁹ As some people summarized and pointed out, China’s countryside would definitely witness a series of chain reactions because of the implementation of household contracting system: The creativity and initiative of the peasants were fully stimulated; agricultural productivity saw unprecedented and rapid improvement; production and income increases were achieved in agriculture; labor and fund surpluses emerged; diversified operation, division of work and business separation, and village industry saw development; households specialized in certain business, new syndicates, various technical service organizations emerged and developed; transformation occurred from self-sufficient and semi-self-sufficient traditional production mode to commercialized and socialized modern production mode; transformations were promoted in rural circulation and financial systems; rural surplus labor flowed into the city and urbanization developed in the countryside; the rudimentary form of socialized and modernized socialist agricultural with

⁹For the references about the part above, see Yu (1983), Li (1983), Tang (1983).

Chinese characteristics emerged; the economic, political, cultural and social life in the countryside achieved comprehensive progress and new socialist countryside was formed.¹⁰

The reform of rural economic system broke through traditional socialist economic theory and rigid socialist mode and achieved victory. This not only caused a chain reaction in the entire rural economy but also resulted in enormous impact on the entire economy system in China, including industry, commerce, finance, fiscal and taxation areas. Rural economic reform broke the administrative system in which government and people's commune were combined and practiced the separation of government and enterprise functions. Production and operation were carried out according to the characteristics of socialized production. People broke the planned system in which monotonous mandatory plans were used for regulation and implementation contract system, in which the interests, rights and responsibilities of the three parties of the state, collective and peasant household were planned and considered in a centralized manner. People broke the simplistic mode in the form of operation in socialist economy and practiced the diversification of the form of operation and thus activated Chinese economy. People broke the distribution system characterized by "iron rice bowl" and "big rice pot" and directly connected labor with labor results so that the distribution of labor results were associated with the obligations undertaken, the rights exercised, and the interests enjoyed. People also broke self-sufficient and semi-self-sufficient natural economic system and promoted production specialization and syndication, which resulted in the disintegration of self-sufficient and semi-self-sufficient natural economy and the development of commodity economy and so on. All these provided referential experiences and directions for the reform of the entire economic system in China. Therefore, it can be said in certain sense that the reform of the rural economic system became the pioneering event of the comprehensive reform in China's economic system.¹¹

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Chapter 10

The Mastering of China's Basic National Situation—The Theory of the Primary Stage of Socialism Gradually Formed with Consensus Achieved on It



Jun Wan

After the founding of the People's Republic of China and particularly, especially after the beginning of the reform and opening up, great achievement was made in socialist construction in China. Productivity saw rapid development, economic aggregate grew constantly, the living standard of the people kept improving, and China had growing importance in the world's economic system and growing influence on international political arena. To carry out economic construction on the basis of China's basic national situation was one of the most fundamental experience of China in achieving these results that caught the attention of the whole world. On the basis of summarizing the experiences and lessons in China's socialist construction and drawing from the historical experiences about the prosperity, decline, success and failure of socialism in other countries, the CPC achieved more profound understanding on the essence of socialism and its development stages and gradually formed and developed the theory of the primary stage of socialism. The theory was the accurate summary of China's national situation and the basic premise that people must follow in building socialism with Chinese characteristics.

The circle of economic theory in China made important contribution in the discussion and exploration on the issue of the essence of socialism and its development stages and, particularly, in the process of the formation and development of the theory of the primary stage of socialism. The theory of the primary stage of socialism specified the institutional background and initial condition of the study of economics in China. Starting from the basic premise of the primary stage of socialism, the circle of economics in China made deeper study on socialist economic system and its operation mechanism, obtained fruitful research results, and achieved several important theoretical breakthroughs. Such progress not only further enriched the connotations of the theory of the primary stage of socialism but also forcefully promoted the construction of the system of socialist economics with Chinese characteristics.

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1 The Marxist Classical Writers and Revolutionary Leaders' Conceptions and Reflections on the Stage of Socialism Development

Through in-depth study on the inherent contradictions in capitalism, Marx and Engels believed that capitalist society will inevitably perish and communist society will definitely triumph. The conception of Marx and Engels on the different stages of communist society was based on their research on the developed countries at the time such as the UK and France. They only made very simple and abstract representations on communist society. Due to the limitations of historical conditions, they did not and could not make specific statements on the essence of socialist society and the development stages that socialism would undergo.

The systematic exploration on the theory and practice of socialism started with Lenin. Lenin inherited and developed the views of Marx and Engels about the development stages of communism. He specifically divided the society after the proletariat gained power into the two stages of socialism and communism. After the victory of the October Revolution, Lenin mainly devoted himself to realizing the transition into socialism in Russia. He did not make further study on the issue of the development stages of socialism after the socialist system was established.

The establishment of socialist system in the Soviet Union was completed under the leadership of Stalin. However, Stalin made simple and mechanical understanding on the future society conceived by Marx and Engels. He regarded socialism as a short historical period for the transition into communism and attempted to quickly complete building socialism and transit into communism. In the book *Issues on Socialist Economy in the Soviet Union* that he wrote in his late years, the essences of socialism as he understood and the ideal model as he conceived was a typical produced economy based on being "large in size and collective in nature". The rigid understanding of Stalin and his successors on the conception of socialist society made by classical writers of Marxism and their wrong understanding on the essence of socialism exerted negative influence over a long period of time on China and other socialist countries.

After the CPC gains powers in the whole country, Mao Zedong made many beneficial explorations on the road of building socialism in China. Although great change occurred to the earlier and later stages of his theory on the essence of socialism and its development stages, his thinking on this issue still left many valuable ideas for later generations. Mao Zedong once believed that the conclusion of the socialist transformation of the ownership system of the means of production only represented the establishment of socialist system but not the completion of socialism.¹ Mao Zedong realized that there needed to be a process from the establishment of the socialist ownership system of the means of production to the full completion of socialist society. The establishment and development of socialist society in China would undergo a transitional period, a stage from the establishment of socialist system, to

¹Xue (1987).

the completion of socialist society, and then to the preparation for the transition into communism.² But he quickly departed from the ideological line of seeking truth from the facts. When reading the *Textbook on Political Economics* published in the Soviet Union from the end of 1959 to the beginning of 1960, Mao Zedong had new thoughts on the issue of the development stages of socialism. He believed that the stage of socialism could possibly be divided into two stages. The first one was undeveloped socialism and the second one was relatively developed socialism. And there might be longer time in reaching the second stage than the first one. In fact, Mao Zedong proposed the idea that socialism might be divided into two stages here. Such theory of the multiple stages in the development of socialist society provided precious ideological sources for the formation of the theory of the primary stage of socialism.

2 The Discussion and Exploration on the Issue of the Development Stages of Socialism in the Circle of Economic Theory Before 1966

From the founding of the People's Republic of China, the circle of economic theory carried out heated discussion and exploration with great enthusiasm on important issues in economic theory in socialist revolution and construction. But in the 1950–60s, China's academic research was often affected by the changes in political environment so that the study on many important issues could not be carried out in depth due to the disturbance of non-academic factors. Nevertheless, the truthful and luminous insights have shined with wisdom even when people examine them today.

In the middle of the 1950s, a great discussion on the basic economic principles of socialism occurred in China. In essence, it was the discussion and exploration on the nature of society and development stage of China in the early period after the founding of the People's Republic of China. Because China's socialist construction did not fully unfold and the atmosphere of "admiring the Soviet Union" exerted its influence at the time, the research methods of the scholars was mainly to apply relevant arguments and statements of Stalin to analyze the issue of China. So there were few new ideas that showed breakthrough against traditional theoretical system. Yet despite of such general situation, some scholars published independent views different from mainstream outlook with respect to China's actual national situation. Wang Xuewen, a scholar who demonstrated that "the Chinese society was a semi-colonial and semi-feudal society" in the great discussion on the nature of Chinese society in 1930s, proposed his distinctive understanding on the nature of Chinese society at the time. He believed that, now that there were many economic sectors in the transitional period, each economic component should have its own basic economic principle or "main economic principle". People could not think that the basic economic laws and principles of socialism was the basic economic laws and principles that determined

²See Shen (1996).

all main aspects and processes in the development of social production at the time because such an understanding would blur out the transitional nature of Chinese society at the time so that various economic sectors actually existing at the time could not be seen.³ In fact, his opinion indicated that, on the basis of the unique national situation in China, various ownership systems should coexist and jointly develop over a very long period of time.

Yang Xianzhen, the then president of the Party School of the CPC Central Committee, had similar views. In the middle of the 1950s, he proposed the “theory of comprehensive economic base” and believed that the economic base of the Chinese society was not limited to socialist public ownership only. It should also include individual economy and private capitalist economy. These economic sectors jointly formed a comprehensive economic base. Yang Xianzhen’s “theory of comprehensive economic base” was different in form with Wang Xuewen’s view but similar in essence. It expressed the same idea that people should realize the mutual integration and joint development of various economic sectors in China at the current stage.⁴

During the period in the end of the 1950s and the beginning of 1960s, the circle of economics in China carried out heated discussion on the relationship between productivity and productive relation and proposed some valuable opinions. Fan Wenlan believed that different nations faced different special conditions and there were certain differences between them. So even though it was a general principle that productive relation had to adapt itself to productivity, it would have complicated and varying specific manifestation forms and hence it could be applied mechanically and simplistically as a formula.⁵ Yan Beiming criticized some people’s position that, only when productive relation developed ahead of productivity, could it promote the development of productivity. He said, “There is a superficial view which understands the main contradiction simply as ‘letting productive relation go ahead of productivity’. Such a view might cause a sentiment about productive relation that ‘everything is fine when it goes ahead’. And such sentiment will bring us harm in practice”. The reformation in productive relation might not definitely promote the development of productivity because the “characteristics of the contradiction between productivity and productive relation will also be seen in the defects in some links in productive relation so that productive relation fails to adapt itself to the needs of the development of productivity”.⁶ In the early 1960s, the circle of economic theory made initial reflection on the issues exposed during the period from 1958–1960 and the Three Years of Difficult Time. Some scholars analyzed the consequence of productive relation from 1958 to 1960 and believed that “people shall not change productive relation beyond the nature and level of the development of productivity. If people change productive relation artificially and too early so that it goes beyond the development stage of productivity, then such productive relation will rise against the development of

³Wang (1955).

⁴See Yang (1980).

⁵See Fan (1957).

⁶Yan (1957).

productivity and cause damage to it.”⁷ Ping Xin took a different approach and made in-depth study on the issue of productivity. He believed that, at the time, there was the mistake in understanding the relationship between productivity and productive relation that people “absolutize productive relation and simplify productivity. They believe that productivity should always depend on productive relation to achieve growth and that productivity cannot have any relatively independent movement.”⁸ It is not hard to see that Ping Xin's view already started to touch the substance of the left-deviated line at the time which departed from China's national situation and development stage.

The discussion on the relationship between productivity and productive relation in the 1950–60s reflected behind itself the concerns of some economists on the situation in China at the time that productivity developed slowly and productive relation went far ahead of current times. Although their views were only expressed indirectly through abstract theoretical analysis, such theoretical exploration was praiseworthy and valuable under the political atmosphere at the time.

The limitations in the way of thinking in traditional political economics and the constant impact of various political movements prevented the circle of economic theory from carrying out in-depth study on the essence of socialism and its development stages. Relevant academic study was completely disrupted from 1966 to 1976. Despite of such a situation, relevant studies before 1966 still formed some important academic results and provided profound ideological enlightenment for the formation of the theory of the primary stage of socialism after reform and opening up.

3 The Formation and Development of the Theory of the Primary Stage of Socialism

The theory of the primary stage of socialism was formed and developed under the new historical conditions of reform and opening up. From the Third Plenary Session of the Eleventh CPC Central Committee, the CPC restored the ideological line of liberating thought and seeking truth from facts and gradually got rid of the influence of dogmatism and left-deviation thought. With the re-understanding of the essence of socialism and the correct analysis on China's basic national condition, the CPC obtained the scientific assertion that China was still in the primary stage of socialism and gradually formed the theory of the primary stage of socialism on such basis.

I. Deng Xiaoping's Important Contribution to the Theory of the Primary Stage of Socialism

In the formation of the theory of the primary stage of socialism, Deng Xiaoping played an extremely important role. After 1976, Deng Xiaoping keenly grasped the trend

⁷Zhang (1963).

⁸Ping (1960).

of development of the time and made profound thinking on the essence of socialism and the national situation of China. Early in 1980, Deng Xiaoping pointed out that “nothing will work if people do not liberate their thought. They should liberate their thought even on the issue what is socialism. The system that renders economy to stay in stagnation over a long period of time should not be called socialism.”⁹ Later he pointed out again, “What is socialism? What is Marxism? We were not completely clear in understanding this issue in the past.”¹⁰ These thoughts showed his huge political courage in opening up a new road for socialist construction and his huge courage in upholding a theory and opening up a new horizon in Marxism.

Through deeply reflecting on the historical experience in building socialism in China after the founding of the People’s Republic of China, Deng Xiaoping realized that China’s socialism construction should not detach from its national situation or go beyond proper stage. He once pointed out that “We should fully study the question of how to do socialist construction. Now we are summarizing the experiences in the thirty years of the foundation of our state. In summary, first, we should never depart from reality, go beyond proper stage and adopt some left-deviation measures. We will never succeed in building socialism in that way. In the past we suffered loss because of left-deviation. Second, no matter what you do, it must be favourable to developing productivity”¹¹ Under the guidance of such an idea, the Sixth Plenary Session of the Eleventh CPC Central Committee proposed for the first time the basic assertion that China was in the primary stage of socialism and such assertion was reaffirmed at the Twelfth CPC National Congress and the Sixth Plenary Session of the Twelfth CPC Central Committee. In order to provide better guidance to reform and opening up and modernization construction, the drafting team of the report at the Thirteenth CPC National Congress intended to take the scientific assertion that “China is in the primary stage of socialism” as the basis to make argumentation. After the conception of the general design of the report was reported to Deng Xiaoping, he gave the instruction that “this design is good”. When he met foreign guests on the eve of the Thirteenth CPC National Congress, he pointed out that “The thirteenth national congress of our party will expound what stage China’s socialism is in. Namely, it is in the primary stage and it is the primary stage of socialism. Socialism itself is the primary stage of communism. And China is in the primary stage of socialism, which is an underdeveloped stage. Everything needs to start with this reality and planning needs to be made on the basis of this reality.”¹² Such idea of his was elaborated in the report at the Thirteenth CPC National Congress and became the basis of argumentation of this report. When commenting the report after the conclusion of the congress, he pointed out that one important characteristic of the report of the Thirteenth CPC National Congress was that it formulated the theory of the primary stage of socialism and it firmly implemented the lines, guidelines and policies established after the Third Plenary Session of the Eleventh CPC Central

⁹Deng (1994, p. 312).

¹⁰Deng (1993a, p. 63).

¹¹Deng (1994, p. 312).

¹²Deng (1993c, p. 252).

Committee.¹³ In his Southern Tour Speech in 1992, he mentioned the primary stage of socialism once again: “Our socialism has just been built for several decades. It is still in the primary stage. There needs to be a very long historical stage for consolidating and developing socialist system. It needs the relentless efforts and struggle of several generations, a dozen of generations or even several dozens of generations. We should never treat the task lightly.”¹⁴ Here he emphasized the secular nature of the primary stage and admonished the entire CPC to continue to work hard and struggle on the road of building socialism.

In the new historical period of reform and opening up and socialist construction, Deng Xiaoping proposed a series of new understandings and insights on the essence of socialism and its development stages, which both inherited the achievement of the predecessors in study and broke through old rules, and made important contribution to the formation of the theory of the primary stage of socialism.

II. The Formation and Development of the Theory of the Primary Stage of Socialism

The formation and development of the theory of the primary stage of socialism roughly underwent three stages:

- (I) The fermentation stage of the theory (from the Third Plenary Session of the Eleventh CPC Central Committee to the Sixth Plenary Session of the Twelfth CPC Central Committee)

In 1981, the Sixth Plenary Session of the Eleventh CPC Central Committee adopted the *Resolution of the CPC Central Committee on Several Historical Issues of the Party from the Foundation of the State*. The document specifically proposed for the first time the assertion that China was in the “primary stage of socialism”. It was pointed out in the *Resolution* that, “although our socialist system is still in the primary stage, it is doubtless that China has already established socialist system and entered socialist society. Any outlook that negates such a basic fact is wrong.” Here it was proposed that China’s socialist system was in the primary stage. But when viewed in the context, these words were used to criticize those who were dubious about China’s socialist system. The focus in such emphasis was that China already established socialist system and entered socialist society. There was no more detailed discussion to further describe the primary stage of socialism. At the Twelfth CPC National Congress, Comrade Hu Yaobang pointed out in the report of the congress that “our socialist society was still in the primary stage of development in which material civilization is undeveloped.” In fact, an important characteristic of the primary stage of socialism was described here, namely that material civilization was undeveloped. But no full discussion was given further about this characteristic. The *Resolution of the CPC Central Committee on the Guidelines in Building Socialist Spiritual Civilization*, adopted at the Sixth Plenary Session of the Twelfth CPC Central Committee in 1986,

¹³Deng (1993d, p. 258).

¹⁴Deng (1993b, pp. 379–380).

reaffirmed that China was in the primary stage of socialism. It briefly summarized the economic feature of the primary stage and formulated the spiritual and cultural statuses of such stage. This indicated that the CPC further deepened its understanding on the primary stage of socialism. But the resolution did not further discuss the connotations of the primary stage of socialism.

In this period, the CPC already proposed the assertion that China was in the primary stage of socialism and reaffirmed it for many times in several important documents of the party. It also achieved basic understanding on some characteristics of the primary stage of socialism and, particularly, the characteristics in the area of economy. But these judgments and understandings were not elevated to the height of a systematic theory. So this period can only be said to be the period of fermentation of the theory of the primary stage of socialism.

(II) The systematic formation stage (from the Sixth Plenary Session of the Twelfth CPC Central Committee to the Thirteenth CPC National Congress)

Through reflecting and summarizing historical experiences, the CPC already formed the basic thoughts on the theory of the primary stage of socialism. However, this important issue did not attract full attention in the circle of theoretical study at the time. There were few in-depth studies and discussions on it. The drafting work of the report of the Thirteenth CPC National Congress greatly promoted the research process of the theory of the primary stage of socialism. Later, the circle of theoretical study carried out heated discussion on the issue of the primary stage of socialism and achieved some research results.

The report of the Thirteenth CPC National Congress gathered together the wisdom of the whole party, absorbed the research results of the circle of theoretical study, and formulated for the first time the theory of the primary stage of socialism in complete form. The report took the fact that China was still in the primary stage of socialism as the basis of argumentation and relatively systematically formulated the basic meaning, basic characteristic, main contradiction and historical mission of the primary stage of socialism. It was pointed out in the report that the primary stage of socialism was the specific stage that China would definitely undergo in building socialism under the conditions of backward productivity and undeveloped commodity economy. In this stage, the main contradiction that confronted China was the contradiction between the constantly growing material and cultural needs of the people and backward social production. In order to resolve this contradiction, people had to vigorously develop commodity economy, improve labor productivity and gradually realize the modernization of industry, agriculture, national defense and science and technology. In addition, they needed to reform the parts in productive relation and superstructure that could not adapt to the development of productivity. On such basis, the report formulated the basic line and objective of struggle of the CPC in the primary stage of socialism: “The CPC leads and unites the people of various nationalities nationwide to take economic construction as the central task, adhere to the Four Fundamental Principles (of adhering to the road of socialism, to the people’s democratic dictatorship, to Marxism, Leninism and Mao Zedong Thought, and to

the leadership of the Communist Party of China), adhere to reform and opening up, follow the motto of self-reliance and hard work, and struggle for building China into a wealthy, democratic and civilized modern socialist country.” The report also proposed the “Three-Step” economic and social development stratagem. Proposing the theory of the primary stage of socialism was a creative contribution of the Communist Party of China to Marxism. It was the first time in the history of Marxism that a communist party proposed the scientific concept of the primary stage of socialism in its party program.

(III) The developing and improving stage (from the Thirteenth CPC National Congress to the present)

Ever since the establishment of the theory of the primary stage of socialism in the Thirteenth CPC National Congress, the CPC has constantly summarized new practical experience and absorbed new theoretical research results in the great practice of building socialism with Chinese characteristics and used new thoughts and ideas to enrich and develop the theory of the primary stage of socialism.

The report of the Fourteenth CPC National Congress started with the actual situation of the primary stage of socialism and achieved new important breakthrough in understanding the issue of the relationship between planning and market. It specifically proposed that the goal of China's economic system reform was to build the system of socialist market economy. The report of the Fifteenth CPC National Congress focused again on discussing the theory of the primary stage of socialism and proposed for the first time the basic program of the CPC in the primary stage of socialism. The report proposed the new assertion that “China is now and will be in a long period of time in the primary stage of socialism”. It emphasized that the primary stage of socialism was a very long historical period and that people needed to fully realize the secular and unsurpassable nature of the primary stage of socialism and thus establish the awareness of struggling in hard work for a long period of time. The report formulated the basic economic system of the primary stage of socialism and proposed the basic goals and policies in economy, politics and culture in building socialism with Chinese characteristics. These goals and policies constituted the basic program of the CPC in the primary stage of socialism. Such basic program was the further specific development of the CPC's base line in the areas of economy, politics and culture and also the summarization of the most important experiences after the beginning of reform and opening up. The report of the Sixteenth CPC National Congress made objective evaluation on the achievements obtained after the beginning of reform and opening up. It pointed out that China was now and would be in a long period of time in the primary stage of socialism. Although China had entered well-off society now, but such well-off status was of low standard, incomplete form and imbalanced development. On such basis, the report formulated the conception of comprehensively building a well-off society.

The report of the Seventeenth CPC National Congress comprehensively analyzed a series of characteristics attributable to development stages in China's development at present and gave new connotations to the theory of the primary stage of

socialism. The report discussed the new characteristics attributable to development stage exhibited in China's economic and social development upon the beginning of the new century in the eight aspects of economic development, economic system, people's life, development coordination, construction of democratic politics, cultural construction, social construction and opening up to the outside world. It was pointed out in the report that, although China's achievements in development attracted the attention of the whole world, its national situation that the country was still and would be in a long period of time in the primary stage of socialism did not change and the main social contradiction, namely the contradiction between the constantly growing material and cultural needs of the people and backward social production, did not change. The characteristic attributable to development stages in China's development at present was the specific manifestation of the basic national situation in China in the primary stage of socialism in the new stage in the new century. The report particularly discussed the scientific outlook of development and pointed out that the scientific outlook of development was "proposed through taking as the basis China's basic national situation in the primary stage of socialism, summarizing China's practice in development, drawing from the experiences of foreign countries in development, and adapting to new development requirements". It was the important guiding thought for China's economic and social development and also the important strategic thought that people had to adhere to and implement in developing socialism with Chinese characteristics. The report also proposed the new requirements on the objective of struggle in comprehensively building a well-off society. It proposed that people should build China into a wealthy, democratic, civilized and harmonious socialist modernized country. The report of the Seventeenth CPC National Congress indicated that the CPC's understanding on China's basic national situation was expanded from the economic characteristics of large population, weak foundation and undeveloped productivity to various aspects in economy, politics, culture and society, that the CPC's understanding on the objective of struggle in the primary stage of socialism was expanded from the integration of the three aspects of "wealth, democracy and civilization" to the integration of the four aspects of "wealth, democracy, civilization and harmony", and that the CPC's understanding on the principles of development in the primary stage of socialism was elevated from promoting economic development to promoting comprehensive development and scientific development. These new contents turned the theory of the primary stage of socialism into a scientific theory with richer connotation and deeper understanding.

In the great practice in building socialism with Chinese characteristics, the CPC's understanding on the primary stage of socialism still kept deepening. In 2007, Premier Wen Jiabao pointed out in the article *Several Issues on the Historical Missions in the Primary Stage of Socialism and China's Foreign Policy* that, "in order to consolidate and develop socialism, people must understand and handle well two major missions: One is to liberate and develop social productivity and greatly increase material wealthy in the entire society. The other is to gradually realize social fairness

and justice and greatly stimulate the creative vitality of the society and promote social harmony. The two major missions above were mutually connected and promotive. They formed a unified whole and were always present in the long process consisting of a series of different development stages in the entire historical period of socialism.”¹⁵ In the 1980–90s, China’s reform and opening up was still in the starting stage. The general standard of productivity in China was relatively backward. The socialist system was still incomplete and imperfect. So people needed to highlight “taking economic construction as central task”. If this situation was true, then people should continue to adhere to taking economic construction as central task unwaveringly when China already achieved development progress that attracted the attention of the whole world through the relentless efforts after the beginning of reform and opening up and its economic aggregate already rose to the second place in the world. On July 1, 2011, Comrade Hu Jintao gave an affirmative answer to this question in his speech at the conference in celebration of the 90th anniversary of the foundation of the Communist Party of China. He emphasized in particular that “We have already made great achievements that attracted the attention of the whole world. However, China’s basic national situation did not change that it is still and will be in a long period of time in the primary stage of socialism. The main social contradiction did not change, namely the contradiction between the constantly growing material and cultural needs of the people and backward social production. China’s international status as the largest developing country in the world did not change. Development is still the key to resolve all issues in China. To firmly get hold of and take advantage of the period of important strategic opportunities is the key for us to win the upper hand, the advantage and the future. It is an important test to the CPC’s ability to run the country and also to the Chinese nation’s ability of self-strengthening. We must continue to focus on carrying out construction, attentively strive for development, and constantly solidify the material base for adhering to and developing socialism with Chinese characteristics.”¹⁶ These views represented a giant step in the Chinese people’s understanding on the historical missions of the primary stage of socialism and enriched and developed the theory of the primary stage of socialism.

The process of the formation and development of the theory of the primary stage of socialism in over twenty years indicated that the CPC achieved more and more profound understanding on the essence of socialism, had more and more comprehensive understanding about the national situation of China, and made deeper and deeper exploration on the road of developing socialism with Chinese characteristics. The great practice of reform and opening up and socialist construction will continue to give new connotations to the theory of the primary stage of socialism.

¹⁵Wen (2007).

¹⁶Hu xinhuanet.com.

4 The Theory of the Primary Stage of Socialism Deepened the Understanding on the National Situation of China

To correctly understand China's basic national situation and the historical stage in which it stood now was the primary issue in building socialism with Chinese characteristics and the radical basis for the CPC to formulate and implement correct lines and policies. It was specifically pointed out in the report at the Thirteenth CPC National Congress that "our country is now in the primary stage of socialism. Such assertion has two implications. One is that our society is already a socialist society. We must adhere to and shall not depart from socialism. Second, our socialist society was still in the primary stage." The primary stage of socialism in China did not generally refer to the initial stage that any country would experience upon entering socialism but a special stage that China had to undergo when it built socialism under the condition of backward productivity and undeveloped commodity economy. Such assertion is a general and radical judgment made on China's national situation. It constituted an important premise in building socialism with Chinese characteristics.

The CPC's understanding on such national situation underwent a process full of twists and turns. During the period of New Democratic Revolution, the Communist Party of China correctly recognized that China was of the social nature of a semi-colonial and semi-feudal society. And starting with such national situation, it creatively combined the general principle of Marxism with the specific reality of the Chinese revolution. Then through profound analysis on the main contradictions in the Chinese society, it proposed correct lines, guidelines and policies and finally won the victory of the New Democratic Revolution. However, after the founding of the People's Republic of China and, particularly, after the completion of the socialist transformation of the private ownership system of the means of production, the CPC detached from the actual situation in China on the road of exploring socialist construction. It disregarded the basic national situation in China characterized by backward productivity, undeveloped commodity economy and imbalanced social development and adopted a series of wrong lines and policies that went beyond proper historical development stage. It overstressed the features of being "large in size and collective in nature and pure in socialism" so that productive relation and superstructure seriously detached from the conditions of productivity at the time, which severely hindered economic development. Moreover, because of the wrong judgments on basic social contradiction, the theory of class struggle prevailed and swelled. Before reform and opening up, China's productivity developed slowly, the living standard of the people saw little improvement, and the superiority of socialism was not fully realized. From the Third Plenary Session of the Eleventh CPC Central Committee, the CPC correctly analyzed the national situation in China and made the scientific assertion that China was and will in a long period of time in the primary stage of socialism. Such assertion both revealed the social nation of China and formulated the social development stage in which China stood at present. It was the most concise and accurate summary of China's national situation.

With the constant development in reform and opening up and socialist construction, the CPC's understanding on the primary stage of socialism became more and more comprehensive and profound, which was epitomized in three aspects:

1. The understanding on basic characteristics of the primary stage of socialism

In the report of the Thirteenth CPC National Congress, the basic characteristics of the primary stage of socialism were summarized into five aspects. Namely, the primary stage of socialism was a stage in which China gradually got rid of poverty and backwardness, in which it gradually transformed from an agricultural country into an industrial country, in which it transformed from a society in which natural and semi-natural economies took up a large proportion in national economy to a society in which commodity economy was highly developed, in which people built and developed socialist economic, political and cultural systems, and in which all people rose with ardor to create new undertakings with hard work and realize the great rejuvenation of the Chinese nation. The report of the Fifteenth CPC National Congress expanded such understanding into nine aspects: China gradually transformed from an agricultural country to an industrial country. It gradually transformed from a country in which natural and semi-natural economies took up a very large proportion in national economy to a market economy country. It gradually transformed from a country of lower population quality to a country of relatively developed science and technology, education and culture. It gradually transformed from a country of low income to a country in which all the people were relatively affluent. The regional economic and cultural gaps would gradually narrow in China. It would have relatively mature and complete socialist market economic system, socialist democratic and political system and systems in other areas. It worked hard to build spiritual civilization while building material civilization. And it gradually narrowed its gap with advanced standard in the world. This indicated that the CPC's understanding on the basic characteristics of the primary stage of socialism already expanded from economic development, system improvement and national rejuvenation to various aspects in economy, politics, culture and society, such as promoting science and technology, education, culture and health, coordinating regional development, improving the people's income, and building spiritual civilization and that the CPC achieved more comprehensive and concrete understanding on the basic characteristics of the primary stage of socialism and its development process.

2. The long-term understanding on the primary stage of socialism

The primary stage of socialism was definitely not a brief historical period that would be completed at one go. It was once pointed out in the report of the Thirteenth CPC National Congress that "there needs to be the time over one hundred years from basically completing the socialist transformation of the private ownership system of the means of production in China in the 1950s to basically realizing socialist modernization. And all of such time belongs to the primary stage of socialism." However, the basic assertion about the basic national situation and social development stage in China in the report of the Thirteenth CPC National Congress was that "China

is in the primary stage of socialism.” From the Fifteenth CPC National Congress, such assertion was revised as that “China is now and will in a long period of time in the primary stage of socialism”. The assertion was reaffirmed in the reports of the Sixteenth and Seventeenth CPC National Congresses. This indicated that the CPC had clearer understanding on the secular and arduous nature of the primary stage of socialism.

At present China already realized the historical leap-forward from resolving the issue of subsistence to generally reaching the goal of building a well-off society. However, China was still in the primary stage of socialism. Underdeveloped productivity inevitably resulted in the situation that the socialist market economic system was not complete enough, that a series of economic and social conditions necessary to building highly democratic socialist policies and harmonious society were still not adequate, and unfair social distribution, embezzlement and corruption, and that other problems still existed. Only through hard work and struggling over a long period of time could China gradually get out of its undeveloped status and basically realize socialist modernization.

3. The understanding on the specific manifestations of China’s basic national situation in the new stage of the new century

The primary stage of socialism was a relatively long historical process. But in the process of development, China would definitely experience several specific development stages in such primary stage. And in different periods, it would show different characteristics attributable to certain stage. The report of the Seventeenth CPC National Congress summarized the new characteristics attributable to certain stage that China exhibited upon entering the new stage in the new century from the eight aspects of general strength, economic system, people’s life, coordinated development, democratic politics, advanced culture, social construction and opening up to the outside world. It was pointed out in the report that the characteristics attributable to certain stage in China’s current development were the specific manifestations of China’s basic national situation in the primary stage of socialism in the new stage in the new century. This required us to deeply grasp the new questions and contradictions that China confronted in its development and take the road of scientific development more consciously. The report revealed the inherent connection between the basic national situation of China in the primary stage of socialism and the characteristics attributable to certain stage in China’s current development. And on such basis, it comprehensively formulated the profound connotation of the outlook of scientific development and further deepened the understanding of the people on the development principles of socialism in its primary stage.

5 The Contribution of the Circle of Economics to the Formation and Development of the Theory of the Primary Stage of Socialism Since Chinese Economic Reform and Opening Up

After the Third Plenary Session of the Eleventh CPC National Congress, the practice of reform and opening up, which developed and thrived, constantly generated new phenomena and posed new questions. These urgently needed the circle of theoretical study to propose new views and theories to explain the reality and guide the reform. With the implementation of the ideological line of liberating thought and seeking truth from facts, the ropes of left-deviated thoughts, which confined the circle of theoretical study, were untied. The circle of economic theories made in-depth discussion and exploration on the unprecedented institutional transformation and economic development in China and achieved copious theoretical research results. Among them, the study centering round the issue of the primary stage of socialism not only greatly enriched China's economic theories. Many important research results were adopted by the CPC Central Committee and the State Council and became components of the economic policies of the CPC and the state.

Early at the end of 1970s, Su Shaozhi and Feng Lanrui proposed the question on social development stages after the proletariat gained power.¹⁷ They believed that the period from capitalist society to the advanced stage of communism could be divided into three stages: The first stage was the transitional stage from capitalism to socialism. It was further divided into two periods: The first period extended from the victory of the proletariat revolution to the basic completion of the socialist transformation of the ownership system of the means of production. The characteristics of such period were that various economic sectors existed and multiple classes existed correspondingly so that it was a period of intense and sharp class struggle. Social development entered the second period after the socialist transformation of the ownership system of the means of production, namely undeveloped socialism. The second stage was developed socialism. Social development entered the stage of communism as its last stage. These authors pointed out that, if people did not distinguish but confused these stages, they might extend the phenomena and factors that existed in certain stage as the phenomena and factors that were present in all of the several development stages of socialism, which would cause serious negative consequences in both theory and practice. For example, if people did not distinguish the stages and regarded the periods from capitalism to undeveloped socialism and from undeveloped socialism to developed socialism as the same historical period, they would consider that the contradictions between the proletariat and the bourgeois and between socialism and capitalism in the first period of the transitional stage were present in the entire historical period and could easily enlarge class struggle. For another example, if people took the things that should be done in developed socialism as their tasks and did them in undeveloped society, it might result in doing things

¹⁷Su and Feng (1979).

too early in eliminating individual economy, cancelling private plots and household sideline production, abolishing distribution according to performance, commodity production and commodity exchange, and even carrying out transition into communism too rashly. The conclusion of this article was that China was still an undeveloped socialist society and it was in the transitional period of socialism. People should not regard China's economic system as one of developed or completed socialism. Zhu Shuxian believed that the social development stages after the proletariat gained power should be divided as follows: The first stage was the transitional period from capitalism to socialism. The second stage was the first stage of communism, namely socialism. It was further divided into two periods: The periods of undeveloped and developed socialism. The third stage was the advanced stage of communism, namely communism.¹⁸ Zhu Shuxian agreed to the view of Su Shaozhi and Feng Lanrui that China was still in undeveloped socialism. But he did not approve of their assertion that China was still in the transitional stage of socialism. He believed that the stage which China was in was the period of undeveloped socialism in the stage of socialism. The view of the circle of economic theories that socialist society should be divided into stages and that China's socialism was in the undeveloped stage exerted very important social influence. In 1981, the assertion that "our socialist system was in the primary stage" started to appear in the documents of the CPC Central Committee. And it was finally formulated systematically at the Thirteenth CPC National Congress and won the consensus of the entire party.

The exploration of the circle of economics on the theory of the primary stage of socialism was in fact the process of re-understanding the essence of socialism from the angle of economics. After the beginning of reform and opening up, the circle of economics carried out a large amount of research work, starting with the actual situation in economic development in China at the time and centering round the economic issues in the primary stage of socialism. The scholars constantly broke through the confines of traditional theories and proposed many new views and understandings. Such work not only deepened the understanding on the primary stage of socialism but also played a positive role in constantly developing and improving the theory of the primary stage of socialism. The deepened understanding and theoretical breakthrough of the circle of economics on the basic economic system of the primary stage of socialism proved the point above.

It was a traditional view to believe that the ownership structure of socialism could only be public and purely public. The purer, the better. Individual economy generated capitalism ceaselessly every day. Private economy was the root of capitalism that had to be eradicated. After reform and opening up began, such understanding started to change. Some economists started to propose the view of the diversity of ownership in socialism and advocated that people should develop various non-public ownership economy, including individual and private economies under the condition that public ownership took up the dominant position. Xue Muqiao was the economist who advocated developing various economic sectors the earliest. In 1979, he proposed that it might bring more benefit than harm to leave a bit individual economy and capitalism

¹⁸Zhu (1979).

in the economic system.¹⁹ As non-public ownership economy developed rapidly in China, the understanding of the circle of economics on the ownership structure of the primary stage of socialism also further deepened. Chen Zongsheng was the scholar who summarized the objective model of China's ownership system reform as a kind of "mixed economy", namely an economy in which public ownership system relatively dominated and private economy, individual economy and state capitalist economy coexisted, integrated and grew among each other. Here, coexistence meant that public ownership and non-public ownership and their various specific forms existed concurrently within the scope of the entire national economy. Integration and growth meant that various ownership forms permeated into and crossed with each other and integrated and developed inside one enterprise. He also stressed that such mode was not a mixed economy in which private ownership dominated relatively but one in which public ownership dominated relatively.²⁰ At the Fifteenth CPC National Congress, taking public ownership as the dominant part and achieving the joint development of the economies of various ownership systems was officially identified as the basic economic system of the primary stage of socialism.

It was a traditional view to believe that whole people ownership had to and could only adopt the form of state ownership. The means of production that owned by the whole people in socialism could only be possessed by the socialist state on behalf of the whole working people. The state imposed direct leadership on the enterprises owned by the state. The leaders of such enterprises were appointed by state organs to manage them. State organs directly planned on all the production activities of these enterprises. In the beginning of reform and opening up, Dong Fureng challenged these views. He believed that the essence of economic system reform was to reform the whole people ownership system as a form of state ownership system. He proposed the idea that state administrative organizations and economic organizations should be set apart. Economic activities should be carried out by various economic organizations. Various economic organizations should have the independence under unified leadership and implement comprehensive, independent and strict economic accounting. They should have their own economic benefits and take the economic responsibilities as provided by the law.²¹ After 1990s and, particularly, after Deng Xiaoping's South Tour Speech, the discussion on the issue of the reform of the state ownership system became unprecedentedly active in the circle of economic theories in China. Zhou Shulian proposed the view that "ownership system is an economic means".²² He believed that ownership system and planning were both economic means. Building state ownership system was to promote the development of productivity. Developing productivity was the true purpose and state ownership system was only an economic means. He criticized that some people regarded state ownership system as the purpose of socialism and had superstition on it. They believed that admitting the ownership title of state-owned enterprises would change the nature of state ownership system

¹⁹Xue (1996).

²⁰Chen (1987).

²¹Dong (1979).

²²Zhou (1993).

and thus destroy the economic base of socialism. In essence, such superstition stressed on the state ownership system under traditional socialist economic system and took ownership system as the goal rather than a means. The Third Plenary Session of the Sixteenth CPC Central Committee affirmed the importance in clearly defining the ownership title of state-owned enterprises and emphasized that it would be favorable to consolidating the dominant status of public ownership economy to build modern property right system characterized by “clearly ownership, specifically defined rights and responsibilities, strict protection and smooth flow”.

It was a traditional view to believe that only whole people ownership and collective ownership were the realization forms of socialist public ownership. Whole people ownership was the advanced form of socialist ownership while collective ownership was its inferior form. Collective ownership would eventually transform into whole people ownership. In early 1980s, He Wei noticed that some new forms of public ownership emerged in real life and proposed that people should re-study the views in the theory of the socialist ownership system of the means of production on the basis of the changes in economic life in reality.²³ Liu Shibai believed that, in undeveloped socialist society, public ownership system was a diverse composite structure in which whole people public ownership dominated and which also consisted of collective ownership, joint ownership and other forms of public ownership.²⁴ Yu Guangyuan’s work *The Economy in the Primary Stage of Socialism in China* was the first book that systematically studied the economic issues in the primary stage of socialism and once selected as one of the “Ten Works of Economics That Influenced the Economic Construction of The People’s Republic of China”. In this book, Yu Guangyuan noticed that various new forms of socialist ownership that were non-basic forms already emerged in China²⁵ and predicted that it was very possible that such composite form of socialist ownership system would have a more important status than non-composite form of socialist ownership in some period in the future. With respect to the specific thinking on reform, Li Yining and some other scholars believed that shareholding system was a better way to realize public ownership and demonstrated the point from many aspects. The report of the Fifteenth CPC National Congress recognized that “the realization form of public ownership could be diversified”. In the *Decision of the CPC Central Committee on Several Issues on Improving Socialist Market Economic System* adopted at the Third Plenary Session of the Sixteenth CPC Central Committee, it was further proposed that people should “make shareholding system the main realization form of public ownership” and required that people should “vigorously develop the mixed ownership economy with

²³He (1984).

²⁴Liu (1986).

²⁵In this book, basic form or non-composite socialist ownership form refers to traditional form of public ownership while non-basic form or composite socialist ownership form refers to the enterprise of public ownership with diversified equity formed through horizontal integration or fundraising between enterprises of public ownership. See Yu (1988).

the participation of state-owned capital, collective capital and non-public ownership capital and realize the diversification of investment entities”.

It was a traditional view to believe that the public ownership of the means of production determined that only distribution according to performance was the principle of distribution in socialism. The participation of land, capital and other factors in distribution was the cliché of vulgar capitalist economics. Gu Shutang and Cai Jiming held that such a view did not apply to the primary stage of socialism. They believed that people could not completely practice distribution according to performance because there were many types of ownership systems in the primary stage of socialism, because state, enterprise and individual possessed relatively independent economic benefits, and also because enterprise and individual both had the autonomy of income distribution and accumulation in different degrees. They proposed that the principle of distribution in the primary stage of socialism was distribution according to contribution. Namely, people made distribution according to the actual contribution of various production factors in the creation of social wealth. In the primary stage of socialism, various kinds of income were distribution in the form of distribution according to contribution. The contribution of various production factors was determined by the marginal revenue of these factors. They emphasized that, only when people implemented the principle of distribution according to contribution in the primary stage of socialism, could they ensure equal opportunities, raise efficiency, realize the optimal allocation of resources, and promote the development of social productivity.²⁶ Their view once caused great controversy, but the development in the practice of reform verified the reasonableness of such view. In the report of the Sixteenth CPC National Congress, it was specifically proposed that people should “establish the principle of the participation of production factors, such as labor, capital, technology and management, in distribution according to contribution and improve the distribution system in which distribution according to performance dominated and various distribution modes coexisted”. Such statement finally recognized the legality of conducting income distribution according to the contribution of production factors.

It was not hard to see that the circle of economics made important contribution in the process of the formation and development of the theory of the primary stage of socialism. “The theory of the primary stage of socialism and the theory of socialist market economy both became the most important and outstanding research results in the study of economic theories from the beginning of China’s reform and opening up and the two pillars of contemporary Chinese socialist political economics. In the present stage in China, the study of all economics issues and the formulation of various need to take these two major theories as basis and guidance.”²⁷ The discovery and demonstration of the theory of the primary stage of socialism was

²⁶See Gu and Cai (1989).

²⁷Zhang (2005, p. 53).

the important contribution and development of the Chinese circle of economics to Marxist economics and the theory of scientific socialism from the beginning of reform and opening up. As reform and opening up and socialist construction kept developing, the circle of economic theories would achieve even deeper understanding on the economic issues in the primary stage of socialism and would definitely further enrich and develop the theory of the primary stage of socialism.

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Chapter 11

The Establishment of the Theory of Socialist Commodity Economy in 1984



Zhouyuan Zhang

The theory of socialist commodity economy established in 1984 was a decisive step toward the theory of socialist market economy. It was another important leap-forward in understanding starting from the idea of “taking planned economy as the dominant part and market regulation as supplementation” in ideology and theory. This wrote a new edition of textbook in socialist political economics.

1 The Debate of Thoughts and Theories on Reform in the 1980s

In 1984, the Third Plenary Session of the CPC Central Committee made the *Decision on Economic System Reform* and specifically stated that socialist economy was planned commodity economy. The meeting made scientific summarization on the discussion on whether socialist economy was commodity economy that started in the beginning of 1980s. This represented a decisive step toward establishing the theory of socialist market economy.

Socialist economy was planned commodity economy on the basis of public ownership system. Such proposition was established as the unified understanding of the entire CPC and the people in China after October 1984. In the Early 1970s and in the beginning of 1980s, there were always people in the circle of economics in China who wrote articles to propose and demonstrate the assertion above. For example, some articles proposed that socialist economy was the unification of planned economy and commodity economy. Some articles held that socialist economy had the features of both planning and market. Some articles proposed that people should clearly realize that China’s socialist economy was socialist commodity economy. Some

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articles even directly stipulated socialist economy as planned commodity economy, and so on.¹ Besides, the economic departments, including those in the system of economic system reform, also carried out extensive study and discussion on the relationship between planning and market. For example, it was said in *Initial Opinions on Economic System Reform*, written by the Office of Economics System Reform of the State Council in September 1980 that “the socialist economy of China at the current stage is a commodity economy in which the public ownership system of the means of production prevails and various economic sectors coexisted.” Xue Muqiao, the main drafter of the document said when he made explanations at the meeting of the secretaries of the CPC committees of various provinces, autonomous regions and municipalities directly under the central government, “Now we propose that China’s socialist economy at the current stage is a commodity economy in which the public ownership system of the means of production prevail and various economic sectors coexisted. It is a challenge to the dogmatism which has dominated for 30 years.”² However, such understanding failed to win recognition at the senior level of the CPC at the time. The view that showed adherence to the understanding that socialist economy was planned economy was still the mainstream. In April 1981, a reference material was printed and distributed in the name of the Research Room of the Secretariat of the CPC Central Committee. In the document, Chinese economists were classified into four types according to their attitude toward planning and market: The first type adhered to planned economy. The second type approved of planned economy but did not show very clear-cut attitude. The third type approved of commodity economy but did not show very clear-cut attitude. And the fourth type advocated developing commodity economy. Xue Muqiao, Liao Jili and Lin Zili were classified as the fourth type.³ In November 1981, Zhao Ziyang, the then Premier of the State Council, proposed in the *Government Work Report* the objective model of reform of “taking planned economy as the dominant part and market regulation as supplementation”. In September 1982, the report at the Twelfth CPC National Congress reaffirmed the principle of “taking planned economy as the main part and market regulation as the supplementary part”.

Nonetheless, there were still some economists who wrote articles and believed that socialist economy possessed the attributes of commodity economy. They believed that, as buyer’s market gradually formed and prices became rational, people needed to gradually narrow the scope of mandatory plans and expand the scope of guidance plans and so on.⁴ However, Yuan Mu and several other people who participated in the drafting the report of the Twelfth CPC National Congress opposed such views and wrote a letter to Hu Qiaomu who was in charge of the work about ideology in the party. It was said in the letter that “Although there are commodity production and exchange in China, we could never summarize our economy as commodity economy. If we make such summarization, we are saying that the relations of common

¹See Liu (1979), Sun et al. (1979), Liu et al. (1979), Xie and Hu (1979).

²See *The Memoir of Xue Muqiao* (1996).

³See Wu (1999).

⁴See Liu (1982).

possession and joint labour among the people under socialism are the relationship of exchange of equivalents between commodities. We will affirm that what controls our economic activities is mainly the law of value rather than the basic economic principles and planned development principles of socialism. Thus we will definitely blur the boundary between socialist economy, which has planned development, and capitalist economy, which is in anarchy, and also the substantive difference between socialist economy and capitalist economy.” They believed that “the mode of planned operation on the basis of commodity economy” “will definitely weaken planned economy and weaken socialist public ownership system”⁵ In August 1982 Hu Qiaomu approved and transmitted this letter. From then on, the theory of planned economy became the mainstream ideology on newspapers and magazines while the theory of commodity economy became the target of criticism so that, for about one year after that, the papers that advocated that socialist economy was also a kind of commodity economy were nowhere to be found. However, the voice of truth could never be suppressed. The practice in economic system reform totally broke the theoretical boxes made artificially in the above. After 1983, the theory of socialist commodity economy reappeared on the arena of theoretical discussion in China with stronger background in reality and more reasonable theoretical demonstration and attracted the attention of thousands. In October 1984, the Third Plenary Session of the Twelfth CPC Central Committee summarized the argument in the circles of economy and economic theories in China over many years. It affirmed in the form of a resolution of the party that China’s socialist economy was a planned commodity economy on the basis of public ownership. This brought the study and discussion of Chinese economists into a brand new stage.

2 The Establishment of the Theory of Socialist Commodity Economy

The drafting of the report of the Third Plenary Session of the CPC Central Committee in 1984 was a process full of complicated struggles. The document started to be drafted in June 1984 and over a month’s time was spent to write down an outline. But this outline did not get out of the old tone of “taking planned economy as the dominant part and market regulation as supplementation”. Hu Yaobang, the then general secretary of the CPC Central Committee, was very unsatisfactory about it. So the drafting team of the document was readjusted. Right at the moment, Ma Hong, the then president of the Chinese Academy of Social Sciences, received an instruction and organized several experts, including Zhou Shulian, Zhang Zhuoyuan, Liu Zenglu and Wu Jinglian, in the academy to write the article “A Re-exploration of the Commodity Economy of Our Country under Socialist System”, which was intended to reverse the case for commodity economy. The article proposed that, when affirming socialist economy was planned economy, people should not “negate that

⁵Peng et al. (2008, p. 120).

socialist economy also possess the attributes of commodity economy at the same time. The opposite of commodity economy was not planned economy but natural economy". People should not set planned economy and commodity economy "in opposition". The article affirmed the formulation that "socialist economy is planned commodity economy", which was negated before. President Ma Hong sent this article to some old-generation revolutionists to solicit opinion. In the end, the article did not cause criticism but won praise from Wang Zhen and other comrades. For example, Wang Zhen said in his letter that this article was well-written and that we should not just repeat what our ancestors had said. We should have creativity. In September 8, Zhao Ziyang wrote to the members of the Standing Committee of the Political Bureau of the CPC Central Committee. The letter was entitled *Opinions on the Three Issues in the Economic System Reform*. The following was written in this letter.

After repeated consideration, it is suggested that the planned system of our country be summarized into the following four implications:

- (I) China practices planned economy and not market economy.
- (II) Spontaneously and blindly regulating production and exchange through market is only limited to small commodities, three categories of agricultural and sideline products, and service and repair industry, which play a supplementary role in the entire national economy.
- (III) Planned economy was not equal to letting mandatory plans dominate. Mandatory plan and guidance plan were both the specific forms of planned economy. China has vast territory and there are the problems of undeveloped modern facilities, inconvenient communications and inadequate information transmission. It is not only impossible but also harmful to prepare all-inclusive mandatory plans. At present and in a very long period in the future, we should gradually reduce mandatory plans and expand guidance plans in planning.
- (IV) Guidance plans mainly rely on economic means in regulation and, in mandatory plans, the role of economic principles and, particularly, the law of value should also be considered. Socialist economy is planned commodity economy based on public ownership system. Planning should be realized through the law of value. People should use the law of value to let it serve planned economy. The representation that "planning comes first and the law of value second" is inaccurate. It is improper to continue to use it in the future. People should unite the two on the basis of reality and not set them apart in opposition.⁶

On September 11, Deng Xiaoping gave a written comment "I approve" on the views above. On September 12, Chen Yun also approved and pointed out at the same time that the three issues mentioned in the letter were important issues confronted China's economic work at present and also the summarization on the experience in urban economic system reform in the recent several years. The four implications on planned system conformed to the actual situation at present. Li Xiannian also

⁶Wu and Zhang (1999).

indicated that the three issues mentioned in the letter were radical issues. The resolution of these issues in a good way would greatly promote the development of social productivity in China.

The State Commission for Restructuring the Economic System also convened a meeting with experts and scholars to discuss the draft of the *Decision* as a document of the Third Plenary Session of the Twelfth CPC Central Committee. At the meeting, some people proposed that the term “commodity economy” should specifically be written into the document. The result of the meeting was written into a brief report and submitted to the central committee. Zhao Ziyang wrote an instruction, which read “Please handle it after considering relevant situation. Comrade Ma Hong was of the same opinion.” on the report and transmitted it to Gao Shangquan, the person in charge of the drafting of the part on economy in the drafting team. In the end, the finalized document specifically stated that people had to consciously base on and apply the law of value in socialist planned economy. And it was planned commodity economy based on public ownership system. This meant that the “planned commodity economy based on public ownership system” replaced the formulation of “taking planned economy as the dominant part and market regulation as supplementation” proposed at the Twelfth CPC National Congress and became the objective model of China’s economic system reform.⁷

3 The Significant Meaning of the Establishment of the Theory of Socialist Commodity Economy

The *Decision on Economic System Reform* made at the Third Plenary Session of the Twelfth CPC Central Committee in 1984 still had certain imperfections. For example, a sentence was added to the discussion on socialist commodity economy, which read, “Under the condition of socialism in China, labor is not commodity. All state-owned enterprises and resources, such as land, mine, bank and railway, are not commodities, either.” But after all, it achieved the important breakthrough in the theory of socialism. Deng Xiaoping commented on this that it was “the political economics with the combination of the fundamental principles of Marxism and socialist practice in China”.⁸

Affirming that socialist economy was commodity economy meant that (1) Socio-economic relations were commoditized and monetized. Commodity production and circulation dominated in socioeconomic activities. All or the majority of products in various kinds were transformed into commodities and involved in commodity circulation. (2) Commodity producers and operators who possessed independent economic interests were the basic factors in commodity economy. There were both

⁷Peng et al. (2008, pp. 199–201).

⁸See Party Literature Research Office of the Central Committee of the Communist Party of China (2004, p. 1006).

exchange relation and competitive relation between them. The occurrence of imbalance between production and consumption and between supply and demand on the basis of production development and technology progress was an inevitable phenomenon in the movement of commodity economy. Temporary balance could be achieved through competition. (3) Market regulation was the basic characteristic in the operation mechanism of commodity economy. The law of value spontaneously regulated commodity production and circulation through market price and its changes so that limited economic resources flowed automatically from industries with low efficiency to industries with high efficiency and so that resources allocation was adapted to the needs in the market and of the society so as to achieve the effective allocation of resources. (4) The expansion of commodity and market relations required that China overcome the isolation and closeness of national economy, practice opening up to the outside world, go into and open up the world market, and gradually integrate into the process of economic globalization.

The establishment of the theory of socialist commodity economy opened the gate for the theory of socialist market economy. After the establishment of the theory of socialist commodity economy in 1984, economic system reform was carried out quickly, including enterprise reform, price reform, macroeconomic management reform, income distribution system reform, and foreign-related economic system reform. From 1984, exploration was made to find the road to realize the separation of the two rights, namely the separation between state ownership right and enterprise operation right, in enterprise reform. In 1985, the restrictions on the prices of the majority of agricultural prices were abolished. In 1987, the State Commission for Restructuring the Economic System entrusted relevant institutions, including the Chinese Academy of Social Sciences, the Development Research Center of the State Council, the Peking University, the Party School of the CPC Central Committee, the China Renmin University, the State Development Planning Commission and the Shanghai Municipality, to organize a research team to study and propose the mid-term plan for China's economic system reform in eight years in the future from 1988 to 1995. The work of the research team was compiled into a book and published.⁹ In 1988, China attempted to "make a breakthrough" in price form. In 1991, the double-track price system of industrial means of production, which was implemented for many years, was unified into single-track market system. In summary, the impact of commodity-money relationship made one after another opening in the traditional planned economic system and market-oriented reform advanced in an unstoppable trend.

⁹See *General Thinking on China's Reform* (1988).

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Chapter 12

The Symposium of Middle-Aged and Young Economists in 1984—The “Moganshan Conference”



Xiuze Chang

The Symposium of Middle-Aged and Young Workers in Economics Science, known as the “Moganshan Conference” in history, was held at Moganshan Mountain in Deqing County in Zhejiang Province from September 3 to 10, 1984. It was the first national symposium of middle-aged and young scholars in economic science in China not just after the beginning of reform and opening up but after the founding of the People’s Republic of China. Middle-aged and young economists initiated, organized and held this symposium by themselves in the critical period of China’s reform before the convening of the Third Plenary Session of the Twelfth CPC Central Committee. This signified the historic rise of middle-aged and young economists in China as a group of people with the sense of responsibility for the era that they lived in. The conference not only provided some important thoughts for the reform and opening up in later period but also played certain promotive role to the development of the theory of economics in The People’s Republic of China. When people celebrated the 30th anniversary of China’s reform and opening up and the 60th anniversary of the founding of the People’s Republic of China, the “Moganshan Conference” was mentioned repeatedly and praised as “one of the thirty major events in the thirty years of reform and opening up in China”.¹ Here the author would like to elaborate

¹The magazine *China Reform* selected the Moganshan Conference as one of the “thirty major events in the thirty years of reform and opening up in China” in the twelfth issue in 2008.

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on the conference on the basis of his own historical materials, the memories of other participants, and relevant references.²

1 Brief Summary of the Background, Preparation and Convening of the Moganshan Conference

I. The Background of the Conference

In December 1978 the Third Plenary Session of the Eleventh CPC Central Committee made the decision on economic system reform and opened up a new era of reform and opening up. In the first several years, the main battlefield of the reform was in the countryside. In the city, people only experimented locally in delegating power and conceding profit at the level of enterprise. As reform deepened, the whole country faced in 1984 the historical question of how to expand rural reform and local pilot projects in enterprises into comprehensive reform. The situation at the time was that certain progress was achieved in rural reform but urban reform did not started at all. Moreover, due to the influence of deeply-rooted planned economic system and also due to ideological reasons, the entire reform advanced with great difficulty. At the moment, new situations and issues that had never been seen before were encountered in both theory and practice. The CPC Central Committee made the decision that It was scheduled that the Third Plenary Session of the Twelfth CPC Central Committee be held in October 1984 to make discussion and important decisions on several important issues in economic system reform.

In theory, a prominent issue that people met at the time was one about the objective model of China's economic system reform, namely whether people should continue to follow the traditional planned economic system or the variation of planned economic system characterized by "taking planned economy as the dominant part and market regulation as supplementation" or they should open up a new road of socialist commodity economy. In practice, even more issues were encountered. For example, what was the central part in the entire economic system reform in China? How could people brave their way out of the thick walls of planned economy? How should they push forward the reform of state-owned enterprises and transform them into commodity producers and operators that operated independently and assumed sole responsibility for their profit or loss? How should they push forward price reform so that prices could provide correct market signal and promote the reasonable allocation of economic resources? How should they implement the separation of administration from enterprise management, break the boundaries of administrative

²The author of this chapter was one of the participants of the symposium who personally experienced this historical event. But as the "Moganshan Conference" was convened in group discussion and the author could only be in one of these groups, he did not have full information about the discussion in other groups although the representatives in the conference had many exchanges and communications in the process of the meeting. Here he could only formulate it on the basis of available historical materials.

divisions, and bring into play the driving role of central cities? How should people further expand opening up and, in particular, how should they open up coastal port cities and establish new economic development zones, and so on? All these questions needed specific answers. Because of this, it was necessary that various parties in the society, including middle-aged and young economists, could make proposals and suggestions to the central authorities before the Third Plenary Session of the Twelfth CPC Central Committee could make the decisions on economic system reform as scheduled.

As far as the community of economists were concerned, a group of middle-aged and young economic scholars started to stand out so that a good many of talents were accumulated in China as the thought liberation movement unfolded after the Third Plenary Session of the Eleventh CPC Central Committee. At the time, there were roughly three groups of workers in economic science that attracted people's attention. The first group was young teachers and students in higher education institutions. The second group was the youth research teams of the Chinese Academy of Social Sciences and local academy of social sciences. And the third group was young research personnel in relevant research institutions under central authorities and the ministries and commissions of the state in Beijing and also research organizations which were attached to relevant ministries and commissions and possessed nongovernmental organizational elements, such as the Research Group of the Issue of Rural Development in China, or the Rural Development Group for short. In addition to the special research teams above, there were also a large number of middle-aged and young citizens among the public who cared about the reform and made persistent explorations.

These workers in economic sciences were from different systems and areas. They deeply rooted themselves on the vast land of China and many of them personally experienced the hardships in rural life. They had relatively profound insights on the true situation in the bottom of the Chinese society and had deeper feeling about the economic recession and the suppression of humanity caused by traditional planned economic system. They had liberated thought, original and novel knowledge and the courage to think and speak boldly and proposed many valuable ideas. For example, young economic scholars in Beijing, including Zhu Jiaming, Wang Qishan, Weng Yongxi and Huang Jiangnan, proposed in early 1980s the *Views on the Issue of the Several Stages of China's Economic Adjustment and Reform*.³ Similar valuable research results were also achieved by young economic scholars in Tianjin, Shanghai, Zhejiang, Guangdong, Inner Mongolia and Shaanxi. All these provided solid ideological and organizational foundation for the convening of the Moganshan Conference.

II. The Consideration and Preparation of the Symposium

Viewed from the historical materials to which the author had access and his personal experience, the Moganshan Conference was a meeting with "non-governmental sponsorship and governmental assistance" which was initiated by middle-aged and young

³Zhu (1981).

scholars as a non-governmental event, sponsored officially by news agencies and local research institutions, and attended and supported by relevant personnel from competent departments in the CPC central and state authorities.⁴ The purpose of this symposium was to “give proposals and suggestions to the CPC and the state” and the central topic was “urban economic system reform”.

The literature available at present indicated that the name of the symposium, the “symposium of middle-aged and young workers in economic science”, and its venue, the “Moganshan Mountain”,⁵ was first proposed after consultation by Zhu Jiaming from the Research Center of Technological Economics of the State Council, which was later merged with the National Development Research Center, Liu Youcheng from the Zhejiang Provincial Economic Research Center, Huang Jiangnan from Institute of Industrial Economics of the Chinese Academy of Social Sciences, and Zhang Gang from the office of the *Economics Weekly*⁶ and supported by Wang Qishan from the Research Office of Rural Policies of the Secretariat of the CPC Central Committee.

Under the circumstances at the time, it was really difficult for middle-aged and young economists to sponsor a national symposium in a non-governmental manner. So people adopted the conference model of letting central journalist units and local research institutions function as sponsors. *Economic Daily*, *Economics Weekly*, China National Radio, *World Economic Herald*, *China Youth Daily*, *China Youth* magazine, *China Village and Town Industrial Information*, *Economic Benefit News*, Zhejiang Provincial Academy of Social Sciences, and Zhejiang Provincial Economic Research Center participated as joint sponsors successively. And among them, the *Economic Daily* played an important role.

On June 12, 1984, the *Economic Daily* published a rather eye-catching news under the instruction of An Gang, general editor, and Ding Wang, vice general editor, entitled *Five Institutions Including the Newspaper Will Convene Symposium of Middle-aged and Young Scholars in Economics and Extensively Call for Paper Contribution*.

⁴The book *Professionalizing Research in Post-Mao China: The System Reform Institute and Policy Making* written by Katherine Keyser mentioned the “Moganshan Conference in 1984”. But some historical facts in this book still needed to be checked and examined.

⁵When the author participated in the Moganshan Conference in September 1984, he became interested in the name of the “Moganshan Mountain”. Later, he knew the legend about the mountain. During the Period of Spring and Autumn (770–476 B.C.), there were a couple of sword forgers called Mo Ye and Gan Jiang. They forged swords for the King of Wu in the mountain. Two swords of superb craftsmanship were forged, one female named after Mo Ye and the other male named after Gan Jiang. These swords could be assembled into one sword or separated as two swords. Later, the King of Wu prosecuted Gan Jiang to death. People in later generations named the mountain Mo Gan to commemorate them. Lu Xun, a modern Chinese literary master, wrote a short story named “Forging Sword” about this legend.

⁶“On the train from Tianjin back to Beijing, they talked about the situation that it would cause incoordination and hence failure if people did not start urban reform as rural reform had been implemented for five years. There were talents in different places and they should meet and exchange. So it was proposed that a conference be convened. And they immediately drafted the ‘Notice on Convening the Conference of Young Workers in Economic Science’”. See Liu (2010a).

Authors of Selected Papers Will Be Invited to Attend the Symposium as Official Representatives. It was pointed out in the news that “The ‘Symposium of Middle-Aged and Young Workers in Economic Science’ will be convened on a joint basis in Zhejiang in early September. The central content of discussion includes the important theoretical and practical issues in the economic system reform of our country. From the middle of this month, we call for extensive paper contribution from the community of middle-aged and young workers in economic science nationwide. Invitation will be given to authors of selected papers to attend the conference as official representatives.” The feature most worth of attention was the model of selecting representative by paper. This news to select people by paper, which disregarded the background of a talent, had great attraction to middle-aged and young people in various industries and areas and caused large response in various places nationwide.

Within two short months from calling for paper contribution on June 12 to August 15, the symposium’s preparatory group received over 1,300 papers from various places nationwide, over 20 of them each day on average. Among the authors of these papers, there were specialized personnel who engaged in theoretical study and also people who worked at the grassroots level in various areas and engaged in theoretical study in spare time. Such a situation reflected their sense of commitment in devoting their talent and wisdom to the great undertaking of reform, as an ancient Chinese saying went, “Even in humbleness, a man dare not to desert his concerns for his nation”.

Middle-aged and young scholars in Beijing undertook the routine work of the symposium’s preparatory group. And the paper review team shouldered heavy tasks. The head of the team was Wang Xiaolu and the vice head Zhou Qiren. Because there was a large flow of paper contribution, the review team was enlarged. Zhu Jiaming, Lu Mai, Gao Liang, Zhang Shaojie, Jiang Yue, Xia Xiaolin and Gao Shan’gang participated in review work successively. In the process of selecting papers, they observed the principle of “selecting people by paper” despite of education background, occupation, professional title and social connections.

After two months of careful review and selection, the list of representatives in the symposium were determined in the middle of August. In addition to the representatives who were selected in paper review, there were also some middle-aged and young scholars who initiated, organized and prepared the symposium and a few who already made certain achievement in economics. Thus there were altogether 124 representatives in two groups. Among them, when classified by work system, there were 38 from higher education institutions, accounting for 30%, 30 from the Chinese Academy of Social Sciences and local academies of social sciences, accounting for 24%, 18 from institutional research organs subordinate to the government, accounting for 14%, 20 cadres from CPC and governmental organs, accounting for 16%, such as Ma Kai, who then worked the Development Planning Commission of the Xicheng District in Beijing, 12 from the circle of enterprise, accounting for 10%, and 8 from the circle of journalism, accounting for 6%. When classified by region, there were 53 from Beijing, including those from the units of the Beijing Municipality and the organs of central authorities in Beijing, accounting for 42%, 11 from Shanghai, accounting for 9%, and 7 from Tianjin, accounting for 6%. In addition to those from

the three municipalities directly under the central government, more representatives came from the regions pioneering in reform and opening up. For example, 10 were from Zhejiang and 8 from Guangdong. Besides, a certain number of representatives were from the western regions. For example, 6 were from Shaanxi and there were also representatives from Xinjiang and Tibet. In addition to the 124 representatives in the above, representatives from competent ministries and commissions of the central government and specially-invited and sit-in representatives from the Zhejiang Province were determined separately.

Before the symposium was convened, the members of the preparatory group reported the preparation of the symposium to the leaders of the CPC Zhejiang provincial committee and the provincial government and won their support. By the end of August, various work items in the preparation were all completed.

III. The Overview on the Convening of the Symposium

Upon the completion of preparation, the Moganshan Conference was officially held on September 3, 1984. Altogether over 180 people attended the symposium, including 124 authors of selected papers and also some representatives of the scholars who prepared the symposium and who were invited, 8 representatives of competent ministries and commissions of the central government, 19 specially-invited and sit-in representatives of the Zhejiang province, and also members of the symposium's leading group, representatives from the circle of journalism, and persons-in-charge of various areas in the Zhejiang province.

It needs to be pointed out here that some attendants of the symposium worked in competent departments of the CPC and the state, such as Wang Qishan from the Research Office of Rural Policies of the Secretariat of the CPC Central Committee, Jia Chunfeng from the Bureau of Theory of the Propaganda Department of the CPC Central Committee, and Yan Huai from the Bureau of Youth Cadre of the Organization Department of the CPC Central Committee. Li Xianglu, the then secretary of Premier Zhao Ziyang also attended the meeting but his name did not appear in the list of representatives of the symposium. These people attended the symposium in their personal name. But because of their occupational background, they formed a powerful support to the symposium.

In order to ensure the successful convening of the symposium according to scheduled objectives, a leading group was established during the symposium, consisting of leaders of the initiating organizations, which included An Gang, general editor of the *Economic Daily*, Ding Wang, vice general editor of the *Economic Daily*, Feng Lanrui, director of the *Economics Weekly*, Wang Ruisun, general editor of the *Economics Weekly*, and Qin Benli, general editor of the *World Economic Herald*. In the secretariat of the symposium, Zhang Gang was general secretary, Liu Youcheng, Xu Jing'an and Huang Jiangnan were vice general secretary, and Zhu Jiaming, Zhou Qiren, Wang Xiaolu and other people were its main members.

Centering round the central topic of urban economic system reform, the symposium were divided into discussions on the following special topics: strategic of price reform, assumption of sole responsibility for the profit or loss by the enterprise itself, opening up to the outside world, financial system reform, bringing into play the role

of central cities, changes in rural industrial structure, economic functions of the government, and basic theoretical issues on socialist economy, such as commodity economy and ownership system. Traditional conference models were discarded in discussion. No paper reading or empty argumentation was allowed in the symposium. People all expressed their own opinions closely centering round the special topics. New meeting forms such as “discussion under hanging shingle” were created in the symposium. All these were filled with the vigor and dynamism of young people.

2 Main Issues and Progress Achieved in Discussion (I): The Proposal of “Combining Lifting Control and Readjusting” in Price Reform

The issue on the strategy of price reform was a special topic that caused the most heated discussion and resulted in the most fruitful achievements. The important meaning of the “Moganshan Conference” laid in the breakthrough in price reform. So the author wrote a whole section on this to account the process of proposing the two thoughts about “combining lifting control and readjusting” in the symposium. The last section in this chapter will also formulate the role and meaning of the two thoughts of “combining lifting control and readjusting”.

I. About the Background of Price Reform and Its Practical Urgencies

About the background of price reform.

At the time, the economic system reform, launched by the Third Plenary Session of the 11th Central Committee of CPC, was carried out for five years. The rural household contracted responsibility system was implemented in the countryside, which was the main battlefield of reform. In the city, comprehensive system reform was not yet carried out but “delegating power and conceding profit” already started in enterprises. As the reform deepened in rural household contracted responsibility system and “delegating power and conceding profit” in enterprise, the issue of interests arose with it and price contradiction became more and more prominent. “Because the price of the products in basic industries such as energy and raw materials was too low and the price of the products in processing industry was too high, basic industry was doing it harder and harder to catch up with the development of processing industry. The State Council held many meetings to discuss the issue of price reform.” “Many plans were made but none worked.”⁷ The discussion on price reform at the Moganshan Conference was carried out in response to such situation.

About the practical urgency of price reform.

Some representatives pointed out that “prices played a guiding role to numberless microscopic economic organizations in the commodity market.” “To a very large

⁷See Xu (2009).

extent, the process of price reform determined the process of the entire economic system reform.” “It is hard to break through such a situation if reform is not implemented with respect to price.”⁸

Some representatives specifically proposed that, “if price system is not reformed, there can be no radical change in other systems.” “In this sense, the reform of price system is the reform of entire system. Price system is the ‘nose of the ox’ in the reform.”⁹

Even the representatives who advocated “taking planned prices as the main part” also believed that, “at present, unreasonable price system seriously hinders economic reform. This attracts the attention of various areas”.¹⁰

It can be said that middle-aged and young scholars had that consensus that “price system must be reformed” at the Moganshan Conference.

II. About the Objective Model of Price Reform and Its Theoretical Basis

In the discussion on reform thinking, it can still be seen that there were differences in objective model and theoretical basis.

One kind of thinking advocated that people should “take planned prices as main part” and “open up part of the prices” at the same time. For example, some representatives pointed out that “the objective model of price reform is roughly taking planned price as main part, including unified price setting and floating price, and opening up the rest of the areas that were not suitable to be included in planned prices and setting them in free price negotiation.”¹¹

The other kind of thinking focused and stressed on “introducing market mechanism”. For example, some representatives pointed out that “the basic goal of China’s economic system reform should be that, through the reform, people should establish planning on the basis of the law of value, introduce market mechanism, and set up a new system of planned economy with autonomous regulation functions.” And in the eyes of these scholars, “the reform of price system is the reform of the whole system.” So it could be inferred from this point that the “basic goal” mentioned above was also the “objective model of price reform”. The representatives who were for such opinion emphasized that “the kernel of market mechanism is price. And the process of the reform of price system is in fact the process of the formation of market mechanism.”¹²

The difference in the objective model of price reform in fact reflected the difference in theoretical basis. The representatives who advocated “taking planned price as main part” emphasized that their theoretical basis was the “price formation theory

⁸See Zhou et al. (1984).

⁹See Zhang (1984).

¹⁰See Tian and Chen (1984).

¹¹Ibid.

¹²See Zhang (1984).

based on the labor theory of value” while those who emphasized the view of “introducing market mechanism” “consciously or unconsciously accepted the theory of ‘equilibrium price’”.¹³

III. About the Route of Price Reform

This was the issue that had the most in-depth discussion and most heated debate in the symposium.

The actual situation of the discussion at the symposium and available literature show that there were no formulations like “shock therapy”, “big shock mode” and “progressive mode”. The formulations proposed at the time were “readjusting” or “lifting control”. Moreover, historical materials indicated that the representatives who held different views in the discussion did not set “readjusting” and “lifting control” in complete opposition, or in a situation of being “either this or that”. Their views all contained the implication of “combining lifting control and readjusting” in different degrees, but their focuses were truly different so that three kinds of opinions were formed as follows:

The first kind of opinion advocated “taking readjusting as the main approach”. Tian Yuan, the Price Research Center of the State Council, believed that “the measure to reform irrational price system naturally is to gradually resolve such issue through adjusting prices in a planned manner except for those prices the control of which can be lifted.” He also believed that “the state completely have the ability to resolve the issue of the irrationality of the prices of the products of primary industry and consumer goods in China’s price system through readjusting in a planned manner”.¹⁴ On the basis of such understanding, a suggestion of “readjusting with large steps” was proposed at the conference.

Zhou Xiaochuan, then an on-job doctor majoring in systems engineering at the Tsinghua University, Lou Jiwei, and Li Jian’ge, who was present at the symposium, both postgraduates of the Graduate School of the Chinese Academy of Social Sciences, proposed the method of “small-step quick readjusting” when submitting their papers. With this method, people could repeatedly readjust price system so that they could both reduce the shock caused in the process of reform and gradually approach market equilibrium price. These young scholars also made models in particular and attempted to create a clear calculation on the base number of the price reform before the symposium.

When writing the report to be submitted to superior authorities after the symposium, Tian Yuan, as a representative among those who advocated “taking readjusting as main part”, stressed on the four constraints in price reform: (1) Reform should not be implemented with large decrease of fiscal revenue or increase of fiscal expenditure. (2) It should not result in the lowering of the living standard of the majority of the mass. (3) There should not be large fluctuation of the market. And (4) General

¹³See Tian and Chen (1984).

¹⁴Ibid.

price level could only rise in a controlled and convergent manner and not in a spiral and pushed-forward manner.¹⁵

The second kind of opinion advocated “taking lifting control as the main approach”. Zhang Weiyong, postgraduate at the Department of Economics of the Northwest University in China, held that people should lift price control and practice market supply and demand price. Zhang Weiyong said, “The so-called reforming price system means that people should lift control over and enliven prices in a planned manner and gradually form a balanced price system that flexibly responds to market supply and demand relations”.¹⁶ At the symposium, Zhang Weiyong also made a comparison about “thermometer” to formulate his view that prices “flexibly respond” to market supply and demand.¹⁷

There was intense argumentation about this view. The representatives who advocated “taking readjusting as main approach” did not approve of the view of “taking lifting control as main approach”. The main reason was that it was not realistic to lift price control all at once under the circumstance when planned economy dominated and there needed to be a process for the market to grow. When the market was not fully grown, it would be hard to achieve market equilibrium price and the prices might not be optimized.

The representatives who advocated “taking lifting control as main approach” did not approve of the view of “taking readjusting as main approach”. In the same “thermometer comparison”, Zhang Weiyong said, “Then what price regulation could be compared to? It was not mercury but an iron bar. When prices needed to drop, it needed to be cut off a bit. When prices needed to rise, it needed to be added to a bit.”¹⁸ He also pointed out, “The problem with prices lies in that the current price system severs the relationship between supply and demand so that prices are no more prices in the true sense. Under such price system, even if initial price is completely reasonable, it will soon become unreasonable unless economy is in absolute static condition. This does not mean to negate price regulation in general. It only means that price regulation is not a way to resolve the issue radically.”¹⁹

¹⁵See Tian and Chen (1984).

¹⁶See Zhang (1984). The historical materials available at present show that Zhang Weiyong made the formulation that “prices in a double-track system should be practiced. Old prices should be managed with old methods while new prices with new methods”. But according to Xu Jing’an’s article, the focus in the discussion at the symposium was the issue whether people should “take readjusting or lifting control as the main approach”.

¹⁷Zhang Weiyong gave the example like this: There was mercury in a thermometer. When temperature rose, mercury rose. When temperature dropped, mercury dropped. Prices needed to rise or drop spontaneously on the basis of the changes in market supply and demand relationship. Then what price regulation could be compared to? It was not mercury but an iron bar. When prices needed to drop, it needed to be cut off a bit. When prices needed to rise, it needed to be added to a bit.

¹⁸See Xu (2009).

¹⁹Viewed from the article “Price System Reform Is the Central Link in Reform” published by Zhang Weiyong, he did “not negate price regulation in general. It only means that price regulation is not a way to resolve the issue radically.” When discussing the “specific method for price system reform”, he wrote, “People may refer to the method for the reform of the prices of agricultural and sideline products and practice double-track price system. Old prices should be managed with old

The third kind of opinion advocated “combining lifting control and readjusting”. In the beginning, argumentation was made between the two opinions above of “taking readjusting or lifting control as main approach”. A third opinion emerged when the debate became intense. Some representatives, including Hua Sheng, He Jiacheng, Zhang Shaojie and Gao Liang, postgraduates of the Graduate School of the Chinese Academy of Social Sciences, and Jiang Yue, postgraduate of the Department of Planning and Statistics of the China Renmin University, absorbed and integrated the views of the two sides after analysis and discussion. They formed and proposed the thinking of “combining readjusting and lifting control” in price reform.

The scholar who advocated the thinking of “combining readjusting and lifting control” held that people should consciously take advantage of the double-track prices of the means of production that had already been formed objectively to make planned prices and market prices gradually converge. In this process, they should gradually reduce the part of the means of production under unified planned allocation and expand the part under free market regulation and eventually achieve the unification of the two kinds of prices.

Hua Sheng wrote “Price Reform Suggestions Part II”, which was reported to senior government leadership after the symposium. It was pointed out that “it is not appropriate to take comprehensive action in price reform. The task should be broken down and resolved bit by bit.” “What is the way out when large- and small-scale readjusting both has limitations?” “The general thinking is to take advantage of the current situation, reform in the outside, and readjust in the inside.” “The procedure is to reform first and readjust later and integrate readjusting in reform.”²⁰ These words can be said to be a concise summary of the thinking of “combining readjusting and lifting control” about price reform.²¹

methods while new prices with new methods. And a brand new price system will be established as replacement in the end.” See “Selected Papers at the Symposium of Middle-Aged and Young Workers in Economic Sciences” in *Economic Daily*, September 29, 1984. When viewed in history, it was “of revolutionary meaning” to propose “taking lifting control as main approach” at the time. (By Xu Jing’an).

²⁰“The Reports of the Symposium of Middle-Aged and Young Workers in Economic Science I” Appendix 2, “Price Reform Suggestions Part II”, written by Hua Sheng, “Academic Reports of Middle-Aged and Young Workers in Economic Science”, originally in Editor’s Office of *Economic Daily, Economic Writings* (Classified Edition), Issue 1, October 18, 1984, *Referential Materials of Economic Research*, April 1985.

²¹Some literature summarized that the argumentation on the issue of price reform at the symposium had two different sides. For example, when Xu Jing’an summarized the argumentation on the issue of price reform several years after the symposium, he pointed out that “the argumentation basically occurred between the sides for ‘readjusting’ and that for ‘lifting control’. Inside the side of ‘readjusting’, there was the distinction between completing through large-scale readjusting and implementing repeated quick small-scale readjusting. Inside the side of ‘lifting control’, there was the difference between lifting control only and combining lifting control and readjusting. Centering round the discussion of price reform, the main focus of the argumentation among middle-aged and young workers in economics was in the discussion whether large- or small-scale readjusting should be implemented.” See Li (1991, p. 754), (Part by Xu Jing’an).

IV. The Formation of Price Reform Report and Its Submission to Superior Authorities

On the basis of discussion, Xu Jing'an, vice general secretary of the symposium from the State Commission for Restructuring the Economic System, wrote a special report after the symposium, which included the thinking on price reform discussed at the symposium as well as his own considerations and was entitled *Two Kinds of Thinking on Price Reform*. It was pointed out in the report that price reform should mainly resolve two issues. One was to take increasing the prices of the products in the extractive industry as the central task and reform the price system of industrial products. The other was to take resolving the issues of the price inversion of agricultural products and the excessive subsidies given to them as the central task and adjust the prices of consumer goods and the charges of public utilities.

The report pointed out that there were two kinds of thinking with respect to reforming the prices of industrial products. Namely, (1) "Combine lifting control and readjusting and take readjusting as the main approach" and (2) "Combine lifting control and readjusting and lifting control first and then readjusting". It also pointed out that, "although the two kinds of thinking above have difference focuses, they do not repel or oppose to each other. In the reform, people can combine 'lifting control' and 'readjusting'. They can lift control where control can be lifted and readjust where it can be readjusted so that the two approaches can promote and supplement each other in implementation."²² The report suggested that control could be lifted over the prices in machinery, textile and light industries in which supply and demand were basically balanced. The prices of the raw materials needed were changed from planned ones to market ones. As price control was lifted in one industry after another, the proportion of unified allocation in the supply of coal and steel would be reduced. When the prices of energy and raw materials were raised largely at such moment, the rise would not cause large impact on the entire national economy. The lifting control in one industry after another would also resulted in the emergence of planned price within unified allocation and market price for the sale of products by enterprises themselves in them.²³

Although the report did not specifically use the category of "double-track price system reform", it was logically true that "combining lifting control and readjusting" would definitely result in the process of reform with double-track price system. Such thinking attracted much attention from leaders of the State Council.

Practice has proven that "taking readjusting as main approach", "taking lifting control as main approach", "combining readjusting and reform" and "combining lifting control and readjusting" all made contribution, in different areas and in different degrees, to the formation of the reform thinking of combining lifting control

²²"The Reports of the Symposium of Middle-Aged and Young Workers in Economic Science I", "Two Kinds of Thinking on Price Reform", written by Xu Jing'an, "Academic Reports of Middle-Aged and Young Workers in Economic Science", originally in Editor's Office of *Economic Daily*, *Economic Writings* (Classified Edition), Issue 1, October 18, 1984, *Referential Materials of Economic Research*, April 1985.

²³See Xu (2009).

and readjusting and pushing forward with double-track system. Viewed from even larger perspective, the thinking of the double-track price system reform in China was the fruit of the joint discussion and collective wisdom of a great number of middle-aged and young scholars at the Moganshan Conference. A special discussion will be made about its role in the fourth section “Influence of the Symposium”.

3 Main Issues and Progress Achieved in Discussion (II): Reform Thinking in Other Areas

I. About Further Expanding Opening up to the Outside World

In addition to the intense argumentation on price reform, there was another very active group discussion at the Moganshan Conference. It was the group about the topic of opening up to the outside world. The head of the group was Zhu Jiaming, one of the main initiators of the symposium. The members of the group were representatives from the capital Beijing, coastal cities such as Shanghai and Tianjin, and inland regions such as Inner Mongolia and Shaanxi. The members of this group generally had international perspective and stronger opening up awareness. Before the symposium, most of the members made field survey and theoretical study on the Shenzhen Special Economic Zone and coastal areas that had been opened up.²⁴ As a result, the focus of discussion was not about whether to expand opening up to the outside world but the strategic question of how to further implement expanding opening up.

(I) About the Opening Up Strategy for Coastal Areas

The coastal opening up areas, including a dozen of port cities, four economic special zones and the Hainan Island, located along the west coast of the Pacific Ocean from north to south, formed the frontline of China's reform and opening up. How to form an organic structure and system with both division of work and connection on the basis of the geographical pattern of the regions was a strategic question that people needed to face first.

Zhu Jiaming, the head of the group, and Du Sha and Li Luoli, representatives from Tianjin, proposed that people should take the four regions of Dalian, Tianjin, Shanghai and Guangdong as the centers to plan the macroscopic productivity configuration of the entire group of opening-up regions. Dalian should focus on introducing

²⁴See *Investigations on Shenzhen Special Economic Zone and Studies on Economic Opening-Up Zones*, Nankai University Press, 1984; with Gu Shutang as chief editor, Yang Yuchuan, Chang Xiuzhe as vice chief editor, and Li Luoli, Ma Jiantang, Liu Xin et al., who participated in investigations, surveys and writing. Also see *Some Conceptions and Suggestions on Building the Tianjin Binhai Economic Opening Up Zone (Blue Book)*, May 1984, printed internally on the basis of the collective research of the Research Group on Economic Development Strategy of the Nankai University, including Du Sha, Li Luoli, Chang Xiuzhe, Jin Yanshi, Hao Yisheng, Ma Jiantang, Yao Lin, and Zhang Zhichao et al.).

projects that could serve the technical transformation of heavy industries in North-east China. Besides, it should bring into its geographical advantages into play to connect with the Eurasia Land Bridge and develop entrepot trade. Tianjin had the largest hinterland area and very rich resources to be exploited. In opening up to the outside, it could gradually transform from the current low-standard export process to the deep processing of resources particular to North China. Thus it could gradually establish the competitive industries for the Bohai Bay Industrial Zone in the future. Shanghai had the conditions to develop sophisticated technology and new type industry and gradually formed knowledge-and-technology-intensive industrial centers. In addition to focusing on developing medium and top-grade consumer goods in the Hong Kong market, Guangdong should also fully consider the prospects of exploring petroleum in South China Sea and timely start developing auxiliary industries for oil exploration and also petrochemical industry.

In the paper submitted by them, Chen Ping, Cai Naizhong and other representatives from Shanghai proposed the conception of the three blocks of China's coastal opening up cities. The first block ran from Dalian to Lianyungang. The cities in it had offshore oil fields in the Bohai and Huanghai Seas. In the east, they mainly linked to Japan and South Korea and, in the west, to the three Eurasia Land Bridges. The second block extended from Wenzhou to Beihai. There were offshore oil fields on the South China Sea. The cities in the block were linked to Taiwan Province, Hong Kong regions, and the countries in Southeast Asia and the Oceania. The third block ran from Nantong to Ningbo. The cities in it were located in the middle of China's coastal line. There were offshore oil fields in southern Huanghai Sea and East China Sea. It faced the Pacific Ocean and had extensive hinterland on the Yangtze River Basin to form a comprehensive foreign-oriented development pattern.²⁵

Centering round the opening up of the coastal areas, the symposium discussed in-depth the issue of how to establish an economic development zone. Chang Xiuzhe from the Institute of Economics of the Nankai University pointed out that, "in history, the first special economic zone in the world was established near the port of the Gulf of Genoa in the northwest of Italy. In reality, the 'export processing zones' or 'free trade zones' established in various other places in the current world are mostly located on the communication lines of international trade." He took the practice of establishing the Shekou Industrial Zone as a "sample". Setting Shekou as the source of thinking and aiming at a goal higher than Shekou, he proposed eight points that people should observe when they established economic development zones in various places in China in the future.²⁶ Li Luoli from the Institute of Economics in the Nankai University further pointed out that "the development zones cannot completely copy the model of Shenzhen. Old enterprises which are favorable to the adjustment of the industrial structures in old urban areas should be allowed to continue to be built in these areas. These enterprises should enjoy the same policies as in the development zones. Besides, the state should specifically provide the ceiling of the standard of land use fee. Isolated foreigner residential zones should be built inside development

²⁵Xia et al. (1984).

²⁶Chang (1984).

zones.”²⁷ Other representatives present at the symposium also pointed that it was necessary to handle well the relationship between the new zones of the development zone and original old zones and proposed the policy position that “new zones serve old zones and foreign investment serve domestic investment”.

(II) Reform in Coastal Opening-up Cities

The representatives present at the symposium had the consensus that, as the frontiers of China’s strategic development, coastal opening up cities needed a full set of new economic system adapted to them. Besides, the reform in coastal opening up cities might also become the point of breakthrough of the reform nationwide. It was believed that it was necessary to explore new reform routes in the two aspects of “regional part of overall reform” and “overall situation of local reform”. It was suggested that people gradually and selectively push forward reform in the following eight areas in coastal opening up regions: (1) Reform of planned system. The direction of reform was to gradually break the planned control in departments and regions so that enterprises could have the power to establish collaborative or supportive relations with foreign-funded enterprises, equity or contractual joint venture enterprises according to the principle of mutual benefit. (2) Reform of circulation system. Domestically-distributed products of solely foreign-funded enterprises and equity and contractual joint venture enterprises should not be subject to unified purchase and sale. The raw materials supplied domestically and collaboratively-manufactured products of these enterprises could be handled directly with order contracts. (3) Price system reform. People might consider implementing on a trial basis the “limited floating price system” in coastal areas. They should respect the right of solely foreign-funded enterprises, equity and contractual joint venture enterprises to determine prices. (4) Reform of foreign trade system. The basic direction was that a small number of foreign trade enterprises would become economic entities. (5) Distribution system reform. Enterprises should transform toward assuming sole responsibility for their own profit or loss. Taxation would be taken as the main form of distribution. (6) Reform of financial system. Share economy should be developed at places where conditions were ripe. Multifunctional local banks would be established gradually. (7) Reform of labor system. Transition would be implemented toward recruitment system. And (8) Reform of the economic functions of local government. Local government would gradually transform from an institution that integrated governmental and enterprises functions to economic coordination institution. The suggestions above showed the thinking of “forcing reform with opening up”.

(III) About the Opening Up of Coastal areas and the Coordinated Development of Inland Regions

Some representatives from Shanghai, including Chen Shenshen, paid great attention to the important role of China’s coastal areas in attracting foreign investment. Other representatives in Shanghai also pointed out in the paper that they submitted that China was the country with the largest population in the world. It had a powerful

²⁷See Li (1984).

“capital gravitational field”. “And, as national or regional economic central cities, the old industrial bases in China’s coastal areas had good economic base and convenient land and sea transportation. These cities were the ideal frontiers for them (the foreign investors—Author’s note) to open up the Chinese market.”²⁸

Guo Fansheng, a representative in the group of West China and from the Research Office of the CPC Committee of the Inner Mongolia Autonomous Region, also participated in the discussion of the group of opening up to the outside world. He challenged the theory of gradient transference, which was popular in the circle of economics over a long period of time. He pointed out that “the theoretical basis of the logic and reasoning in the theory of gradient transference is basically to regard China as a closed system in self-seclusion.” “At present, we are facing the challenge of the new technological revolution, which gives undeveloped regions an opportunity to achieve leap-forward development.” Therefore, he believed that “the domestic gradient transference of technology cannot be taken as a pattern.” Such a view caused heated discussion and provided new theoretical support to the cross-gradient-pattern development of the western and central regions in China.²⁹

On the basis of the discussion above, Zhu Jiaming wrote a special report. It was pointed out in the report that, while coastal areas should be opened up to the outside world, inland regions also should. The priority of the opening up of inland regions was to use foreign investment to exploit resources. This would not only benefit the development of inland regions but also promote the opening up of the coastal areas to the outside world. First, using foreign investment to exploit resources in inland regions could resolve the issue of balance caused by repatriated profits, which arose after the products of high technological industries were all sold domestically. Second, when foreign investment went deeply into China’s hinterland to exploit resources, it was necessary to create a window for exporting in coastal areas. Thus, the resources transportation line would be built to connect China’s hinterland and coastal areas, which would create conditions for coastal areas to attract foreign investment. Third, once resource transportation line was connected, a group of enterprises might rise with it so that primary processing industries could be removed from coastal areas to hinterland with such trend. Fourth, the formation of a complete production network across regions also could resolve the issue of achieving joint opening up and prosperity between coastal and inland regions, which would influence the macroscopic configuration of productivity nationwide. This involved a major macroscopic decision that required the state to consider through centralized planning.

On the basis of the understandings above, the representatives present at the symposium made several suggestions as follows: (1) People should gradually open up land ports such as Erenhot and Manzhouli and select several inland regions that had good conditions to use foreign investment to experiment in establishing “inland development zones”. (2) People should encourage foreign investments to operate mines and

²⁸Lu and Zhang (1984).

²⁹Guo (1984a). Guo Fansheng and other representatives from West China advocated “cross-gradient-pattern development” at the symposium, which was very impressive. Also see Liu (2010b, pp. 465–482).

build roads and railways in inland regions through joint ventures or solely-foreign-funded companies. (3) People should encourage foreign investment to operate in primary and deep processing of resources in inland or coastal areas. But they needed to impose limitations on enterprises that caused serious pollution. (4) People should encourage inland regions to directly introduce internationally first-rate technologies to carry out key construction projects and provide certain preferential policies and funding. (5) People should encourage some provinces and autonomous regions in inland regions to exert their current advantages in national defense industry and space industry to develop some related high technology industries. And (6) People should encourage coastal and inland regions to carry out cooperation in various forms. Provinces and autonomous regions in inland regions could go to coastal development zones to establish enterprises through joint ventures. They might also form equity or contractual joint ventures on the condition of providing raw material supplies. And they should enjoy preferential conditions identical to those for foreign investors.³⁰ The suggestions above not only had application value at the moment but also possessed strategic meaning to the opening up and development in the long term in the future.

II. About the Reform of State-Owned Enterprises

Related to the issues of price reform and the strategy of opening up to the outside world mentioned above was the issue of enterprise reform and, particularly, the reform of state-owned enterprises, which was called state-operated enterprises at the time. When determining the selected topics of the meeting, the organizers of the symposium realized that price reform and opening up to the outside world needed corresponding microscopic foundation, namely that state-owned enterprises had to become market entities that assumed sole responsibility for their profit or loss. Only in this way could the enterprises made reasonable response to price signal and domestic and foreign markets. Centering round this issue, three points emerged in the discussion.

(I) About the Basic Direction and the Starting Point in the Reform of State-Owned Enterprises

With respect to the view that state-owned enterprises were regarded in a long period of time as “attachments to government administrative institutions”, it was specifically proposed in the symposium that “state-owned enterprises should become commodity producers and operators that operate independently and assume sole responsibility for their profit or loss”, namely “market entities”. On the basis of such theoretical understanding, it was proposed in the symposium that state-owned enterprises should take “assuming sole responsibility for their profit or loss” as the basic direction and promote enterprise reform in such direction.

³⁰“The Reports of the Symposium of Middle-Aged and Young Workers in Economic Science IV” “Suggestions on Several Issues about the Opening Up to the Outside World in Fourteen Coastal Cities”, written by Zhu Jiaming, *Referential Materials of Economic Research*, October, 1984.

The symposium specifically proposed the thinking of “starting reform with small state-operated enterprises and collective enterprises”. First, small state-operated enterprises and collective enterprises were of extensive coverage and large number. Their reform would exert important influence on the entire industry and national economy. Second, their reform could explore the roads for the reform of large- and medium-sized state-owned enterprises. Third, small state-operated enterprises and collective enterprises had high flexibility and strong adaptability. Their reform could reduce the cost of reform. Strategically speaking, what was proposed at the symposium was a reform road of “marginal evolution”. In this way, people could build a reliable reform base and form a tendency of siege over large- and medium-sized state-operated enterprises. The conclusion drawn upon discussion was that the direction of the reform of state-operated enterprises was to practice the principle of operating independently and assuming sole responsibility for their profit or loss under different conditions and in different degrees.

(II) About Two Ways of Reform of “Profit Retention” and “Shareholding System”

1. A large number of representatives advocated the reform of state-operated enterprises through “profit retention”

On the basis that state-owned enterprises practiced the principle of assuming sole responsibility for their profit or loss, a large part of the representatives suggested to implement “profit retention” reform in a style resembling “net revenue distribution system with cost deduction” in small state-operated enterprises and collective enterprises. After the reform described above was implemented, an enterprise should “fully submit the quota of the state and take the rest for themselves”. Thus it would have both great vigor and face great pressure. This practice was in fact the recognition of the residual claim of the enterprises.

2. A small number of representatives tentatively proposed implementing “shareholding system” reform

The representatives who held such new idea believed that implementing shareholding investment system would transform unitary decision making of the state into diversified decision making of investors and also turn the risk-taking solely by the state in investment into that by multiple investors. These people advocated that “small state-operated enterprises may issue shares with part of their equity. They may also issue shares for expansion and technical transformation”. Their formulation showed very prudent attitude and they did not boldly proposed that “large- and medium-sized state-operated enterprises may issue shares with part of their equity.” After all, it was a proposal about implementing “shareholding system” reform, which was of great importance to the reform of state-owned enterprises.

(III) About the Bankruptcy of State-Owned Enterprises

In the discussion, people came to the issue whether an enterprise should be allowed to go bankrupt when it was not run well. At the time, the circle of theoretical study and the society still stuck to traditional outlook on this issue and believed that socialist

enterprises should not go bankrupt. In opposition to such traditional theory, the symposium specifically proposed that “an enterprise can go bankrupt”.³¹ It was also sharply proposed that “whether an enterprise is allowed to go bankrupt is the sign about whether an enterprise implements the principle of assuming sole responsibility for its profit or loss truly or falsely and fully or halfway”.

The symposium suggested that the state should formulate the “regulation on enterprise bankruptcy” or the “enterprise bankruptcy law” as quickly as possible and put it into trial implementation among small state-operated enterprises or collective enterprises. This was an earlier and specific proposal on “enterprise bankruptcy” in the circle of economics. And it resulted in the birth of the “enterprise bankruptcy law”.³²

III. About Financial System Reform

Finance was the kernel of modern economy. Cai Zhongzhi, Liu Yu and Qi Yonggui from the Institute of Finance of the Head Office of the People’s Bank of China were representatives from the circle of finance. They were very active about the issues on financial system reform and, particularly, banking system reform and share issuing.

(I) About the Thinking on Financial System Reform in Recent Time

Representatives present at the symposium pointed out that China basically implemented the fund management system characterized by “unified deposit and lending” at the time. On the one hand, such practice severed the horizontal fund flow in the credit business between grassroots banks. On the other hand, it severed the direct connection between industry and commerce and the banks at various corresponding levels. As a result, funds flowed slowly and brought poor economic benefits. Moreover, the four major banks in China, namely Industrial and Commercial Bank of China, Agricultural Bank of China, Bank of China, and China Construction Bank, operated in parallel with the central bank. Because there was no financial market and also nothing like the three major regulatory means of the required reserve ratio determined by the central bank, the open market business of government bonds, and securities rediscount, the central bank had very weak coordination and control ability over specialized banks. With respect to such a situation, the symposium proposed

³¹For example, Guo Zhenying then worked at the Tianjin Municipal Economic System Reform Office and later became the director of the Department of Industry and Communications of the Research Office of the State Council. His paper was selected but he could not attend the meeting at the time. In the paper that he submitted, entitled “Assumption of the Sole Responsibility of Profit and Loss and Expansion of the Enterprises’ Power”, he discussed the “issue of the bankruptcy of state-operated enterprises”. He pointed out that, “due to bad operation and management, an enterprise will naturally go bankrupt when the losses that it has sustained reach a certain amount. But in practice, we subsidize enterprises in loss with the money from other enterprises to maintain its withered corpse. The adoption of such a measure has everything to do with a kind of theory that ‘state-operated enterprises never go bankrupt’ that has existed for a long time. We should discard such theory”. See Guo (1984b).

³²“The Reports of the Symposium of Middle-Aged and Young Workers in Economic Science III” “Practicing the Assumption of Sole Responsibility of Profit and Loss by Enterprises Should Start with Small State-Operated Enterprises and Collective Enterprises”, *Referential Materials of Economic Research*, April 1985.

the suggestions such as taking expanding the autonomy of the provincial specialized banks at local levels as the first step and strengthening the horizontal flow of funds and the supportive measures in financial reform.

(II) About Issuing Shares and Developing Share Economy

This was one of the most sensitive and challenging topic raised at the symposium. Before the symposium, Cai Zhongzhi and other representatives proposed “building financial market”, showing the spirit of “boldly being the very first in the world” as said in a Chinese saying. And it attracted the attention of all the symposium.³³

It was pointed out in the discussion at the symposium that stock and bond businesses were exceptionally complicated economic activities. Particularly, they involved the rights to property and the distribution of interests related to ownership rights. They were subject to the influence of market to a very large extent. It was extremely important to establish rules commonly accepted by the society. People absolutely should not suppress some good burgeoning trends that were to ripen. It was suggested that they follow the principle of “observing first, then guiding and then managing”.

At the time, the majority of stocks and bonds were issued directly and not through certain financial intermediary institutions. The stocks and bonds issued were not allowed to circulate. Representatives pointed out with regard to such a situation that this was not convenient for social supervision and the operation of stocks and bonds. And it did not conform to their original nature, either. It was suggested that governments at various levels should provide conditions to make stock and bond transactions in private become public and socialized. Before the government established specialized stock and bond institutions, the trust departments of banks should undertake the issuing, purchase, conversion and payment of stock and bond. In order to protect the legal rights and interests of the issuing and purchasing parties of stocks and bonds and handle the disputes between the two sides, it was suggested that proper arbitrary institutions be established. The symposium also proposed different stock and bond issuing policies with respect to enterprises of various natures. And it was suggested that income tax be imposed on the income of enterprises from stocks and bonds. This was the systematic suggestion on issuing stock and developing shareholding system, which was proposed in earlier times in China. It was of pioneering meaning to the development of capital market in China.

IV. About Rural Reform and Development

The group of rural development already made in-depth study on the issue of rural reform and development. Because of a group of scholars who studied rural development for a long time, such as Wang Qishan, Chen Yiluo, Zhou Qiren, Pei Changhong, Bai Nansheng, and Zuo Fang, participated in the symposium as representatives, the

³³See Li (1991, p. 754) (Part by Cai Zhongzhi). The author was assigned to the group of finance in the beginning and heard Cai Zhongzhi speak of his opinion on establishing financial market on the day of September 2, 1984, and felt deeply impressed.

discussion on agriculture and rural reform and development was relatively in-depth and reached the frontier areas in the study.³⁴

(I) About Rural Reform and the Judgment on the General Situation of Development

The symposium believed that China's rural areas faced new turns. On the one hand, successful reform in several consecutive years proposed the new historical mission of deeply reforming rural economic system and of comprehensively reorganizing rural industrial structure. On the other hand, such reform prepared the conditions for completing such more profound transformation. In particular, the comprehensive reform of the entire economic system was fermenting in China. And the huge productivity which was originally confined in the city and major industries were released initially. These phenomena converged with the reform already implemented in the countryside. They stimulated each other and formed an unstoppable trend. The new situation posed a series of new questions. It was urgent that people propose ideas, understandings and solutions that could be referred to in decision making on the basis of systematic investigation and study.

The symposium focused on discussing new issues posed by the new situation. It was believed that new difficulty emerged after successive increases of agricultural production and, particularly, the increases of grain output and it was the so-called grain "overplus" issue. On the surface, it was manifested as "granary storage crisis" and, in substance, it was the concentrative embodiment of the original contradictions under new conditions in the industrial structure, circulation system and income structure of the entire national economy. People should never infer from such a situation that China's grain issue was resolved fundamentally and they could drop their concerns forever. The further increase of China's grain production could not rely on forcing producers to accept low-price unified quota assignment for its realization or on largely increasing state fiscal subsidies for its continuation. The truly reliable foundation should be the demand in the society with real purchasing power. At present, the effective demand on grains did not fully and sufficiently manifest itself. The potential of the demand in these areas should be fully tapped and exploited.

(II) About the Reform of the Purchase and Sale System of Agricultural Products (Grains at the first)

The scholars present at the symposium believed that the main obstruction that affected the full realization of the effective demand mentioned above was the irrational purchase and sale system of grains and other agricultural productions. So it was more urgent to implement a radical reform on the purchase and sale system of agricultural products and, first of all, grains. Under new conditions, supply-typed production and distribution-typed commerce had to be changed to a different track. Therefore, it was suggested that people start with the delegation of power related to grains and implement a comprehensive reform of the purchase and sale system of grains and other agricultural products. The specific conceptions were (1) paying subsidies in

³⁴Liu (2010c, pp. 407–426).

predetermined lump sum, (2) delegating power, and (3) establishing central reserve and implementing protective price system.

(III) Transforming Rural Industrial Structure

The symposium believed that transforming rural industrial structure was the foundation to radically resolve the issues about the price system and purchase and sale system of agricultural products. The fundamental route to resolve relevant contradictions laid in freeing part of rural population from land management and taking the road of industrialization and urbanization. Because of this, scholars present at the symposium gave the suggestions of making good choice on forerunner industry, making good use of rural funds, and handling well the relationship between government and enterprise. It was estimated in prediction that over 300 million rural population needed to be transferred by 2000. On average, nearly 20 million rural population needed to be transferred each year. Correspondingly, about RMB 20–30 billion yuan funds was needed each year.

The results of the discussion on agriculture and rural development was finally written into a report entitled “Reforming Grain Purchase and Sale System and Rural Industrial Structure” and reported to the central authorities. Three months later, the Central Document No.1 issued by the CPC Central Committee in 1985 specifically proposed “implementing the second step of the reform of the unified quota assignment and purchase system of agricultural products in the countryside”.

In addition to the topics mentioned above, the symposium also discussed the issues about bringing into play the functions of central cities, about the economic functions of the government, and about basic theories on socialism discussed in the group of basic theory. Due to the limited length of this book, the author will not elaborate on them. Of course, under the circumstances at the time, the discussion did not cover the relationship between fairness and efficiency, which was related to humanistic concern, the distribution of income, and the establishment of social insurance system. For example, Yao Xianguo from the Zhejiang University once proposed a paper entitled “The Duality of Socialist Labor Fund and China’s Wage Reform”. But the symposium did not set up a special topic group to discuss it.

4 The Effect and Influence of the Moganshan Conference

When examined from the angle of the history of China’s reform, two meetings stood out among those organized by middle-aged and young scholars in economics from the Third Plenary Session of the Eleventh CPC Central Committee in 1978 that might be recorded in history forever: One was the Moganshan Conference held in September 1984 and the other was the “Ten Years of Reform and Opening Up: The Symposium of Middle-Aged and Young Scholars on Theory and Practice” held at the Jingfeng Hotel in Beijing or the “Jingfeng Conference” for short from late March to early April 1989. And as the first national symposium of middle-aged and young workers in economic science from the beginning of China’s reform and opening up, the effect

and influence of the Moganshan Conference were far-reaching and manifold. Representatives were selected among excellent talents on the basis of the papers that they contributed before the symposium. The representatives carried out free discussion and persisted in innovation at the symposium. And they submitted proposals and suggestions for achieving transformation and progress after the symposium. The symposium attracted the attention of all over China and shone with everlasting brilliance even after the start of the new century. The historical value of this symposium was still to be determined by historians in the future in further study and evaluation. Its effect and influence at the time of its convening were mainly exhibited in the following several aspects:

I. Directly Providing Thoughts and General Plan for the Decision Making of the Central Authorities on Reform

After the conclusion of the Moganshan Conference, Xu Jing'an, Zhu Jiaming, Wang Qishan, Huang Jiangnan and Zhou Qiren were responsible for drafting the special report planned to be submitted to senior authorities on the basis of the discussion at the symposium. A number of young scholars, including Du Sha, Cai Zhongzhi, Tian Yuan, Jiang Yue and Liu Yu, participated in writing the report or its outline. After several days of intense work in analysis and sorting, eight special reports were completed on September 15: "Two Kinds of Thinking on Price Reform" (attached with two appendixes), "Several Issues Related to Price Reform", "Suggestions on Coastal Opening Up Cities", "Practicing the Assumption of Sole Responsibility of Profit and Loss by Enterprises Should Start with Small Enterprises (There should be a word "state-operated" here—a note by Chang Xiuzue) and Collective Enterprises", "Several Opinions on Financial System Reform", "Several Issues on Developing and Managing Share Economy", "Reforming Grain Purchase and Sale System and Rural Industrial Structure", and "About the Economic Functions of the Government in China in the Current Stage".³⁵

After the eight special reports were completed, representatives were sent to report to Zhang Jinfu, the State Councilor in charge of State Development Planning Commission and State System Reform Commission. After hearing the report, Zhang Jinfu asked about some things in it and gave the first instruction on the report on September 20, which read, "'The two kinds of thinking on price reform', proposed at the symposium of middle-aged and young workers in economics, is of great referential value". After that, Zhao Ziyang, premier of the State Council, instructed on October 10, "'The two kinds of thinking on price reform' is very mind-opening. The general topic is how to achieve and flexibly apply the combination of lifting control and readjusting. Such measure takes advantage of current trends and guides things to develop in the favorable direction. It both avoids great shock and resolves issues. Guangdong has started with price management system. Town and township

³⁵"Academic Reports of Middle-Aged and Young Workers in Economic Science" was originally published in Editor's Office of Economic Daily, *Economic Writings* (Classified Edition), Issue 1, October 18, 1984; half a year later, seven reports were selected and published under the title of "The Reports of the Symposium of Middle-Aged and Young Workers in Economic Science" on April 3, 1985 in *Referential Materials of Economic Research* Issue 52, 1985 or No. 1252 totally.

enterprises in Jiangsu succeeded in finding their own way. Collaborative coal prices have lowered. Large amounts of grains, cotton and edible oil have been purchased at extra-quota purchase price, which has resulted in the emergence of proportionally calculated price. All these are in substance the successful cases in combining lifting control and readjusting.”³⁶

In addition to the instructions of the leaders in China, several theoretical views and thoughts on countermeasures proposed at the symposium, for example, the view that “enterprises are commodity producers and operators that operate independently and assume sole responsibility for their profit or loss”, and some conceptions, such as “further opening up coastal port cities”, were incorporated into the *Decision of the CPC Central Committee on Economic System Reform*, adopted at the Third Plenary Session of the CPC Central Committee held in October 1984. It can be said that the Moganshan Conference provided powerful intellectual support to the decision making of the central authorities in China.

Of course, when people see the positive effect of the thinking of reform of “double-track price system”, they should also see its historical limitations and the negative effect that it caused to reform. In particular, the rent-seeking behavior, which was generated from the interest arbitrage in double-track prices, resulted in the growth of corruption in the society. This caused new social contradictions. So people should evaluate the “double-track price system” in an objective manner.

II. Promoting the Deepening of the Theoretical Study on China’s Economic Reform

In addition to provide proposals and suggestions to central authorities, the Moganshan Conference also promoted the deepening of the discussion and exploration on the theories of China’s economic reform.

Soon after the conclusion of the symposium, nine papers of the symposium were published as theoretical research results in three special pages of *Economic Daily* on September 25, 28 and 29 under the title of *Exploring the Theoretical Issues in Economic Reform—Selected Papers at the Symposium of Middle-Aged and Young Workers in Economic Sciences*. The two papers selected and published on September 25 were “Assumption of the Sole Responsibility of Profit and Loss and Expansion of the Enterprises’ Power” by Guo Zhenying and “Comprehensively Employing Various Economic Levers in Planned Management” by Wu Ke. The four papers selected and published on September 28 were “Revelations Obtained in the Development of the Shekou Industrial Zone” by Chang Xiuze, “Talking about the Principle of Gradient Transference of Technology” by Guo Fansheng, “The Strategic Status of Coastal Opening Up Regions” by Xia Yulong, Tan Dajun, Chen Ping and Cai Naizhong, and “Where Is the Gravity to Attract Foreign Investment?” by Lu Ding and Zhang Yining. And the three papers selected and published on September 29 were “Price Reform Does Not Entail the Increase of Financial Burdens” by Zhou Xiaochuan, Lou Jiwei and Li Jian’ge, “Price System Reform Is the Central Link in Reform” by Zhang Weiyong, and “About the Thinking on the Thinking of Price Reform” by

³⁶This paper entitled “Two Kinds of Thinking on Price Reform” was written by Xu Jing’an.

Tian Yuan and Chen Dezun. Papers of the symposium were also published in other newspapers and magazines.

The research results of the symposium published in the above involved important theoretical questions on reform and development. The publishing of these results triggered the study on some other important issues, such as the basic theoretical questions on macroeconomic regulation and control, fiscal and financial system reform, industrial structure adjustment, and ownership system relation reform. In the study people started to pay attention to introducing the beneficial elements in western economics. Chinese and western studies were combined and foreign studies were applied in Chinese ones. Many young scholars in economics actively published articles to formulate their own views. Thus a climax was formed in the middle and late periods of 1980s in which middle-aged and young scholars in economics engaged in in-depth academic research. Such trend exerted influence on the study of economics in China in the 1990s and also in the early period of the 21st century.

III. Promoting the Growth of the Team of Middle-Aged and Young Economic Scholars

Analysis on the long history of economics in China shows that the rise of the young generation of economists was inevitable in the first half of 1980s. The Moganshan Conference played a large promotive role to the rise of the young generation at the time.

First, the symposium pushed a group of middle-aged and young scholars onto the stage of history. A group of talents stood out in the symposium. Leaders of central authorities not only valued the results of the symposium but also started to pay much attention to this group of middle-aged and young scholars. Zhao Ziyang, Zhang Jinfu and other leaders had discussions with them. After the symposium, a group of them were recruited into governmental departments. For example, Tian Yuan was appointed member of the State Commission for Restructuring the Economic System. The commission also established in particular the Institute of China's Economic System Reform and recruited scholars who participated in the Moganshan Conference. These middle-aged and young scholars injected fresh blood into governmental departments and relevant institutions after they were recruited. Of course, they were confronted with the test of how to respond to the assimilation of bureaucratic system. In addition to central authorities, local governments also paid great attention to bringing into play the role of young scholars. Municipalities directly under the central government such as Beijing and Tianjin and other provinces established the societies of middle-aged and/or young economists.³⁷

³⁷For example, the members of the Tianjin Society of Middle-Aged and Young Economists, of which the author was also a member, included Li Jianguo, the current vice chairman of the Standing Committee of the National People's Congress, Zheng Wantong, vice chairman of the National Committee of the Chinese People's Political Consultative Conference, Li Shenglin, minister of communications, Wang Xudong, former minister of information industry, Luo Baoming, governor of Hainan province, and Xing Yuanmin, president of the Tianjin Municipal Committee of the Chinese People's Political Consultative Conference. Similar emergences of elite talents also occurred in other provinces and cities.

Second, the symposium directly resulted in the establishment of the magazine *Forum of Middle-Aged and Young Economists*. Soon after the conclusion of the symposium, the *Forum of Middle-Aged and Young Economists*, a periodical established by middle-aged and young economists themselves, published its inaugural issue in April 1985. The striking birth of the magazine signified that middle-aged and young scholars in economics in China had their own academic arena. This academic periodical was in fact a non-governmental magazine. It took Beijing, Tianjin and Shanghai as its kernel areas of activity and gathered middle-aged and young economists with influence and energy of action throughout China. The first editorial committee was composed of 35 middle-aged and young scholars.³⁸ The *Forum of Middle-Aged and Young Economists* became one of the periodicals on economic theories with large influence at the time.

Lastly, the symposium promoted the emergence of more new talents. The beautiful staging of middle-aged and young economists shown in the Moganshan Conference aroused the enthusiasm of more middle-aged and young scholars. Half a year later, the second symposium of middle-aged and young workers in economic science was held in Tianjin. The symposium selected 125 authors as representatives on the basis of 2,615 papers contributed. Ma Biao, Lu Zhongyuan, Ma Jiantang, Feng Lun, Liu Wei, Zhu Min and Hong Yinxing stood out in this symposium.

IV. Forming a New Conference Style and Influencing Later Generations

The conference style and writing style of the Moganshan Conference were relatively distinctive. This group of young workers in economic science brought fresh atmosphere with them and challenged the tedious and rigid conference style and the stereotyped party writing style that prevailed in China for a long time. The symposium had two outstanding features in style.

One was “selecting people by paper”. This was the most shining part in conference style in the symposium. The several “disregards” implemented in the selection of papers showed great attraction to middle-aged people and youth in various industries and areas. The 125 representatives to the second symposium of middle-aged and young workers in economic science were selected according to the principle of “selecting people by paper” and publicized nationwide on the *Economic Daily*.

³⁸The general editor of the editorial committee was Ding Wang. Wang Xiaolu, Xing Yuanmin, Chen Shenshen, Jin Guantao and Hao Yisheng were vice general editors. The members of the committee were, listed in the order of the number of strokes in their surnames, as follows: Ding Wang, Wang Luolin, Wang Zhan, Wang Xiaolu, Zuo Zhi, Lu Jian, Tian Yuan, Xing Yuanmin, Liu An, Liu Youcheng, Sun Hengzhi, Qiao Tongfeng, Liu Jinglin, Zhu Min, Zhu Jiaming, Wu Jixue, Yang Mu, Li Luoli, Du Sha, Chen Yizi, Zhou Tianbao, Chen Shenshen, Jin Guantao, Chen Weishu, Zhou Qiren, Jin Yanshi, Zhang Gang, Luo Baoming, Yao Lin, Zhang Chaozhong, Hao Yisheng, Gao Tiesheng, Guo Fansheng, Huang Jiangnan, Chang Xiuze and Cai Zhongzhi. In the second year of its establishment, the magazine made adjustment to its editorial committee. Zhu Jiaming was appointed as general editor. Luo Baoming and Huang Jiangnan were appointed as new vice general editors. Sun Xian, Zhu Xiaoping, Wu Xiaoying, Hua Sheng, He Ling, Yang Xiaokai, Chen Qiwei, Zhang Xiangrong, Zhang Wei, Zhang Siping, Xu Jing'an, Yuan Zhongyin and San Xiangping were added as members of the committee.

The other was free discussion. In addition to “selecting people by paper”, the Moganshan Conference particularly encouraged academic contention and paid great attention to maintain academic democracy and freedom. Wang Qishan said that it was very important to retain the independency of academic research. “It is terrible that a person’s talent is not recognized, but it is worse when he loses the freedom to make his own choice.” The symposium advocated criticism, pursued truth, and paid attention to the role of brainstorming. As debates became very intense, the symposium invented the method of “discussion under hanging shingle”. Such method was inherited. It was adopted during the “Ten Years of Reform and Opening Up: The Symposium of Middle-Aged and Young Scholars on Theory and Practice” held at the Jingfeng Hotel in Beijing during the end of March to the early April, in 1989. The conference style characterized by free discussion and pursuit of truth had important influence on academic research in later times.

Of course, while elaborating on the historical role of the Moganshan Conference, people should think over it with a level-headed attitude. At the time, some scholars pointed out that “a master of economics should come out of this generation of workers in economic science.” Yet twenty-six years has passed. There has been no sign of the rise of any master of economics until now. Perhaps, time is still short for it or conditions are not ripe. But this indicates exactly that there is still a very long road to run for the development of economics in China in the future. It is still a hard road and it needs the persistent exploration and hard work of all economists and, particularly, middle-aged and young scholars.

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Chapter 13

The Introduction of Macroeconomic Management Theory and Experience from Western Countries at the “Bashan Tourist Ship” Conference in 1985



Zhouyuan Zhang

1 Background: How Macroeconomic Management Could Follow up After Microscopic Economy Started to Be Opened up and Enlivened

Following the start of the reform and opening up in 1979, people continued to implement market-oriented reform. First, microscopic economy was opened up and enlivened. In the countryside, the rural household contracted responsibility system was put in place and peasants began to operate as independent commodity producers and operators. In the city, people expanded the autonomy of enterprises and allowed non-public ownership economy to exist and develop. Market competition unfolded in the city and a situation emerged that enterprises got into a race in the market. China's national economy started to become active.

However, market competition also brought some kind of disordered status. For example, the expansion of investment and consumption caused the excessive distribution of national income. Currency issue went beyond the needs of economy and resulted in price rise and inflation. Under such circumstance, it not only did not work but also failed to achieve any effect to continue to employ the methods used during the period of planned economy, which took mandatory plans as their main features, in carrying out the management of macroscopic economy. It was urgent to explore effective approaches and methods to manage macroscopic economy under new conditions. First, Chinese economists knew from works on economics that, although market had the advantage of optimizing resource allocation under market economy, it did have its own weakness and negative side that required the government to carry out regulation and management on macroscopic economy. But a market economy country would not adopt the form of direct management when managing its macroscopic economy but mainly implement indirect management. It mainly

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employed economic and legal means, supplemented with necessary administrative means, to regulate and control economic aggregate and major economy structure so that its national economy could run stably and healthily. But this was not enough. Many insightful personages believed that foreign experts in this area should be invited to come to China and introduce their theory and experience in managing macroscopic economy under market economy. Thus people could employ their theories and experiences creatively in combination with the considerations on China's own national situation to improve and better China's regulation and management of its national economy.

Under such background, Mr. Edwin Roca Lim, director of the Beijing Office of the World Bank, invited a group of renowned foreign experts. These eleven experts included James Tobin, US Nobel Prize laureate, Sir Alec Cairncross, former president of the Royal Economic Society of the UK, Otmar Emminger, former vice president of the Central Bank of Federal Republic of Germany, Janos Kornai, a Hungarian economist, Michel Albert, Chairman of the Board of the Assurances Générales de France, Aleksander Bajt, member of the Yugoslavian Economic Reform Executive Committee, Leroy Jones, professor of the Boston University of the USA, Włodzimierz Brus, a Polish economist, Kobayashi Minoru, director of the Industrial Bank of Japan, Edwin Roca Lim, representative of the World Bank, and Adrian Wood, a British economist. Together with Chinese experts and scholars Xue Muqiao, Ma Hong, An Zhiwen, Liu Guoguang, Wu Jinglian, Tong Dalin, Gao Shangquan, Chen Rulong, Shang Ming, Hong Hu, Yang Qixian, Gong Zhuming, Xiang Huaicheng, Zhou Shulian, Zhang Zhuoyuan, Zhao Renwei, Chen Jiyuan, Dai Yuanchen, Lou Jiwei, Guo Shuqing, He Jiacheng, Li Zhenning, Tian Yuan and Wu Kaitai, more than 30 economic personages held an international symposium on macroeconomic management. The symposium was jointly sponsored by the Chinese Academy of Social Sciences, the China Society of Economic Reform, and the World Bank and held from September 2 to 7, 1985 on the Bashan tourist ship, which sailed from Chongqing to Wuhan along the Yangtze River. In this symposium, in-depth discussion was made on the issue of macroeconomic management in market economy country and, particularly, the issues on macroeconomic management and other important issues that China encountered in economic system reform. Renowned foreign experts and scholars systematically introduced the theories, policies and experiences of market economy countries in macroeconomic management at the meeting. And they also exchanged viewed and achieved some common understandings with prestigious Chinese experts and scholars on the issues of how to carry out and improve macroscopic economic management in the process of China's marketization reform and other important issues that China had met in such reform. Because of these, it can be said that the "Bashan Tourist Ship" Conference opened a new stage of China's theoretical study on macroscopic economy.

The China Society of Economic Reform compiled the results of the symposium into a book entitled *The Management and Reform of Macroscopic Economy—A Selection of Opinions and Views of the International Symposium of Macroeconomic Management*, published by The Economic Daily Press in June 1986, with 20,000 copies printed. Before the symposium, Zhao Ziyang, the then premier of the State

Council, met foreign experts who attended the symposium and main Chinese participants. After the symposium, the Chinese Society of Economic Reform and the Chinese Academy of Social Sciences jointly wrote *A Report on the Main Situation of the International Symposium of Macroeconomic Management* to the State Council on October 12, 1985.

2 Main Issues and Views of the “Bashan Tourist Ship” Conference

The shift from mainly implementing direct management to mainly implementing indirect management was the kernel of the macroeconomic management reform in the former planned economy countries. This was also the consensus of Chinese and foreign experts who attended the “Bashan Tourist Ship” Conference on China’s macroeconomic management reform. This shift signified one leap-forward made by Chinese circle of economics in the understanding on the theory of macroeconomic management.

Summarized on the basis of the symposium, the main topics and views discussed at the “Bashan Tourist Ship” Conference can be divided into the follow three aspects.

I. About Mid- and Long-Term Goal and Steps in Economic System Reform

The experts present at the symposium believed that there had to be one specific mid- and long-term goal and relatively concrete short-term measures for economic system reform. As far as the mid- and long-term goal of reform is concerned, Janos Kornai, renowned Hungarian economist, believed in his analysis that the macroeconomic management model of various countries in the current world could be divided basically into two types. One type achieved coordination through administrative means and the other type through market mechanism. The former could be further divided into direct and indirect administrative coordination while the latter into completely non-controlled coordination through market mechanism and coordination through market mechanism under macroscopic control. The characteristic of the first type, namely coordination through administrative means, was that there was subordinate relation between enterprises and the state and economic activities were coordinated mainly in reliance to vertical information flow and centralized decision making. The characteristic of the second type, namely coordination through market mechanism, was that there was no subordinate relation between enterprises and the state and economic activities were coordinated mainly in reliance to horizontal information flow and non-centralized decision-making. He said, of course, this was only an abstract theoretical summarization. In reality, various models often interacted and coexisted with each other. Such classification was only the main model of regulation. The so-called completely non-controlled coordination through market mechanism does not exist in any country in real life.

The target model of the economic reform of a socialist country mainly involved the management of state-owned enterprises. Janos Kornai believed that people could choose either coordination through indirect administrative means or coordination through market mechanism under macroscopic control. Both models required basically cancelling the management through mandatory material planning targets. The economic activities of enterprises were mainly controlled by the state through economic means. The main difference between the two was that the coordination through market mechanism under macroscopic control was that the state managed enterprises through formulating uniform and stable economic regulation and control measures and economic regulations and laws. An enterprise had to handle its matters in accordance with the law and did not rely on vertical administrative protection and care. Coordination with indirect administrative means was not very effective in general although the state also formulated some economic regulation and control measures and economic laws and regulations. Enterprises could eventually bargain with vertical management organs of the state through various channels so that their prosperity and existence still relied on vertical administrative protection and care. The reason that the reform in Hungary failed to achieve the effect that people expected was mainly that the country was stuck in a dilemma between choosing one of the two target models for a long time. Enterprises continued to stay in a status of "soft budget constraining" through bargaining with the state. So people who implemented reform in China needed to choose one from the two models and he tended to support the second model. But he believed that conditions needed to be created in three aspects. First, people needed to carry out price reform resolutely to ensure the correctness of price ratio. Second, they needed to strictly implement various economic laws and regulations so that enterprises had to become the final taker of the economic responsibilities related to the consequences of its operation. Third, people should gradually open up fund market as an intermediary link of economic activities. Professor Janos Kornai also believed that, because the nature, ownership structure, distribution system, the role of planning, and social moral standard of a socialist country was different from those of a capitalist country, the adoption of such a model had substantial difference to the market economy in the west.

Professor Leroy Jones believed that, because market was undeveloped and incomplete in a developing country and it only played a limited role, it might end up in failure to adopt regulation purely through administrative means or market mechanism. China should choose a model that integrated both and distinguish and handle various situations differently. In the areas where market was in full competition, the government might make no intervention. If market competition was still a potential, the government should take measures to promote competition. Where there were no conditions to start competition, the government should make administrative intervention selectively. Polish economic expert Wlodzimierz Brus also said that the key to achieve the goal of economic system reform was to create sufficient conditions for bringing the role of market mechanism into play. But market was not almighty, planning had to play a necessary guiding role so as to overcome the mistakes and weaknesses of market.

With respect to the methods and steps of reform, foreign experts and scholars believed that, for state-owned enterprises, China's economic management system was still in a stage of transition from coordination through direct administrative means to that through indirect administrative means. There needed to be a long process if people wanted to reach the model of market coordination under macroscopic control. The method of reform was that people should first adopt indirect administrative means, such as finance, currency, fiscal measures and taxation, as much as possible to carry out the control and regulation of economy. Then they should supplement with direct administrative means in regulation when necessary. There were different views on the steps of reform in the discussion. Wlodzimierz Brus held that people should start with the current situation in China and carry out the transition toward the final goal in different stages. People could use different methods to manage in different economic departments in different periods. They should use new methods in some places and continue to use old methods temporarily in some other places. Jonas Cornai believed that people should not handle the issue about the steps of reform in a simplistic way. The reform in some areas needed to be implemented in steps. For example, in the adjustment of ownership structure, people should carry out the diversification of ownership system under the condition of taking public ownership system as the dominant one. They should reward the development of joint ownership systems across industries and regions and of shareholding systems that consisted of different economic sectors. The reform in some other areas, such as the reforms of planning system, price system, wage system and financial system, should be carried out in a packaged manner. British economic expert Sir Alec Cairncross believed that reform should be carried out in a packaged manner and it was possible only under the circumstance that general supply and general demand were in relative balance. However, the countries that implemented a reform often did not possess such condition in the beginning. So reform should be carried out step by step and with a progressive method to achieve transition gradually. After the World War II, the UK spent about nine years to transform from controlled economy to the economic system in which demand was mainly controlled macroscopically. And the control over foreign currency was not cancelled until 1979.

Under the circumstance that demand expansion emerged in the current Chinese economy, it was necessary to adopt some direct administrative control over economic management, such as setting up credit limits, controlling the growth range of wages, and controlling the use of foreign exchange. But it should be noticed that such measure had certain practical danger. Namely, people could easily turn such temporary measures to solve problems into permanent management methods and thus return to the system of excessively concentrated power and depart from the correct direction and goal of reform.

II. About the Main Regulatory measures in Indirect Macroeconomic Management

Experts and scholars present at the symposium agreed that, if people wanted to realize the model of coordination through market mechanism under macroscopic control, the state had to lift the direct control over the microeconomic activities of enterprises.

Besides, they had to strengthen the indirect control over macroscopic economy. Its kernel was to effectively control the reasonable growth of general demand and correspondingly establish and improve various means of regulation and control for indirect management. The summarization of the discussion in the symposium shows that the views were mainly about reforming and improving the systems of finance, currency, fiscal measures, taxation, income distribution, international balance of payments and planning.

(I) Finance and Currency

The experts all emphasized that the improvement of the system of finance and currency played a critical role among the means of regulation and control for indirect macroeconomic management. In order to fully bring into play the role of financial and monetary means which they should play, people should take the following measures:

First, people should establish broad currency aggregate index or currency base index as the important means to control total demand. Otmar Emminger, former vice president of the Federal Bank of Germany in the Federal Republic of Germany, believed that broad currency aggregate index should include currency issue, current deposit, fixed term deposit and savings deposit and these could be calculated through weighted average with different weights. But, China was now in the process of building a new financial system and its currency circulation still did not have stable patterns. So a scientific index of broad currency aggregate could not be established within a short time. In view of this, people could temporarily use the method of setting up credit aggregate to control inflation and ensure steady economic growth. US economic expert James Tobin believed that there was still controversy in developed country on whether there should be a broad currency aggregate index. So it might not be applicable to China's reform in the present stage. As long as the increase of money did not concern inflation, people could just leave it uncontrolled. In China, savings deposit was the only method for its citizens to accumulate wealth. If people included long-term savings deposit into currency aggregate index, it was the same as limiting the growth of deposit and thus unfavorable to economic development. Therefore, people should control currency supply and inflation with the method of controlling currency base, namely controlling cash and central bank debts as the equivalent to cash.

Second, people should complete and improve the system of required reserve. Commercial banks paid required reserves according to certain proportions to the deposits that they accepted. This was an important financial means in western countries to limit the ability of commercial banks to issue loans and to ensure monetary stability. Experts believed that the required reserve ratio of 10%, according to which the specialized banks in China currently paid required reserves to central bank, was not low at all. But different ratios were not stipulated according to different terms of deposit. The central bank paid interests on required reserves. Besides, the central bank provided funds to specialized banks according to plans rather than the amount of required reserves paid to it. All these offset the role of the required reserve system that it should play and thus were unfavorable to the control and regulation of macroscopic economy.

Third, people should bring the regulatory role of interest rate into full play. Interest rate was an important signal for indirect control of macroscopic economy. It played an important guiding role to the effective allocation of resources, the adjustment of industrial structure, and the improvement of microscopic efficiency. In general, the control over interest rate should be lifted. The central bank could determine a uniform refinancing interest rate on the basis of the situation of currency demand and supply on the market. Except this, people should not impose administrative intervention on the interest rate of loans of the commercial banks. Because of the current situation in China, it was impossible to regulate its economic activities completely through interest rate. But people had to change the situation of negative interest rate in which deposit and loan rates were lower than inflation rate. People would adopt the measure of using administratively-stipulated interest rates and then gradually shift to the method of implementing floating interest rate according to the needs in economic development and the situation of the market and currency and thus promote the enterprises to make necessary response to interest rates.

Fourth, people should build a complete banking system. Central bank took the main responsibility in bringing into play the role of the financial and currency means mentioned above. So people had to strengthen the statuses of central bank. In western countries, the central bank basically had two kinds of statuses. One was that it was under the leadership of the parliament and had larger independency like the situation in the Federal Republic of Germany, the USA, Switzerland and the Netherlands. The other was that it was under the leadership of the government and there was interdependency between them like the situation in the UK, France and Italy. The two practices caused different effects in controlling currency stability and inflation. It was unimaginable that China's central bank became independent of its government. But it was still necessary for it to retain a powerful central bank. The People's Bank of China could not be turned into the money management unit and cashier organ of China's planning and financial departments. Moreover, people should gradually establish a banking system that was controlled by the central bank and composed of multiple banking forms including various specialized and local banks. Various kinds of banks other than the central bank should be gradually operated as enterprises. And the role of financial means should be brought into better play through the competition among them.

(II) Fiscal Levy

The experts believed that budget was a powerful means for macroscopic control. Fiscal policies had two kinds of influence on economy: One was direct influence, namely that the government decided on its budgetary revenue and expenditure. The other was indirect influence, namely that the government depended on bank loans to make up its fiscal deficit. The government's fiscal policy could be restrictive, namely that the government intended to increase tax income and reduce spending. Or it could be expansionary, namely that the government intended to increase spending and reduce tax income. Or it could be neutral, namely that the government intended to resolve government fiscal deficit problems through issuing government bonds.

Fiscal policy and monetary policy had close relation and had to be employed in combination. It was believed in general that, under the circumstance that economic growth became overheated and there was excessive demand in China at present, both fiscal department and the banks should adopt restrictive policies. In the long run, people should adopt restrictive fiscal policy and loose monetary policy under the circumstance of relatively coordinated economic development and avoid adopting loose fiscal policy and restrictive monetary policy. At present, the USA adopted the latter measure but did not achieve satisfactory result. However, Japanese economic scholar Kobayashi Minoru proposed that Japan implemented expansionary fiscal policy and tight financial policy similar to the current policies of the USA during the period of high-speed economic growth. In the end, there was no financial deficit in certain fiscal years. This was because the income tax paid to the government by enterprises and individuals increased largely as economy grew. The key issue here was how to complete taxation system and fully exert the role of taxation so as to ensure that the fiscal revenue of the government would grow correspondingly when the economy grew. Experts present at the symposium all emphasized that fiscal deficit should be shifted to the banks under no circumstance. It should not be made up through issuing currency but mainly through issuing bonds. Under the circumstance that there was inflation in China, the banks should tighten credit. In addition, the central bank should freeze fiscal surplus if there was such surplus so as to reduce the amount of currency in circulation and retain the stability of currency and price.

(III) Income Distribution

Experts and scholars present at the symposium all pointed out that too fast wage growth and over-expansion of consumption demand was one important reason that caused economic difficulty and inflation in western developed countries and some East European countries at present. Western countries generally adopted the method to determining wage growth rate according to inflation rate and the increase range of labor productivity. Now it was proved that this was not a good method because both inflation rate and the growth of labor productivity were hard to predict accurately. When people took these factors as the basis for wage growth, they in fact set the tone for the inflation rate in the future. This would definitely result in the spiral rise of wage and inflation. People should pay sufficient attention to such lesson when they formulated income distribution policies in China's economic reform. Hence, the experts and scholars believed that it might not be a good method to link wage growth to profits in state-owned enterprises. This was because the growth of profits of the state-owned enterprises had direct relation with external factors like the amount of the state's investment and resource conditions. The standards of wage should not have too large gap between different enterprises. Otherwise, wage would not be able to truly embody the principle of distribution according to performance in socialism. If the wage in some enterprises grew too fast, such tendency would spread to other enterprises. And some enterprises would transfer the raise of wage cost to the prices of their products. Hence, a strong pressure would form in the society so that people got into a race of raising wages. This would push wages to rise comprehensively and cause the emergence and deterioration of inflation. The experts held that the state

had to strictly control the range of average wage growth. Among the rises of wages in enterprises and among their employees, those that exceeded average social growth had to be given to units and individuals who truly made above-norm contribution. China now implemented the system of imposing tax on bonuses for topping quotas. At present, it seemed to be a good method. And people should implement it strictly and universally. But in the long term, people had to look for a better approach to reform wage system, such as implementing time rate wage and linking wage to physical output.

(IV) International Balance of Payments

Włodzimir Brus proposed that the controlling of foreign economic relations, investment and income distribution represented three indispensable factors in the state's planned management of its economy. Controlling foreign economic relations did not mean to monopolize foreign trade. Rather, it meant to make the country retain its appropriate payment ability so that it could selectively introduce foreign advanced technology and management experience for its own use after evaluation and filtering. Perhaps, such evaluation and filtering process might cause certain situations of direct control, such as controlling foreign exchange and controlling the import and export of some products. A major country like China could not afford to allow its domestic economy to be influenced by foreign factors. It had to retain necessary independence and self-reliance. James Tobin also believed that it was not something at present or in the near future for China to control the balance of foreign exchange with indirect methods. It was something for the future. It was unnecessary for China to sacrifice its domestic macroeconomic balance to retain the balance of foreign exchange. China should not stop its control on the flow of international capital in the foreseeable future. Neither at present nor in a very long time in the future should China create the freedom for its citizens to obtain foreign exchange at will.

The experts believed that China could borrow from abroad in a planned manner to retain domestic economic growth and maintain the balances of employment and of supply and demand. It could also keep reasonable deficit on its current account in foreign trade. The reason was that to use foreign investment to retain certain investment level and to use foreign investment to retain better living standard were of different natures. But China had to pay sufficient attention to the benefits from the use of foreign exchange and ensure its ability to pay back in the future. It was a key issue in the implementation of an open economy to establish and keep balanced exchange rate. Adjusting exchange rate would become inevitable under the circumstances of imbalanced current account of foreign exchange, depressive export and overvalued Renminbi. But only under the circumstance that excessive domestic demand was put under control could such adjustment work. Otherwise, the benefits of adjusting exchange rate would be quickly offset by rising domestic prices.

(V) Programs and Plans

French economic expert Michel Albert proposed that, in addition to using well the several means of regulation and control mentioned above, how to use well the means

of programs and plans was also an important aspect in implementing market regulation under macroscopic control. Particularly, in semi-developed countries, it had a role not to be neglected in promoting technical innovation and industrial structure adjustment to use plans to reduce “uncertainties” and carry out comprehensive research on the market. For example, France formulated the programs to develop key industries after the World War II. And it achieved great success in stimulating the scientific research and technical innovation of companies and enterprises with the mid-term orders of public sector. Thus France quickly became the second largest country in nuclear energy industry, the third largest country in arms export, and a major country in aircraft manufacturing, space and communications industries. Yet there were two types of plans. One was the plans that stood in opposition to market. Such plans were mandatory and used as the means of economic centralization. The other was the plans that worked in the market. They were non-mandatory and used as the means of economic decentralization. The correct practice should be to combine the two ways above. In China, the state still should control and take responsibilities in certain economic activities, such as the development of economic infrastructure, communication and transportation, energy and emerging industries. Only in this way could people make the changes of industrial structure adapt to the needs of international and domestic market competition. However, these enterprises had to make decentralized decisions on their own production and operation. Sir Alec Cairncross believed that mandatory plans were effective in resolving short-term shortage. But if the imbalance was long-term, it should be resolved through adjusting price or taxation. If mandatory plans were used improperly, they might damage the initiative in production and cause vicious cycles in production. The guidance of economic activities should only be made in reliance to agreement, persuasion and consultation. It was inadvisable to brutally compel with centralized plans.

III. About the Necessary Conditions to Implement Indirect Control on Macroscopic Economy

Experts and scholars present at the symposium pointed out that the influence and action of the indirect control of macroscopic economy was determined to a large extent by the response of microeconomic units. If enterprises could not produce sensitive response to interest rate, tax rate, exchange rate, wage and price under the circumstance of the implementation of indirect control, then the means of indirect control of macroscopic economy failed to play an important role. Therefore, people had to resolutely create various external and internal conditions that could promote enterprises to make sensitive response to the means of indirect control of macroscopic economy.

(I) Establish a Relatively Complete Market System

Experts and scholars all held that there had to be relatively complete market conditions before the implementation of the indirect management of macroscopic economy. In particular, they had to establish and complete commodity market and fund market.

First, people needed to fully open up commodity market, including consumer goods market and the market of means of production. Except for the time of war, the method to implement control and allocation on many kinds of products was unfavorable to economic development. The economy during the time of peace should be handled mainly through managing demand rather than organizing supply. The practice of controlling physical products was hateful to both consumer and producer because it repelled competition and stifled the stimulus for economic development. The price of such practice was very expensive. But opening up commodity market did not mean that the government had nothing to do. It still needed to employ various indirect economic means to influence and guide the economic activities of enterprises through the action of market mechanism. However, the measures that the government adopted had to be favorable to competition and the retention of the unity of the market and also to prevent any separation and division of the market. Włodzimierz Brus believed that the serious difficulty that emerged in the economy of Yugoslavia was caused to a certain extent by the situation that the eight administrative regions in the country all operated on their own so that they were separated from and closed to each other and failed to form a unified market.

Experts generally believed that people had to open up factor market at the same time when they open up commodity market. Without a normal factor market and, in particular, financial market, there could not be a normal commodity market. This was because it was a very important condition to bring into full play the role of financial and currency means if people wanted to implement indirect management of macroscopic economy. It was inconceivable that people established commodity market first and then established financial market. At present China had to establish a developed banking system. In addition to that, the time was ripe for building a bond market although it was not the time for building a stock market. People should gradually develop bond market while opening up commodity market. Such measure was favorable for enterprises to raise fund through issuing bonds and improving the benefits of fund use. It was favorable for the government to make up financial deficit through issuing bonds and reduce the pressure of central bank. It was also favorable for increasing the long-term wealth of the citizens and reduced the impact of the flowing idle funds of the public on the market. In addition, because the interest rate of bond and its term of repayment of capital were fixed in advance so that it could not be traded at a high price in speculation, this was favorable for preventing the speculation activities that might arise after the fund market was opened up. Yet there were two forms of bond issuance. One type was of purchase according to state quota and the other was of free purchase. The former was in fact equivalent to turning over funds to the state while the latter was bonds in the true sense. So the first type should be avoided as much as possible. Besides, it was necessary to make laws to ensure the rights and interests of bond holders. James Tobin believed that China could not only open up bond market but also should consider opening up stock market. It was an issue that should be addressed seriously and prudently how to establish a relatively complete fund market in China without sacrificing the principles of socialism.

Włodzimierz Brus also pointed out that the situation that China did not have labor market to a certain extent would affect the considerations on the reform goals in

the future. Under such a circumstance, the management of state-owned enterprises definitely required more than the traditional means of the west where people mainly employed financial and currency means in management. And the role of market mechanism would be limited. The Soviet Union acted more flexibly than China in the area of the flow of labor and China should consider the situation there.

(II) Carry Out Price Reform Positively and Resolutely

Most experts believed that people had to lift the control over commodity prices and change the situation of price distortion if they wanted to establish a complete commodity market. For such purpose, they had to distinguish the price rise caused by structural price adjustment from inflation. This was very important. As long as the price rise was not caused by excessive currency issue, it was not inflation when certain pressure in economic life drove the price up. For example, when certain kind of product had lower price for a long time, it was necessary to make reasonable price adjustment. Crop failures might cause grain prices to go up. The price fluctuations on the international market might trigger domestic price rise. All these rises were not inflation. As long as total money supply was under reasonable control, it would not cause comprehensive price rise to lift the control over physical products. The key to price control laid in the control of three kinds of strategic prices, namely fund price or interest rate, labor price or wage, and foreign exchange price or exchange rate. It was not about controlling the prices of physical products. Edwin Roca Lim, an economic expert of the World Bank, pointed out that people should seize the opportunity and resolutely reform prices under the circumstance that China now achieved higher economic growth rate. The kernel of this reform was to change the approach of determining prices with administrative means because it was impossible for any official to calculate the exact figure of the price of each kind of commodity. According to the existing experiences of some socialist countries, people needed to spend two years to collect information when they wanted to determine prices with administrative means. Then two more years would be spent to do research and get a conclusion. Finally, half a year would be spent to print the price list. At least four or five years were needed for implementing such price list. When everything was in place, much time had passed and things were different. It can be seen that adjusting price system mainly with administrative means not only needed very long time but also could hardly achieve the desired effect.

There were two kinds of evaluations on the situation that there were two kinds of prices for one type of commodity in China and other socialist countries. Jonas Cornai believed that commodity prices were interdependent. The irrationality in one link would quickly spread to other links. When part of the prices were market price and part of them were administrative price, the prices could not give accurate signal and it would be hard to solve the problem of the “soft budget” of the enterprises. But Wlodzimierz Brus believed that the “double-track system” price that China implemented on the means of production might be a kind of useful invention. This was because other socialist countries only had two prices for consumer goods and never implemented two prices for the means of production. Such a method was favorable for the transition from one price system to another price system. It could

be a bridge for the smooth transition from the determination of price directly by administrative officials to the determination of price by the market. But people should be aware that it was not at all perfect. And more importantly, the time of implementing “double-track system” prices should not last too long for whatever reason.

(III) Implement Diversified Ownership Systems and Operation Modes

Włodzimierz Brus proposed that it should be recognized that the public ownership enterprises could play an important role for economic development in socialist countries. But it should also be seen that there was the necessity to realize the diversification of ownership systems under the condition of socialism. This was because it was still hard to prove until now that there was one kind of ownership system that possessed absolute superiority over another kind. In socialist countries, traditional views often took state-owned enterprises as the best and most ideal form of ownership. But in reality, it was never the single form of state ownership. For example, the Constitution of the Soviet Union claimed that there were only two kinds of ownership systems, namely whole people and collective ownerships, in the country. But the terms did not match what was in the reality. And people already held an attitude of despise and repulsion against collective and individual ownership systems. They transformed collective ownership into a form roughly equivalent to whole people ownership. The management method of such ownership system had little difference from that of state-owned enterprises. In some socialist countries, for example, in agriculture in Poland, individual economy was often prosecuted in frontal attack or surrounded with the expectation that it would collapse someday although such ownership played a dominant role for a long period of time. Even in the period when the most tolerance was given to it, it was just allowed to exist at the most. Therefore, it can be said that there was no relatively complete form of diversified ownership system in socialist countries until now. And such ownership system was what people truly and greatly needed.

The diversification of ownership system should include both state-owned economy and collective and individual economies. One very important point was to give collective economy adequate socialist nature and status. People could adopt traditional ownership forms as the operation and management modes of state-owned enterprises. And there could also be new forms such as implementing joint operation and shareholding system, which would be more beneficial to the development of economy. China now started to pose and consider such questions, which was very good because reasonable ownership structure and operation mode would have very important influence on the benefits of the enterprises. The outstanding achievements in China's agricultural reform and the results achieved from the increasing dynamism of its non-state-owned economy had already proven this point in a noticeable way. Michel Albert also believed that the role of market was far more important than the issues about the ownership system of the means of production. It was necessary to implement nationalization in some areas, but the premise was that state-owned enterprises should participate in market competition and should not obstruct the operation of the market.

(IV) Give Enterprises Necessary Independence

Experts proposed that state-operated enterprises could achieve and enjoy higher benefits. The necessary conditions for this were as follows: First, enterprises should be given necessary independent power to make decisions. Enterprises should not only have the power to make decision on its routine operation activities but also the necessary power to make decisions on investment. Wlodzimierz Brus believed that one of the main reasons that the economic reform in Hungary fell into stagnation was that the power to make decision on investment in the enterprises were basically concentrated in hands of the state and controlled by means of direct planning. Michel Albert made a comparison about this. He said, because of such approach that enterprises decided on routine production and operation and the state decided on development direction, product structure and investment, the management of the enterprises had to set one eye on their superior authorities and the other eye on the market. It was like that a person chased two rabbits at the same time. Under such a system, no one could be responsible for the enterprises and no good effect could be achieved. Second, enterprises should be given a fair competition environment. The enterprises not only needed to compete with each other domestically within one industry in which all monopoly should be abolished but also to participate in international competition under possible conditions. People should avoid administrative intervention and protection as much as possible so that not a single competitor was given special care. If an enterprise operated badly for a long time, it should be restructured or shut down. Subsidies were nothing but “sleeping pills” rather than “tonic” not only for state-operated enterprises but also private enterprises. The Ministry of Finance could just save all these money. Third, state-owned enterprises should be placed under the supervision of the public so that an enterprise would not damage the interests of the state, the society and consumers because of their own interests.

Moreover, people should change the functions and methods of the government in managing enterprises. The government organs might refer to the experience of transnational companies in the management of enterprises. These mainly included the following: (1) Appointing a general manager, (2) Setting and assigning specific goals, (3) Supervising the operation activities of the enterprises, (4) Implementing reward and punishment system, (5) Providing necessary funds and making investment decisions, and (6) Making long-term coordination plans. The government took care of nothing else expect for the above and left the rest of the matters for the enterprises to decide on by themselves. The board of directors should consist for personages who represented the interests of the three parties of the state, the employees and consumers. Among them, the people who represented the interests of the state should be the majority. In order to make the behavior of enterprise leaders conform to the interests of the global situation. Their wages and bonuses should be determined by the state. If the enterprises operated badly, they should be removed or replaced at any time.

(V) Establish Complete Economic Information and Supervision System

Experts generally believed that it was an extremely urgent task to build a complete information system so as to manage well a huge open economy like China. James Tobin said, I made such a suggestion when I visited China in 1972. Today I would like to make the suggestion once again. Without reliable statistical data and economic analysis as the basis, people could not make accurate economic predictions and correct macroscopic decisions. Michel Albert also emphasized that the economic development of any country proceeded with the development of information. People had to put economic information onto a position as important as economic planning. The plans formulated without accurate information were often blind ones.

Experts also proposed that, in order to ensure the effective implementation of various means of regulation and control in the indirect management of macroscopic economy, people had to strengthen relevant economic legislation and establish a nationally unified accounting system and an independent auditing system. Without a nationally uniform accounting system, it would be hard for people to make accurate evaluation on the operation results of the enterprises and to achieve good benefits in the allocation of social resources. Without strict auditing system, it was impossible for people to prevent the fraud and illegal acts of the enterprises and to earnestly implement and enforce economic laws and regulations.

Many of the results of the discussion in several aspects as mentioned in the above were of certain value for people to draw from or refer to in China's economic system reform. As China's economic system kept deepening, people should adhere to the principle of starting with China's actual situation and continue to carry out international communication on the experience of economic management in various ways while paying more attention to studying the new situations and issues that emerged in the reform and earnestly summarizing the practical experiences of its own. Such practice was truly conducive.¹

3 Several Comments

The International Symposium on Macroeconomic Management held on the Bashan Tourist Ship in 1985 was of very important meaning, or to a certain extent of monumental meaning, to the theories on macroeconomic management and even those on economic system reform in China. The symposium was also very meaningful to practical work. As Xue Muqiao said in his opening speech, "If people want to enliven microscopic economy, they must strengthen the control over macroscopic economy. Now we are not good at strengthening macroscopic management. So many loopholes emerge after microscopic economy is loosened and enlivened. From the fourth quarter last year to the first quarter this year, people lost control over bank credit fund and consumption fund, which compounds the difficulty in the economic system

¹The above was taken from China Society of Economic Reform (1986), pp. 3–15.

reform this year. Therefore, it is of particularly important meaning to hold an international symposium on economic planning and macroscopic management. We have great expectation on the symposium.”²

It is believed that the following several common understandings achieved through discussion at the symposium were particularly important:

First, after microscopic economy was loosened and enlivened, the government’s management on macroscopic economy should transform from originally implementing direct and planned management to mainly implementing indirect management. Namely, People mainly employed economic and legal means, supplemented with administrative means, to carry out management. This was also the main content in the reform of macroeconomic management system.

Second, the economic means of macroeconomic management was mainly to implement proper fiscal policy and monetary policy. Generally speaking, when macroscopic economy became overheated, namely general demand was larger than general supply, it was appropriate to implement tight macroeconomic policies and to tighten fiscal budget and credit. On the contrary, when macroscopic economy became overcooled, namely general supply was larger than general demand, it was appropriate to implement expansionary macroscopic policy and to let fiscal budget operate on deficit and allow credit expansion. In general, people should implement different fiscal policies and monetary policies on the basis of the changes in macroeconomic situation and form good matching between the two. Under special circumstances, for example, the situation in China in 1985, the way to regulate and control was to adopt the policy of “Three Tightens” of tightening fiscal budget, currency and revenue because the country was confronted with the danger of serious inflation.

Third, market coordination mechanism under macroscopic control was favorable to optimal resource allocation. It was the most efficient system and it could become an important reference for China to select mid- and long-term reform goals. It was consistent with the market-oriented reform in China after 1979. Therefore, people had to implement a fundamental reform on the planned economic system main characterized by mandatory plans.

Fourth, in order to make the government’s indirect management of macroscopic economy effective, people needed to deepen the reform of state-owned enterprises and develop non-public ownership economy so that each enterprise truly became an independent entity. Namely, each of them became an entity of interest that could make sensitive response to market signals and, in particular, signals like interest rate, exchange rate and price. Therefore, state-owned enterprises needed to change their status under “soft budget restriction”. They should not set one eye on the market and the other on the government.

²China Society of Economic Reform (1986), p. 59.

Fifth, people needed to establish effective macroeconomic management system and also establish and improve market system. In particular, they should establish and improve financial market and labor market. They should positively and resolutely reform price formation mechanism and price system. They should establish and complete economic information and economic supervision system. They should improve income distribution policy and prevent the overexpansion of consumption demand, and so on.

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Chapter 14

The Formulation of the Compendium on Mid-Term Reform Program by Eight Units Organized by the State Commission for Restructuring the Economic System in 1987



Zhouyuan Zhang

From October 1987 to June 1988, the research teams of the Chinese Academy of Social Sciences, the Peking University, the Party School of the CPC Central Committee, the Renmin University of China, the Institute of Development of the Rural Development Research Center of the State Council, and the State Development Planning Commission, Wu Jinglian's Research Team, and the Shanghai Research Team respectively submitted their reports on the "Compendium on China's Mid-Term Reform Program (1988–1995)" under the organization of the State Commission for Restructuring the Economic System. The period represented a key period in which China's economic system reform shifted from old systems and mechanisms to new ones. The State Commission for Restructuring the Economic System entrusted over a hundred scholars in competent economic departments, scientific research organizations, colleges and universities, and some municipality directly under the central government to provide specific thoughts, conceptions and program compendiums on how to carry out economic reform in five to eight years in the future. The successful practice of China's economic reform indicated that many views, thoughts and conceptions proposed in the reports on the program compendium were realistically well-targeted, foresighted and innovative and they played a good role in promoting economic reform. Therefore, this initiative was a successful exploration in concentrating the wisdom of various parties to provide proposals and suggestions about China's reform. The reports of the eight research teams above together with the report of the Department of Comprehensive Planning of the State Commission for Restructuring the Economic System in summarization of those reports were compiled into a book entitled *General Thinking on China's Reform*, published by the Shenyang

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Press in July 1988 with 50,000 copies printed. Because of its important theoretical innovation and practical value on China's economic reform, the book was honored the Sun Yefang Award of Economic Science.

1 The Successful Attempt in Encouraging Exploration and Concentrating Wisdom

After the reform and opening up started in 1979, the Chinese circle of economics, guided by the ideological line of the CPC of liberating the thought, seeking truth from facts, and uniting as one and looking to the future, constantly broke through various constraints in thought, acted very positively and created a situation of one hundred flowers blooming and one hundred schools of thought contending. The formulation of the compendium on China's mid-term reform program also fully exemplified this situation at the time.

The most noticeable characteristic of this initiative in which eight research teams respectively proposed their reports on the compendium of the mid-term reform program was that these teams showed the courage and bravery to explore and innovate and submitted different specific reform thoughts and plans. People had the consensus that China's economic system reform should adhere to the direction of marketization or market-orientedness. But in the aspects of how people should promote market-oriented reform specifically, what the main line of mid-term reform was, how should people properly handle the relationships between reform, development and stability, and whether the change of track should be implemented quickly within a short period or gradually within a longer period, these teams proposed their own views and they argued with each other, not easily conceding their positions. This ended up in a truly gratifying situation in which it seemed that one hundred schools of thought contended with each other.

The aspect that caused the biggest debate was about what the main line of mid-term reform was. Three different types of views were proposed as follows:

The first type was represented by the research teams of the Peking University and the Party School of the CPC Central Committee. They advocated the theory of taking enterprise reform or ownership system reform as central task. Namely they held that people take enterprise reform as the main line in mid-term reform and positively push forward building shareholding system and establishing modern enterprise system.

The second type of views was represented by the Wu Jinglian's research team. They advocated that people take price reform as the main line and work hard to realize the change of track in economic operation mechanism so as to provide a good market environment for enterprise reform and other reforms and innovations.

The third type of view was represented by the research team of the Chinese Academy of Social Sciences. They advocated the theory of two main lines, namely people push forward reform in the two main lines of enterprise reform and price reform and of ownership system reform and economic operation mechanism reform.

They believed that these two aspects of reform were like the two sides of one coin. Neither should be left behind. People should coordinate and match them in action.

Centering round the three different types of views on the main line of reform, the research teams made large amounts of systematic demonstration about their own positions. It should be said that all these demonstrations were sound and reasonable and each of them could stand as a self-consistent theory.

In addition, these research teams exchanged their own positions and views at a hotel in Huairou, a suburban country of Beijing, in the winter of 1987. These people also carried out heated discussion and friendly debate on various views. A large group of economists sat together to make debate on the issues about China's economic reform and no one would concede easily. This scene always feels very interesting when anyone who has attended the meeting recalls it today. As one of the persons-in-charge of the research team of the Chinese Academy of Social Sciences at the time, the author also positively took part in discussion and debate at the meeting.

The debate on main line could be traced back to one year or two years before this event. At the end of 1986 and in the beginning of 1987, there were already the contention of different views in the arena of theoretical discussion on whether there was the difference between the primary or secondary statuses or between the superior or inferior statuses with respect to enterprise reform and price reform. On November 3, 1986, Professor Li Yining published the article "The Choice between the Two Thoughts of First Reforming Price or Ownership System" in the *World Economic Herald*. He advocated that people should first carry out ownership system reform and then price reform and believed that there were ten major problems that should be addressed in ownership system reform in comparison with price reform. Some economist held different views from those of Prof. Li Yining's and wrote an article entitled "Price Reform Was Still the Key to Economic System Reform" and published in *Materials about Cost and Price*, Issue 1, 1987 to argue with him. Over twenty years had passed after the debate on the main line of reform. When looked back now, the contention then shows meaning far beyond the result about who was correct. The most important thing was that it encouraged economists to positively participate in China's economic reform and devoted their own wisdom.

Another hotspot issue in the discussion at the time was about the issue of the environment of economic reform, namely the issue of whether reform needed a relatively stable economic environment. In early and mid-1980s, there was a relatively intense controversy in Chinese circle of economics on whether people could use inflation policy to support rapid economic growth. Some economists advocated or tended to use inflation policy to support rapid economic growth so as to make the "cake" bigger as quickly as possible. They preached the theory that inflation was harmless and also beneficial and also believed that China's economic reform could only be pushed forward under the condition of inflation. Other economists opposed that people use inflation policy to support rapid economic growth and believed that inflation was unfavorable not only to the long-term stable development of economy but also to the successful advancement of reform. The research team of the Chinese Academy of Social Sciences supported the latter and proposed the thought of "making progress while maintaining stability" in reform and development. They advocated that people

should take stabilizing economy and controlling inflation as the main task so as to create relatively generous environment for reform in the first three years from 1988 to 1990 and make larger steps in reform in the five years from 1991 to 1995 after that. In general, people gradually achieved relatively consistent understandings in the contention about this issue only after the efforts in price reform breakthrough were forced to stop in 1988.

How much time did it need to establish the leading status of new economic system? There was disagreement in this respect in the programs proposed by different research teams. The most optimistic opinion about the period suggested four years. Namely, people first made preparation in one year through “getting started while maintaining stability” and then implemented the final move in the following three years. In this period, people should basically achieve retracking through the reform in two aspects of sorting out and streamlining economic parameters and establishing organizational institutions and systems that conformed to the development of commodity economy in China. Most plans suggested that people should work hard to establish the leading status of new economic system within eight years or longer. When viewed from the present, many economists might have underestimated the complexity and arduousness of retracking in reform at the time. Their conception about the time needed for realizing the basic retracking of systems and mechanisms were shorter. Nonetheless, people should still fully recognize the enthusiasm of the economists about reform and their eagerness and expectation about retracking.

2 Remarkable Features in Theoretical Innovations About Reform and Practical Policy Suggestions

In the reports on the compendium on mid-term reform program (1988–1995) formulated by the eight research teams, there were many theoretical innovations about reform and practical policy suggestions. And many remarkable points can be found in them even when people read them nowadays. This fully exhibited the deep accomplishments of Chinese economists in economics and their superior reform stratagems.

First, they accurately grasped the basic framework of new economic system. Just as the Department of Comprehensive Planning of the State Commission for Restructuring the Economic System pointed out when summarizing the reports of these eight research teams, the relatively consistent view in these reports was that the goal of mid-term reform should be to establish the leading status of the new system of socialist commodity economy through the shift of new and old systems. The basic framework of new economic system was that “the government regulates and controls the market and the market guides enterprises”. It included interconnected contents in the transformation in three aspects, namely “the marketization of economic operation, the corporatization of the form of enterprises, and the indirect implementation of

macroscopic regulation and control". It sees now that the summarization of the transformation in these three aspects was rather original. Even today when it has already been established that the goal of economic system reform is to establish socialist market economic system, the transformation in these three aspects still seems to be a relatively accurate summarization to the framework of this new system.

Second, they specifically proposed that the central task of enterprise reform was to create and build modern enterprise system. The research team of the Party School of CPC Central Committee proposed in the beginning of their report that "More than nine years of practice has proved repeatedly that the foundation of productivity exists in enterprises and the foundation of economic system reform also exists in enterprises. Whether people can truly enliven enterprises and make them commodity producers in the real sense concerns the general situation and fate of reform. From 'streamlining administration and delegating power to the lower levels', 'reducing tax and conceding profits' and two-step reform of 'replacing profit submission with tax payment' to generally implementing contracted managerial responsibility system, we have already done much work and achieved noticeable results. Now, the development of the situation requires that our reform goes further up a level: from improving enterprise operation mechanism to comprehensively creating and building modern enterprise system." The research team of the Peking University proposed something similar to the above, "Generally speaking, the priority of enterprise system reform shall gradually shift from contracting system to shareholding system, or from the reform of operation mechanism and property relations at lower levels to that at higher levels, in the eight years from 1988 to 1995." "The result of sorting out and arranging property relations is the corporatization of the form of enterprises." As it is known to all, it is shown in the official documents of China's central authorities that it was resolved at the Third Plenary Session of the Fourteenth CPC Central Committee in 1993 that the direction of enterprise reform was to establish modern enterprises. But more than five years before that when people formulated the compendium on mid-term reform program, some reports specifically held that the central task of enterprise reform was to build modern enterprise system. This shows the foresightedness of the reports.

Third, they specifically proposed establishing market economic system with macroscopic management. Wu Jinglian's research team stated in their report that "the development of the world's economy does not allow us to repeat the chaos in the early period of primitive market economy when we build planned commodity economic system, namely the market economic system with macroscopic management. It does not allow us to follow the method of making small tests and experiments in exploration for a long time. The formulation and selection of our reform strategy and methodology must be made at the height of modernization. It must be fit for China's national situation and based on the general principles and common experience in developing commodity economy and practicing marketization. People need to spend a not very long period of time to build a market order of socialist economy guided with development strategy and industrial policy at a higher starting point."

It was a piece of major progress in reform theory and strategy and had remarkable foresightedness to interpret the common understanding on planned commodity economic system as an equivalent to building market economic system with macroscopic management. In the discussion, members in Wu Jinglian's Research Team specifically proposed the theory of "taking market-price reform as central task". They believed that the key to market-oriented reform laid in price reform. When mandatory plans were cancelled, the entire economy would fall into chaos inevitably if people did not timely open up prices to form market at the same time. To open up prices and thus build competitive market system was a basic condition to bring the general function of the new system into play. Therefore, market-price reform is the center of economic system reform. Mid-term reform plan had to take implementing price reform and building market as the basic guideline. Now it seems that the actual situation in China's reform has basically followed the thinking of this research team except that the duration has been expanded much longer. From the end of 1980s to 1990s, China's price reform has always led the entire economic reform and thus promoted the realization of the basic retracking of economic operation mechanism by the end of the 20th century. Opening up prices and forming market quickly activated national economy and the important transformation from seller's market to buyer's market started to be realized. But during the same period, the reform in state-owned enterprises was confronted with many difficulties. People were still working hard to extricate large- and medium-sized state-owned industrial enterprises from difficult position from 1998 to 2000. The reform in state-owned enterprises was gradually accelerated only after the start of the new century. And substantial progress was then gradually achieved in building modern enterprise system and modern corporate system.

Fourth, they proposed that what the government should do should be determined by what market could not do. The reports of several research teams proposed the indirect implementation of macroeconomic regulation and control. For this purpose, people needed to practically transform the functions of the government and thoroughly change the economic management system in which the government directly intervened the production and operation activities of the enterprises so that all the economic functions of the government were established centering round the market and realized through the market. That is to say, what the government did was determined by what market could not do. And how the government did it should be realized through the medium of the market. Specifically speaking, it meant that the state shifted from employing administrative means and targets of physical goods to implement direct planned control over enterprises to mainly employing economic means to carry out indirect guidance to the behavior of enterprises through the market. The main task in state plans was changed from allocating money and goods and carrying out the management of physical goods to formulating and implementing national economic development strategy, industrial policy, and fiscal, monetary and income policies to retain the proper proportions of accumulation and consumption and the balance of the aggregate of macroscopic economy and also to promote the sustained and stable development of national economy. Now it seems that the views

above conformed to the reality of China's reform in general and they were of great instructive meaning and practical value.

Fifth, people proposed the thought of "promoting progress while maintaining stability" in reform and development. This was the contribution of the research team of the Chinese Academy of Social Sciences and it was represented the view of a group of economists of the Chinese Academy of Social Sciences, including Liu Guoguang, Zhang Zhuoyuan, Dai Yuanchen, Shen Liren and Chen Dongqi. Later, these people were categorized as representatives of the "school of steady reform". Promoting progress while maintaining stability meant that people should guarantee reform with economy-stabilizing measures and, at the same time, stabilize economy with the method of deepening reform. In order to establish the reform thinking of promoting progress while maintaining stability, people needed to pay further attention to the issue of inflation. The kernel of stabilizing economy was to stabilize price. The guideline of stabilizing price should never be discarded. In order to stabilize economy, people had to tighten currency issue and control inflation when economic became overheated. In order to achieve this goal, people had to stabilize the growth rate of economy, control the totals of investment demand and consumption demand, and eliminate abnormal cyclic fluctuations. Therefore, because people needed to eliminate or dilute the uncertainties in economy in the earlier period on the basis of adjusting and calibrating the guiding thoughts of macroscopic policy, the phasal strategy of "promoting progress while maintaining stability and taking stability as priority" would be adopted in the reform in the first three years. Then in the following five years, the priority of phasal strategy might be adjusted from "stability" to "progress" and reform could proceed with larger and faster steps. The practice in the reform and opening up in thirty years proved that the thinking of "promoting progress while maintaining stability" was advisable. And it was gradually adopted as an important guideline of the CPC and the government in directing economic development and reform. Perhaps this was a relatively important contribution of the economists of the Chinese Academy of Social Sciences to China's reform and opening up and to its construction of socialist modernization.

3 Great Attention from State Leadership and Profound Influence

State leadership paid high attention to the formulation of the compendium on mid-term reform program entrusted to eight research teams. When the research teams exchanged views at Huairou, Li Tieying, member of the Political Bureau of the CPC Central Committee and director of the State Commission for Restructuring the Economic System, personally presided over and participated in the discussion. An Zhiwen and other leaders of the commission attended the discussion in the

whole course to hear the introductions of the research teams on their own report and exchange views with them. There were consensus on the general understanding of reform as all the people adhered to market-oriented reform and thus the common ground for discussion was established. Disagreement mainly existed in different estimations on reform strategy and speed of progress. So the debate was about minor differences under general consensus. The argumentation was heated but the atmosphere was friendly.

On June 1, 1988, Comrade Li Peng, the then premier of the State Council, met members of the research teams and heard the reports of the eight research teams. Each team was given five minutes to make their report and explain their main views. Then Premier Li Peng discussed with them the issue on mid-term reform program. This fully indicated that the CPC Central Committee and the State Council attached great importance to the formulation of the compendium on mid-term reform program.

When the State Commission for Restructuring the Economic System entrusted eight research teams to formulate the compendium on China's mid-term reform program, it actually organized and mobilized the extensive community of workers in economic theories to positively study the experience and theory of Chinese economic reform. Therefore, such initiative powerfully promoted the extensive community of workers in economic theories to further liberate their thought, adhere to reform and opening up, and provided intellectual support to deepening reform and opening up. It played a good role in promoting China's reform and opening up and its undertakings in the construction of socialist modernization.

The practice in the formulation of mid-term reform program also indicated that it was favorable to improve the scientific nature of the decision making about reform that experts and scholars from various areas formulated a compendium of reform program that represented interests beyond departments and organizations. This could effectively prevent the interference of the interests of departments, regions and certain interest groups to the practice in reform. Thus it was also favorable to help the reform to win the support and participation of the extensive community of the people and the mass and to share the fruits of reform with all the people. With over thirty years of hard work, China has achieved substantial progress in economic system reform. Socialist market economic system has been initially established and gradually improved. In the process of improving new system, there were also some tasks to tackle key difficulties which would affect the interests of certain groups of vested interests. Therefore, these tasks involved large difficulty and resistance. Such tasks required that the CPC and the government push them forward powerfully, overcome the interference of the groups of vested interests, and constantly improve the scientific nature of the decision making about reform and strengthen the coordination in reform measures. In these aspects, it was of important practical meaning to borrow in a good way the experience of organizing many units to formulate the compendium on reform program over twenty years ago.

Part IV
The Period of 1992–2011

Chapter 15

The Establishment of the Theory of Socialist Market Economy in 1992 and Its Rise as the Theoretical Pillar for China to Deepen Reform and Opening Up



Zhouyuan Zhang

How should people determine the target model of China's reform after the reform and opening up started in 1979? This was a question that people in various areas cared about and explored all the time. It was also a key area in the study of the Chinese circle of economics. After the political turmoil at the end of spring and in the beginning of summer of 1989, some people negated the market-oriented reform from 1979 and required to turn around and go back to the old way of planning-oriented system. But very few people responded to such an opinion. The majority of Chinese economists believed that people should adhere to implementing market-oriented reform, further bring into play the role of the market in allocating resources, and promote rapid economic growth. Yet some economists still had doubts and concerns about whether people could run socialist market economy in China and whether the theory on socialist market economy would work. Under such a circumstance, the fourteenth CPC National Congress in 1992 determined that socialist market economic system should be the target model of China's reform and thus established the theory of socialist market economy. Such decision was naturally of immeasurable meaning to the deepening and development of China's reform. It drove China's reform and opening into a new stage of comprehensive deepening.

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1 The Establishment of the Theory of Socialist Market Economy in 1992

After establishing the socialist commodity economy in 1984, Chinese economists did not stop there but continued to explore. In the second half of 1980s, they further proposed that people should specifically determine that China's economic reform was market-oriented reform or marketization reform. Its content included the following: People should permit the existence and development of non-public ownership economy. Enterprises should become main entities in market competition. The goal of price reform was to establish market price system and establish and develop a market system that included commodity market and factor market. Production factors should participate in distribution. Macroeconomic management should transform from implementing direct management to mainly implementing indirect management. China should implement all-round opening up to the outside world and participate in international market competition and so on. In 1986, some articles believed that the main line in the target model of macroeconomic management was that the state controlled the market, namely the state regulated supply and demand mainly through economic means and market parameters and thus realized the "power of leadership" over the market, and market guided enterprises. Or "the state regulates and controls the market and the market guides enterprises".¹ In the early 1990s, Wu Jinglian et al. specifically proposed that the goal of reform was to establish socialist market economic system and made relatively detailed demonstration on the framework of a new system.²

However, there were some economists who did not approve that China should implement socialist market economy. In 1990 and 1991, some articles were published in newspapers and magazines with an attempt to negate the theory of socialist market economy. This showed that disagreement in understanding did exist.

The political wisdom of the leaders of the CPC and the state and their spirit of courageously making theoretical innovations played a decisive role in establishing the theory of socialist market economy and making it a mainstream view. In 1979, Deng Xiaoping, the chief designer of China's reform and opening up, pointed out that market economy could be implemented in socialism. In the spring of 1992, Deng Xiaoping further expounded his view on the question of the relationship between planning and market in his South Tour Speech. He said, "Whether there is more planning or market is not the essential distinction between socialism and capitalism. Planned economy is not equal to socialist economy. There is planning in capitalism. Market economy is not equal to capitalism. There is market in socialism. Planning and market are both economic means." In September the same year, the report of the Fourteenth CPC National Congress determined under the guidance of Deng Xiaoping's South Tour Speech that the objective model of China's economic system reform was to establish a socialist market economic system so that market could play

¹ See Li (1986).

² Wu and Liu (1991).

a fundamental role in resources allocation. This symbolized that the understanding on the theory of economic reform reached a brand-new stage, namely the stage in which people recognized the theory of socialist market economy and took it as the theoretical support in deepening reform and opening up.

As China's economic reform deepened, the theory of socialist market economy also deepened. In 1993, the Third Plenary Session of the Fourteenth CPC Central Committee adopted the *Decision on Several Issues in Building Socialist Market Economic System* and determined the basic framework of the socialist market economic system. This framework included the following points: People should adhere to the policy of taking public ownership system as the main part and achieving the joint development of multiple economic sectors, further transform the operation mechanism of state-owned enterprises, and establish modern enterprise system that adapted to the requirements of market economy, characterized by clearly-defined ownership title, specifically-determined rights and responsibilities, separation of administration and enterprise functions, and scientific management. People should establish a nationally unified open market system, realize the close combination of urban and rural markets, set up the interconnection between domestic and international markets, and promote the optimal allocation of resources. People should transform the government's function in management economy, establish a complete macroscopic regulation and control system mainly in reliance to indirect means, and guarantee the healthy operation of national economy. People should establish an income distribution system that took distribution according to performance as the main part and prioritized efficiency with due consideration to fairness. They should encourage some regions and some groups of people to become rich first and take the road of common prosperity. People should establish multileveled social insurance system and provide social insurance to urban and rural residents that were adapted to China's national situation so as to promote economic development and social stability. People had to establish corresponding legal system centring these main links. The above was the famous five major pillars to socialist market economic system. The Fifteenth CPC National Congress in 1997 proposed the task of strategically adjusting the overall arrangement of national economy and required that people should run state-owned economy well in general. And it was specifically stated that non-public ownership economy, such as individual economy and private economy, were organic components of socialist market economy. The Sixteenth CPC National Congress in 2002 proposed in its report the tasks of finishing building a complete socialist market economy by 2020 and of building the state-owned property management system, in which central and local governments respectively performed the functions and duties of investor on behalf of the state and enjoyed the rights and interests of owner so as to achieve the unification of right, obligation and responsibility and the combination of the management of property, personnel and matters. The Third Plenary Session of the Sixteenth CPC Central Committee in 2003 pointed out the task of improving socialist market economic system and proposed the scientific outlook of development characterized by people-orientedness, comprehensive coordination and sustainability. And it also proposed the ideas that shareholding system

was the main form for realizing public ownership system and that modern property right system should be established in China. The Seventeenth CPC National Congress in 2007 proposed the tasks of pushing forward scientific development, promoting social harmony, and transforming the mode of economic development. It also proposed that people should speed up building state-owned capital operation budget system, improve the price formation mechanism for production factors and resources that reflected supply and demand relation on the market, resources scarcity and environmental damage costs, build social insurance system with full coverage, and deepen the reforms in government, fiscal matters and taxation, finance, and the countryside.

During the same period, economists made heated discussion on the issues in the theory of socialist market economy and published a large amounts of papers and treatises so that the theory of socialist market economy gradually won public support. The Chinese circle of economics carried out in-depth research on the theories of modern enterprise system, corporate governance, foreign investment utilization, capital market, market price, public finance, financial innovation, social insurance, relationship between efficiency and fairness, market economy under the rule of law, combination between public ownership system and market economy, income distribution, economic transition, open economic, transforming the mode of economic growth and development, Renminbi's internationalization, Renminbi exchange rate formation mechanism, international financial market and crisis, the "Three issues of agriculture, the countryside and farmers" issue, and so on. Among them, some research results are foresighted.

When reviewing the study and exploration of the Chinese circle of economics on the relationship between planning and market and economic system reform since the reform and opening up, people might get the following several understandings:

First, the question on the relationship between planning and market is the kernel question in the theory of socialist economy. The radical defect in traditional theory of socialist economy lies in that advocating planning or market, either of which is in fact a means of economic regulation, is said to be the basic sign that draws the line between socialist and capitalist economic systems and that planning is taken as socialism while market as capitalism. Such understanding completely disagrees with the practices of economic development in various countries in the world. After the World War II, many developed capitalist countries also formulated various kinds of economic development plans to regulate the operation of macroscopic economy. Because of derogating and expelling the role of market, the countries that practiced traditional socialist planned economic system stifled the vitality and vigor of their economy so that they lost in the peaceful economic race. Reality makes more and more economists become aware that, only by resorting to the market, can a socialist country revive its economic activities completely fettered in mandatory plans. Only by bringing into play the fundamental role of the market in resources allocation can it improve its economic efficiency. Of course, market is not omnipotent. It is necessary to have a "visible hand", such as the macroscopic regulation of the government, to correct the defects of the market to ensure the healthy operation of the economy.

Second, the scientific nature of the socialist political economics relies to a large extent on whether people can scientifically expound the relationship between socialism and commodity economy and market economy so that socialism and market economy can adapt to and combine with each other. Thus, the construction of socialist economy with Chinese characteristics is to develop socialist market economy. Today, scientific and technological progress is picking up speed in the world and the trend of economic globalization is unstoppable. Only through rapidly developing socialist market economy can the Chinese people rejuvenate the nation and realize industrialization, urbanization and modernization. China can effectively participate in international market competition and the Chinese nation becomes a member of the world family of nations. Then people can prove the establishment and maturity of the theory of socialist market economy with China's brilliant economic achievement and construct the great structure of socialist political economics.

Third, transition economics or transitional economics, as an important component of socialist political economics, takes discussing the transitional process from planning dominant economic system to socialist market economic system and its principles as its main content. China is a large country with one and a half billion population. Up to the present, only the experiences and regularities of China's economic system transition have the most typical meaning. Revealing the regularities of China's economic system transition will add new chapters to modern economic science and in turn enrich and develop modern economic science.

Fourth, the theory of socialist market economy is a brand new theoretical system. This theory needs the practice in the development of socialist market economy to provide material and nutrition for it. It also needs economists to make arduous exploration and theoretical summarization. It needs these scholars to display their courage of upholding a theory and their spirit to surmount the peaks in science. The process of understanding the truth is complex and full of twists and turns. Sometimes, truth is in the hands of the few. There needs to be a process for the truth to be understood by most people. To truly implement the "Double Hundreds" policy of letting a hundred flowers blossom and a hundred schools of thought contend in academic research in China is the heartfelt expectation of Chinese economists. And this is also the important guarantee to prevent the tragedies of killing the truth and suppressing the people who stood up for the truth from recurring.

2 The Comprehensive Development of China's Reform in Big Steps After the Establishment of the Theory of Socialist Market Economy

First, the reform of state-owned enterprises shifted from delegating power and conceding profit in the past to system innovation. The enterprises took building modern enterprises system as direction and worked hard to adapt to the development of market economy. With the strategic adjustment to the distribution and structure of state-owned economy and the reform of corporate system and shareholding

system in large- and medium-sized state-owned enterprises, state-owned economy was brought out of difficulty. Many large- and medium-sized state-owned enterprises transformed their operation mechanism and improved their market competitiveness and dynamism. The controlling power of state-owned economy was enhanced. In 1997, there were 254,000 state-owned enterprises nationwide and the figure was reduced to 115,000 in 2007, showing a decrease of over a half. But the aggregate of state-owned economy kept expanding and its comprehensive strength also improved constantly. In 1997, the total assets of state-owned enterprises nationwide amounted to 13.9 trillion RMB in 1997 and the figure rose to 53.5 trillion RMB in 2009. In 1998, over 2/3 of state-owned enterprises suffered loss. The total profits of the state-owned enterprises throughout the country were only 21.37 billion RMB. In 2010, the total profits of state-owned enterprises in China amounted to 1987.06 billion RMB, indicating that large increase was achieved. By the end of 2010, all 122 central enterprises in China accrued 24.3 trillion RMB total assets, 9.5 trillion RMB net assets, 849 billion RMB net profits, and 1.4 trillion RMB tax deliveries. At present, the coverage of system transformation reached over 80% among local state-owned enterprises. The coverage of the transformation into corporate system or shareholding system rose from 30.4% in 2002 to 64.2% in 2007 among central enterprises and their subordinate enterprises. Among over 1500 listed companies in China's A-share market, over 1100 had state-owned capital participation. There were also 78 listed companies controlled by central enterprises that were listed on overseas capital market. All these indicated that substantial progress was achieved in China's state-owned enterprise reform.

Second, important reform was implemented in fiscal system. In 1994, the reform of tax distribution system was implemented to adapt to the development of market economy. Namely, tax distribution system was implemented between the two levels of central and local fiscal organs. This changed the original measure of implementing predetermined fixed payment from local fiscal organs. In tax distribution system, value added tax was the most important tax type. Tax distribution was implemented with it between central and local levels. The central authorities would have 75% while local authorities 25%. Consumption tax was completely submitted to central authorities. The part of increase in value-added tax and consumption tax in comparison with the figures last year would be refunded to local authorities at a ratio of 1:0.3. On the one hand, such reform promoted the rapid increase of fiscal revenue. In 1993, national fiscal revenue reached 434.895 billion RMB. Then in 2010, national fiscal revenue leaped to 8.3 trillion RMB, showing an increase of 18 times. On the other hand, the proportion of central fiscal revenue increased quickly in total revenue. In 1993, the proportion of central fiscal revenue to national fiscal revenue was 22%. Then in 2007, this proportion rose to 51.2%. Upon the beginning of the 21st century, important transformation was made in fiscal system once again. Namely, there was the transformation from a fiscal system that prioritized economic construction to one that prioritized public service. It was also promised that people would gradually realize the equalization of basic public services. This meant that important adjustment would be made to the structure of fiscal expenditure. Namely, people would

raise largely the parts in fiscal expenditure used in public service, for improving people's livelihood and for aiding underdeveloped regions and low-income groups.

Third, China completed its accession to the World Trade Organization (WTO) in November 2001. It indicated that China's reform and opening up entered a brand-new stage. This represented an important move of China to conform to the trend of economic globalization. It was of milestone meaning. Making this decision was the most brilliant historical feat of the third generation leadership of the People's Republic of China. In the negotiations on the accession to the WTO, many people were greatly worried that the accession might affect China's national economic safety and many industries in China, including finance, commerce, agriculture and information, would suffer huge impact so that it might result in more problems than benefits or at least so in short term. However, the experience after the accession to the WTO in many years indicated that the accession brought more benefits than problems to China. Many things worried about in the past did not emerge at all. China benefited from economic globalization. The accession to the WTO raised China's economic rate of return. After its accession to the WTO, the growth rates of China's economic aggregate, foreign trade, foreign investment utilization and foreign exchange reserves all picked up. In 2000, China's total goods import and export amounted to USD 474.3 billion. Then in 2010, the figure grew to USD 2972.8 billion, showing an increase of over five times. China's average annual contribution to the world's economy exceeded 15%. Moreover, opening-up promoted reform. The accession to the WTO resulted in the abolition and modification of a large group of laws, regulations, rules and policies that contradicted with general principles of market economy. Many industries and enterprises made efforts to improve independent innovation ability and enhance their competitiveness in the market. Many enterprises "went to the outside world" to fully take advantage of two markets and two kinds of resources to achieve growth and prosperity. By 2010, Chinese enterprises made direct foreign investment amounting to USD 220 billion accumulatively. The operating amount of foreign project contracting and labor service cooperation reached USD 335.2 billion.

Fourth, individual, private and other public ownership economies saw great development. After the reform and opening up started, individual and private economies were first allowed to exist and develop. After 1992, individual, private and other non-public ownership economies started to develop in large scale. The number of entities in private economy showed increases over 50% in 1993, 1994 and 1995. In 1997, the Fifteenth CPC National Congress further recognized that individual, private and non-public ownership economy were important components to socialist market economy. By the end of September 2010, the number of private enterprises reached 8,188,000, their registered capital amounting to RMB 17.73 trillion yuan. 91,839,000 employees worked in these enterprises. There were also 34,065,000 individual industrial and commercial enterprises which had 1.27 trillion RMB funds and 69.83 million employees (see *People's Daily*, January 1, 2011). Over many years, individual, private and other non-public ownership economies had been important economic growth points in China, the main channel to provide new jobs, and the dynamic force to satisfy the diverse and constantly growing needs of the people in China in their physical and cultural life. The great development of individual,

private and other non-public ownership economy resulted in a situation of competition among diverse market entities in China and also vigorously pushed forward the deepening and development of the reform for public ownership enterprises to adapt themselves to market economy.

Fifth, people positively pushed forward the reform in social fields. Upon the beginning of the new century, the reform in social fields started quickly and social construction accelerated. Tuition and fees were all cancelled in the stage of compulsory education, namely the stage of elementary and junior middle schools. Employment issue was prioritized. People strengthened vocational training and employment service and promoted building harmonious labor relations. Subsistence allowance system was expanded from the city to the countryside. People were also positively exploring the construction of urban and rural resident pension security system. Quick progress was achieved in building urban resident basic medical insurance system and new-type rural cooperative medical care system. At present, 1.267 billion Chinese citizens have benefited from these systems. People also worked hard in building low-rent housing and other affordable housing. During the Twelfth Five Year Plan, 36 million housing units were to be built. The coverage of urban affordable housing nationwide would gradually reach around 20%, which would resolve the difficulty of urban low-income household in housing, and so on.

Sixth, people stepped up the reform of administrative management system and transformed the functions of the government. In order to adapt to the development of socialist market economy, people positively pushed forward government reform and government function transformation. The government was transformed from an all-round government and economic-construction-type government to public-service-type government. People implemented the separation of administration from enterprise management, the separation of administration from state-owned property management, the separation of administrative units from institution units, and the separation of government organs from market intermediary organizations. The government practically implemented the functions of economic regulation, market supervision, social management and public service. People promoted the reform of the examination and approval system, reduced matters subject to examination and approval, and implemented examination and approval in accordance with the law. The government stopped directly intervening in the production and operation activities of the enterprises.

During this period, people also completed the entire-company listing of large state-owned commercial banks, implemented the equity division reform on capital market, cancelled agricultural tax, carried out collective forest right system reform, and unified the enterprise income tax for domestically- and foreign-funded enterprises. They also pushed forward marketized price reform for some resource products and implemented spin-off projects on the enterprises in some monopolized industries and introduced competition mechanisms. They also implemented the reform of cultural administrative system.

As many reforms mentioned above had been pushed forward rapidly and smoothly in the 1990s, China initially established socialist market economic system by 2000

and market started to play a fundamental role in resource allocation. Upon the beginning of the new century, new systems were being improved in accordance with the requirements in developing socialist market economy and centering round the economic transformation and the transformation of development mode, both carried out for realizing scientific development. Thus the entire national economy would become full of vigor, greatly efficient and more opened-up. It would continue to provide powerful dynamism and system guarantee for developing socialism with Chinese characteristics. People would endeavor to finish building a complete socialist market economic system by 2020. China would become one of the high income countries, namely that its per capita GDP exceeded USD 12,000, converted into and calculated with the US dollar in 2009. By the time, the theory of socialist market economy would have the support of new system and rapid economic development and it would be truly established.

3 Organic Combination of Socialism and Market Economy: A Theoretical Innovation with Epoch-Making Significance

Chinese economists wrote many treatises and articles after 1992 and systematically and profoundly formulated the important meaning of establishing the theory of socialist market economy. They pointed out that the basis for establishing the theory of socialist market economy was that socialism and market economy could combine with each other and they were not completely contradictory as considered in traditional theory. People needed not only to demonstrate in theory that these two could combine but also to repeatedly and extensively prove in practice that these two could combine. The market economies in the past were combined with capitalism or private ownership system. The most important characteristic of socialist market economy was that market economy was combined with public ownership system. Therefore, it was unprecedented and brilliant pioneering undertaking that China developed market economy under the condition of socialism. It was also a brand-new task. The theory of socialist market economy summarized on the basis of successful practice was an important theoretical innovation about scientific socialism made by members of the Communist Party of China and Chinese Marxist economists. It was also an epoch-making contribution to economic science.

The key difficulty in the theory of socialist market economy laid in organically combining public ownership system with market economy. China already established the basic economic system that took public ownership system as main part and achieved the joint development of multiple ownership economies. In this basic economic system, there was no problem to combine individual, private and other non-public ownership systems with market economy. The question was whether public ownership system and, particularly, state ownership system could not combine with market economy and how they could combine with market economy. This was a

question not only in theory but also in practice. Under traditional planned economic system, it was hard for public ownership system and state ownership system to combine with market economy. After the beginning of reform and opening, people in various areas were all trying hard to find the form of realization of public ownership system and state ownership system that could combine with market economy. After many years of exploration and practice, people finally found that shareholding system could be an effective form of realization of public ownership system, including state ownership system that could combine with market economy. In 1997, it was pointed out in the report of the Fifteenth CPC National Congress that “Shareholding system is a capital organization form of modern enterprises that is favorable to the separation of the rights of ownership and operation and to improving the operation efficiency of enterprise and capital. Capitalism can make use of it; socialism can also make use of it.” In 2003, it was further pointed out at the Third Plenary Session of the Sixteenth CPC Central Committee that people “should adapt to the trend of the constant development of economic marketization and further strengthen the vigor of public ownership economy. They should largely develop mixed ownership economy with the participation of state-owned capital, collective capital and non-public capital. They should realize the diversification of the main parties of investment and make shareholding system the main form of realization of public ownership system.” The practice in the reform of Chinese state-owned enterprises proved that promoting the reform of publicly-owned enterprises, including state-owned enterprises, into corporate system or shareholding system could adapt publicly-owned enterprises to the development of market economy. It could change publicly-owned enterprises into market entity and legal person entity that operated independently and assumed sole responsibility of their profit and loss. And these enterprises could gradually improve their corporate governance structure under the framework of corporate system and shareholding system. Therefore, people could reform publicly-owned enterprises and, in particularly, large- and medium-sized state-owned enterprises into modern companies. Among them, important enterprises could be controlled by share by the state. Some of those could also be solely funded with state-owned capital. Thus, these enterprises could operate in line with modern companies in regular market economy countries. They could not only engage in fair competition with non-public ownership market entities, such as foreign-funded enterprises and private enterprises, but also enter international market and participate in international competition. So it can be seen that people found with shareholding system a form or approach in which China’s public ownership system and, in particular, state ownership system, could combine with market economy.

Socialist market economy was the organic unification of market mechanism and government regulation and control in which market played a fundamental role in resource allocation first while the government implemented macroscopic regulation and control on national economy. The dominance of public ownership system in a socialist country could guarantee that the government’s macroscopic regulation and control could become more powerful and effective so as to promote the steady and healthy operation of socialist market economy.

When people developed market economy under socialist condition, it was required that they took people-orientedness as principle, took realizing common prosperity as the goal, and prevent social polarization. The General Secretary, Hu Jintao pointed out in the report of the Seventeenth CPC National Congress that “people should always take realizing, maintaining and developing in a good way the fundamental interests of the most extensive community of the people as the starting point and endpoint of all the work of the party and the state. They should respect the people’s dominant position, bring into play their pioneering spirit, and guarantee various kinds of interests of them. They should take the road of common prosperity, promote the comprehensive development of the mankind, and succeeded in achieving development for the people, realizing development in reliance to the people, and sharing the fruits of development with the people.” This required that people adhere to and improve the distribution system in which distribution according to performance dominated and various modes of distribution coexisted and that the people throughout China could share the fruits of reform and development. People not only needed to make the cake bigger but also needed to divide and share the cake well. They should pay more attention to generally improving the people’s livelihood and upholding fairness and justice. They should adhere to the principle of the dominance of public ownership system. The state should promote the implementation of fair income distribution policy, the establishment of public financial system, and the equalization of basic public service. They should establish complete social insurance system, prioritize the development of education, and realize fairness in education. These would powerfully promote and guarantee the development along the road of common prosperity. At present, there were many practical issues in this area. The gaps of income were too large between different regions and groups of people. Social fairness was confronted with serious challenges. The CPC and the government were taking various measures to resolve such an issue.

The combination of socialism and market economy represented a process in which socialism, in which public ownership system dominated, and market economy adapted to each other. On the one hand, great efforts needed to be made to adapt public ownership system to market economy. State-owned enterprises and enterprises of other public ownership systems needed to constantly deepening the reform into corporate system and shareholding system. Thus state ownership system and public ownership could combine with market economy through the form of shareholding system. On the other hand, when developing socialist market economy, people needed to focus on adapting to the goal of common prosperity and work hard to prevent social polarization, about which the market economy with private ownership system often brought.³ In this way, people could realize the organic combination of socialism and market economy. With over 30 years of reform and opening up, China has effectively realized such combination of socialism and market economy. But people need to do better in this area. Chinese economists were full of confidence in the successful practice in such combination and hence in the scientific nature of the theory of socialist market economy.

³See Peng et al. (2008), p. 394, Zhang (2008).

4 The Explorations on the Characteristics of Socialist Market Economy and Several Principles About It

Upon the beginning of the 21st century, China's economy achieved rapid development, showed great dynamism, and became increasingly open as the system of socialist market economy was initially established and then gradually perfected. Under such a circumstance, the Chinese circle of economics started to pay attention to and study the characteristics and inherent principles of socialist market economy so as to theoretical basis and intellectual support to the decision making of the CPC and the Chinese government.

Some articles believed that there were mainly the following several aspects to consider when people wanted to grasp well the characteristics and inherent principles of socialist market economy on the basis of the current reality in China:

I. Market Played a Fundamental Role in Resource Allocation and the Law of Value Regulated Social Production and Circulation

The biggest difference between socialist market economy and traditional planned economy laid in that market played completely different roles in resource allocation in them. In the former, it played the role of the main regulator while, in the latter, it played no role at all or only a very small role. According to the language of Marxist economics, the law of value was the main regulator in social production and circulation in socialist market economy. In traditional planned economy, the law of value did not play a regulatory role. It was the mandatory plans of the state that regulated social production and circulation. The practice in China and abroad until the present indicated that it could achieve higher efficiency than allocating resources according to the mandatory plans of the state to carry out the allocation and re-allocation of limited social resources according to market signals and, mainly, price signals. This was because, under the circumstance of socialized mass production, products and services were of a multitude of types and kinds and in a quantity scale of thousands and millions. In addition, the demands of society and people also varied in a complicated way and kept developing. State planning departments could never connect and coordinate social supply and social demand in an organic manner even if they adopted modern computing technology and implemented strict administrative regulation. The signals on social demand, fed by the market through the rise and fall of prices, were much more accurate and timelier than the information from any planning department that gave instruction. Thus, various entities in economic activities could carry out production and operation and provide service on the basis of the demand in the society and also avoid serious waste and loss of resources. In other words, social resources autonomously flew from industries with lower benefits to those with higher benefits under the action of the law of value. The industries with higher benefits were those with stronger demand in the society. And there would be a Darwinian process among different enterprises in the same industry or industrial sector. This would result in more effective use and allocation of social resources.

II. Enterprises Were the Main Entities in Market Economic Activities and People Should Truly Realize the Separation of Administration from Enterprise Management and State-Owned Property Management

Under the circumstance of socialist market economy, an enterprise was no longer an attachment to its competent superior administrative department. It was an independent economic entity which operated independently and assumed sole responsibility to its profit and loss. Market played a fundamental role in resource allocation. This was achieved through one after another enterprise operating as the most important microeconomic entity. An enterprise decided on what and how much commodity to produce or what and how much service to provide on the basis of market signals, or mainly price changes, so as to maximize its profits. It was the activities of one after another enterprise to pursue economic benefits that realized the more effective distribution of social resources into the areas in the society that needed them. This meant that enterprises became the hero in market economic activities and the government was no such hero any more. Therefore, if people chose to implement socialist market economy and let market play a fundamental role in resource allocation, they had to make enterprises independent market entities and interests entities that operated independently, assumed sole responsibility to their profit and loss, and bore risks independently. This was in fact what people proposed in the early time of the reform, namely making enterprises independent commodity producers and operators. It was relatively easier to realize this with non-state-owned enterprises. Nonetheless, there was still much administrative intervention from the government until the present and people needed to make great efforts to overcome such problem. And such change was rather difficult for state-owned enterprises. The experience in the reform and opening up in the recent thirty years indicated that it meant a thorough remolding and transformation for state-owned enterprises to get out of the status as attachments to their original competent departments and become independent market entities. On the one hand, enterprises originally depended on their competent superior departments in everything. They followed their orders when handling matters. They did not care about how good or bad their economic benefits were and had no initiative and spontaneity to improve operation and management. They had no dynamism. Now they needed to transform into independent market entities that operated independently and assume sole responsibility to their profit and loss. They had to work hard to adapt themselves to the market and participate in market competition at their own risk. If they ran well, they could keep developing and growing and their operators and employees could increase their own benefits. Otherwise, they might suffer loss or even go bankrupt. Market mechanism was like a ruthless whip. It urged the enterprises to constantly improve their technology and better management and operation. They needed to keep advancing and never stopped making progress and became sluggish. On the other hand, the government and competent departments originally directly commanded various microeconomic activities and carried out examination and approval on and gave instructions to various economic activities of the enterprises. Enterprises were often managed by multiple superior authorities without clearly-defined functions. When an enterprise did well in production and

operation, various departments rowed with each other to record the honor in their own name. Once anything went wrong, they would try to shuffle the responsibility to others. No one wanted to take the responsibility. The most important thing in pushing forward marketization reform was to transform government functions and realize the separation of administration from enterprise management and state-owned property management. The government would no longer intervene in the production and operation activities of the enterprises. Some departments specialized in managing enterprises were cancelled. The functions of the government in public management and as state-owned assets investor were separated. Because such reform would affect the interests of many administrative management departments and their officials, it often faced many difficulties caused by the obstruction of these departments. These competent departments were used to be in the role of a commander. Once they could not give orders, they would find it hard to adapt to the situation. Therefore, if people really want state-owned enterprises to truly become independent market entities, they had to adhere to the principle of the separation of administration from enterprise management and state-owned property management. The transformation of government functions had to be implemented as a supportive measure. The government would stop intervening microeconomic activities. The government's functions in this area changed into economic regulation, market supervision, social management and public service. Namely, they were mainly turned into serving market entities and creating a good development environment.

III. The State's Macroscopic Regulation and Control Was Mainly Implemented for the Purpose of Realizing the Outlook of Scientific Development and Promoting the Steady and Faster Development of National Economy

In modern market economy, people did not completely give free rein market mechanism in the regulation of economy but put the economy under the macroscopic regulation and control of the state. It was the same in socialist market economy, It was proposed in the report of the Sixteenth CPC National Congress that "people should take promoting economic growth, increase employment, stabilize prices, and guarantee balance of international payment as the main goal in macroscopic regulation and control." This point was the scientific summarization of China's rich experience in macroscopic regulation and control since the reform and opening up. It conformed to the principles of the development of market economy. Many market economy countries in the world took the four aspects above as the main goal of the macroscopic regulation and control of the state. The practices in China and abroad indicated that people needed handle well the relationship between growth and stability under the circumstance of market economy. Namely, they needed to both promote economic growth and retain economic stability. In the long run, it was the most advisable and quickest to achieve economic growth in economic stability. In the opposite, if people pursued quick economic growth one-sidedly, paid no attention to economic stability, and did not try to achieve growth in stability, there could easily be big rises and falls in economy. And such fluctuations would definitely result in the waste and loss of productivity. In the long term, the development and growth of economy would look slower because of many wrong turns. Among the four major targets mentioned in

the above, the first one was to promote economic growth. The rest three were about retaining economic stability. So people could summarize the macroscopic regulation and control of the state as promoting the steady and faster development of national economy. The practices of economic development in China and abroad indicated that market signals were relatively stable and accurate under the condition of stable economy. And the functions of the market in effectively allocating resources could be brought into play in a better way and thus be favorable to promoting economic growth and realizing faster development.

In socialist market economy, people need to establish and earnestly practice the outlook of scientific development and realize comprehensive, coordinated and sustained development if they wanted to handle well macroscopic regulation and control. This was an important summarization of the experience of China in developing socialist market economy. The basic content of the outlook of scientific development was to follow the principle of people-orientedness and promote comprehensive, coordinated and sustained development. People needed to achieve centralized planning in five areas, namely the centralized planning of the development of the city and the countryside, of the development of different regions, of the development of economy and society, of the harmonious development of man and nature, and of domestic development and opening up to the outside world. The substance of centralized planning was coordination. The substance of the centralized planning in the five areas was to realize coordinated development in these areas. When people achieved the centralized planning in five areas, they could both effectively retain economic stability and promote economic growth at proper timing. Hence, they could realize the steady and faster development of national economy.

IV. People Needed to Evaluate the Effect of the Activities in Market Economy Scientifically and Ensure That Socialist Market Economy Could Achieve Sustained Development

China's socialist market economy was government-guided market economy. The government played an important role in such market economy. The difficulty in scientifically evaluating the effect of the activities of market economy did not lie in the enterprises because it was already generally accepted that the main indexes or central indexes to evaluate the effect of the economic activities of enterprises were profits and profit rate. What was really difficult was how to evaluate the administrative performance of local governments and their officials when the government and, mainly, local governments became an important role in economic activities. In the past, people generally took GDP, namely gross domestic product, and its growth rate as the main criteria to evaluate the performance of governmental organs. Evaluation was made annually to determine their rankings. When GDP growth rate was high in some places, the administrative performance of the local government there was good. When it was low in some places, the administrative performance of the local government there was bad. In the end, local governments in different places got into a race and did everything to achieve fast GDP growth. And all of them wanted to be the top player in this area. When one got faster GDP growth, others wanted to have even faster growth than it. Because of this, people nicknamed these

local governments GDP government. However, many years of practice and, particularly, the practice in recent years indicated that doing things in such a way resulted in many problems. First, when people took GDP growth rate as the sole or most important index in evaluating the administrative performance of the government, they would definitely overlook the development of various social undertakings. This would result in the situation of incoordination in which economic development went farther while social development lagged behind. Second, such practice would stimulate the short-term behavior of the government. It would promote economic growth in an extensive manner, which was characterized by outward expansion and would affect the sustained development of the economy. Finally, such practice would drive some government officials to fake their performance. So it was necessary to draw up scientific evaluation system in order to make China's socialist market economy develop in a sustained manner. For the entire country or just a region, people first needed to gradually change the single index of GDP growth in evaluation into indexes in many aspects. For example, the Commission on Sustained Development of the United Nations proposed indexes in four aspects: (1) society, (2) environment, (3) economy and (4) system. People might draw from such indexes. Second, people needed to gradually develop GDP index into green GDP index or GDP index with green factors. Besides, they needed to strengthen the verification of figures and seriously investigate and punish those who faked their figures so as to enhance the transparency and accuracy of statistical information. So it can be seen that it was of very important meaning to the healthy and sustained development of socialist market economy to find an index system that could correctly evaluate the effect of the activities of socialist market economy. In 2005, the Compendium of the Development Program in the Eleventh Five Year Plan of the state divided for the first time the main indexes of national economy into mandatory indexes and anticipated indexes. This was an exploration and attempt of great value.

V. People Should Regulate the Activities of Market Economy in Accordance with the Law to Guarantee the Healthy Operation of Market Economy

Modern market economy was economy under the rule of law. The economic practice in China and abroad indicated that market economy could play its positive role more effectively and lessen various negative effects caused by its spontaneous regulation only when it operated on the track with the rule of law. Socialist market economy was also economy under the rule of law. Market economy was economy with competition. People advocated fair competition to improve efficiency. Hence people had to regulate the way of competition and form effective competition rules or game rules. This was the same as that people had to observe the rules of the game when they were in a sport game. So the healthy development of socialist market economy could be guaranteed only when it operated on a track with the rule of law.⁴

Some economists examined the objective principles of market economy from the angle of the enterprises. They pointed out that at least the following contents should be included in the understandings on the objective principles of market economy that

⁴See Zhang (2004).

people obtained from the economic practice in China since the reform and opening up and also from large amounts of the rise and fall of foreign enterprises: (1) Market was always in constant change. (2) People needed to establish correct risk awareness. (3) Getting close to customers was the fundamental way for an enterprise to survive. (4) There were market opportunities everywhere and at any time. (5) People needed to address well the relationships between tangible and intangible values and between short- and long-term interests. (6) People needed to promote the evolution from “zero sum game” to the new “win-win” pattern of competition.⁵

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⁵See Pan (1999).

Chapter 16

Breakthrough in the Theory on Ownership System and the Establishment of the Basic Economic System of Socialism



Zhouyuan Zhang

Socialism = Public Ownership System + Planned Economy + Distribution according to Performance, this formula became a doctrine that people in China followed without any change for many years. Here public ownership system was the sole economic basis of socialist society. And there were only two forms of public ownership system, namely whole people ownership system and collective ownership system. Both were unshakable as the doctrine stipulated. From the 1950s to 1970s, the doctrine above gradually developed into its extreme. People believed that the larger public ownership system became, the better things were. They followed the principle of being “large in size and collective in nature” and tried to upgrade ownership systems. They sought to realize completely pure public ownership system and eradicate all private ownership elements. However, the attempt and practice above were hit hard in reality. The seemingly advanced productive relations created with it were dragged down by backward productivity. People were punished with material shortage, difficulty in raising living standard, and lack of dynamism in economy for their mistake. After reform and opening up, the Chinese circle of economics and other social circles found the rope that tied up the development of productivity in China when they reflected on the reason why Chinese economy could not take off in a good way. This rope was the ownership system theory and policy that advocated the principle of being “large in size and collective in nature” and went beyond proper development stage. Then in the process of reform and opening up, people gradually established the basic economic system of socialist primary stage in which public ownership system dominated and different ownership economies developed jointly. While continuing to develop public ownership economy, people permitted

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and encouraged the development of individual, private and non-public ownership economies. Thus they greatly liberated social productivity and mobilized positive elements in various aspects to speed up and promote the construction of socialist modernization. China's economy quickly took off and created the "China Miracle" that attracted the attention of the whole world.

The following was a brief review on the evolution of the theory of ownership systems during over sixty years from the founding of the People's Republic of China.

1 The Socialist Transformation of Private Ownership in the 1950s and the Scourging on Private Ownership System from that Time to the 1970s

From 1953 to 1956, China carried out large scale socialist transformation on individual agriculture and handicraft industry and private capitalist industry and commerce, which were based on private ownership system of production means. The book *Socialist Transformation of the National Economy of China*, written jointly by Xue Muqiao, Su Xing and Lin Zili and published by the People's Publishing House in 1959, was a representative research result in this area. At the time, the circle of economics emphatically formulated that China's socialist transformation took the unique road of starting from the national situation in China, which mainly included guiding individual agriculture and handicraft to take the road of cooperative transformation and adopting the policy of peaceful redemption with private capitalist industry and commerce. In this way, important progress was achieved within a short period of several years. After 1976, some economists and personages in other circles believed that there were some defects and mistakes in the socialist transformation in the 1950s. With respect to this situation, the *Resolution on Several Historical Issues of the Party since the Founding of the People's Republic of China*, adopted at the Sixteenth Plenary Session of the Eleventh CPC Central Committee held in June 1981, stated that "There are defects and deviations in this work. After the summer of 1955, the cooperative transformation of agriculture and the transformation of handicraft industry and individual commerce showed too rash requirements, too rough work, too fast change and too simplistic and monotonous form so that some problems were left unsolved over a long period of time. After the transformation of capitalist industry and commerce was basically completed in 1956, the use and handling of some of the former industrial and commercial workers was rather improper. But on the whole, it was indeed a great historic victory as such complex, difficult and profound social transformation was relatively smoothly completed in a large country of several hundred million population, which promoted the development of agriculture and the entire national economy."

From the basic completion of socialist transformation to the time before 1976, the mainstream view in the arena of economic study was still the doctrine of Stalin. Namely, it was believed that socialist public ownership was the only economic basis

of a socialist society. Socialist public ownership only included whole people ownership and collective ownership. Whole people ownership was the superior form while collective ownership was the inferior form. As social productivity developed, collective ownership should transform into whole people ownership and form single and all-round ownership of the whole people. During the People's Commune Movement in the countryside in 1958, people sensationally followed the "communism fad" characterized by "equalitarianism and indiscriminate transfer of resources". The peasants were deprived and the principle of exchange at equal values was negated. In the end, such practice caused devastative consequence and seriously damaged social productivity. Agricultural production suffered great retrogression. People started to correct the wrong practice above from 1959. They recognized once again the collective ownership of the peasants and also recognized developing commodity production and practicing exchange at equal values and distribution according to performance. However, these efforts did not last long. From the end of 1962, it was proposed again that people should "never forget class struggle" and take class struggle as key task. People kept removing individual and private economies and eliminating capitalism. The practice of cancelling individual economy took the mainstream position in policy. Because of it, only 150,000 urban individual commercial and industrial workers were left nationwide in 1977. In 1978, there were only 259 such workers in Beijing. There were only 13,000 in Shanghai. Table 16.1 shows such a situation.

Private economy did not exist at all from the basic completion of socialist transformation in 1956 to the time before the reform and opening up. Statistical data showed that the employees in private enterprises in China amounted to 2.96 million in 1949, accounting for 36.5% of the total of employees and 3.67 million in 1952, accounting for 22.8%. Then in 1957, there were only 20,000 left and basically none of them afterwards. The industrial output of private enterprises reached RMB 6.83 billion yuan in 1949, accounting for 48.8% of China's gross industrial output, RMB 10.52 billion yuan in 1952, account for 30.7%, RMB 7.27 billion yuan in 1955, accounting for 13.2%, and only RMB 40 million yuan in 1957. From 1957 to 1978, various data about private enterprises disappeared from statistical materials.

The gradual extinction of individual and private economies not only seriously affected economic development but also caused a series of difficulties in people's life. The difficulties to provide resources and services for public transport, housing, food, clothing, shopping, repairing, bathing and even haircutting caused great trouble in the everyday life of Chinese citizens.

2 Some Valuable Views Proposed Before the Reform and Opening up

From the 1950s, there were Chinese economists and government leaders who made objective and level-headed analysis and study on the question of the structure of ownership system in socialist society and proposed some views and policy positions opposite to traditional doctrines.

Table 16.1 The number of workers in urban individual economy in China before the reform in 1978. Unit: 10,000 persons

Year	Total	Individual industrial and commercial workers					Other Individual operators
		Industry	Construction	Transportation	Commercial food and beverage service	Sub-total	
1952	883	360	83	56	318	817	66
1953	898	375	80	65	318	838	60
1954	742	342	86	50	209	687	55
1955	640	205	143	54	171	573	67
1962	216	49	4	8	71	132	84
1963	231	49	4	10	66	129	102
1964	227	48	5	10	58	121	106
1965	171	39	5	10	48	102	69
1971	81	21	3	6	24	54	27
1972	66	18	3	5	20	46	20
1973	51	15	3	4	16	38	13
1974	36	10	2	3	14	29	7
1975	24	6	2	2	12	22	2
1976	19	4	2	1	11	18	1
1977	15	3	1	1	9	14	1
1978	15	3	1	1	9	14	1

Data Source Zhang Zhuoyuan, Hu Jiayong, Liu Xuemin, *On China's Ownership System Reform*, Jiangsu People's Publishing House, 2001, pp. 49–50

After the three major transformations were basically completed in 1956, Chen Yun proposed that people should permit some free production of individual operations and some free market as supplementation in economy.¹ At the time, his view was regarded as something very original.

In the early 1960s, Deng Zihui, who was in charge of rural work, and also Deng Xiaoping, Chen Yun and Tian Jiaying indicated that they supported the policy of fixing farming output quotas by household so as to facilitate the development of agricultural production.²

In 1958, the People's Commune Movement failed in the countryside and brought with it three years of severe economic difficulty in China. After that, many articles were published in the arena of economic study to demonstrate the necessity of the existence of small collective economy, starting from the fact that China's productivity was rather backward, and also the necessity of the existence of the peasants'

¹Chen (1995).

²Bo (1993).

private plots and household sideline production and rural fair trade.³ Such discussion declared the complete failure of the idea of being “large in size and public in nature” and of the theory and policy about the so-called transition into communism.

Sun Yefang proposed in 1961 that the right of ownership of production means could be separated from its rights of possession, use and dominion. He believed that, under the ownership of the whole people, “the issue of operation and management right should take the place of ownership system and become the first of the three aspects in production relation studied in socialist political economics.” “The central question in financial and economic management system is the right and obligation of enterprises as independent accounting unit and their relationship with the state, namely the question of the operation and management right of enterprises.”⁴ Su Shaozhi also held similar views. Su Shaozhi said, “Within the limit that the ownership right of the means of production has been determined, its rights of ownership, possession, disposal and use, namely the ownership right and operation and management right of enterprises, are not at all absolutely inseparable. Under the condition of private ownership system, the several ‘rights’ could belong to different classes or individuals. Under the condition of public ownership system, they could belong to different units or departments.”⁵ Zhu Jiannong said, “In the state-owned enterprises in socialist countries, the rights of ownership, possession and disposal of all the means of production given by the state for use belong to the state.” “The enterprises enjoy the right of use of the means of production given by the state for them to use.”⁶

Luo Gengmo proposed in 1959 the distinctive view that there was “minor whole people ownership” in “major whole people ownership”. He believed that, “in socialist stage, the production means and products under the ownership of the whole people also contains the relation of local whole people ownership in certain scope and to certain extent. Namely there are relations of ‘minor whole people ownership’ in ‘major whole people ownership’.” “In the final analysis, such crossing relation between major and minor whole people ownerships was caused by the situation that the development standard of productivity was not high enough and the communist consciousness of the people was also not high enough. These two facts make it necessary for the state, which represents the whole people, to utilize proper material interests to promote its local economic organizations and the economic organizations of various departments as well as grassroots enterprises and institutions to work hard to manage production well. This is just like the fact that the state must properly utilize the principle of ‘distribution according to performance’ to drive the people to work hard.”⁷

In 1957, Luo Gengmo proposed the view that collective ownership was “public inside and private outside”. He said, “Although collective ownership economy was socialist economy, it was the public ownership of groups of people but not ownership

³See Yi (1961).

⁴Sun (1979).

⁵See Su (1962).

⁶See Zhu (1962).

⁷Luo (1959).

of the whole people. I believe that it can even be said that such collective public ownership economy of groups of people is ‘public inside and private outside’. Namely, it is public ownership in the inside but it contains more ‘remnants of private ownership’ to the state than the enterprises and individuals in the whole people ownership economy to the state.”⁸

3 The Establishment of the Basic Economic System of the Primary Stage of Socialism with China’s National Situation as Starting Point After the Beginning of Reform and Opening up

Soon after the founding of the People’s Republic of China, the problem of rash advance regardless of current development stage in the area of ownership relations emerged in the country. There were repeated movements aiming at being “large in size and collective in nature” in the city and the countryside. Non-public ownership economies were seen as forces alien to socialism and rejected. Once these economies emerged, they were purged as remnants of capitalism. In the city, state-owned economy almost dominated everything. In 1978, there were only 150,000 individual commercial and industrial workers in the cities nationwide. The scope of operation of their businesses was strictly limited to the several areas in repair, service and handicraft industries.

From the beginning of the reform and opening up, people gradually realized that China’s productivity was at a development level far behind the extent to which people could implement comprehensive transfer into public ownership and eliminate non-public ownership economies. Because China’s economy was rather backward, it was necessary for the economies under various ownership systems to coexist and develop so as to mobilize resources and forces in various areas to get the country out of the status of poverty and backwardness and promote the rapid development of its economy. In particular, the Chinese circle of economic theories proposed the view that China’s socialism was still in the primary stage, namely an underdeveloped stage, in the period at the end of 1970s and in early 1980s, which exerted important social influence. In 1981, Deng Xiaoping presided over the drafting of the *Resolution on Several Historical Issues of the Party Since the Foundation of the People’s Republic of China*. It was specifically proposed in the document that “our socialist system is still in the primary stage.” The Thirteenth CPC National Congress systematically discussed the theory on the primary stage of socialism, which gradually won the consensus of the people. Such development helped China find a practical and feasible approach to build socialism under China’s conditions.

The connotation of the theory of the primary stage of socialism was that China was still in the primary stage of socialism from the basic completion of socialist

⁸Luo (1957).

transformation in 1956 to the basic realization of modernization in the middle of the 21st century, which would last a century. China was originally a semi-colonial and semi-feudal society troubled by huge population, weak economic foundation, inferior standard of productivity, low degrees of commercialization and marketization of economy, and lower GDP ranking in the world. According to the report of the World Bank economic mission on their research tour in China in 1980, China's per capita GDP in 1952 was about USD 50 after conversion, which was lower than that of India and equal to only over 1/5 of the USD 240 per capita GDP of the Soviet Union in 1928.⁹ Even after nearly 60 years of construction, no radical change has occurred to the situation that productivity was still not adequately developed in China. In 2008, China's per capita GDP still amounted to USD over 3,000, ranking around the 100th place in the whole world. There were over 70 million people living in the countryside among the 1.3 billion population. Agricultural yield was heavily affected by climate conditions. Agricultural labor productivity was low. Some modernized industries coexisted with a large amount of backward industries below the level of modernization. Some cities where market relations were relatively developed coexisted with backward rural areas where there was still self-sufficient natural economy to a certain extent. A small amount of sciences and technologies at advanced standard existed in the situation that science and technology was low in general and there were a certain proportion of illiterates and semi-illiterates in China population. All these indicated that China was obviously in a status characterized by dual economic structure. In 2007, there were 43.2 million impoverished population in the countryside in China, whose per capita annual net income was lower than RMB 1,067,¹⁰ and there were over 20 million population in the city living in poverty. Although Chinese people reached the living standard of a well-off society in general, they were not yet affluent. Chinese people needed to work hard and struggle for forty years from the present if they wanted to basically realizing modernization.

The main contradiction of the primary stage of socialism was the contradiction between the constantly growing material and cultural needs of the mass and backward social production. The basic task of such primary stage was that people needed to take the theory of socialism with Chinese characteristics as the guideline, adhere to the basic line of the CPC, take economic construction as central task, concentrate resources and forces to develop social productivity, and gradually achieve industrialization, urbanization and modernization through the socialization, commercialization and marketization of economy. In order to realize the magnificent goal of modernization, people needed to fully mobilize the initiative of various parties and vigorously develop productivity. All non-public system economies that conformed to the Three Favorables criteria of whether it was favorable to developing the productivity of socialist society, to enhancing the comprehensive national strength of the socialist country, and to improving the living standard of the people could and should be used to serve the realization of modernization in China. Therefore, people should permit and encourage non-public ownership economies, including individual, private and

⁹See World Bank Economic Mission (1983).

¹⁰See *Information for Leaders' Decision Making*, Issue 15, 2008.

foreign-funded economies to develop under the guidance of national policies and supervised and managed in accordance with the law. Hence, people could mobilize more funds to be used in economic and social constructions, find jobs for more people, produce more and better products, provide more and better service, satisfy the needs of the society in various aspects, and promote China's modernization process.

Therefore, when starting with the basic national situation that China was still in the primary stage of socialism in the present stage, people had to continue to develop public ownership economy and permit and encourage the development of non-public system economy. And the original idea and practice to pursue the total domination of public ownership and state ownership would definitely damage productivity, just like the situation from mid-the 1950s to 1976.

The elevation and transformation of understanding required corresponding adjustments to original policies. Soon after the beginning of the reform and opening up, the CPC and the government formulated the guideline of achieving the dominance of public ownership and the joint development of multiple economic sectors. People should permit and encourage the development of non-public ownership economies, such as individual, private and foreign-funded economies. And it was affirmed repeatedly that such principles would be adhered to over a long period of time. It was also recognized that non-public ownership economy was the necessary and beneficial supplementation of socialist economy. Thus, people gradually eliminated the trammels caused to productivity by irrational ownership system structure during the period before the establishment of such understanding. This mobilized the initiative of various parties and promoted the development of production and the improvement of the people's living standard.

The Fifteenth CPC National Congress in September 1997 further summarized taking public ownership as the dominant one and achieving the joint development of multiple ownership economies as a basic economic system for China in the primary stage of socialism. This meant another major policy adjustment because, now that it was a basic economic system, it was not just an ordinary policy or guideline, nor a measure of expediency, but an institutional arrangement with stability and secular nature. This was the specific application and important development about the theory of the primary stage of socialism and an important component of the theory of socialism with Chinese characteristics.

Starting with the provision on the basic economic system of the primary stage of socialism in the above, the report of the Fifteenth CPC National Congress made a new assertion of important guidance meaning to non-public ownership economy: "Non-public ownership economy is an important component in China's socialist market economy." This assertion was more positive and accurate than the formulation generally quoted in the past that non-public ownership economy was the supplementation to socialist economy. In order to realize modernization, which was the basic task and magnificent goal in the primary stage of socialism, people need to fully mobilize the initiative of various parties and vigorously develop productivity. People needed to regard non-public ownership economy as an important component of socialism

market economy rather than an ordinary supportive role. They needed to take advantage of all non-public ownership economies that conformed to the Three Favorables in a good way to serve the realization of modernization.

Taking public ownership as the dominant one and achieving the joint development of multiple ownership economies included the meanings in three aspects: (1) Public ownership system dominated. (2) State-owned economies controlled important industries and key areas that were regarded as the lifelines of national economy and played a dominant role in national economy. And (3) Economies under multiple ownership systems developed jointly over a long period of time. China was a socialist country. In China, people had to let public ownership system dominate. They should not take the road of privatization, namely comprehensively restoring private ownership system. This was a principle that people should follow unswervingly.

The most fundamental thing about the dominance of public ownership system was that publicly-owned assets took up an advantageous portion in total social assets. Or it can be said that publicly-owned capital took up an advantageous portion in aggregate social capital. State-owned economy controlled the lifeline of national economy and played a dominant role to economic development.

The dominance of public ownership was an important characteristic of socialist market economy. Why should public ownership dominate? This was because the dominance of public ownership system was favorable to mobilizing the initiative of the extensive community of workers, to achieving the common prosperity of the mass, and thus to liberating and developing the productivity of socialism. So to adhere to the principle of the dominance of public ownership conformed to the criterion of productivity, namely whether something is favorable to liberating and developing productivity.

In socialist market economy, public ownership did not equal to state ownership. Public ownership economy included not only state ownership economy, collective economy and cooperative economy but also the state-owned and collective-owned elements in fixed ownership economy. During nearly 30 years, state ownership economy, collective economy and cooperative economy experienced obvious growth and development, so did the publicly-owned elements in mixed ownership economy. This was the achievement obtained from the reform and opening up.

4 Looking in Theory and Practice for the Realization Form of Public Ownership System that Could Be Combined with Market Economy

China's economic system reform was market-oriented and the goal of reform was to build socialist market economic system. If people wanted to develop and improve the basic economic system of socialism with the dominance of public ownership, they needed to resolve the issue about the mutual adaptation between public ownership system and market economy and reform traditional socialist ownership system. As

state ownership system had the problem of mixing up the functions of government and enterprise and thus could not adapt to socialist market economy, the task was to work hard to find the realization form of state and public ownership systems that could promote the development of productivity and adapt to socialist market economy and then further adjust and improve the structure of ownership system according to the requirements in developing socialist market economy.

In the early period of the reform and opening up, some economists advocated developing share economy and endeavored to find the realization form of public and state ownership systems that could combine with market economy. In the beginning of 1980s, some economists proposed that, as the reform advanced, public ownership system would not be limited to the two forms of whole people ownership and collective ownership. "At present, many forms emerged in socialist public ownership system." "We should re-study the theory on socialist ownership system of production means on the basis of the changes in actual economic life rather than mechanically applying available theories on the complex situations in actual life."¹¹

Some economists also proposed the concept of the diversity of socialist ownership system. They pointed out that, in an underdeveloped socialist society, public ownership system was not "one size that fits all" or uniform in all cases. Rather, it was a complex structure with diversity. It was a system of possession relations in multiple levels and tiers, which took whole people ownership system as dominant one, consisted of collective ownership, joint ownership and other forms of public ownership system, and showed a scale of degrees of socialization from high to low. The complexity of such public ownership system matches the imbalance and multi-level of productivity. People should examine the combination, interlacing and mutual permeation of various possession relations in the movement of socialist commercial reproduction and then further analyze and reveal the very rich specific forms of socialist public ownership system.¹²

From the middle of 1980s, China started to develop shareholding system economy in its socioeconomic life. This was a kind of mixed ownership economy. In this economy, large amounts of shareholding system economy controlled by public ownership components should be regarded as a form of public ownership. Economists did not have much controversy in this respect. At the end of 1980s and, particularly, in the 1990s, various kinds of shareholding cooperative system economies emerged in different places in China. It is generally believed that the economies under shareholding cooperative system possessed public ownership properties in different degrees. Among them, the shareholding cooperative system, which mainly contained the conjunction between capital and the labor of workers, was a new form of public ownership.

In 1987, the State Commission for Restructuring the Economic System entrusted some units, including the Chinese Academy of Social Sciences, the Party School of the CPC Central Committee, and the Peking University, to study and propose the reports on mid-term reform planning (1988–1995). Almost all these reports made the

¹¹He (1984).

¹²Liu (1986).

suggestion on the transformation of state-owned enterprises from the current contract system into shareholding system. It was pointed out that, because contract system did not radically change the congenital weaknesses in traditional property right system of state-owned enterprises, enterprise reform had to develop towards the direction of restructuring property right relations, namely of shareholding system. The research team of the Peking University also proposed specific measures for the transformation: The enterprises that already operated through contracting management might adopt the mode of transformation of “contracting first and shareholding later”. The enterprises that did not operate through contracting management might adopt the mode of transformation of concurrent contracting and shareholding or “shareholding first and contracting later”. Newly-formed enterprises should all adopt shareholding system as their enterprise organizational form.¹³

The report of the Fifteenth CPC National Congress made important breakthrough in the search for the form of realization of public ownership system. The report proposed that the form of realization of public ownership system could and should be diversified. All operation modes and organization forms that reflected the principles of socialized production could be utilized with confidence. People should endeavor to search the form of realization of public ownership system that could greatly promote the development of productivity. Shareholding system was a capital organization form of modern enterprises that was favorable to the separation of the rights of ownership and operation and to improving the operation efficiency of enterprise and capital. Capitalism could make use of it; socialism could also make use of it. So people could not say in a general way that shareholding system belonged to public or private ownership. The key resided in which party had the controlling stake in hands. A company controlled by the state or the collective through shareholding possessed obvious public ownership nature. Such a situation was favorable to expand the scope of domination of public capital and strengthen the role of public ownership as the dominant part. This statement in the report of the Fifteenth CPC National Congress had important guiding meaning. After the conclusion of the Fifteenth CPC National Congress, some articles listed the new forms of realization of public ownership other than state-owned and collective ownerships since the reform and opening up: shareholding cooperative system, mass organization ownership, lease, entrusted operation, local mass organization ownership, company limited by share controlled by public ownership, and ownership systems of town, township, village and villager’s group.¹⁴

In 2003, *the Decision of the Third Plenary Session of the Sixteenth CPC Central Committee on Several Issues about Improving Socialist Market Economic System* further proposed the assertion that shareholding system was the main form of realization of public ownership system. It was pointed out that people “should adapt to the trend of the constant development of economic marketization and further strengthen the vigor of public ownership economy. They should largely develop

¹³See Department of Comprehensive Planning of the State Commission for Restructuring the Economic System (1988).

¹⁴See Wei (1997).

mixed ownership economy with the participation of state-owned capital, collective capital and non-public capital. They should realize the diversification of the main parties of investment and make shareholding system the main form of realization of public ownership system.” Some economists believed that the diversification of the forms of realizations had been achieved in public ownership system and shareholding system became the main form of realization of public ownership system. This indicated that China found the correct approach to combine public ownership system with market economy and that the theory of socialist market economy had more complete and solid argumentation basis.

The development of shareholding and mixed ownership economy was the objective requirement of the development of socialist market economy. This also indicated that the diversification of economic and market entities was inevitable. There should be economic and market entities under non-public ownership economies as well as the market entities under public ownership economies, such as state ownership economies. These market entities all put their own effects into exertion, competed in equality and promoted mutual development. As it was pointed out in the report of the Seventeenth CPC National Congress, people should make efforts in forming a new situation in which economies under various ownership systems competed in equality and promoted mutual development in the future so as to adhere to and improve China’s basic economic system.

In the process of pushing forward rural reform and developing household contracted responsibility system, a large group of township and town enterprises rose as a special force. Over 100 million people worked in these enterprises. Various forms of organizations under cooperative economy also saw great development. Both collective economies like township and town enterprises and cooperative economies were organic components of public ownership system. Under the condition of socialist market economy, people had to develop collective and cooperative economies in various forms.

There was the problem of unclear ownership rights in China’s collective economy, such as township and town enterprises. Over many years, great progress had been achieved in the reform focused on clearly establishing ownership rights. According to the introduction of some article, two ownership system transformations were implemented from 1997 in the township and town enterprises in southern Jiangsu province with a coverage as high as 80% so that large change occurred to the ownership structure of these enterprises. Take the city of Wuxi as an example. The ownership system structure defined according to gross industrial output in Wuxi in 2005 was as follows: State-owned enterprises accounted for 5.4%, collective enterprises 12.1%, enterprises with joint stock cooperative system, 7.4%, enterprises with shareholding system 22.8%, foreign-funded enterprises 29.2%, individually-operated enterprises 1.0%, and private enterprises and joint ownership enterprises 22.1%. This indicated that, while collective ownership enterprises still took up certain proportion after the reform, rapid development was achieved in enterprises with shareholding system, enterprises with joint stock cooperative system, and private enterprises and joint ownership enterprises. Reform promoted the development of production and the improvement of the standard of income of the peasants. The per capita net income

of the peasants in the rural areas in Wuxi was 7,115 RMB in 2004 and 8,004 RMB in 2005, both higher than national averages.¹⁵

Peasants' specialized cooperative organizations were indispensable for constantly improving the standard of income of the peasants. Various kinds of peasants' specialized cooperative organizations were of important meaning for and played an important role in improving the degree of organization of the peasants, lowering the expenses in trade, raising the position of the peasants in market negotiation, enhancing their ability to respond to natural and market risks, and increasing the economies of scale. The practice that various kinds of peasants' specialized cooperative organizations gradually developed at the end of 1980s proved this point. According to statistics, there were 110,900 peasants' specialized cooperatives in China by the end of 2008. Among them, those in Shanxi were of the largest number, the figure reaching 12,800. Those in Jiangsu had the largest amount of member capital contribution and the largest number of members.¹⁶ In the future, people needed to further develop various peasants' specialized cooperative organizations so as to push forward the construction of socialist new countryside and promote the growth of the peasants' income.

Finally, there was the issue of mixed ownership economy. In 1993, it was proposed in *Decision on Several Issues on Establishing Socialist Market Economy* at the Third Plenary Session of the Fourteenth CPC Central Committee that, with the flowing and restructuring of ownership right, there would be more and more economic units with properties owned in a mixed manner and this would result in new property ownership structure. In 1997, it was proposed in the report of the Fifteenth CPC National Congress that the realization form of public ownership system could and should be diversified. Shareholding system was a form of capital organization in modern enterprises, which could also be used in socialism. In 2002, it was proposed in the report of the Sixteenth CPC National Congress that people should positively implement shareholding systems in enterprises except for a very few that had to be solely-funded and operated by the state and develop mixed ownership economy. It was further proposed in the report of the Seventeenth CPC National Congress that people should take modern property right system as foundation, complete modern enterprise system, and develop mixed ownership economy. From the reform and opening up and, in particular, from the beginning of the new century, state-owned economy continued to develop and its total and net assets both saw continuous growth. Besides, rapid development was also achieved in collective economy, cooperative economy and non-public ownership economies, such as individual and private economy. An enormous amount of foreign investment was utilized. China implemented the policy to permit domestic non-governmental capital and foreign capital to participate in the restructuring and reform of state-owned enterprises. As a result, state-owned capital and various non-state-owned capital permeated and merged with each other. And mixed ownership economy, with shareholding system as its main form, saw rapid

¹⁵See Fan and Sun (2007).

¹⁶See Information for Leaders' Decision Making, Issue 663, published in May 4, 2009.

development. Some materials showed that a large amount of newly-formed enterprises were in shareholding system in recent years, except for individually-operated businesses. Some economists estimated that mixed ownership economy, in which the entities with shareholding system dominated, would play an increasingly decisive role in national economy. In 1999, mixed ownership economy with the dominance of shareholding system accounted for 33% of Chinese economy in general. And the figure would become higher in the future.¹⁷ The development of mixed ownership economy also indicated that people find a form and approach with which they could combine China's public ownership system and, particularly, its state ownership system with market economy.

5 The Theory and Practice About Vigorously Developing Non-public Ownership Economies Such as Individual and Private Ownership Economies After the Reform and Opening up Began

After the beginning of the reform and opening up, the Chinese circle of economics achieved a series of important breakthroughs in the theory of ownership system. First, in the area of ownership structure, it was believed that, under the condition that China's productivity development standard was still low and it was in the primary stage of socialism, people had to allow the existence and development of non-public ownership economies, such as individual economy and private economy. As early as 1979, China's prestigious economist Xue Muqiao boldly made the important suggestion of developing various economic components and broadening the channels of employment in response to the actual situation that there were more than 20 million urban personnel waiting for employment nationwide at the time, which affected social stability. He specifically proposed that, "at present, there might be more benefit than harm to leave a bit of the tail of individual economy and capitalism". "We could not eradicate capitalism for now. There is nothing to fear if there is a bit of it."¹⁸ He was the economist who advocated the development of various economic components the earliest after China started reform and opening up.

Some other economists also said that, "because of the imbalance in productivity in China currently, people need to retain the multileveled nature or diversity in ownership system structure so as to adapt to it. There need to be the whole people ownership, which take up the leading position, and various socialist ownership elements, which took up the advantageous positions. Besides, people need to retain some elements in individual and private ownership systems and state capitalism as supplementation." Moreover, "because people advocate the joint operation in various forms

¹⁷See Chi (2003).

¹⁸See Xue (1996).

between different ownership elements, China's ownership structure will exhibit a very complex picture."¹⁹

During the same period, the CPC and the government repeatedly promulgated documents that encouraged the development of individual economy. In August 1980, it was pointed out in the *Notice of the CPC Central Committee on Transmitting the Documents at the Work Meeting on Labor and Employment* that "It shall be permitted that individual workers engage in individual labor that does not involve the exploitation of other people within the scope as permitted by law. Such individual economy is the indispensable supplementation to socialist public ownership economy. It will play a positive role within a fairly long historical period in the future. It should be developed properly." In July 1981, the State Council promulgated *Several Policy Provisions on Urban Non-Agricultural Individual Economy*. And it was pointed out that "people should earnestly give aid to the development of urban non-agricultural individual economy and provide support and convenience in the aspects of fund, supply of goods, premise, taxation and market management." In December 1982, the Fifth Meeting of the Fifth National People's Congress adopted the inclusion of the development and protection of individual economy into the *Constitution of the People's Republic of China*. "The individual economy of urban and rural workers within the scope in the provisions of the law constitutes the supplementation to socialist public ownership economy. The state protects the legal rights and interests of individual economy." As documents that encouraged individual economy was promulgated in succession, the status of individual economy was recognized and improved and, as a result, it achieved rapid development.

As individual economy developed rapidly, the question how to understand and treat private economy was proposed. Around 1981, operation with hired labor became popular in the countryside. According to a survey on 36,667 households in rural areas nationwide, organized and conducted by the Rural Development Research Center of the State Council in 1984, 203 households among them hired long-term laborers who would work for six months a year. On average, each household hired 4.1 laborers. Among them, 25 households hired more than eight laborers. And the laborer working in these 25 households had an annual income of 541 RMB. The annual income of the employers was 9,920 RMB. Several kinds of views emerged in the circle of theoretical study on the issue of hired laborer. The first kind held that it had the nature of capitalist laborer hiring. The second kind believed that this was a form of commodity economy that belonged to socialist economic system. The third kind believed that operation with hired labor possessed uncertainty and plasticity under public ownership system and should be encouraged to develop. The fourth kind held that it belonged to state capitalism. And the fifth kind believed that the substance of operation with hired labor was capitalist. But in China, people needed to analyze on the basis of specific situation and should not impose uniformity in all cases.²⁰ During this period, the policy of the central authorities was that people should not argue about it but wait and see. Deng Xiaoping advocated that people should leave the case that

¹⁹See Wang and Du (1980).

²⁰See Peng et al. (2008, pp. 182–184).

Nian Guangjiu, an entrepreneur of a private business, created a nationally-renowned snack brand called “Sha Zi Gua Zi”, untouched. This was because, once anything was done about the case, people would say that China’s policy was changed and thus there would be more loss than gain.²¹

In the beginning of 1992, Deng Xiaoping proposed the famous principle of Three Favorables in his South Tour Speech, which opened up people’s view greatly and powerfully promoted the development of private and foreign-funded economies. The role of private economy enlarged gradually in national economy. In 1997, it was proposed specifically in the report of the Fifteenth CPC National Congress that “taking public ownership as the dominant one and achieving the joint development of multiple ownership economies is a basic economic system in the primary state of the socialism in China.” And “non-public economy is an important component of China’s socialist market economy.” In March 1999, the *Amendment to the Constitution of the People’s Republic of China* provided that “the state adheres to the basic economic system of taking public ownership as the dominant one and achieving the joint development of multiple ownership economies in the primary stage of socialism”. “Non-public ownership economy, such as individual economy and private economy, existing within the scope as provided by the law, is an important component of socialist market economy.”

The practice of the reform and opening up in 30 years proved that, permitting the development of non-public ownership economy, such as individual economy and private economy, recognizing non-public ownership economy, such as individual economy and private economy, as important components of socialist market economy, and establishing the basic economy system of socialism, these efforts greatly liberated social productivity. Non-public ownership economy, such as individual economy and private economy, gradually became a new growth point in national economy and a main channel to provide new jobs.

Table 16.2 presented a vivid summary of the great development of individual and private economies after the reform and opening up started.

As socialist market economy developed, non-public ownership economies, such as individual economy and private economy, would continue to develop rapidly. Their proportions to China’s GDP would further improve. Some treatises pointed out that individual and private economies would play the following positive role in the development of China’s socialist market economy.

First, individual and private economies promoted the rapid growth of national economy. China’s national economy achieved an average annual growth rate of 9.9% after the reform and opening up started. And the average annual growth rate of individual and private economies reached over 10% and became an important factor that supported the rapid development of the entire national economy in China. With the rapid development of individual and private economies, their GDP contributions rose from less than 1% in 1979 to over 30% in 2006. The sales revenue that private industrial enterprises above designated size gained increased from 479.2 billion RMB in 2000 to 4,410.7 billion RMB in 2005. The figure grew by 8.21 times within five

²¹See *Selected Works of Deng Xiaoping*, Vol. 3, People’s Publishing House, 1993, p. 371.

Table 16.2 A table about the development of individual and private economies in China from 1990

Year	Number (1,000)		Employee (1,000 persons)		Registered capital (RMB billion Yuan)		Total turnover (RMB billion Yuan)	
	Private	Individual	Private	Individual	Private	Individual	Private	Individual
1990	98	13,283	1,700	20,928	9.5	39.74	–	–
1991	107	14,168	1,840	22,580	12.3	48.82	–	–
1992	139	15,339	2,320	24,677	22.12	60.09	11.36	223.89
1995	655	25,285	9,560	46,136	262.17	181.31	149.92	897.25
2000	1,762	25,714	24,065	50,700	1,330.77	331.53	988.41	1,985.55
2002	2,430	23,770	34,090	47,430	2,475.6	378.2	1,436.9	2,083.4
2005	4,300	24,640	47,140	55,060	6,147.5	580.9	3,037.36	2,623.96
2006	4,974	25,760	63,955	75,000	7,500.0	651.7	3,495.9	2,548.95
2007	5,513	27,415	72,530	54,960	–	–	–	–
2008	6,574	–	137,000	–	11,740.0	–	–	–
By the end of September 2010	8,189	34,065	91,839	69,824	17,730.0	1,270.0	–	–

Data Source A Tutorial Reader on the Decision of the CPC Central Committee on Several Issues of Improving Socialist Market Economic System, People's Publishing House, 2003, pp. 40–44; A Tutorial Reader on the Report of the Seventeenth CPC National Congress, People's Publishing House, 2007, p. 173; *China Business Times*, February 24, 2009; and *People's Daily*, January 1, 2011

years with an average annual growth of 55.9%. The proportion of the sales revenue that private industry gained to that of all industrial sectors rose from 5.7% in 2000 to 18% in 2005. The added value that private industrial enterprises above designated size gained increased from 131.9 billion RMB in 2000 to 1,180.7 billion RMB in 2005. Its proportion to total industrial added value increased from 5.2% in 2000 to 17.8% in 2005.²² In 2006, the proportions of the number and registered capital of private enterprises in the primary, secondary and tertiary industries were respectively 1.96%, 33.34% and 64.7% and 1.83%, 37.48% and 60.7%.²³ This indicated that private enterprises made greater contribution to the development of secondary and tertiary industries. In some coastal areas, non-public ownership economy already became a critical factor in economic growth. For example, the added value, tax payment and total export of non-public ownership economy in Zhejiang province in 2002 respectively accounted for 47%, 40.6% and 79% in the entire province.

Second, individual and private economies increased employment in the society. And recently, they developed into the main channel for creating new jobs. By 2010, over 160 million people worked as employees in individual and private economies

²²See Research Team of the All China Federation of Industry and Commerce (2007).

²³See School of Economics and Resource Management of the Beijing Normal University, Report on the Development of China's Market Economy 2008, Beijing Normal University Press, 2008, p. 31.

nationwide. The reports published by National Bureau of Statistics indicated that the proportion of employed population in urban non-public ownership units increased from 0.2% in 1978 to 75.7% in 2007. From 1990s, the annual net increase of jobs in China's individual and private enterprises reached 4.2 million, accounting for 58.7% of the annual urban new jobs.²⁴ These enterprises became the main channel for creating new jobs. The development of non-public ownership economy also promoted the transfer of surplus rural labor and accelerated China's industrialization and urbanization processes. According to estimations in general, over 100 million labor population would be transferred from the countryside in the process of industrialization and urbanization in the future. They would be given new jobs mainly through developing non-public ownership economy, such as individual and private economies.

Third, individual and private economies drove the development of a group of emerging industries. Such a situation was prominently shown in the rapid development of the tertiary industry and, particularly, private scientific and technological enterprises. The majority of private scientific and technological enterprises were established by scientific and technological personnel. These enterprises practiced the principle of "raising funds by themselves, forming firms voluntarily, operating independently and assuming sole responsibility for their profit and loss". These enterprises were freed from the restrictions of administrative system, taking market as their orientation and operating according to the principles of the market. They mainly engaged in the businesses such as technological development, transfer, consultation and service and the industrialization of scientific and technological research results. From the beginning of the reform and opening up and, particularly, from 1992, the total revenue in technology, industry and trade and the tax payment to superior authorities grew at the average rate of around 30%. From the beginning of the reform and opening up, 70% of China's technical innovation, 65% of its domestic invention patents and 80% of new products came from medium- and small-sized enterprises, which were mainly private enterprises. There were over 150,000 private scientific and technological enterprises in China. Among the enterprises in 53 state level high and new technology development zones, over 70% were private scientific and technological enterprises. Individual and private economies already became a remarkable highlight in China's national economy.

Fourth, individual and private economies pushed forward the adjustment and optimization of ownership structure. The development of individual and private economies changed the situation that public ownership system dominated nationwide and the entire national economy lack dynamism. It promoted the joint development of the economies under various ownership systems and promoted the development of mixed ownership economy. The development of non-public ownership economy created an institutional environment full of dynamism in which diverse market entities competed with each other. Such development became the direct driving force for adjusting industrial structure and improving competitiveness. It also promoted

²⁴See *Beijing Daily*, November 4th, 2008.

Table 16.3 The changes of the proportions of the organizational forms of private enterprises. Unit: %

Year	Sole proprietorship	Partnership	Limited liability company	Others	Total
1993	63.8	16	16.5	3.7	100
1995	55.8	15.7	28.5	0	100
2002	28.7	5.7	65.6	0	100
2004	22.5	7.4	62.9	7.2	100

the restructuring of assets and the transformation of enterprise mechanism in state-owned and collective economies. Private enterprises also developed in the direction of establishing modern enterprise system in the process of such development. See Table 16.3.²⁵

The development of non-public ownership economy powerfully promoted the improvement of basic economic system. Where individual and private economies were active, commodity, labor, capital and technology markets also grew faster. Such a situation in turn promoted the emergence of market competition, the establishment of market rules and the development of market system. Besides, such development also urged state-owned enterprises to adapt to the market and participate in market competition.

It was proposed in the report of the Seventeenth CPC National Congress that people should unswervingly encourage, support and guide the development of non-public ownership economy. They should adhere to practice the equal protection of property rights and form a new situation in which various ownership economies competed equally and promoted the development of each other. After the publishing of the *Property Law*, the legal impediment was removed for the equal protection of property rights and thus it was easier to put the protection into practice. What was difficult was to form the conditions for the economies under various ownership systems to compete equally and to eliminate the discrimination to non-public ownership economies, such as individual and private economies, and to establish thresholds to limit market access. All these needed to be resolved in the future.

At present, there were some institutional and policy restraints for the development of non-public ownership economy.

First, people's outlook and understanding did not follow such development. Because of the influence of traditional outlook over a long time, some comrades always believed that non-public ownership economies were contradictory and repulsive to socialist economy. They failed to see that public ownership economy and non-public ownership economy were mutually permeating and that they could promote each other and develop jointly. Hence, these comrades took restrictive and suppressive measures against non-public ownership economy in their action and affected the smooth development of non-public ownership economy.

Second, discriminatory laws, regulations and policies still were not completely removed. Like public ownership economy, non-public ownership economy, such

²⁵See the Research Team of the All China Federation of Industry and Commerce (2007).

as individual and private economies, was also an important component of socialist market economy. However, such problems as numerous limitations, complex formalities in examination and approval, and unfair treatment often occurred in relevant policies, such as those related to market access, enterprise financing, and land use.

Finally, the management of the government did not adapt well to the needs in the development of non-public ownership economy. Many governmental departments were still used to take public ownership economy as the main target of their service. They failed to truly and fully practice social public management, in which they should treat the enterprises under various ownership systems in the whole society in the same way. Sometimes, some governmental departments followed the old management mode under planned economic system. They directly intervened in the production and operation activities of the enterprises or even gave targets and tasks and replaced service and supervision with inspection and charge collection. And they did poorly in providing market supervision and creating the environment for the fair competition of various kinds of enterprises.

In response to the situation above, it was pointed out in some treatises that people had to do well in the work in the following several aspects in order to vigorously develop and positively guide non-public ownership economy, such as individual and private economies:

First, people should further liberate thought and practically transform their outlook. Developing non-public ownership economy was the requirement in adhering to and improving basic economic system. Therefore, people should change the wrong view that public ownership system was a superior ownership system while private ownership system was an inferior one. They should discard the theory of the unique importance of class origin with respect to ownership systems and take productivity as the criterion in judgment. They should unswervingly encourage, support and guide the rapid and healthy development of non-public ownership economy which was beneficial to the development of social productivity in the present stage. The practice after the beginning of the reform and opening up fully proved that, in whichever region non-public ownership economy developed faster, its economy would become more active and develop rapidly. One of the important reasons why many regions in China's middle and western parts failed to achieve fast economic development was that people did not fully liberate their thought and outlook so that non-public ownership economy developed slower, which resulted in insufficient market dynamism and the gap in development speed with eastern regions.

Second, people should improve relevant laws, regulations and rules. Various specific supportive measures for promoting the development of non-public ownership economy were basically formulated and completed. They needed to be promulgated as quickly as possible. For example, the Commission of Science, Technology and Industry for National Defense promulgated the *Guide for Non-Public Ownership Economy to Participate in the Constructions in Science, Technology and Industry for National Defense*. It was stipulated that non-public ownership enterprises might participated in the following specific areas: Investment in the infrastructure construction for military industry, basic scientific research projects for national defense, supportive scientific research projects for military industry, and restructuring and

system transformation of military industrial enterprises. Non-public ownership enterprises might cooperate with military industrial enterprises in various ways and participated in the development of high technology for both military and civil purposes and also the industrialization of such technology.²⁶

Third, people needed to change discriminatory policy and realize fair competition. First, people need to loosen market access and permit non-publicly-owned capital to enter infrastructure, public utilities and other industries and areas not prohibited by laws, regulations and rules. In all the areas that people encouraged and permitted foreign investment to enter, they should also encourage and permit private capital to enter. In February 2005, the State Council promulgated *Several Opinions on Encouraging, Supporting and Guiding the Development of Non-Public Ownership Economy, Such as Individual and Private Economies* in 36 articles. The document made specific provisions on non-public economies entering many important areas and monopolized industries, aiming at creating a fair competition environment for the development of non-public economy. Then in March 2007, the Fifth Meeting of the Tenth National People's Congress adopted the *Property Law*. It was provided in the law that the state practiced socialist market economy and guaranteed the equal legal status and right of development of all market entities. State, collective and private property rights and the property rights of other right holders were under the protection of the law. No organization or individual shall violate such rights. The equal protection of property right was determined by the characteristics of China's socialist market economy. Market economy required that market entities enjoyed the same right, observed the same rules and bore the same responsibilities. Adhering to the equal protection of property rights and, in particular, the equal protection of private property rights like that of state and collective property rights, was beneficial to improving China's market environment for equal competition and selecting the superior and eliminating the inferior and to improving modern property right system and modern enterprise system. Adhering to the equal protection of property right is the basis for realizing the fair competition and mutual promotion of the economies under various ownership system. Many personages in non-governmental economy reported that there were still "glass gates" and "spring gates" in the area of market access. It seemed that the walls were demolished and people could go in. But in fact they could not enter. There was still an invisible glass gate or a spring gate through which people could enter but was bounced back immediately. In response to the situation above, *Several Opinions of the State Council on Encouraging and Guiding the Healthy Development of Non-Governmental Investment* was officially published on May 13, 2010. It was pointed out in the document that the state encouraged and guided non-governmental capital to enter the industries and areas the access to which were not specifically prohibited by laws, regulations and rules. The state encouraged and guided non-governmental capital to enter the areas of basic industry and infrastructure, municipal public utilities and policy-related housing, social undertakings, financial service, commerce, trade and circulation, and science, technology and industry for national defense. The state encouraged and guided non-governmental

²⁶See *Shanghai Securities News*, August 7, 2007.

capital to participate in the reform of state-owned enterprises through restructuring and joint venture and to positively participate in international competition. And the state promoted private enterprises strengthening independent innovation and their transformation and upgrading. People should reform investment system, change the discriminatory policy on the investment to non-public ownership economy, reduce the links in examination and approval, and lower administrative charges. Individual and private economies did not need to pass the formalities in examination and approval through giving bribes. People should implement the system of registration for record for non-governmental investment projects in the industries that the state supported and encouraged their development. The state encouraged and guided non-governmental capital to participate in the restructuring and reform of state-owned enterprises, in the Great Development of the West and the rejuvenation of old industrial bases in China's Northeast and other regions. Non-public ownership enterprises should enjoy the same treatment with other enterprises in the areas of taxation, investment, financing, land use, talent recruitment and foreign trade. At present, one prominent problem was the difficulty in financing. In the future, people should vigorously develop medium- and small-sized financial institutions in various ownership and operation forms to provide better service to medium- and small-sized non-public ownership enterprises. Large banks should provide more petty loans and provide retail service in a good way. Competent departments in related areas should take more forceful measures to properly resolve the issue of the financing difficulty of non-public ownership enterprises.

Fourth, people should transform the functions of the government and improve the service, supervision and management of the government to non-public ownership enterprises. The government should first do well in providing service to these enterprises and then carry out supervision and management in accordance with the law. People should further improve policy and service environment and truly apply to non-public enterprises the same policies that supported the development of public ownership enterprises, such as bank interest discount, for example, national debt interest discount, use of risk fund, and enterprise ownership system transformation and listing on stock market. People should encourage and support non-public ownership enterprises to grow bigger and stronger through establishing joint ventures and cooperate with state-owned, collective and foreign-funded enterprises and also through merger and acquisition so that a number of large companies or enterprise groups that possessed independent intellectual property rights and strong international competitiveness could be formed. People should establish and improve service system. They should establish service system oriented towards medium- and small-sized enterprises and timely provide to individual and private enterprises the service in funding, technology, information and law. People should expand the channel of direct financing for medium- and small-sized enterprises. They should guide individual and private enterprises to observe the ethics of patriotism, dedication to work, sincerity and law abiding through publicity and education. They should guide individual and private enterprises to play a positive role in the areas of industrial structure adjustment, Great Development of China's West, urbanization, and exploring international market. They should guide and support non-public ownership enterprises to

increase investment in science and technology, speed up technological transformation, and vigorously support them to establish research and development institutions and postdoctoral centers.

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Chapter 17

The Study on the Evolution of Enterprise System and the Reform of State-Owned Enterprises into Company and Shareholding Systems



Zhouyuan Zhang

After the founding of the People's Republic of China, socialist transformation was carried out and completed in the middle of the 1950s. Then China started to implement the traditional planned economic system. Under such a system, state-owned enterprises dominated nationwide except for the countryside. Urban collective enterprises were in fact local state-owned enterprises. These state-owned enterprises were not market entities and corporate legal entities in the true sense that possessed independent economic interests. They were attachments to their superior competent administrative departments like beads on abacus. They produced and operated in accordance with the mandatory plans of the state and all or almost all their profits were submitted to superior authorities. The wages of their workers were subject to uniform provisions of their competent departments. These enterprises were operated with egalitarianism like feeding from a giant rice pot and their workers were given life-long fixed positions like having an iron rice bowl that would never break. Both the enterprises and their workers were treated indiscriminately regardless of the quantity and quality of their work. Such practice seriously confined the initiative and creativity of the enterprises and their workers. Such a situation lasted until 1978. During such a period, the circle of economics made much discussion and study on improving the systems and management of enterprises during this period. Many valuable views were proposed, but no change was made to economic system in general. These valuable views were difficult to implement in reality and were even criticized.

After China started implementing reform and opening up at the end of 1978, the reform of state-owned enterprises began with expanding the autonomy of enterprises.

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It was pointed out in the communiqué of the Third Plenary Session of the Eleventh CPC Central Committee that “one serious shortcoming of the economic management system of China at present is too much concentration of power. The power should be delegated to lower levels boldly under leadership so that local enterprises and industrial and agricultural enterprises have more operation management autonomy under the guidance of the centralized state plans.” Around this period, the circle of economics made theoretical demonstrations that state-owned enterprises should be independent commodity producers and operators and main entities of economic interests under socialist system. Jiang Yiwei proposed the famous “enterprise standard theory”.¹ Some economists proposed the theory of “separation of the two rights of ownership and management right” and the theory of “contract system”. As market-oriented reform deepened, people found that delegating power and transferring interests without restraining mechanisms might result in short-term action and drain of state-owned assets. Some economists proposed the road of reform of implementing shareholding system and modern company system. In 1993, the Third Plenary Session of the Fourteenth CPC Central Committee adopted the *Decision of the CPC Central Committee on Several Issues on Building Socialist Market Economic System*. It was specifically proposed that the direction of the reform of state-owned enterprises was to establish modern enterprise system. Centering round the reform of establishing modern enterprise system, economists made in-depth study on the theories of shareholding system, monopoly and competition, and the equal competition of market entity. Moreover, non-public ownership enterprises, such as individual and private enterprises, mushroomed and developed. A large number of private enterprises faced the issue of transforming into modern enterprises just like public ownership enterprises. From then on, the innovation in enterprise theory reached a new height. It can be expected that, as enterprise reform further deepened and system innovation kept improving, enterprise theory would also keep advancing in development.

In the following, the author will examine how enterprise theory kept achieving innovations during over 60 years from the founding of the People’s Republic of China, which mainly came from the improvement of enterprise system and the strengthening of management and, in particular, with the deepening of the reform of state-owned enterprises and the accumulation of practical experience after 1978. He will also examine how such innovated enterprise theory vigorously promoted the deepening of the reform of state-owned enterprises and various other kinds of enterprises and how it would guide the gradual improvement of new systems in the future.

¹ See Jiang (1980).

1 The Study and Discussion on Enterprise System and Management Before the Reform and Opening up

There were a considerable amount of studies and discussions in this area before the reform and opening up. The author now selects some important ones to make some comments.

I. About the Issue of Expanding the Autonomy of Enterprises

Under traditional planned economic system, enterprises did not have much power in operation and management. Such a situation caused the doubt of some economists. In the middle of the 1950s, Gao Shangquan proposed in an article that he published that he found after field survey that there were many problems caused by the situation that enterprises had too small autonomy and competent organs concentrated too much power over too many details: First, such practice caused great waste to the state in manpower and fund to the state. It resulted in the problems that too many personnel were designated by enterprises to handle matters in the capital, that the central authorities needed to prepare too many statistical reports and tables for the enterprises, and that organs and institutions were expanded at various levels and their authorized staff numbers were increased. Second, such practice limited the initiative and spontaneity of enterprises so that their potential could not be brought into full play. Third, such practice encouraged the evil trends of bureaucracy, red-tapism and routinism in central organs.²

The person who proposed more innovative insights was Sun Yefang. In 1961, he clearly proposed in a research report that the matters within the simple reproduction of the value of fund were under the minor right of enterprises. The state should leave them out in its management. He said, "The core issue in financial and economic system was the one about the operation and management right of the enterprises. The divide between major and minor rights, which allowed the management with flexibility and without rigidity and chaos, was first of all the divide between extended reproduction and simple reproduction." "I believe that the divide between 'major right' and 'minor right' and between 'rigidity' and 'flexibility' in financial and economic system was the line to define extended reproduction. The matters that belong to the scope of extended reproduction are the 'major right' of the state. The state must manage strictly. If its management is absent or loose, there will be chaos. The matters that belong to the scope of simple reproduction are the 'minor right' that the enterprises should manage themselves. If the state intervenes too much, its management will become too rigid." There were the following shortcomings in the current system:

"First, the state replaces the enterprises in managing the matters that enterprises should be responsible for making general planning within the scope of simple reproduction."

"Second, enterprises are not responsible for updating fixed assets and, particularly, equipment. They do not have general plans and mechanically divided infrastructure

²See Gao (1956).

and major repairs that belong to the scope of updating fixed assets, namely within the scope of simple reproduction, which obstructs technological progress.”

“Third, the state undertakes too much management work on the matters within the scope of simple reproduction that thousands of enterprises under independent accounting should take care of themselves. In the end, it is trapped in routine work and because of this it lets loose the important planning work about the construction of the country in the long run, namely the matters within the scope of extended reproduction and the work of balancing national economy.”³

Regrettably, the very original views of Sun Yefang in the above were not studied and discussed in a good way. Rather they were criticized severely as revisionist views soon after.

II. Whether Strengthening Management in Enterprises Only Meant to “Control, Block and Hold Down”

In the early 1960s, China implemented the guideline of “adjustment, consolidation, repletion and improvement”. In order to put the guideline into practice and rectify the order in enterprises, the CPC Central Committee promulgated in September 1961 the *Work Regulations on State-Owned Industrial Enterprises (Draft)*, namely the famous “Seventy Articles on Industry”. Ma Hong, a famous Chinese economist, was one of the main drafters of the document.⁴ The “Seventy Articles on Industry” summarized the relationship between the state and enterprises into five fixings and five guarantees. The five fixings were as follows: The state fixed product plans and production scale, staff and organs, consumption quota and source of supply of main raw materials, fixed assets and working fund, and collaborative relations. The five guarantees of the enterprises to the state were as follows: The enterprises guaranteed that products be manufactured according to predetermined type, quality and quantity, that the gross payroll not exceed predetermined amount, that the cost plan be completed, that predetermined profits be paid to superior authorities, and that the service life of main equipment be met. The document also provided the operation rules and functions of the administrative production command system, which was implemented uniformly in an entire factory and headed by the director of the factory.⁵ But these measures were accused of being the “control, block and holding down” of the working class on the eve and during the period of 1966 to 1976. The “Seventy Articles on Industry” were criticized as a revisionist enterprise management program.

Related to this situation, a great wave of fervently breaking regulations and systems rose at the end of the 1950s and in the early 1960s. Many indispensable regulations and systems were abolished, which caused many serious consequences. In response to such problem, some economists proposed that reasonable regulations and systems were necessary. Each enterprise had to establish regulations and systems and examine and reform various irrational regulations and systems on the

³See Sun (1979a, pp. 140–144).

⁴See Bo (1993). In the book, he said, “Main authors who participated in drafting the regulations were several comrades including Ma Hong, Mei Xing, Liao Jili, Dong Feng and Zhang Pei”.

⁵See Rong and Wu (1999).

basis of the objective situation that had developed. “Reasonable regulations and systems are scientific regulations and systems. In general, they should conform to three criteria: (1) They should correct reflect the nature of socialist industrial enterprises and conform to the basic principles of enterprise management. (2) They should correctly reflect the objective principles in production and meet the actual needs in work. And (3) They should be accessible to common people and easy to understand, clear in order, specific in conception, and simple and convenience in formality. Among them, the first two are basic criteria and the last is specific criterion. People must strictly comply with reasonable regulations and rules.”⁶

In April 1969, Premier Zhou Enlai immediately delivered a speech after a serious quality accident occurred in the Factory No. 401 which engaged in the manufacture of airplanes because of abolishing inspection system. It was pointed out that “some people want to smash all systems. This is an extreme leftist thought trend.” People should “not just gradually but immediately restore” quality inspection system. “When reforming irrational regulations and systems, those rational should be retained. To abolish everything just does not conform to the Mao Zedong Thought and means disrespect to science.”⁷

About the Issue of Reforming Equipment Management System

In 1963, Sun Yefang wrote a research report entitled “Fixed Assets Management System and the Issue of Socialist Reproduction”. He vigorously advocated reforming the prevailing equipment management system and pointed out that “the biggest shortcoming in our enterprise management system lies exactly in the situation that the state imposes too loose control over new investment but too tight control over the extended reproduction that only needs to be realized through technical transformation and equipment updating without any new investment of the state. People have split different updating measures, such as reconstruction, overhaul, and technical innovation, which similarly belong to the scope of updating existing fixed assets, into various complex systems so that these measures were controlled according to different categories by enterprises and different competent government organs. Such practice greatly limited the progress of technology and the development of productivity and the initiative and pioneering spirit.” He suggested that people should recognize moral depreciation, increase depreciation rate, and shorten depreciable life so as to promote technological progress. They should assign the work of updating in production that belonged to the scope of original capital, including that of fixed assets or mainly technical equipment, to enterprises. Overhaul might not be more economical than replacement or reconstruction. Relevant matters should be given to the enterprises to make decisions on them.⁸ After 1976, Sun Yefang wrote another article in 1979 to reaffirm his view in the above, which was entitled “Starting with the Situation That People Must Reform the Equipment Management System Which Causes the

⁶See Rong (1960).

⁷See Zhou (1984).

⁸See Sun (1979a).

‘Replication of Age-Old Things and the Freezing of Technological Progress’” and published in the sixth issue of the magazine *Red Flag* in 1979.

The Status Issue of Profit as an Index in the Economic Accounting of Enterprises

Sun Yefang was the economist who proposed and advocated the earliest that profit should be taken as a central index in evaluating the performance of an enterprise. In 1957, he published an article and commented that, “Among various indexes in the accounting of an enterprise, there should be one that could be taken as a central one. If people grasp this one, it will drive the accounting of all other indexes. It cannot be total or net output value. Nor be it production, product type or any other index. It can only be the index of ‘profit’. Profit is the most concentrative indication of an enterprise’s performance in operation.”⁹ In 1963, he further pointed out that “Average social profit rate on funds is the standard that each enterprise has to reach. Those that achieve profits higher than average social profit rate on funds are superior enterprises. Those that fail to reach the standard are inferior enterprises.”¹⁰ Shen Jingnong had similar views. He believed that there could be only one central or commanding index rather than two or more. Otherwise, there would be nothing meaningful in being central. The central index in a system of economic accounting was the index of profit.¹¹

Similar to the view above, some article was of the opinion that cost and profit could be taken as the main indexes in evaluation the economic effect of an enterprise with equal weights attached to them. This was because product cost was the most important component of the labor consumption of product. To certain extent, the value of product cost directly reflected the value of labor consumption in the production of product. It was a comprehensive index of the technological and economic activities of an enterprise. Profit index reflected both the factor of the value of cost and the influence of other indexes on economic effects that other indexes could not reflect. Both were comprehensive indexes and should be given equal weight.¹²

It can be seen in the above that, before the reform and opening up, the Chinese circle of economics carried out very meaningful study and discussion on the issues about the autonomy, economic accounting and operation management of the enterprises and proposed many views with innovative value that exerted certain beneficial influence to economic activities in China.

⁹See Sun (1957).

¹⁰Sun (1979b).

¹¹See Shen (1962).

¹²See Yang and Li (1962).

2 Important Progress in the Reform of State-Owned Enterprises and the Theoretical Innovation of Modern Enterprises After the Beginning of State-Owned Enterprises

The reform of state-owned enterprises was the reform with the largest difficulty and the most controversy in the process of the reform of Chinese economic system. The reform of China's state-owned enterprises started in 1978. In particular, substantial progress was achieved in the reform after modern enterprise system was established as the direction of reform in the early 1990s. Although there were still some tasks in tackling and cracking key difficulties, the most difficult period of the reform of state-owned enterprises already passed. Generally speaking, the reform of state-owned enterprises in the future involves further deepening and improving new system and basically completing the task of strategic adjustment in the distribution and structure of state ownership economy. The reform of company and shareholding systems would be basically completed in large- and medium-sized state-owned enterprises. The reform in monopolized industries would be sped up. State-owned capital management system would be basically completed. In this way, the dominant role of state ownership economy would be brought into better play in national economy so as to promote the healthy development of socialist market economy.

In the very beginning of the reform and opening up, the circle of economic theories carried out discussion on the nature and status of state-owned enterprises. In early 1979, three different types of views emerged in the discussion on the reform of the industrial management system in the circle of economics in the capital. The first kind of view believed that the problem at present was not that there was too much centralization to the state but such concentration was still insufficient. The second kind of view believed that the problem at present was indeed too much centralization. But it was mainly that there was too much centralization to central authorities. People should delegate power to local authorities so that a province or a municipality had the independency and autonomy to manage enterprises. The third kind believed that the fundamental problem at present was that an enterprise lacked autonomy so that it could not bring its initiative and spontaneity into play. In the discussion, Jiang Yiwei proposed the famous enterprise standard theory. He believed that the economic system in the past was established according to the "state standard" principle. It took the entire country as a single economic organization. Central and local governments functioned as the superior organs inside this single but giant economic organization to command the branches directly affiliated to them. The "enterprise standard theory" that he advocated was completely different from the "state standard theory". He advocated that people should take enterprises as basic economic units and let them carry out "independent operation and independent accounting" under the unified leadership and supervision of the state. An enterprise was a basic unit of modern economy and it was an active organism that should possessed independent economic interests. Such economic interests were the driving power for the development of the enterprise. The state should adopt economic means

and enforce economic legislation in the management of enterprises. Jiang Yiwei's "enterprise standard theory" conformed to the reform direction of China's socialist market economy. It won the approval of many economists and workers in economy and exerted important influence to the enterprise reform later.

Echoing the "enterprise standard theory", some economists proposed the theory that enterprises be transformed from abacus beads to economic organizations that could regulate themselves spontaneously. They believed that people had to change the situation that enterprises depended on the push of administrative organs from the outside in their operation. They moved when pushed. No push no move. People should make socialist enterprises automated. Such automation of enterprises meant that enterprises exerted their spontaneity all the time and worked hard to develop socialist production and satisfy the needs of the entire society and its members.¹³ Such a position agreed with the then prevailing view that enterprises should be independent commodity producers and operators.

Driven by the innovations in enterprise theory, the reform of Chinese state-owned enterprises gradually unfolded.

The reform of state-owned enterprises started from the end of 1978 and could be divided into two major stages. The first stage lasted from 1978 to 1992. It mainly involved delegating power, conceding profit and exploration the separation of the two rights of ownership right and management right. The second stage lasted from 1993 to the present. It specifically took building modern enterprise system as its direction and constantly deepened the reform of company and shareholding systems and improved new systems.

In October 1978, six enterprises, including the Ningjiang Machine Tool Factory in Sichuan province, implemented pilot projects on expanding the autonomy of enterprises. It was determined that enterprises could take some profit retention on the basis of the growth of income and their employees might get some bonuses. It was permitted that state-owned enterprises engage in the production outside the mandatory plans of the state and that exporting enterprises keep part of income in foreign exchange at their own disposal. From 1983, the payment of profit to the government was replaced by the income tax on profit. In October 1984, the Third Plenary Session of the Twelfth CPC Central Committee made the decision on economic system reform and confirmed that socialist economy was planned commodity economy. On the basis of the requirement on developing socialist planned commodity economy, it was decided that people should comprehensively push forward the economic system reform to strengthen the dynamism of the enterprises and, particularly, of large- and medium-sized state-owned enterprises, taking cities as the key area. The goal of the reform of state-owned enterprises was that people should make enterprises truly become economic entities that were relatively independent, socialist commodity producers and operators that operated independently and assumed sole responsibility for their profit and loss, and legal persons that possessed the ability to transform and develop themselves and had certain rights and obligations. According to such a goal, the reform of state-owned enterprises turned to implementing the separation

¹³See Zhou et al. (1979).

of the two rights, namely the separation of the ownership right of the state and the operation right of the enterprises. In December 1986, the State Council proposed that people should push forward the contracted managerial responsibility system in various forms and give the operators sufficient autonomy in operation. In 1987, enterprise contracted managerial responsibility system was pushed forward in general in large- and medium-sized state-owned enterprises. By the end of 1987, the coverage of such contracted system among the enterprises within fiscal budget nationwide reached 78% and that among large- and medium-sized state-owned enterprises 80%. In 1990, over 33,000 industrial enterprises within fiscal budget finished the term of the first-round of contracting, accounting for 90% of the total of contracted enterprises. And the second round of contracting started immediately.

With the reform from expanding the autonomy of operation to delegating power and conceding profit with contracting system, enterprises started to show certain dynamism. However, contracting system also had serious defect. The “one-on-one” contracting system strengthened the mixing-up of the functions of government and enterprise. In contracting system, there was only stimulation but no restriction. Although ownership right and operation right were separated, ownership right could not control operation right. Operators abused the autonomy of operation to seek personal interests or the interests of their small groups. Such a situation caused insider control and short-term behavior so that there was the loss of state-owned assets in each round of enterprise contracting in general. The consequence was serious as it was vividly described as “making the monk rich but the temple poor”. Practice indicated that the reform of state-owned enterprises could not take contracting system as direction. People had to set establishing modern enterprise system as direction and practice system innovation. Many economists challenged contracting system and believed that contracting system could not resolve the problem of mixing up the functions of government and enterprise. It could not get different enterprises into fair competition and would cause the short-term behavior of the enterprises. They advocated that large- and medium-sized state-owned enterprises should establish modern enterprise system to replace contracting system.¹⁴ Some proposed carrying out shareholding system transformation in large- and medium-sized state-owned enterprises.¹⁵

In 1992, the Fourteenth CPC National Congress established socialist market economic system as the target model of China’s economic system reform. In November 1993, the Third Plenary Session of the Fourteenth CPC Central Committee made the *Decision of the CPC Central Committee on Several Issues on Building Socialist Market Economic System* and specifically proposed for the first time in the documents of the CPC and the Chinese government that the direction of the reform of state-owned enterprises was to establish modern enterprise system. It was

¹⁴See Wu et al. (1993).

¹⁵See Li (1987).

also pointed out that the characteristics of modern enterprise system were clearly-defined ownership title, specifically-determined rights and responsibilities, separation of administration and enterprise functions, and scientific management. From then on, the reform of state-owned enterprises entered the stage of system innovation.

Contracting system failed to promote state-owned enterprises to adapt to the development of market economy but brought forth the drain of state-owned assets and pushed many state-owned enterprises, including large- and medium-sized enterprises, into difficulty. In 1997, the CPC and the government proposed the task of helping state-owned enterprises to get out of difficulty. The target was that people should spend about three years' time from 1998 to help the majority of large- and medium-sized enterprises to get out of difficulty and that they should endeavor to initially complete building modern enterprise system in the majority of large- and medium-sized enterprises at the end of the 20th century. By the end of 2000, this target was basically achieved. At the end of 1997, there were 16,874 large- and medium-sized state-owned and state-controlled industrial enterprises in China. Among them, 6,599 ran at a loss, accounting for 39.1%. By 2000, the number of money-losing enterprises reduced to 1,800, decreasing by 3/4. In order to help large- and medium-sized state-owned enterprises to get out of difficulty, people used from 1997 to 2000 over 150-billion-RMB bank bad debt reserves, around 20 billion RMB loans with interest discount for technological transformation, and 405 billion RMB for debt-to-equity swap.¹⁶ While helping large- and medium-sized state-owned enterprises to get out of difficulty, people implemented pilot projects on modern enterprise system, gradually pushed forward the reform of company and shareholding systems, and endeavored to make state-owned and state-controlled enterprises into market entities and legal person entities adapted to the development of socialist market economy.

After many years of efforts, huge progress was achieved in China's reform of state-owned enterprises into company and shareholding systems.

First, at the end of 2005, 1,331 among the 2,524 state-owned and state-controlled enterprises among state key enterprises in the statistical data of the National Bureau of Statistics were transformed into shareholding enterprises with diverse shareholders. The coverage of the transformation was 52.7%. The coverage of medium- and small-sized state-owned enterprises exceeded 80%. Among them county-owned enterprises had the largest coverage in the transformation. This figure exceeded 90% in some counties. In 2008, 4,651 more state-owned enterprises were transformed into companies nationwide. And 2,724 collective enterprises were turned into companies.¹⁷

Second, 32 among the central enterprises, which was the backbone force of state-owned enterprises, including the Baosteel Group Co., Ltd., implemented system transformation in accordance with the *Company Law* by 2010. Pilot projects on board of directors were carried out in these enterprises. Outside directors exceeded half of the member of the board of directors in the enterprises in the pilot projects. Such

¹⁶See Zhang (2004).

¹⁷See *China Business Times*, February 25, 2009.

experimentation achieved the separation of the decision making level and executive level of the enterprises and improved corporate governance structure.

Third, the proportion of enterprises with company system among central enterprises already reached 70% at the end of the Eleventh Five Year Plan. A group of large state-owned enterprises were listed successively in domestic and overseas capital markets. At present, 52.55% of the total assets, 68.05% of the net assets, and 59.65% of the operating revenue of central enterprises came from listed companies.¹⁸

Finally, the reform of equity division of listed companies was basically completed. This was an important progress achieved in the reform in recent years. By the end of 2006, 785 among 801 state-controlled listed companies nationwide completed or launched shareholding system reform procedures, account for 98% of the total, except for the listed companies controlled by state-owned financial institutions. In the process of the reform, a large number of enterprises underwent assets restructuring. Many enterprises were shut down and went bankrupt. By the middle of the year 2008, 5,000 state-owned industrial and commercial enterprises implemented shutdown and bankruptcy projects on according to relevant policy. Ten million people were relocated. By the end of 2007, a total of 1,299 large- and medium-sized state-owned enterprises separated secondary lines of business from core business and turned secondary lines into independent companies with transformed ownership systems. 2,338,000 surplus personnel were diverted and relocated.¹⁹

Corporate governance was the kernel of the modern enterprise system. Chinese circle of economics started discussing the theory of corporate governance in the early 1990s. In 1999, it was pointed out in the Fifth Plenary Session of the Fourteenth CPC Central Committee that corporate governance structure was the kernel of company system. People needed to specifically define the functions and duties of the board of shareholders, the board of directors, the board of supervisors and the management and form a corporate governance structure with coordinated operation and effective check and balance in which each party took its own responsibilities. The practice in reform indicated that it was the most important link in the reform of large- and medium-sized enterprises into company system to establish and improve corporate governance structure. Economists pointed out that the essence of corporate governance was to resolve the issue of principal-agent relationship caused by the separation of ownership right and right of control, namely the issue on the relationship between the board of shareholders, the board of directors, and management. In China, there was also the issue on the relationship between the Three New Meetings, namely the board of shareholders, the board of directors and the board of supervisors, and the Three Old Meetings, namely the CPC committee, the trade union and the workers' congress. The board of directors held a particularly important position in corporate governance. As it was very likely that "insider control" emerged in a state-owned enterprise in China, people needed to pay special attention to and complete the system of the board of directors. The board of directors was elected by the board of shareholders and the shareholders' meeting. The board of directors was entrusted by and responsible to the

¹⁸See *China Daily*, January 25, 2011.

¹⁹See *Economic Daily*, August 28, 2008.

board of shareholders. It made decisions on the development objectives and major operation activities of the company and recruit operators and managers to implement its decisions. The relationship between the board of shareholders, the board of directors, the board of supervisors, and management was specifically defined by the Corporate Law²⁰ and such provisions became the principles for improving corporate governance. Some economists studied and compared the theories and practices abroad so as to further improve China's corporate governance.²¹

In the future, China needed to continue to push forward the reform of large- and medium-sized state-owned enterprises into company and shareholding systems. In this aspect, the task related to central enterprises was particularly urgent. Central enterprises were the backbone force of China's state-owned enterprises. By 2010, only 32 companies carried out company system reform and formed solely state-funded companies and their board of directors. Only several enterprises in total implemented shareholding system reform and realized the diversification of equity. The majority of these enterprises were waiting for the reform into company and shareholding systems. Chinese and foreign materials indicated that a company with diversified equity had much better performance than solely state-funded enterprises. Some people's calculation showed that the profit ratio of sales of solely state-funded companies in China was 6.12% in 2004 while other companies with limited liability achieved a profit ratio of sales of 6.67% and the companies limited by share achieved a profit rate of sales of 9.38%. In 2008, the profit ratio of net assets of the state-owned enterprises among the industrial enterprises above designated size was 11.71%, that of private enterprises was 25.12%, and that of foreign-funded enterprises was 16.72%.²² This indicated that the state-owned enterprises failed to achieve satisfactory benefits. Therefore, people should focus on pushing forward the reform of central enterprises and companies into company and shareholding systems. They should positively introduce strategic investors or got listed on capital market as an entire entity so as to achieve the diversification of investment entities. Important enterprise should be controlled by share by the state. And people should improve their corporate governance structure and improve competitiveness on such basis.

Some scholars proposed that the goal of reform was basically achieved at present that Chinese state-owned enterprises transform from being the attached institutions to government departments in the past to becoming the entities in market economy that operated independently. In the next stage, the deepened reform of state-owned enterprises should proceed according to the following positioning and directions. First, it should realize the direction of the reform of state-owned enterprises to stabilize general supplies in infrastructure and basic industries, which would be more favorable to the effective operation of Chinese economy in general and guaranteeing

²⁰*The Company Law of the People's Republic of China* was adopted at the Fifth Meeting of the Standing Committee of the Eighth National People's Congress on December 29, 1993. On October 27, 2005, the Eighteenth Meeting of the Tenth National People's Congress revised the law. And the revised version took effect on January 10, 2006.

²¹See He (2004).

²²See Zhang (2011).

the people's basic livelihood. Second, it should achieve a more effective functions in realizing the transformation of the mode of economic development, building major people's livelihood undertakings and projects, and realizing the key breakthroughs in the development of emerging strategic industries, and in particular, in forming crisis emergency response mechanisms that could guarantee national security. Third, it should play a positive role in the area of improving the order of market operation and the organizational structure of industries. Fourth, it would play a positive role in the direction of exerting its function as "benchmark of fairness" in income distribution and turning around the situation that there were too large gaps in the distribution of social income.²³

3 The Positioning of State Ownership Economy and the Strategic Adjustment of the Distribution and Structure of State Ownership Economy

How should people determine the status and role of state ownership economy under the condition of socialist market economy? There were different understandings and discussions among economists. One understanding with general consensus was that state ownership economy should play a dominant role in national economy in the present stage. State ownership economy should control important industries and key areas that concerned the lifeline of national economy and gradually withdrew from general competitive industries. State ownership economy should pay more attention to areas with prominent social benefits. State ownership economy and non-state ownership economy should supplement each other with their own advantages, compete in equality, promote the development of each other, and develop jointly and so on. On the basis of the understanding above, people should focus on operating well state ownership economy in general in the process of the reform of state-owned enterprises rather than seeking to operate well each state-owned enterprise.

The practice in the reform of state-owned enterprises over many years told us that it was impossible to operate well each of the more than ten thousand state-owned enterprises. A large number of medium- and small-sized state-owned enterprises that engaged in production and operation in general competitive industries did not possess advantages and showed inferior competitiveness. In the report of the Fifteenth CPC National Congress in 1997 and in the *Decision on Several Important Issues on the Reform and Development of State-Owned Enterprises* made at the Fourth Plenary Session of the Fifteenth CPC Central Committee in 1999, people proposed the task of strategically adjusting the distribution and structure of state ownership economy and the policy of focusing on large ones and letting go of medium- and small-sized ones in response to such a situation. It was required that people should operate well state ownership economy in general and bring its dominant role into play. State ownership economy mainly control important industries and key areas that concerned the lifeline

²³See Jin (2010).

of national economy, including the industries involving national security, those of natural monopoly, those that provided important public products and services, and important backbone enterprises in pillar industries and industries in high and novel technology. People should operate well large enterprises and open up and enliven medium- and small-sized enterprises.

From then on, substantial progress was achieved in the task of adjusting the distribution and structure of state ownership economy after ten years of hard work. State ownership economy and state-owned capital gradually concentrated into important industries and key areas that concerned the lifeline of national economy and into large enterprises. They gradually withdrew from general competitive industries. The situation started to change that state-owned enterprises were of a large number, extensive industry coverage, and too dispersive distribution. In 1998, there were altogether 238,000 state-owned industrial and commercial enterprises nationwide. In 2007, the number of state-owned enterprises reduced to 115,000, showing a decrease over a half. In 1997, the state-owned industrial and commercial enterprises nationwide gained 80 billion RMB profits. In 2010, the state-owned enterprises nationwide gained nearly 2 trillion RMB profits, growing by nearly 24 times. Among these, central enterprises gained 1,341.5 billion RMB and paid 1,405.8 billion RMB taxes. In 2008, the total profits of state-owned enterprise showed certain decrease due to the impact of international financial crisis and domestic economic recession, amounting to 941.9 billion RMB. Among these, the profits of central enterprises were 665.29 billion RMB.²⁴ From 2002 to 2010, the total assets of central enterprises grew from 7.13 trillion RMB to 24.3 trillion RMB. Their net assets amounted to 9.5 trillion RMB. From 2006, central enterprises started to pay state-owned capital gains to the state, which amounted to RMB 137.1 billion accumulatively.²⁵ After many years of adjustment in the distribution of state ownership economy, 82.8% of the assets of central enterprises concentrated in the eight industries of petroleum and petrochemical, electric power, national defense, telecommunications, transportation, mining, metallurgy and machinery in 2008. According to relevant statistics, central enterprises undertook almost all the oil, natural gas and ethylene production and provided all basic telecommunications services and the majority of value-added services. Their electric power generation accounted for 55% of the production nationwide. Their total turnover of civil aviation transportation accounted for 82% of the service nationwide. The turnover of water goods transportation was 89% of the figure nationwide. The output of automobiles was 48% of the figure nationwide. The high value-added steel that they manufactured was about 60% of the production nationwide. The hydroelectric equipment that they manufactured was 70% of national output and the thermal power equipment that they manufactured was 75% of national output.²⁶

Table 17.1 was a brief table about the situation in the development and reform of China's state-owned industrial and commercial enterprises from 1998.

²⁴See *Economic Information Daily*, May 7, 2009.

²⁵*People's Daily*, January 25, 2011.

²⁶See *Economic Information Daily*, August 26, 2008.

Table 17.1 Several economic indexes on the development and reform of China's state-owned industrial and commercial enterprises from 1998 to 2008

Year	1998	2003	2004	2005	2006	2007	2008	2010
Number of state-owned enterprise	238,000	146,000	136,000	126,000	119,000	115,000	113,700	
Sales revenue (by RMB billion Yuan)	6,468.5	10,016.1	12,072.2	14,072.7	16,200.0	18,000.0		
Total profits (by RMB billion Yuan)	80 (1997)	485.2	736.4	919.0	1,200.0	1,620.0	941.9	1,987.0
Profit ratio of sales (%)	0.3	3.0	6.1	6.8	7.4	9.0		
Taxes paid (by RMB billion Yuan)		814.0		1,007.5	1,400.0	1,570.0		
Number of employees	63,940,000	30,670,000	36,600,000	32,090,000				
Number of central enterprise		196			157	150	143	122
Total profits of central enterprises (by RMB billion Yuan)		300.6	487.72	637.7	768.15	996.85	665.29	1,341.5 (Net Profits: 849.0)
Taxes paid by central enterprises (by RMB billion Yuan)		356.3	465.52	577.99	682.25	830.32	991.4	1,405.8

Data Source Zhang Zhuoyuan, Zheng HATHANG ed., *Reviews and Prospects of the Thirty Years of China's State-Owned Enterprise Reform*, People's Publishing House, 2008, p. 5; *Economic Information Daily*, May 7, 2009; *People's Daily*, June 30, 2009; *People's Daily*, January 25, 2011; and *China Economic Times*, May 4, 2011

After many years for reform and system innovation, China's state-owned enterprises not only got out of difficulty but also became market entities with higher labor productivity, stronger profit-gaining ability and stronger competitiveness. State ownership economy constantly concentrated into important industries and areas in which they could exert their advantages and also into large enterprises. It stood firmly on its own position and became a backbone force in China's socialist market economy that dominated the development of national economy. This indicated that the policy of the CPC on pushing forward the reform of state-owned enterprises was correct. The several groups of figures in the following fully proved that the benefits and competitiveness of state-owned enterprises showed remarkable improvement. In 2005, the proportion of the number of state-owned and state-controlled industrial enterprises to all the industrial enterprises nationwide was 11%. But the proportion of their operating revenue to those nationwide was 35%, that of profits gained was 45%, and that of taxes paid was 57%. From January to November 2007, state-owned and state-controlled enterprises among the industrial enterprises above designated size nationwide gained 966.2 billion RMB profits, showing a year-on-year increase of 29.6% in comparison with last year, which exceeded the 25.2% increase of profits gained in collective enterprises in the same period and came close to the 35.1% increase of the profits gained in shareholding enterprises.²⁷ In the list of the top 500 Chinese enterprises in 2008, there were 331 state-owned and state-controlled enterprises, accounting for 66.2%. These enterprises achieved an annual operating revenue of 18.2 trillion RMB, accounting for 83.1% of the revenue of the top 500 enterprises. Among the top 500 enterprises in manufacturing industry in China in 2008, there were 229 state-owned and state-controlled enterprises, accounting for 45.8%. These enterprises achieved an operating revenue of 8.38 trillion RMB, accounting for 62.9% of that of all the 500 enterprises. Among the top 500 enterprises in the service industry in China in 2008, there were 278 state-owned and state-controlled enterprises, accounting for 55.6%. These enterprises achieved an operating revenue of 7.95 trillion RMB, accounting for 86.6% of that of all the enterprises.²⁸ Yet, people still need to see with a clear mind that they were confronted with some reform tasks in tackling and cracking key difficulties in the reform of state-owned enterprises and the adjustment of the distribution and structure of state ownership economy, which were expected to be completed by 2020.

At present, there were still too many state-owned enterprises in China, around 110,000 in number. The main reason for this was that there were too many local medium- and small-sized enterprises. A large number of these enterprises still operated in general competitive areas and could not bring into play the advantages of state-owned enterprises. People needed to continue to push forward the strategic adjustment of the distribution and structure of state ownership economy, such as assets restructuring. According to the data in the *Yearbook on the Supervision and Management of State-Owned Assets in China*, state ownership economy involved 94

²⁷See *Securities Times*, December 28, 2007.

²⁸See Research Team of the China Enterprise Confederation and the China Enterprise Directors Association (2009).

major categories among the 95 major categories of national economy. Among these, state ownership economy was present in 380 industries among the 396 industrial categories in national economy. The coverage of industries reached 96%. About 2/3 of the state-owned enterprises and 40% state-owned assets were distributed in the industries of general processing and commerce and trade service. The tasks in the assets restructuring of central enterprises were yet to complete. After the establishment of the State-Owned Assets Supervision and Administration Commission of the State Council in 2003, many central enterprises were restructured. The number of central enterprises reduced from 196 to 122 in 2010. It was believed in general that state-owned enterprises had advantages in the areas that involved large investment, long construction cycle, noticeable economies of scale, and prominent social benefits. Therefore, people needed to further push forward the concentration of state-owned capital into important industries and key areas that concerned national security and the lifeline of national economy and into large enterprises when adjusting the distribution and structure of national economy in the future. People should speed up forming a group of superior enterprises that possessed independent intellectual rights, internationally renowned brands and stronger international competitiveness. And state-owned capital should gradually withdraw from general competitive industries. People should also open up and enliven most of the medium and small-sized state-owned enterprises.

Some people believed that there might be too few state-owned central enterprises if the number of them were reduced to 100 in the future. They even thought that this would affect the dominant status of public ownership system. But such concern was unnecessary. Take the year 2006 as an example. In 2006, there were only 157 central enterprises in China but they possessed 16,373 affiliated enterprises. These enterprises achieved 8,293.97 billion RMB operating revenue, 768.15 billion RMB total profits, 682.25 billion RMB tax payment, and 2,463.77 billion added value. These enterprises accounted for nearly 12% of China's GDP. In particular, central enterprises controlled important industries and key areas that concerned the lifeline of national economy and played a crucial role in national economy. The enterprises mentioned here were only central enterprises and did not include local enterprises in the first place. Second, only industrial and commercial enterprises were included and not financial enterprises. If local state-owned enterprises and state-owned financial enterprise were added to them, state ownership economy would take up nearly 30% of China's GDP. So state ownership economy continued to play a dominant role. If other public ownership economies and state-owned natural resource assets and state-owned non-profitable assets were also included, there would be no doubt that publicly-owned assets took up a dominant position. The dominant status of public ownership was not affected by the deepening of the reform of state-owned enterprises and adjusting the distribution and structure of state ownership economy.

In 2009, the central authorities implemented a RMB four trillion investment stimulation plan and some local authorities such as Shanxi implemented the principle of "letting major ones run and putting down minor ones" in resource exploitation. Under such a circumstance, some economists believed that there was the problem of the advancement of state capital and the retreat of private capital in China, which was

opposite to the direction of marketization reform. Such a view triggered a discussion and different views were presented.²⁹ But because there were no statistical data that supported the view on the advancement of state capital and the retreat of private capital in general,³⁰ the discussion lasted for a while and then quieted down.

4 Introducing Competitive Mechanism and Strengthening Government Supervision—The Necessary Choice of the Reform of Super-Large State-Owned Monopolistic Enterprises

Monopolized industries were the areas where state ownership economy concentrated the most and had the strongest control power in China. Almost all the major backbone enterprises in monopolized industries were state-owned enterprises and also central enterprises. As China's reform deepened, the reform of monopolized industries already became the key area in the reform of state-owned enterprises in the future and caused extensive attention and discussion in the Chinese circle of economics.³¹

According to the spirit of the report of the Seventeenth CPC National Congress in 2007, the key tasks in deepening the reform of monopolized industries included implementing the separation of administration from enterprise management and from state-owned property management and introducing competitive mechanism, which included the introduction of strategic investors or new manufacturers, namely market entities. At the same time, people should strengthen government regulation and social supervision so as to improve the efficiency of resource allocation and effectively protect the interests of consumers.

Upon the beginning of the 21st century, the reform of monopolized industries in China gradually unfolded. But the development was imbalanced. Generally, the tasks in tackling and cracking key difficulties were yet to complete. According to the strategic arrangements on deepening the reform, people needed to push forward and deepen reform by industrial category in the future on the basis of the reform processes in different monopolized industries.

One category included electric power, telecommunications, civil aviation and petroleum industries in which people already implemented the separation of administration from enterprise management and from state-owned property management, carried out initial enterprise spin-off and introduced competition mechanism. In these industries, people needed improve reform measures and deepen reform. For example, people needed to open up market access and introduce new manufacturers to participate in market competition. In particular, people needed to open up

²⁹See "The Debate on 'the Advancement of State Capital and the Retreat of Private Capital'", *Articles for Internal Reference of the Chinese Academy of Social Sciences*, Issue 3, 2010.

³⁰"Statistical Data Did Not Support the View of 'the Advancement of State Capital and the Retreat of Private Capital'", *Beijing Morning Post*, August 2, 2010. Han (2010), Ma (2009).

³¹See Wang et al. (2002), Wang and Zhou (2004), Qiu and Wang (2006).

market in a large amount of non-natural monopolized businesses and permit domestic non-governmental capital and foreign capital to enter and participate in competition so as to improve efficiency. For example, people should implement separation of power plant and grid and price bidding for grid purchase in the sector of electric power. Telecommunications operators should engage in competition. People should allow non-governmental capital to invest and operate airlines. In 2008, seven non-governmental airlines received their operation licenses. The market of refined oil products should be opened up. Even some naturally monopolized businesses, such as production and supply of tap water and sewage treatment, could also have certain competition and hence increase efficiency through the public auction of operating concessions. In 2006, the reform of postal service, which had been considered for eight years, was launched. The separation of administration from enterprise management and from state-owned property management was initially achieved. Such reform still needed to be improved constantly.

The other category was those in which no substantial system reform was implemented yet, such as railway, salt industry, and public utilities in certain city. In these industries, people should positively push forward the reform of the separation of administration from enterprise management and from state-owned property management and of the separation of administrative units from institutional units. The reform of the investment and financing system of the railway already started. Such areas as railway construction, transportation, transportation equipment manufacturing, and diversified operation were already opened to domestic non-publicly-owned capital. However, the separation of administration from enterprise management and from state-owned property management was yet to be implemented in the entire railway industry. When discussing speeding up the reform of administration system, the report of the Seventeenth CPC National Congress proposed that people needed to explore the large ministry system with the organic unification of functions. If the separation of administration from enterprise management and from state-owned property management was not achieved in the railway department, it was very hard to establish a unified Ministry of Transport.

Domestic and foreign experiences indicated that people had to combine the introduction of competition mechanism in monopolized industry with the strengthening of government regulation and also with social supervision. People needed to strengthen the supervision both on security, environment protection and universal service and on prices, which included implementing price hearing system, so as to maintain the legitimate rights and interests of the public. In the trend of privatization in the 20th century, a large number of originally state-owned monopolistic enterprises were privatized. However, the practice indicated that privatization had great limitation. The privatization of monopolized industries brought forth many negative effects, such as damages to the environment, damages to public interests, and occurrences of major accidents, such as large area blackout. Therefore, the introduction of market mechanism into monopolized industries had to be implemented gradually and combined with the strengthening of government supervision and with social supervision.

Some economists suggested that people needed push forward the Four Transformations, namely the commercialization of operation environment, the transformation

into fair market competition, the diversification of investment entities and the transformation into scientific government supervision, in the next step of the reform of monopolized industries.³²

At present, the public had much discontent on the problems such as that the employees in many monopolized industries had excessively higher income, that the enterprises built higher access barriers to maintained their own vested interests, and that the businesses provided poor service at high charges and low efficiency. This indicated that the reform of monopolized industries was a true battle to tackle and crack key difficulties. The practical situation that the reform of monopolized industries did not proceed smoothly indicated that the reform of monopolized industries had to rely on the powerful push of the CPC and the Chinese government. People needed to boldly introduced market mechanism and to break various barriers, “glass gates” and “spring gates” set up by the vested interests. They should gradually improve regulatory systems so as to steadily push forward and deepen the reform of monopolized industries in China.

Some economists did not show approval and support to deepening the reform of monopolized industries. They feared that the deepening of the reform would affect the status and dominant role of state ownership economy. Such a view was not helpful to deepening the reform of state-owned enterprises and to optimizing resource allocation. In addition, it would cause damage to the interests of the public. Economists pointed out in their research that there were three major types of monopoly. The first type was called natural monopoly. It was based on the presence of a transmission network system and determined by the characteristics of the economies of scale and the economies of scope corresponding to such presence. Different from the situation that free competition could promote efficiency, it would be more efficient to let one enterprise rather than many enterprises operate a network natural monopolized business. This required that people strengthen government regulation and social supervision to protect consumers. The second type was called administrative monopoly, which meant to abuse administrative power to limit competition. This needed to be opposed and prohibited specifically. The third type was called economic monopoly, which included price alliance between enterprises and merger and acquisition of enterprises in an attempt to monopolize market. This also should be limited and prohibited.³³ It was gratifying that the Standing Committee of the National People’s Congress adopted and promulgated the *Anti-Monopoly Law of the People’s Republic of China* on August 30, 2007 with the efforts of various parties. The law would take effect on August 1, 2008. It stipulated three kinds of monopolistic conducts, namely that operators reached monopoly agreement, that operators abused their dominant status on the market, and that the concentration of operators had or possibly had the effect of excluding or limiting competition. It was provided in the law that the state protected the legal operation activities of the operators in the industries that concerned the lifeline of national economy. And it was prohibited

³²See Chang (2008).

³³See *A Tutorial Reader of the Report of the Sixteenth CPC National Congress*, People’s Publishing House, 2002, pp. 178–179.

that operators damaged the interest of consumers by means of its controlling status. People could believe that the common understandings achieved in the innovative study in anti-monopoly started to be incorporated into the anti-monopoly law. And with the regulation of the anti-monopoly law, the reform of monopolized industries and monopolistic enterprises would be pushed forward quickly on a track of healthy development.

5 The Reform of State-Owned Assets Management System and Relevant Theoretical Innovation

In the process of the reform of state-owned enterprises in China and, in particular, in the process of implementing the “separation of two rights” of ownership right and management right and the contracting system, the phenomenon of “insider control” in which there was the absence of owners, or owners not being in place, in general. This triggered the study and discussion on the issue of the management system of state-owned assets or capital in the circles of economic work and of economics.

The reason for the absence of owners in state-owned enterprises was that a number of departments split and exerted the functions of investor. This was compared to “five dragons regulating the rivers”, namely that the planning commission took in charge of project establishment, the economic commission of operation, the Ministry of Finance of property registration, the CPC organizational department and the personnel department of the appointment and dismissal of cadres, and labor departments of wages. However, no one was responsible for preserving and increasing the value of state-owned assets. After China implemented the tax distribution system in 1994, it became unreasonable for all the state-owned assets formed through local fiscal investment to be allocated to the central authorities in general. After the beginning of the new century, many scholars wrote articles and suggested that people should change the original system of unified ownership and level-to-level management and implemented level-to-level ownership and management and that they should combined the management of assets, people and matters. Besides, the scholars advocated that people should start with the reform of the huge operational assets management system of state-owned industrial and commercial enterprises.

As it is known, China had huge state-owned assets. According to the statistics in final accounting, China’s aggregate state-owned assets totaled RMB 9,885.92 billion yuan by the end of 2000. Among those, the total of operational state-owned assets was RMB 6,861.26 billion yuan, accounting for 69.4% of the aggregate while the total of non-profitable state-owned assets was RMB 3,024.66 billion yuan, accounting for 30.6%. The situation was shown as in Table 17.2.

What needed to be paid special attention to among the aggregate of state-owned assets was the operational assets of state-owned industrial and commercial enterprises. This part of assets showed very fast growth from 1998. The situation was as shown in Table 17.3.

Table 17.2 The aggregate and structure of state-owned assets nationwide in 2000, Unit: RMB billion Yuan

Item	National total	Central sub-total	Proportion (%)	Local sub-total	Proportion (%)
Total	9,885.92	4,793.82	48.5	5,092.1	51.5
I. Operational state-owned assets	6,861.26	4,076.85	59.4	2,784.41	40.6
A. General industrial and commercial enterprises	5,755.44	3,069.04	53.3	2,686.4	46.7
B. Financial and insurance enterprises	830.39	746.76	89.9	83.63	10.1
C. Overseas enterprises	119.57	105.19	88.0	14.38	12.0
D. Various construction funds	155.86	155.86	100	–	–
II. Non-profitable state-owned assets	3024.66	716.97	23.7	2,307.69	76.3
A. Administrative and institutional units	2,165.37	434.94	20.1	1,730.43	79.9
B. Capital construction units	859.29	282.03	32.8	577.26	67.2

Data Source See *Economic Daily*, July 26, 2001

Table 17.3 Total and net assets of non-financial state-owned and state-controlled enterprises. Unit: billion RMB

Year	Total assets	Net assets	Total assets of central enterprises	Net assets of central enterprises
1998	13,478	5,037.1		
2000	16,006.8	5,797.6		
2003	19,997.1	7,099.1	8,328	3,600
2004	21,560.2	7,676.3		
2005	24,256	8,738.7		
2006	29,000	12,200	12,200	5,390
2007	35,500		14,800	
2008			17,700	
2010			24,300	9,500

Data Source *China Economic Times*, December 24, 2007; *Economic Daily*, December 11, 2008; *People's Daily*, June 30, 2009; and *People's Daily*, January 25, 2011

In 2002, the Sixteenth CPC National Congress specifically determined the policy of reforming the management system of state-owned assets, which was to bring into full play the initiative of central and local authorities under the premise of adhering to the principle of state ownership. The state needed to formulate relevant laws and regulations and build a state-owned assets management system in which central and local governments respectively represented the state to perform the functions and duties of investors, enjoyed the rights and interests of the owners, unify relevant rights, obligations and responsibilities, and combined the management of assets, people and matters. The central government performed the functions and duties of investors on behalf of the state in large state-owned enterprises, infrastructure and important natural resources that concerned the lifeline of national economy and national security. Local governments performed the functions and duties of investors on behalf of the state with respect to other state-owned assets. From then on, China's reform of state-owned assets management system achieved remarkable effects. First, relevant institutions were formed. The State-Owned Assets Supervision and Administration Commission of the State Council was formed in 2003. After that, all the state-owned assets supervision and administration commissions of 31 provinces, autonomous regions and municipalities directly under the central government and the Xinjiang Production and Construction Corps were formed by until June 2004. At present, the work on forming the state-owned assets regulatory institutions at prefectural and municipal levels was basically completed. Moreover, people formulated the *Interim Regulations on the Supervision and Administration of State-Owned Assets of Enterprises* and its supportive regulations. *The Law of the People's Republic of China on the State-Owned Assets of Enterprises*, which was drafted in great difficulty in for fourteen years, was finally listed in the agenda of the Standing Committee of the National People's Congress in December 2007 and adopted at the Fifth Plenary Session of the Standing Committee of the Eleventh National People's Congress on October 28, 2008. The law took effect on May 1, 2009. Second, people strengthened the supervision and administration of investors. They stressed on financial supervision and risk control and carried out the pilot projects on building the board of directors in solely state-funded companies. They openly recruited senior operation and management personnel in central enterprises. By 2008, 103 senior management positions in 100 central enterprises-times were successively opened to the whole Chinese society for talent recruitment.³⁴ People also verified and determined the main businesses of central enterprises to improve the core competitiveness of these enterprises. Third, people pushed forward the reform of large- and medium-sized enterprises into company and shareholding systems and improve corporate governance structure. The coverage of the reform of central enterprises and its affiliated enterprises into company and shareholding systems improved from 40% in 2005 to 70% in 2010. 43 central enterprises fulfilled the listing of their whole main business on the stock market. There were 336 domestic and overseas listed companies controlled by central enterprises.³⁵ Besides, people regulated the system transformation and

³⁴See *Economic Daily*, December 11, 2008.

³⁵See *Shanghai Securities News*, February 23, 2011.

property right transfer in state-owned enterprises. The trading of state-owned property rights were introduced and openly conducted in property right exchange market. This avoided the drain of state-owned assets in large amounts. Practice indicated that the reform of the state-owned assets management system implemented from the Sixteenth CPC National Congress effectively pushed forward the deepening of the reform of state-owned enterprises and also the rapid development of state ownership economy and the exertion of its dominant role.

Some economists proposed that, viewed on the basis of the experience in the reform of the state-owned assets management system in recent years, people needed to adhere to the separation of administration from enterprise management and from state-owned property management in the future and further improve state-owned assets management system. The state-owned assets supervision and management commissions mainly performed the functions and duties of investors. They should reduce the work that did not belong to investors as much as possible. They should maintain various rights of enterprises that they enjoyed as market entities in accordance with the law. They should adhere to the separation of ownership right from operation right and fully respect the operation autonomy and legal person property right of the enterprises. People should promote the system and management innovation of enterprises, improve corporate governance structure, and encourage and support the development of a batch of internationally competitive large enterprise groups. They should explore effective operation forms for state-owned capital and improve the operation efficiency of capital. They should formulate and specifically define the regulatory system of state-owned natural resource, financial and non-profitable assets. Many years passed after the Sixteenth CPC National Congress in 2002 and such a task should not be delayed any longer.

Upon the approval of the State Council, the Ministry of Finance promulgated *the Measures for the Collection and Management of the Gains of State-Owned Capital in Central Enterprises* in conjunction with the State-Owned Assets Supervision and Administration Commission at the end of 2007. It was stipulated that the proportion of the profits that central enterprises should turn in should be determined on the basis of the three types of enterprises in different industries. The first type was the enterprises with resource features such as those in tobacco, petroleum and petrochemical, electric power, telecommunications and coal. And the proportion was 10% for them. The second type was enterprises in general competitive industries such as steel and iron, transportation, electronics, trade and construction. And the proportion for this type was 5%. And the third type was military industry enterprises and enterprises formed in the system transformation of scientific research institutions. The proportion for them would be determined three years later.³⁶ At the end of 2010, the Ministry of Finance transmitted to lower levels the *Notice on Relevant Matters Concerning the Improvement of the Operational Budget of State-Owned Capital Managed by Central Authorities* and specifically raised the proportion of dividend paid by central enterprises to superior authorities. After the adjustment, the proportion of the dividend collected from monopolized central enterprises such as those in

³⁶See *Securities Times*, December 12, 2007.

petroleum and petrochemical industry was 15%. The proportion of dividend collection for competitive central enterprises such as those in steel and iron industry was 10%. And the proportion of dividend collection for central enterprises in military industry and those formed in the system transformation of scientific research institutions was 5%.³⁷ This indicated that the building of the system of operational budget of state-owned capital was already launched and being improved. Some economists proposed that people should vigorously push forward the shareholding system reform of state-owned enterprises. Hence state-owned shares could gain dividends in a relatively regulated manner like non-state-owned shares. This would be beneficial to building and improving the profit payment system of state-owned capital.³⁸

There was still a large amount of work to do in improving state-owned assets management system. People needed to work harder. Even in this way, it was estimated that such work would be basically completed by 2020. Therefore, people needed to further deepen the study on the theory of the management of state-owned assets so that such reform could be pushed forward relatively successfully.

6 The Study on the Basic Experience in the Thirty Years of State-Owned Enterprise Reform

The 2008 was the 30th anniversary of state-owned enterprise reform in China. In this year, some treatises discussed the basic experience of the thirty years of state-owned enterprise reform in China. People could see in them some principles and patterns in the process of state-owned enterprise reform in China.

Some articles summarized the basic experience of the thirty years of state-owned enterprise reform in China into eight aspects:

- (1) People adhered to the direction of socialist market economic reform, made state-owned enterprises market entities that adapted themselves to market economy, and realized the reconstruction of microeconomic foundation.
- (2) People adhered to the principle of advancing progressively from delegating power and conceding profits to specifically setting the construction of modern enterprise system as direction and from clearly defining property rights to putting state-owned capital investor in place. They paid more attention to system construction and innovation and deepen the reform step by step.
- (3) People adhered to the principle of operating well state ownership economy as a whole and letting state ownership economy play a dominant role in national economy. They did not seek to operate well each state-owned enterprise.
- (4) People adhered to the principle of “focusing on large ones and letting go of medium-sized and small ones” and made efforts in operating well central enterprises.

³⁷See *Shanghai Securities News*, February 23, 2011.

³⁸Zhang (2010).

- (5) People persisted in pushing forward the reform of monopolized reform, introduced competitive mechanism and strengthened government supervision and social supervision.
- (6) People persisted in building a state-owned assets management system in which central and local governments respectively represented the state to perform the functions and duties of investors, enjoyed the rights and interests of the owners, unified relevant rights, obligations and responsibilities, and combined the management of assets, people and matters. People also sped up building the system of operational budget of state-owned capital.
- (7) People persisted in building a good external environment for state-owned enterprise reform, sped up building a complete social insurance system, pushed forward debt restructuring, and stripped off the social burdens of enterprises.
- (8) people persisted in timely elevating the successful experiences in reform into theory or law to guide the regulated progression of the reform.³⁹

Some articles summarized the basic experience of state-owned enterprise reform into the following:

- (1) Use the “trial-and-error method” as the basic methodology in state-owned enterprise reform, which respected facts and permitted errors in trials.
- (2) Select a “progressive” basic road for state-owned enterprise reform.
- (3) Adopt the “self-adaptive” basic mechanism in state-owned enterprise reform.⁴⁰

Some articles summarized the experience of China’s enterprise reform as follows: People closely combined state-owned enterprise reform and the development of non-state-owned enterprises so that the two could advance together. People set up the goal of reform as making enterprise independent commodity producers and operators and the entities in market economy. People practiced progressive reform model and gradually pushed forward the reform with centralized planning. People addressed well the relations between enterprise reform and other reforms and take implementing enterprise reform and enhancing the dynamism of enterprises as the central link. People closely combined enterprise reform with strengthening and improving enterprise management. People both relied on the authority of the central government and respected the initiative of local government and the enterprises. And people constantly improve laws and regulations to consolidate and develop the fruits of enterprise reform.⁴¹

People believed that, with the deepening of China’s enterprise reform and the further accumulation of experiences, enterprise theory would achieve further innovation and the principles and regularities of enterprise reform would be revealed more comprehensively.

³⁹See Zhang (2008).

⁴⁰See Huang (2008).

⁴¹See Chen (2009).

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Chapter 18

The Study, Discussion and Innovation in Market System Theory



Zhouyuan Zhang

The People's Republic of China was founded in 1949 and socialist transformation was basically completed in 1956. After that, the scope and role of market gradually reduced in China. In theory, market was often regarded as the opposite side of planning and an alien force to socialism. From the establishment of traditional socialist planning economic system to the beginning of the reform and opening up, China only had a rather incomplete consumer goods market. Fair trade markets were often suppressed. There were no markets for the means of production and for other factors such as capital and labor. Resource allocation was only regulated with plans. After the beginning of the reform and opening up, people started to introduce market mechanism into economic activities. The most important measure was to gradually open up market, open up price and cultivate and form market. First, they expanded and developed the markets for agricultural and sideline products and for industrial consumer goods. Then they developed the market for the means of production. And then they gradually establish and develop the markets of productive factors such as capital market, labor market and land market. After thirty years of hard work, China initially has established a unified and open modern market system with orderly competition that included commodity market and productive factor market. People were also gradually improving such market so that market began to play a fundamental role in resource allocation.

Whether the market could thrive was a sign whether there was strong economic dynamism in a society. After the reform and opening up started, China's economic dynamism kept increasing and its economic growth accelerated. The important reason for this was that people broke the confines of traditional socialist economic theory

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and gradually understood the function and role of the market. They formed relatively complete socialist market theory and established relatively sound and complete socialist market system, which brought growing prosperity to social and economic life.

1 The Study and Discussion on the Issue of Circulation Before the Reform and Opening Up Under the Circumstance that There Was Only Rather Incomplete Consumer Goods Market

After the basic completion of socialist transformation, China gradually implemented the traditional planned economic system. People stressed on the planned and unified nature of economic work and repelled market and market mechanism. They stressed on the role of the principle of planned development and repelled the role of the law of value. China's economic theory received profound influence of the book *Issues on the Socialist Economy in the Soviet Union* written by Stalin. It was believed that the law of value did not play a regulatory role in production and the means of production was not commodity. And it "gets out of the scope of the action of the law of value and only retains the appearance of commodity, such as pricing".¹ Therefore, there was the thought of despising circulation and commerce and even the thought of the "theory of no circulation" in the study of economic theory. The system and theory above determined that commodity circulation was strictly restricted within a certain scope in China before the reform and opening up. There were only a rather incomplete consumer goods market and a rural fair trade market which was often subject to limitation.

During this period, the Chinese circle of economics made study and discussion on the issue of market and circulation and proposed some valuable views.

First, Sun Yefang lectured on "An Introduction on Circulation" and criticized the theory of no circulation and the theory of national economy when he taught at the Department of Economics of the Renmin University of China in the early 1960s. He believed that there were two reasons for the generation of "the theory of no circulation" and "the theory of natural economy". First, the elimination of private ownership system and, in turn, the elimination of the blind and spontaneous market exchange caused by it gave people certain illusion. As a result, they believed that circulation, which functioned as the connective tie or played an intermediary role between various units in the division of work in the society, did not exist at least as far as the productive relations inside the whole people ownership system is concerned. Second, socialist countries generally adopted the mode of supply of providing materials, technology and equipment. This was a necessary measure adopted under the situation that there was scarcity of materials and that supply could not met demand.

¹Joseph (1962).

It was absolutely not a normal form of product exchange or circulation that emerged on the basis of division of work in the society. Sun Yefang believed that the theory of no circulation caused great harm to socialist economy and seriously obstructed people to achieve the correct understanding on socialist economy in theory. He advocated that the theory of socialist political economics should be established with the starting point set at objective economic process. Such economic process included both productive process and independent circulation process. People also needed to strictly distinguish the concept of circulation from the concept of distribution.² It must be pointed out that Sun Yefang's criticism on the "theory of no circulation" was far-reaching and insightful under the conditions at the time.

Second, some economists studied some issues on circulation economy and the principles of circulation. Xu Dixin proposed that there were three channels in socialist commodity circulation: (1) State-owned commerce was the commerce under the whole people ownership system. It was based on the whole people ownership system of the means of production. (2) Supply and marketing cooperatives were based on the collective ownership system of the means of production. It was the commerce under collective ownership system. (3) Fair trade took as its conditions the private plots and household sideline production of the members of the people's commune in the countryside and a very small number of independently operated handicraft production. The economic connections between various collective economic organizations were also the condition for the existence of fair trade.³

Some economists studied the principles of circulation. For example, some papers believed that there were ten principles on socialist commodity circulation: (1) the principle of the general transition of socialist commerce; (2) the principle that socialist commodity circulation kept growing; (3) The principle that the contradiction between social production and social needs was quickly reflected on the market and constantly connected in a planned way and then resolved through commerce; (4) The principle on the objects of commodity purchase; (5) The principle that commodity sale kept improving; (6) The principle that commodity transfer and its direction of flow became rational increasingly; (7) The principle that the capacity of commodity storage kept strengthening; (8) The principle that state-operated trade and foreign trade were of the relationship of mutual connection and restriction; (9) The principle that the expenses of commodity circulation kept decreasing; And (10) The principle that the profits of commerce kept growing.⁴ Now it seems that such exploration was meaningful.

Third, it was advocated that the means of production transferred inside the whole people ownership system should also be regarded as commodity and included in the process of circulation. In 1957, Nan Bing et al. published an article and started to criticize Stalin's assertion that the means of production distributed among state-operated enterprises were not commodities. They believed that, under the condition of the implementation of economic accounting system, various state-operated enterprises still needed to regard each other as different and relatively independent economic

²Sun (1979).

³See Xu (1964).

⁴See Chen (1963).

units as a Chinese saying went that “Even blood brothers need to keep clear accounts with each other”. So when the means of production was distributed among state-operated enterprises, it should be treated as commodity between these enterprises. Such purchase and sale economic relation was absolutely not of “notional” or “symbolic” meaning but possessed real economic content that concerned the interests of these enterprises. The authors of the article demonstrated in detail the necessity for the labor used to produce the means of production to turn into value.⁵ Fan Hong had similar views. He believed that material encouragement could, in the present stage of socialism in China, still be a relatively important factor that promoted the development of social productivity. Among the state-operated enterprises that produced the means of production, those good should be given material commendation and encouragement while those bad material criticism and punishment. In order to implement the principle of material encouragement, people needed to continue to keep the relation of commodity in the material transfer inside state-operated enterprises. In the present stage of socialism in China, all other ways could not effectively be the main method to promote productivity in the long run.⁶ The above view was fairly forward-looking and the practice in the economic life later proved that it was correct.

Fourth, the leaders of the CPC and the Chinese government also proposed important views with far-reaching influence. In 1956, Chen Yun proposed a rather original view on the relationship between planning and market. He said, “As far as production planning is concerned, the main part of the industrial and agricultural products nationwide was produced according to plans. But there was also a part of them which was produced on the basis of market change and within the scope as permitted by state plans. Planned production was the main part of industrial and agricultural production while free production on the basis of market change and within the scope as permitted by state plans was the supplementation to planned production. “China’s market is absolutely not the free market of capitalism but the unified market of socialism. In the unified socialist market, state market is its main part, but it is attached with free market led by the state within certain scope. Such free market functions as the supplementation to state market under the leadership of the state. So it is the component of a unified socialist market.”⁷

In March 1959, Mao Zedong criticized the “communism fad” characterized by “equalitarianism and indiscriminate transfer of resources”. He made the following instruction in a report, “I wrote the saying that people generally do not do old accounts in the speech at Zhengzhou. It was wrong. It should be changed into that people generally should do old accounts. Only when people do their accounts can they implement the law of value that exists objectively. This law is a great school. Only through utilizing it can we teach our cadres in millions and our people in hundred millions and can we build socialism and communism. Otherwise, nothing is possible.

⁵See Nan and Suo (1957).

⁶See Fan (1959).

⁷See Chen (1995).

We will not be able to remove the discontent of the mass and we will destroy our cadres. This is one hundred percent harmful without a bit good.”⁸

2 The Realization Problem Still Existed in Socialist Economy

After the important decision on implementing reform and opening up was made at the Third Plenary Session of the Eleventh CPC Central Committee at the end of 1978, traditional socialist planned economic system and economic theory was under continual and intense impacts. China’s economic system gradually changed onto the track of socialist market economic system and the theory of socialist market economy took root in the mind of the mass by and by.

The most important sign about the transformation from traditional socialist planned economic system into socialist market economic system was that market played a fundamental role in resource allocation and that the law of value regulated social production and circulation. And in order to bring into play the function and role of the market in regulating resource allocation, the market had to be unified and open and had orderly competition. It had to be in the form that various kinds of markets, including commodity market, capital market, currency market, land market, labor market, and technology market, were all relatively advanced and formed a unified system. Namely, it had to be a modern market system. After the beginning of the reform and opening up, China’s market system experienced rapid development and it was in the process of gradual improvement. In China, various kinds of markets were developing and gradually becoming standardized. This was closely related to the exploration and innovation in the theory of market system. Such exploration and innovation represented the efforts of the Chinese circle of economics to deepening and developing the study on the relationship between planning and market.

Over a long period of time, the Chinese circle of economics held a negative attitude toward the issue whether there was the realization problem, namely the problem of the change of form of funds, in socialist economy. It was believed in traditional socialist economic theory that the commodity-money relationship was outside socialist economy. Various kinds of labor consumption in socialist planned economy was the consumption of social labor in the beginning, namely that labor possessed direct social nature. Hence, the realization problem naturally did not exist and market issue was expelled outside the gate of socialist political economics. Therefore, if people wanted to develop socialist market system, people had to first affirm that there was the realization problem in socialism. Sun Yefang criticized “the theory of no circulation” and emphasized the study on circulation process. Thus he emphasized at the same time that there was realization problem in socialism.⁹

⁸See *Manuscripts of Mao Zedong from the Founding of the People’s Republic of China*, Book 8, Central Party Literature Press, 1993, p. 172.

⁹See Zhang (1983).

As people had confirmed the commodity attribute of socialist economy, more and more economists recognized that there was still the realization problem in socialist economy, namely that the problem that fund transformed from the form of product into the form of money. Of course, under the condition of socialism, such transformation had some differences from the change of form of the rotation of capital in capitalism. But the rotation of fund in the sense of the double-nature of commodity, namely value compensation and substitution of materials, still existed. This meant that there was still the contradiction of local labor and social labor under socialist system. And there was still the problem that the local labor of enterprise was transformed into socially necessary labor. And such transformation had certain economic interest relation with enterprises and employees. When enterprises were operated and managed well, their products were readily marketable, and they achieved high economic benefits, the enterprises and their employees could obtain more material interests. Otherwise, things would go to the opposite. It should not be that things were the same whether the operation of enterprises was good or bad. When the enterprises were operated and managed well, their particular labor consumption was lower than the consumption of socially necessary labor but the enterprises and their employees could not have more benefits. On the opposite, when the enterprises failed to be operated and managed well so that their particular labor consumption was higher than the consumption of socially necessary labor, the enterprises and their employees did not get less benefits. And it absolutely should not be that, for example, all losses and wastes should be borne by the society or the state when an enterprise produced waste products and could not sell them so that its labor expenditure was not recognized by the society and that its local labor of could not be transformed into social labor. Commodity production was the production carried out for other people or for social needs. According to Karl Marx, before commodity could be realized as value, it had to prove that it was use value because the human labor spent on commodity counted only when it was spent on a form useful to other people. But whether such labor was useful to other people and whether its product could satisfy the needs of other people could only be proved in commodity exchange.¹⁰ When a product was transformed into commodity so as to realize its value, the society, namely consumers, needed to inspect the labor used to produce such product in terms of quality and quantity. Vladimir I. Lenin said when he spoke of commodity exchange that commodity production was the productions of individual producers connected with each other through the market. Only when the products of individual producers, provided for the consumption for other people, adopted the form of money, namely only when there was the social calculation in the two aspects of quality and quantity in advance, could such products reach the hands of consumers so that the producers were entitled to obtain other social products. Such calculation was carried out behind producers through market fluctuation.¹¹

Under the condition of socialism, the society carried out social calculation on the labor in producing commodity in the two aspects of quality and quantity in

¹⁰Karl (1972).

¹¹Vladimir (1955).

advance, but it was not completely behind producers. However, as the products produced in socialist enterprises were commodities, such social calculation or inspection was necessary. In such calculation, people should first determine the average labor consumption of the products. Besides, people should, on the one hand, carry out the comparison of the effect of usefulness with respect to whether a product possessed the same quality and social use value with other products of its kind. And on the other hand, people should carry out the comparison of the effect of usefulness and social needs with respect to whether the amounts of production and supply of certain product adapted to the amounts needed in the society. Hence, whether a product possessed use value and to what extent it satisfied social needs could play an important role in transforming particular labor consumption into the consumption of socially necessary labor, namely the formation and realization of commodity value. In the past, people did not truly recognize that socialist enterprises were relatively independent commodity producers and operators, namely independent market entities. And they disrespected the role of the law of value and implemented unified purchase and sale. As a result, the problem occurred repeatedly that enterprises disregarded social needs and produced for the warehouses, which caused overstock and waste and enormous loss. Such a situation became increasingly serious when they pursued high speed and high targets one-sidedly.

The practice in socialist construction indicated that China's original economic system, which implemented the unified purchase and sale of production and the unified revenue collection and spending in fiscal administration just like that everybody ate from a big rice pot, was not at all sensible. All kinds of problems stemmed from this system. It was also the reason why some socialist countries, including China, were confronted with the situation that products became unmarketable goods that were overstocked in large amounts, which wasted social labor, under traditional planned economic system. Such a situation made people understand and stress that they should produce on the basis of demand and realize the connection between production and demand in socialist society. In order to achieve such a goal, people needed to strengthen the macroscopic regulation of social center or the state on national economy, improve the scientific quality of macroscopic regulation, and employ economic leverage to guide the economic activities of enterprises so that the activities could conform to social needs. In addition to this, the main approach was to link through market regulation the economic activities and operation decisions of the enterprises with the economic interests of the enterprises and their employees so that the enterprises could have the spontaneity and pressure to endeavor to product on the basis of demand and care about the issue of transforming their local labor into social labor. The pressure mentioned here referred to the situation that if the products produced in an enterprise were not readily marketable and did not sell well, its labor expenditure would not have the recognition of the society and its economic loss would be borne by the investors and employees of the enterprise. Hence, the realization problem became a problem that existed objectively in socialist economy. At the same time, this situation also made circulation departments the most sensitive department in the economy of a country. Many economic issues and, first of all, production issue would be exposed in the process of circulation. This was because

both blind production and construction and the disproportions of national economy would be exhibited as the situations in circulation process, such as that goods would not sell or became sold out or that cash flow became difficult or blocked and so on. Namely, chaos emerged in the entire production, supply and distribution system. The situation mentioned here that problems emerged in circulation process was in fact that there were problems in the realization of products, namely that there were problems in marketing. Obviously, the progress and breakthrough in the theories above played an important promotive role in making people recognize and attach importance to the realization problem in socialism and strengthen the study on the issue of socialist market and circulation.

As an independent economic process, socialist circulation possessed important meaning in socialist reproduction and the entire cycle of national economy. It was absolutely not insignificant. This means that market signal was the most important signal. It was the truthful reflection of the current situation in social supply and demand. Market was the hub that connected macroscopic and microscopic economies and the key link for socialist market economy to operate smoothly. The concept of market was the kernel in the conceptions of socialist commodity economy and market economy. It was crucial to explore the regularities in the development of socialist market and handle matters on the basis of the principles and laws of socialist market not only to the development of the entire national economy but also to the pursuit of economic benefits of various departments, regions and enterprises. All these greatly raised the importance and urgency of the study on the issues related to socialist market.

3 The Progress and Breakthrough of Market Theory After the Establishment of the Theory of Socialist Commodity Economy

The establishment of theory of planned socialist commodity economy raised the issue of market to a prominent position. The Thirteenth CPC National Congress proposed that “the state regulates the market and the market guides the enterprises”. This specifically determined that market would enjoy a central status in the new conception on the operation mechanism of the economy. From then on, the study of China’s market theory showed noticeable progress and breakthrough. The progress in this aspect emerged together with the practice in economic system reform and the development of the theory of socialist commodity economy. But such progress was more profound than the theory of commodity economy. When examined from the reality in market-oriented reform with the summarization of the theoretical studies and discussions in the 1980s taken into consideration, the progress and breakthrough included at least the following several aspects:

I. Market Relations Were Basic Economic Relations in Socialism and People Could Avoid the Issue of Market

Traditional economic theory in China regarded market as something alien to socialism. It negated the presence of realization problem in socialist economy, which was namely the issue of market, the double-character of labor, and the necessity to transform local labor into social labor. Hence, it laid the theoretical basis for the “big rice pot” system.

Theoretical study and reform practice proved that there was still realization problem in socialist economy, namely the issue of market. The reason why there was realization problem in socialism was because commodity relation and market relation were still basic economic relations in socialism. Although labor had certain direct social directionality, it could be truly transformed into social labor only through exchange and market. The test of the market was the best way to prove the effectiveness of labor. The pressure of the market had the strong power to break the “big rice pot” system and to promote enterprises to improve operation and management and raise their economic benefits so that the enterprises truly implemented production on the basis of demand so as to increase effective supply. The enterprises could have dynamism and hope only when they reached the horizon of the market and underwent the test of competition.

II. The Scope of Action of Market Mechanism Covered the Entire Society

From the beginning of the reform and opening up, the Chinese circle of economic theories gradually broke through the views that contained very narrow understanding on market mechanism. Namely, they broke through the idea that market mechanism was only limited to its role in commodity market and consumer goods market, which did not include housing. It was believed that, in order to establish and complete socialist market system, people needed first to expand their efforts to the range of establishing the market of the means of production as the first step, then to building the markets of fund, labor, technology, information and real estate as the second step, and finally to creating the foreign exchange market as the third step. The expansion of the scope of action of market mechanism concurred with the expansion of the scopes of commodity and of commercialization. It developed in the same pace with the opening up of the prices of consumer goods, production means and production factors. If prices were not opened up, it was impossible to bring into play the role of market mechanism. At present, people tended to agree on the following several understandings: (1) The issue of commodity economy was in essence the issue of market. (2) Commodity-market relation was the basic economic relation of socialism. (3) The scope of action of the market covered the entire society. And (4) The expansion of market relation was orderly.¹²

III. The Operation of Socialist Economy Mainly Relied on Market Coordination

Under traditional economic system, a kind of direct planning mechanism prevailed in product economy, in which the state held excessively swollen management power

¹²See Wu and Duan (1992).

and became the sole regulator of economy. In correspondence to this, it was believed in traditional theory that planning mechanism was the sole regulatory mechanism in socialism. There was no place for market coordination. Market coordination could only bring anarchic state and economic crisis. It was completely opposite to planning mechanism so that the two repelled each other. The practice in socialist construction over several decades proved that such a theory was trapped in bureaucratic fantasy. It stifled the vitality and dynamism of economic activities. And it could not ensure that social economic life achieved a normal virtuous cycle. On the contrary, it drove the economy into a dead end. There was a large amount of production only for the warehouse so that resource allocation degraded and astounding loss and waste occurred. Many economists proposed that, now that socialist economy was still a kind of commodity economy or market economy and now that commodity relation and market relation were still its basic economic relation, market mechanism, characterized by the embodiment of horizontal economic connections, became the main regulatory mechanism. The goal of China's economic system reform was to make socialist economy operate mainly in reliance to market coordination and to gradually strengthen the guiding role of the market to various economic activities of enterprises and then to social production and consumption. The state would focus more on regulating market in a planned manner so as to guide the economic activities of thousands of enterprises and lead commodity economy into the track of mutually coordinated development. The overall function of market coordination included to promote the optimization of resource allocation and achieve Pareto optimum on the one hand and, on the other hand, to improve the benefits of microscopic operation—to achieve more output with less investment through establishing the connection and competition between the two sides of production and demand.

Some articles proposed that the system basis for the organic combination of planning and market was commodity economy, the microscopic basis for such combination was the situation that enterprises truly became independent commodity producers that assumed sole responsibility for their profit or loss; the objective basis for such combination was the law of value so that market regulation was not limited to microscopic economy, and the objective condition for such combination was the establishment of the concepts of modern commodity economy and marketing.¹³

IV. The Situation that Supply Fell Short of Demand Was not the Inherent Principle in Socialist Economy

Traditional theory believed that the situation that supply fell short of demand was an inherent principle of socialist economy. From 1930, one of Stalin's view became very popular that the growth of demand backed with purchasing power always exceeded the growth of production in socialist country. He called this the superiority of socialist system. Due to the influence of such theoretical view, China suffered the shortage of material supply like some other socialist countries over a long period of time. The products of production units were like "the daughters of an emperor who never worried about their marriage". The units could not feel the pressure from the market.

¹³See He (1992).

Now more and more economists believed that the situation of supply falling short of demand and economic shortage was the product of traditional system. It was not the inherent attribute of socialist economy. China's reform of economic system was to change such phenomenon of supply falling short of demand and economic shortage. This was because that the theme of economic system reform was to develop socialist commodity economy. And this required that there was the balance between supply and demand. It was the best that a buyer's market, in which supply slightly exceeded demand, was formed. This was because that the balance between supply and demand and a buyer's market, in which supply slightly exceeded demand, was favorable to market coordination and to the development of commodity economy.¹⁴

V. Market and Planning Were not Mutually Repulsive but Complementary

Traditional economic theory believed that planning and market was mutually repulsive. There was complementary opposition between them like the two parts on a Tai Chi diagram. The expansion of the scope of planning meant the reduction of the scope of market. Various economic activities were implemented in a top-down manner which mainly consisted of mandatory plans comprised of physical targets that were broken down and carried out level by level through various planning and fiscal organs. Such practice stifled the vitality and dynamism of the enterprises.

With the establishment of the theory of commodity economy, the combination between planning and market became inevitable. From the reform and opening up, the understanding of Chinese circle of economics on planning and market underwent three stages from seeing them as being mutually repulsive, to finding their combination by blocks, and then to finding their inherent combination with mutual permeation. The complementary relationship between them was exhibited in the following: (1) Planning ensured the general coordination of macroscopic economy and controlled the balance of aggregates and the adjustment of industrial structure in the long run. Market invigorated and enlivened microscopic economy and controlled the balance of individual quantities and the adjustment of industrial structure in the short term. (2) Planning should take market as its basis and objective with the respect to the law of value while market should be put under the regulation of planning in which indirect regulation would be the main approach.

VI. To Establish Socialist Market System Was a Basic Content in Economic System Reform

As economic system reform was pushed forward, the circle of theoretical study achieved many new understandings on the important status and role of establishing socialist market system in the economic system reform. (1) The substance of economic system reform was to introduce market mechanism and enliven the market. It was the general direction of economic system reform to fully utilize market mechanism. (2) Market was the arena for the activities in commodity economy. Different commodity producers and operators competed with each other to show their superiority and achieve victory in this arena. The competitive market provided identical

¹⁴See Liu (1983).

opportunities for different enterprises so that they could race from the same starting line. (3) Market was the hub that linked macroscopic economy and microscopic economy. The state regulated the market and the market guided enterprises. This was a new operation mode of commodity economic system. (4) It was the inherent requirement of planned commodity economy to implement macroeconomic management in which the state imposed indirect control over enterprises. Such management entailed two basic conditions that enterprises operated independently and assumed the sole responsibility to their profit and loss and that market system was generally complete. (5) The establishment and completion of market system turned enterprises into real commodity producers and operators. It enabled the gradual transition of the state's management of enterprises from mainly relying on direct control to mainly relying on indirect control and mainly employing economic and legal means. Hence, a new socialist macroeconomic management system was established. (6) The market was a system of markets but not a group of markets isolated from each other. Only through establishing and improving socialist market system, could people bring into play the overall function of the market.¹⁵

Some treatises made special discussions on the establishment and development of socialist market system. Some articles held that the reform should be divided into two major stages. "The main purpose of the first stage is to build a relatively complete commodity market. The main purpose of the second stage is to establish a complete market system on the basis of improving commodity market. This is because commodity market is the premise or basis for labor market, land market and capital market both in history and in logic. Of course, these markets can not exist absolutely independently. In fact, the process of forming and improving commodity market is mutually restrictive and promotive with the process of forming and improving other markets. Therefore, while implementing the reform of establishing and improving commodity market, people should also start forming other markets in the first stage."¹⁶ John C. H. Fei and B. Reynolds, professors of the Yale University in the USA, divided China's economic system reform into the early period (1978–1985), the middle period (1986–1997), and the late period (1998–2006) in the general program of China's economic system reform (1986–2006) that they conceived. And various kinds of markets established in certain order were taken as the important marks of these three periods. The first period was marked by the emergence of monetary economy, the second period by the establishment of commodity market, and the third period by the establishment of capital market and labor market.¹⁷ Economists in some developing countries in Asia also believed that the development of market relations in a developing country was in certain order, which was roughly as follows: first establishing commodity market, then financial market and finally labor market.¹⁸

¹⁵See Chen (1988).

¹⁶See Guo et al. (1986).

¹⁷See "An Exploration on the Reasonable General Order of China's Economic System Reform", *Study Materials for Economic Workers*, Issue 11, 1987.

¹⁸See Zhang and Wu (1987).

The practice of China's economic system reform and of China's market economy proved that the above conception was correct in general. From the end of 1978, China mainly opened up the market and prices of agricultural and sideline products, then those of industrial consumer goods, and then those of the means of production. By the early 1990s, China already formed a relatively developed commodity and service market system. During the same period, productive factor markets, such as capital market, labor market, and land market, started to be established gradually and achieved certain development. There was rather noticeable mutual promotion between the development of market theory and the expansion of market system in China. As it was pointed out in some articles, China's market was gradually established and achieved development from nothing to taking form, from simple form to complex form, and from single form to its supportive forms after the start of the reform and opening up. It gradually replaced the practice formed under the planned economic system over a long period of time in which various resources were allocated through distribution and transfer. The construction of market system already reached certain scale now. First, the infrastructure construction of the market already reached certain scale. Second, market system was basically established and constantly improved. Commercial service facilities that spread all over the city and the countryside formed a giant commodity network. Diverse commercial forms emerged in succession, such as chain supermarket, warehouse supermarket, auction supermarket, flea market, e-commerce, and online shopping. Third, the rationalized pattern in which diverse entities participated in the main market structure was formed. Such structure included private, jointly-operated, and foreign operated commercial enterprises as well as state-owned and collective ones. Fourth, the fundamental role of market mechanism in resource allocation became noticeably stronger. A market-dominated price mechanism was established. And fifth, market laws and regulations were constantly improved and market management was gradually strengthened. The accession to the WTO promoted China's efforts to get in line with international standards.¹⁹

4 The Shift of Priority to Developing Productive Factor Market After the Establishment of the Theory of Socialist Market Economy

After the Fourteenth CPC National Congress determined the target model of socialist market economic system in 1992, the priority in establishing and developing market system was transferred to developing productive factor market in both theoretical research and the practice of reform because people could make the market playing the fundamental role in resource allocation only if they endeavored to develop productive factor market.

From the end of 1980s and the beginning of 1990s, many economists proposed that China needed to form a unified and complete market system. For example, some

¹⁹See Zhang and Wang (2000).

articles proposed that “socialist market system includes various types of markets, such as consumer goods market, financial market, labor market, real estate market, production means market, technology market and enterprise property right market. Only when there is a complete array of market types can there be a complete series of means in market system and can the organic connection be formed between various market parameters. This is a key point in socialist market system. Second, market system needs to be formed according to certain rules and such rules need to be uniform to various kinds of markets. For example, price needs to be formed basically with supply and demand relations on various kinds of markets. Thus, the connection between various types of price parameters can truly reflect the entire market system. There should be a complete set of market organizations and there should be various organizations that serve the market and provide adequate support. After all, the activities of the market depend on the activities of people and the activities can be efficient when there is organization. The modernized market system has to make operating organizations complete and powerful so that the market can be full of dynamism.”²⁰

In November 1993, the Third Plenary Session of the Fourteenth CPC Central Committee made the *Decision on Several Issues on Building Socialist Market Economic System*. There was a special part that discussed “the Growth and Development of Market System”. It was proposed specifically that “people must grow and develop market system in order to bring into play the fundamental role of market mechanism in resource allocation” and to “form a unified, open, competitive and orderly large market”. It was proposed in particular that “the priority in growing the market system at present is to develop financial market, labor market, real estate market, technology market and information market”. It was worth noticing that the documents of the CPC in the past always used the term “labor service market”. Here it was the first time that the term “labor market” was used specifically. Economists made their contribution in this issue because some economists spared no efforts to advocate that people should use the term “labor market” rather than the ambiguous concept of “labor service market”. They won the support some comrades in the CPC leadership so that the concept of labor market was written into the official documents of the CPC.²¹

The Chinese circle of economics started the study on labor market at an earlier time. Many people realized that labor still possessed the nature of commodity under the condition of socialism. This was the radical economic reason for the existence of labor market. For example, some economists pointed out that the combination of worker and production means under the condition of socialism was in fact still a kind of exchange relation. If people did not recognize that labor was commodity, they would definitely deny that labor had value so that they could not scientifically explain the principles of the operation of socialist commodity economy. And as commodity, labor had to depend on the market and enter the market. China practiced the labor management system characterized by centralized management and allocation over

²⁰See Li (1992).

²¹See Gao (2005).

a long period of time. The system in fact artificially closed the labor market that existed objectively.²² There were also some scholars who demonstrated the attribute of labor as commodity from the angle of labor market. For example, it was also generally accepted that the primary stage of socialism was market economy. Market economy required that all resources, including labor resource, be allocated mainly by the market. It required that productive factors, including labor, could flow freely and that labor and employment be marketized and the quantity of wages be regulated by the market. All these determined that labor had to become commodity. People could draw the conclusion that labor had to be commodity solely from the indispensability of labor market. All productive factors in market economy were commodity and labor was no exception.²³

The re-understanding on labor as commodity and labor market was of very important meaning. It was an important manifestation of the thought liberation in the study of economics and also important innovation in economic theory. This was because people would negate the necessity and economic rationality of the flow of labor as an important productive factor when they negated labor market and the attribute of labor as commodity. As a result, workers would not be able to choose their occupation independently and hence socialist commodity economy or socialist market economy could not operate in a normal manner.

China's had a population of 1.3 billion and hence the largest labor market in the world. And China was in the process of industrialization and modernization. In 2009, there were 145 million rural migrant workers in China.²⁴ But there were still about 100 million surplus labor in the countryside. These people needed to be transferred into the secondary and tertiary industries in the process of industrialization. This was also an important approach to build socialist new countryside and increase the income of the peasants. In 2009, the average monthly wage income of rural migrant workers was RMB 1,659 yuan. Being a migrant worker became an important way for peasants to change their job and increase income. It can be seen from this that it was of important meaning to vigorously develop labor market at present for the development of China's socialist market economy, the expansion of employment, and the resolution of the "Three issues of agriculture, the countryside and farmers" issue. It was pointed out in the report of the Seventeenth CPC National Congress that people should "complete the vocational education and training system oriented towards all the workers and strengthen the employment training for the transfer of rural surplus labor. They should establish unified and standardized human resource market and form the system for the equal employment of urban and rural workers". Besides, people should develop various kinds of talent markets. This was very important to encourage and guided college graduates to find jobs in the countryside and at the grassroots level. In recent years, five or six million college students tried hard to find

²²See He et. al. (1986).

²³See Jian (1999).

²⁴See *A Tutorial Reader on the Suggestions of the CPC Central Committee on Formulating the Twelfth Five Year Plan on National Economic and Social Development*, People's Publishing House (2010, p. 5).

their jobs each year, which caused great employment pressure. Moreover, people needed to improve the employment assistance system oriented towards all the mass in difficulty and timely help zero employment families solving their job difficulties. Employment was the foundation of people's livelihood. The most important thing in expanding employment was to improve market employment mechanism. Therefore, it was favorable to better resolve the issue of people's livelihood to develop various kinds of talent markets and to promote the scientific, standardized and modernized construction and development of labor market.

Besides, people needed to regulate and standardize the development of land market. China had a large population but relatively little land. Its per capita arable land was only 40% of the world's average. People had to cherish land resources very much and use them reasonably. They should strengthen land management, practically protect arable land, and strictly control the conversion of agricultural land into non-agricultural land. In 1996, China's total area of arable land was 1.951 billion *mu* (*mu* is a traditional Chinese measurement of area approximately equal to 666.67 m²). At the end of 2006, the figure reduced to 1.827 billion *mu*. The net decrease reached 124 million *mu* in 10 years. In 2010, the figure further reduced to 1.818 billion *mu*. China did not realize industrialization and urbanization yet. China's central authorities repeatedly emphasized that people needed to implement the strictest land management system. It was required in the *Compendium of the Twelfth Five Year Plan* that China's cultivated land stock should be kept at 1.818 billion *mu* by 2015. Namely, the total of arable land would not reduce any more. So the regulation and standardization of land market was particularly important. It was proposed in some articles that "people should, on the one hand, push forward the reform of land requisition system in accordance with the requirements of saving in land use and guaranteeing the rights and interests of the peasants. Thus they could gradually arrange well the distribution relations with respect to the value-added income obtained after agricultural land was turned into construction land in land requisition. In this way, the peasants could share the fruits of industrialization and urbanization in a greater extent. On the other hand, people needed to positively and steadily push forward the regulation and control of rural land and improve the management mechanisms for the circulation of rural collective operational construction land and for homestead. Thus people could endeavor to realize the requisition-compensation balance with respect to arable land requisition in the process of industrialization and urbanization, to strictly implement the management of homestead, and to guarantee the usufructuary rights of the homestead of rural households. Moreover, they should explore establishing the system to transfer the land use right of the rural collective operational construction land obtained in accordance with the law in an open and standard manner through unified and visible land market so as to realize the added value of idle collective assets."²⁵

Another problem that existed in the land market in recent years was that many local governments paid too low compensation when they requisitioned the peasant's land. The land-lost peasants only got a small amount of compensation in many places.

²⁵See Chen(2010).

They found it hard to make a living with it and it was not easy for them to find a job or other means of livelihood so that land-lost and jobless population emerged in a considerable size in China. Some economists estimated that the figure could be twenty to thirty million. It became a severe social problem. Some people estimated that the loss caused by the land loss of peasants might reach RMB one trillion yuan. Some local government requisitioned land from the peasants at a low price and then sold them to realtors or set up development zones with it to earn lots of money after they carried out infrastructure construction on the land. In 2009, the income of local governments from selling land reached RMB 1.5 trillion yuan and the figure reached a high of RMB 2.9 trillion yuan in 2010. Such a situation was ill-regulated, abnormal and unsustainable.

Technology and information markets saw very quick development. It was particularly true after people proposed working hard to improve the ability to independent innovation and speeding up developing modern service industry. In 2007, the amount of transaction of technical contract reached RMB 220 billion yuan, showing an increase of 21% in comparison with last year. In 2010, 230,000 technical contracts were signed nationwide. The amount of transaction of technical contracts was RMB 390.6 billion yuan, showing an increase of nearly 80% in comparison with 2008.

Capital market was the center of modern market system. On the basis of the actual situation in China, people needed to make efforts to develop multileveled capital market, develop corporate bond market, change the situation that the proportion of indirect financing was too high in enterprises, and raise the proportion of direct financing in them. As China's economic center, the city of Shanghai possessed relatively complete financial market system. In 2010, the total amount of transactions in financial market, that of foreign exchange market not included, exceeded RMB 380 trillion yuan. The turnover of stock transaction in the Shanghai Stock Exchange ranked the third place on the globe. The situation in this aspect was introduced in particular in a separate chapter in this book.

People had to develop various market intermediary organizations in order to establish and develop modern market system and raise the degree of marketization of China's national economy. It was pointed out in the *Decision of the Third Plenary Session of the Fourteenth CPC Central Committee* that people should "develop market intermediary organizations and bring into play their roles in service, communication, notarization and supervision. At present, people should prioritize the development of accounting, auditing and law firms, notary and arbitrary organizations, metrological service and quality inspection and certification organizations, information consulting organizations, and assets evaluation and credit assessment organizations. They should bring into play the role of industry associations and chambers of commerce. Intermediary organizations needed to pass qualification recognition procedures in accordance with the law, establish self-disciplinary operation mechanism on the basis of market rules, bear corresponding legal and economic responsibilities, and receive the management and supervision of competent governmental departments." From then on, various market intermediary organizations mushroomed quickly and gradually became the organic components of modern market system. The

Chinese circle of economics also carried out systematic study on market intermediary organizations and published many treatises on such topic.

Some treatises pointed out that, after the transformation of China's economy into socialist market economy, the government's management to economy changed from carrying out direct management to mainly implementing indirect management. It did not have direct relations with individual enterprise in general. As a result, there needed to be intermediation between the government and the enterprises objectively, namely market intermediary organizations such as industry association, trade guild and chamber of commerce. These organizations were designed to coordinate the relationship between the government and the enterprises and to transmit downwards the intent of the government to the enterprises and report upwards to the government the appeal and request of the enterprises. They also undertook some social functions and handled some economic matters that originally belonged to governmental departments. Besides, after the enterprises had transformed their operation mechanisms and went into the market, they needed market intermediary organizations to timely provided them with services in raw material purchase, product marketing, employee recruitment, information consultation, financial auditing, notarization, arbitration, credit assessment, and quality inspection. Market intermediary organizations played the role of lubricant, coordination valve and stop button under market economic system. Without the development of intermediary organizations, the normal operation of market economy would meet limitation and obstruction.²⁶ Some treatises further expounded that the market intermediary organizations that needed to be developed positively could be roughly divided into two categories. First, people needed to vigorously develop specialized market intermediary service organizations. These mainly included: (1) Legal and financial service organizations; (2) Information consultation service organizations; (3) market transaction intermediary organizations; and (4) market supervisory and authentication organizations. These organizations needed to be independent and fair and operate in a standardized manner. Second, people needed to regulate and develop industrial self-regulatory organizations in accordance with the principle of marketization. People should pay attention to retaining the non-governmental nature of these organizations so as to avoid that they turned into "secondary government".²⁷

5 Breaking Departmental Monopoly and Regional Blockade and Regulating Market Order

From 1979, China persisted in market-oriented reform and constantly broke through the old boxes in traditional planned economic system. One batch after another physical products and services turned from the distribution of mandatory plan to the

²⁶See Song (1997).

²⁷See *One Hundred Tutorial Questions for Studying the Decision of the Third Plenary Session of the Sixteenth CPC Central Committee*, Party Construction Readings Press, 2003, pp. 97–98.

market. Various productive factors also gradually entered the market so that the degree of marketization of China's national economy gradually improved. After 20 years of hard work, the degree of marketization of China's national economy already reached over 50% by the end of the 20th century. Some articles proposed that, according to initial measurement and calculation, the degree of China's production marketization reached 71.16%, the degree of productive factor marketization 41.58%, the degree of enterprise marketization 51%, the degree of adaptation of the government to the market 40%, and the degree of opening up to the outside world of the market 23.3%.²⁸ It was pointed out in some research report that the degrees of marketization of Chinese economy in 2001 and 2006 reached 69% and 77.7% respectively.²⁹ In other words, market mechanism already played a dominant role in China's social and economic life. Socialist market economic system was already established initially. Such judgment referred to the national economy in general. The degrees of marketization were different in different areas, departments and regions. Some were higher and some lower. For example, the areas of commodity and service had higher degree of marketization while the area of productive factors was lower. The degree of marketization of non-state-owned departments was higher and that of state-owned departments was lower. That of competitive industry was higher while that of some natural monopolized industries lower. That of eastern regions was higher while that of central and western regions was lower, and so on. China was a large country with vast territory and huge population. The economic development of various places was imbalanced and the development of economic reform was also imbalanced. People adopted a progressive approach in China's economic reform. They broke through from relatively weak areas in traditional planned economic system and gradually expanded and deepened the reform. Hence, it was a natural situation that different areas and departments had different degrees of marketization.

China's marketization reform was not completed yet. The degree of marketization of national economy needed to be raised further. Some treatises pointed out that China needed to make larger steps in raising the degree of marketization of national economy in the future. In particular, people needed to make new substantial steps in further breaking through departmental and industrial monopoly and regional blockade, regulate market order, and establish an open market system.

First, people needed to break through departmental and industrial monopoly and encourage market competition. At present, there were several types of monopoly in China: The first type was administrative monopoly. Functional government departments employed the power in their hands to make forced deals and required consumers to purchase the products and services that it designated at the price that it reviewed and determined. This also included the situation that local governments did not permit some commodities to enter the region under its jurisdiction or gave local enterprises some business monopolistic rights. The second type was industrial monopoly. It referred to the act of forced deal or competition restriction

²⁸See Chang and Gao (1998).

²⁹See Institute of Economics and Resource Management of the Beijing Normal University (2008, p. 3).

conducted by public utilities enterprises or other operators that possessed independent status in accordance with the law. Some industries of natural monopoly, such as electric power industry, could limit the competition in certain areas that originally allow the introduction of market competition. For example, power plants might be required to connect to power grid through price bidding. The third type was economic monopoly. For example, some enterprises set up price limitations, formed price alliance between each other, entered into anti-competition merger and acquisition between them with an attempt to monopolize the market, and so on. This was the reason why the anti-monopoly law in many countries provided that enterprise merger and acquisition should be subject to review and inspection so as to prevent such merger and acquisition from causing material injury to market competition. Except for natural monopoly, people should prevent and object the several types of monopoly in the above. After several years of hard work, the Standing Committee of the National People's Congress adopted the *Anti-Monopoly Law of the People's Republic of China* on August 30, 2007. It took effect on August 1, 2008. The law provided the legal basis for opposing monopoly and protecting competition in the future.

Second, people should break local blockade and establish a nationally unified market in which commodities and productive factors could flow freely. In the early period of the reform, local blockade exhibited under the condition of the seller's market as the situation that people set up checkpoints and kept watch and did not allow scarce materials such as grains, live pigs, cotton and coal to be sold to other places. After the buyer's market was formed in the middle of 1990s, local blockade emerged as the phenomenon that people did not allow products manufactured in other places, from beer and medicine to automobiles, to enter local market or provided various preferential treatments to the sale of local products so as to protect backward local production. Under the condition of local blockade, some commodities could not participate in fair market competition in a good way. The distortion of the market caused the distortion of market prices so that market-regulated price could not be truly formed. After China's accession to the WTO, China needed to cancel non-tariff trade barriers in foreign trade, such as quota and licenses, and permit foreign commodities to circulate freely after paying tariffs. Therefore, it violated the WTO rules to implement local blockade with administrative means. It can be seen from it that the accession to the WTO and the participation in international market competition also required to establish and improve the nationally unified market, remove various local barriers, and facilitate the free flow of commodities and productive factors in the nationally unified market. In recent years, various local blockade was restricted and opposed under the impact of the great trend of market competition. But they were not at all eliminated. Some local authorities even formulated local regulations to impose market blockade. In the future, people needed to adopt more powerful and effective measures to oppose various kinds of local blockade so that the nationally unified market could be truly established.

In order to establish an open market system, people also needed to conform to the requirements on the accession to the WTO, push forward step by step the opening up in the service areas such as banking, insurance, securities, telecommunications,

foreign trade, domestic trade and tourism, and gradually provide national treatment to foreign investments.

It was also important to regulate market order. In the early period of the reform and opening up, the situation occurred that counterfeit and shoddy products inundated and the society lacked good faith seriously soon after the market was opened up. Rectifying market order and strengthening market supervision became important functions and duties of the government at various levels. One prominent manifestation of irregular market order was that various forms of price alliances were established openly or in disguise. In 1998 and 1999, some industries implemented self-regulated industrial prices with the support of relevant competent departments. Some enterprises with good competitiveness were not allowed to sell products at prices lower than average social cost and higher than the production costs of these enterprises themselves. Such practice protected backward production and enterprises and suppressed market competition. These industries held the slogan of fighting unfair competition but formed industrial price cartel actually, which obstructed price competition and opposed the survival of the superior and the elimination of the inferior. Because such practice violated the objective requirements of socialist market economy, it was criticized and opposed by various parties. It only existed in name and then disappeared very soon. After that, price competition rose wave after wave inside these industries and showed great progress and development. In recent years, the problem emerged more often that some major enterprises inside an industry colluded to form price alliance. In response to this problem, competent departments in charge of price explicitly stated that any price conduct had to be carried out in accordance with the law. Whoever carried out price self-regulation and formed price alliance and thus obstructed market competition would be punished pursuant to the Price Law. For example, a colored-television price alliance once emerged, which obviously violated certain articles in the Price Law, such as that “operators shall not collude with each other to manipulate market prices and damage the lawful rights and interests of other operators or consumers” and “shall not make up or spread information about price rise and whoop up prices”. Manufacturing enterprises in the sectors of automobile, medicine and air-conditioner also had similar conducts. The price of medicine was falsely high over a long period of time. Pharmaceutical enterprises sold their products to hospitals at a high discount so that medicine charges became abnormally high. The citizens had great discontent about this problem. Such practice also affected the advancement of medical reform, because medicine production had very high excessive profits. Many manufacturers entered the pharmaceutical industry so that the supply of many drugs exceeded demand and a price war of drugs became inevitable. The situation affected the interests of drug producers and hospitals. A few years ago, a hospital in Chengdu summoned drug dealers, hospital pharmacies, and competent price departments to hold a joint meeting and required that drug dealers and pharmaceutical factories should not supply drugs to low price drugstores. Otherwise,

the hospitals would stop procuring drugs from these drug dealers or pharmaceutical factories. This was a very absurd occurrence.³⁰ Besides, food safety was a very prominent problem in recent years. Clenbuterol and plasticizer really made the citizens feel uncomfortable and uneasy about their own food plate. It was an urgent task in the regulation market behavior to vigorously strengthen the supervision on food safety.

The Chinese circle of economics also carried out extensive study on how to regulate market order. The book *A Study on the Market Order under the Circumstance of Transition Economy*³¹ edited by Prof. Ji Baocheng was representative in certain extent in this respect. According to the views in the book, the regulation and control of market order in China fell into the distressful situation that problems and chaos emerged repeatedly despite of repeated prohibition and regulation and the key cause to this problem was that there was great defect in the theoretical bases and measures for regulating the chaotic market order in China in the past. If people wanted to get out of such a situation and radically resolve the problem of China's chaotic market order, the most important thing was that people needed to re-understand the substance of market order and re-determine the core principle of regulating and controlling market order. It was pointed out in the book that market order was in substance the status of resource allocation and the system of interest relations characterized by harmony of interests, moderate competition, and sharing of benefits. A country needed to establish a harmonious market order. This required people to make necessary legal system construction, administrative management and moral restriction. And more importantly, people had to fully reconcile various interest conflicts, reconstruct and guide various interest relations, and radically prevent various social economic entities to gain extra benefits from disturbing market order and damaging the interests of other economic entities. Market order was the product of the situation that various social and economic entities observed various laws, regulations and codes of conduct used to maintain market order, being attracted and guided by normal and lawful interests. Therefore, the kernel principle in regulating market order should be that people carried out the reconstruction and coordination of interest relations on the basis of necessary legal system construction, administrative management and system improvement and completion. They should eliminate the interest conflicts between various economic entities, between governments and between the government and various social and economic entities so as to realize the harmonization of interests and the orderliness of market under such harmonization.

Establishing and completing social credit system was also very important. The decision of the Third Plenary Session of the Sixteenth CPC Central Committee listed it as a separate article in the content about improving socialist market economic system. It was pointed out that "forming a social credit system with ethics as support,

³⁰See *Economic Daily*, July 27, 2000.

³¹The book was published by the China Renmin University Press in December 2003.

property right as foundation and the law as guarantee is a necessary condition for building modern market system. It was also a policy that would provide a radical solution in regulating and standardizing the order of market economy. People should strengthen the credit consciousness of the whole society. The government, enterprises, institutions, and individuals should all take honesty and integrity as their basic code of conduct. People should speed up building enterprise and personal credit service system in the directions of improving laws and regulations, franchising and licensing, carrying out commercial operation, and providing specialized service. People should build credit supervision and credit breaking punishment system and gradually open up credit market.”³² At present, the People’s Bank of China and other institutions already initially established enterprise and individual credit reporting system. This would play a powerful promotive role in establishing effective credit incentive and credit breaking punishment system and strengthening the credit awareness and good faith conduct of the whole society.

China also initially completed the laws and regulations for maintaining the order of commodity market. There were laws and regulations for protecting and encouraging competition, including Anti-Unfair Competition Law, Price Law, Anti-Dumping and Anti-Subsidy Regulations, Regulations on the Administrative Punishment of Price-Related Illegal Conducts, Regulations on Preventing the Conducts of Low-Price Dumping, and Anti-Monopoly Law. There were also laws and regulations about market access and market management, such as Interim Regulations on the Management of Futures Market, Measures for the Registration and Management of Commodity Market, Measures for the Management of Wholesale Markets, Measures for the Management of Auction Market, and Opinions on the Standards and Norms for the Operation and Management of Chain Stores. At present, there were issues in this respect: First, some important laws and regulations were yet to promulgate, for example, a relatively comprehensive state-owned assets law. Second, some laws and regulations needed to be further improved, such as Price Law. And third, law enforcement was not adequate. There were many problems like that some laws were not abided by or enforced, that some market entities resisted law enforcement, that law enforcement was often disturbed by local protectionism, and so on. As socialist market economy developed toward legalization and the experience accumulated in regulating market order, the laws for maintaining market order would be gradually improved and completed in China.

³²See the *Decision of the CPC Central Committee on Several Issues on Improving Socialist Market Economic System* (October 14, 2003).

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Chapter 19

The Study and Discussion on the Theories on Industrial Structure and Industrial Organization and Relevant Progress



Jinzhui Cheng

From the founding of the People's Republic of China, the study of theories on industrial structure and industrial organization in China experienced important changes in methodology and object of study. Before the reform and opening up, the study in the theory of industrial structure was carried out within Marx's paradigm of the "two departments". The questions in the study mainly concentrated on the relations between agriculture, light industry and heavy industry. After the beginning of the reform and opening up, the study in the theory of industrial structure was carried out within the paradigm of the Three Industries of the primary, secondary and tertiary industries. The content of study included the transformation and evolution of the Three Industries and the relations between the variables of economic development stages, economic cycle and government behavior. Before the reform and opening up, there was only limited discussion on the issue of industrial organization in the directions of division of work and collaboration and enterprise efficiency. After the beginning of the reform and opening up, the study of the theory of industrial organization was basically the same as that in relevant disciplines abroad, which discussed the operation of the market and the relationship between government and market.

Focusing on the historical mission given by the times, the Chinese circle of economic studies kept exploring with the current situation in reality at certain time in the study on industrial structure and industrial organization. The study in these areas from the founding of the People's Republic of China could roughly be divided into four periods on the basis of relevant epochal background and the characteristics of research.

The chapter was expanded on the basis of the author's article "The Study, Discussion and Progress of the Theories of Industrial Structure and Industrial Organization", in Zhang (2009).

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The first period was the thirty years from the founding of the People's Republic of China to the eve of the reform and opening up. In this period, China gradually established and improved planned economic system. After the founding of the People's Republic of China, the country's economic development started with much difficulty due to weak fundamental conditions and unfavorable development environment. Besides, the central government undertook all economic functions and duties in a centralized economic system. Therefore, how to plan and guide economic development became an important function and duty of the government. It was also a topic that caused heated discussion in the circle of academic studies. In this period, how to quickly realize the industrialization of the country was the kernel question in the discussion in the theory of industrial structure. The understanding on the relations between agriculture, light industry and heavy industry also kept deepening.

The second period lasted from the beginning of the reform and opening up to the beginning of 1990s. This was the period of exploration in China's economic system reform. It was also a period in which the elements of planned economy kept decreasing while the elements of commodity economy kept increasing. Commodity economy increasingly took the place of the planned system established after the founding of the People's Republic of China so that shortage changed from an implicit problem to an explicit one and structural imbalance became increasingly prominent. The theoretical framework established for the original planned economy was not fit for the new economic situation under such circumstance. The academic circle demanded for new economic theories. To introduce new economic thoughts and apply those to analyze the reality in China became the most important characteristic in the study of the theory of industrial structure in the period. In this period, the Chinese government started to extensively implement industrial policy. The National Industrial Policy promulgated in 1989 included all major categories of industries in agriculture and industry.

The third period lasted from the Fourteenth CPC National Congress in 1992 to the beginning of the 21st century in which China officially set up the goal of its reform, namely building socialist economic system. In this period, China's price reform was basically completed, shortage economy ended and buyer's market started to take form. Under such macroeconomic background, the study of the market became a research topic that the academic circle needed to address head-on. So the introduction and application of a large amount of modern theories on industrial organization became a reasonable phenomenon. In the area of policy implementation, the adoption of the *Anti-Unfair Competition Law* and the reform of the telecommunications industry signified the start of the government's efforts to maintain the effective operation of the market and promote competition. In this period, the merging of Chinese economy into the world's economy kept deepening and the study on industrial structure under the condition of opening up also became key content in research.

The fourth period lasted from the accession to the WTO in 2001 to the present in which Chinese economy basically reached the standard of a well-off society. How to respond to the trend of globalization and how to improve the quality of economic operation became the key issue in the study of the academic circle. The conditions

of opening up and the road of industrialization were the two keywords in the study on industrial structure. The study on the theory of industrial organization unfolded, centering round the issues of enterprise competitiveness and market performance. Relatively important events in policy implementation included the formulation of state-level industrial development policies such as *Automobile Industry Development Policy* and *Steel and Iron Industry Development Policy* and also the establishment of *Anti-Monopoly Law*.

In general, tremendous change occurred to Chinese economy during over 60 years from the founding of the People's Republic of China. The study on the theories of industrial structure and industrial organization experienced constant adjustment and change with the evolution of the times. The progress of the research of the academic circle in this area during the 60 years from the founding of the People's Republic of China mainly included contents in five aspects: the translation and introduction of relevant foreign economic thoughts, the study on industrial structure in reality, the study on the policy of industrial structure, the study on industrial organization in reality, and the study on the policy of industrial organization. In the following, the author would give a brief account on the research progress in the five aspects in the theories on China's industrial structure and industrial organization during the four periods from the founding of the People's Republic of China as defined in the above.

1 Research Progress from the Founding of the People's Republic of China to the Eve of the Reform and Opening up

After the founding of the People's Republic of China, how to quickly develop economy and realize industrialization became the most important task of the Chinese government. In the 1920s–the 30s, the Soviet Union quickly realized industrialization through developing heavy industry and became the sole superpower that could rival the USA in the world after the World War II. The guiding thought in such achievement was the principle of prioritizing the growth of the production of the means of production proposed by Lenin and the statement of Stalin that the road of socialist industrialization started with heavy industry. The Chinese government and academic circle paid great attention to the success of the Soviet Union. Many important policies and theoretical studies and discussions in China took the statements of Lenin and Stalin as starting points.

I. Exploration and Discussion on the Theory of Industrial Structure under the Framework of Reproduction

(I) The Theory of Reproduction

Marx discussed the reproduction of capitalist society and its structural proportions through the two-fold division of aggregate social product. Namely aggregate social

product could be divided into constant capital, variable capital and surplus value in the form of value and into the means of production and of consumption in the form of use value. Chinese economic scholars believed that there would definitely be certain comparative relations between various sectors and the two departments of social production in any form of society. Marx's reproduction theory possessed generality so that people could employ such theory to analyze China's socialist economy. The difference between socialist society and capitalist society laid in that the comparative relations of social production were formed in an anarchic way in capitalist society while they were formed in a planned way in socialist society. Such difference was determined by the different modes of possession of the means of production in the two forms of society.¹ Proportional relations could be realized in different ways in different forms of society. When analyzing the proportional relations in the structure of China's national economy, people should focus on examining two proportions: one was the proportion between the production of the means of production and that of the means of consumption and the other was the proportion between industry and agriculture.²

Some scholars attempted to expand Marx's reproduction model. Dong Fureng broke down the mode with respect to the products in the two major departments according to their final direction of use when concretizing Marx's reproduction formula. He introduced the factors in the different approaches to achieve extended reproduction into the reproduction formula and then examined the changes of different parameters in such formula, such as those between labor productivity and worker production-fund-to-equipment ratio, between the labor productivities and the average actual income of workers in the two departments, and so on. He also made other beneficial explorations on the deepening of the reproduction formula.³ These attempts of his expanded the possibility for the formula of social reproduction to reflect various proportional relations so that it could be used to analyze more specifically the changes in the major proportions in social reproduction.

(II) The Principle of Prioritizing the Growth of the Production of the Means of Production

On the basis of Marx's Reproduction Theory, Lenin pointed out that technological progress, increase of labor productivity and rise of the organic composition of capital were all inevitable phenomena brought about by the replacement of manual labor with machine production and the constant technological progress on the basis of machine production. On such basis, Lenin summarized the principle of prioritizing the growth of the production of the means of production. Such principle became an important guiding thought for China's economic development from the founding of the People's Republic of China to the eve of the reform and opening up.

Chinese scholars made extensive discussion on the principle of prioritizing the growth of production of the means of production. Ding Xiaokui used mathematical

¹ Wu (1957).

² Editorial Office of Economic Research Journal (1959).

³ Dong (1963a), (b), (1964).

method to prove the principle of prioritizing the growth of production of the means of production under extended reproduction and examined the role of various factors and relations of reproduction in the growth of production in the two major departments.⁴ Zhang Huaxia pointed out that a simpler formula could be used to replace Ding Xiaokui's complex formula and that Ding Xiaokui used unnecessary hypotheses to prove the principle. Zhang Huaxia believed that the prioritization of the growth of the means of production under extended reproduction was a general principle.⁵ The generally-accepted view in the academic circle at the time was that the principle of prioritizing the growth of production of the means of production was applicable to China's socialist extended reproduction. Such principle had important theoretical and realistic meaning for people to study socialist reproduction, formulate economic development plans, and study the balance sheet of national economy.

The prioritization of the growth of production of the means of production meant that the development of some departments was faster in economy in reality. Yang Jianbai believed that the general trend of socialist economy was to develop in a proportionate manner. But there were certain imbalance and disproportion in the process of economic development. When confronted with the imbalanced development between different department, people should adhere to positive balance, object to negative balance, and take key proportional relations in hands.⁶ In addition, the principle of prioritizing the growth of the means of production was limited by the means of livelihood. Ji Chongwei proposed in earlier time that the means of consumption should also be kept within certain growth proportions so that people could guarantee the satisfaction of the often increasing needs in material and cultural life in the whole society.⁷

(III) The Issue of Input and Output between Different Departments

In the 1940s–the 50s, the capitalist world kept deepening the study on input and output while the socialist camp carried out the study on the balance relations among the connections of different sectors on the basis of Marx's reproduction theory. The balance sheet of sector connections in the socialist camp had the same features with the input-output tables in the capitalist world in many aspects. The Chinese academic circle started to introduce the balance sheet of sector relations in the beginning of 1960s. The balance sheet of sector relations included that represented in currency and that represented in kind. People could resolve the issue on the linking between the balance sheet of national economy and the balance sheet of particular products and materials through the study on the economic content, statistical organization and mathematical processing of the balance sheet of sector relations. Such balance sheet also allowed the introduction of a new index—complete consumption index—for planning work. People could also employ the approaches in mathematical programming to determine the optimal plan among a series of possible balance plans.

⁴Deng (1956).

⁵Zhang (1957).

⁶Yang (1960).

⁷Ji (1958).

Chinese scholars believed that the balance sheet of sector relations could improve the quality of planning work and put planning work on the basis of more accurate calculation and analysis.⁸ In the 1970s, China prepared the first material-type balance sheet of sector relations. This document included 61 main products in 1973 and covered about 85% agricultural products, 30% light industry products, 60% heavy industry products, 43% construction industry, and 66% rotation volume of goods transport.⁹

II. The Study on the Policy of Industrial Structure

(I) The Selection of the Road of Socialist Industrialization

After the founding of the People's Republic of China, the most fundamental task that China faced was to build a complete industrial system and realize industrialization as quickly as possible. In the early period of The People's Republic of China after its foundation, the country only had very weak basis in heavy industry and the capitalist world imposed trade embargo and blockade on China. Besides, the view proposed by Stalin was very popular at the time: Capitalist industrialization started with light industry while socialist industrialization started with heavy industry. Prioritizing the development of light industry was the road of capitalist industrialization while prioritizing the development of heavy industry was the road of socialist industrialization.¹⁰ Chinese scholars believed that prioritizing the development of heavy industry conformed to the principle about the comparative relations between the two major departments in extended social production proposed by Marx. Heavy industry mainly realized the production of the means of production while agriculture and light industry mainly realized the production of the means of consumption. The mutual relations between agriculture, light industry and heavy industry reflected the relationship between the two major departments of social production. The proportional relationship between the production of the means of production and that of the means of consumption were concretized through the proportions of agriculture, light industry and heavy industry.¹¹ Hence, China's industrialization undertakings took the development of the production in heavy industry, namely the production in the industries of the means of production, as its basis.

It was generally believed that the basic content of socialist industrialization was to make the output value of modern industry have considerable proportional advantage in the gross output value of agriculture and industry and make modern industry the leading force in national economy. Wang Sihua pointed out that China had to have highly developed heavy industry in order to realize its national industrialization and had to start the construction of socialist economy from building and developing heavy industry. But while developing heavy industry, people needed to adopt various measures to guarantee the development of agriculture, light industry, transportation

⁸Wu and Zhang (1962).

⁹Jiang Xiaojuan, "The Theories of Industrial Structure and Industrial Organization", in Zhang (1999), p. 471.

¹⁰Editorial Office of Economic Research Journal (1986), p. 337.

¹¹Yang (1959), Yu (1960).

and cultural and educational undertakings in correspondence. In particular, people needed to guarantee the development of agricultural production in correspondence because agriculture not only determined the speed of industrial development but also constituted an important condition for realizing socialist industrialization.¹²

Yang Jianbai proposed the conditions to apply the principle above in the road of industrialization that prioritized the development of heavy industry. The first condition was the actual standard of the productivity of heavy industry. The second condition was the degree of adaptation of agriculture, light industry and other sectors to the demand of heavy industry and the degree of demand of these sectors to the products of heavy industry. The third one was the scale of labor resources and material resources in the whole society and, in particular, their scale of accumulation. These three conditions were mutually connected and inseparable. They converged at one point, namely that industrialization was determined by the scale of accumulation and the direction of its use.¹³

In policy practice in reality, China set the capital construction of industry as the center of the First Five Year Plan, in which it was specifically stipulated that people would concentrate main forces and resources to develop heavy industry. From 1952 to 1956, the average annual growth of the production in heavy industry in China was 23.9%, that in light industry 14.8%, that in handicraft industry 12.6%, and that in agriculture 4.4%.¹⁴ The effect of implementation of the First Five Year Plan showed that the result completely met the policy design that prioritized the growth of heavy industry.

(II) From Prioritizing the Growth of Production of the Means of Production to One-Sidedly Pursuing “Taking Steel as the Central Task”

The successful completion of the First Five Year Plan caused the central authorities to wrongly estimate the situation and believed that China could further speed up its economic development and industrialization process. The principle of prioritizing the growth of the means of production was summarized as the guiding thought of prioritizing the development of heavy industry and then further as prioritizing the development of steel and iron, coal and machine tool. It was believed that people had to guarantee key areas in industrial production and construction. The central issue of industry was the production of steel and iron and of machinery and the development of machinery was determined by the development of steel and iron production. Hence, the guideline was proposed of achieving full-scale leap-forward through taking steel and iron and machinery as the leading areas, electric power, fuel and transportation as the pioneering areas, and steel as the central task. During the period of 1958–1960, it was required that steel and iron production be doubled within one year in 1958 and the slogan was proposed that “the output of steel and iron and other major industrial products catches up and exceeds that of the UK within fifteenth years or shorter time and people might also endeavor to basically realize

¹²Wang (1956).

¹³Yang (1961).

¹⁴Wu (1957).

such goal within the time of around ten years.” The mainstream thought during the period of 1958–1960 was to pursue high targets in steel and iron and other heavy industries unrealistically and take such targets as the sign that distinguished socialist industrialization from capitalist industrialization.¹⁵

(III) Recognizing the Fundamental Role in Agriculture

Although Marx’s reproduction theory emphasized the decisive role of the prioritized development of the first major department to the growth of the production in the second major department, it also pointed out that the growth of the second major department had a restrictive role to the prioritized development of the first major department and hence was necessary. Chinese scholars pointed out such issue in the later period of the First Five Year Plan. The period of 1958–1960 taught people a bitter and painful lesson, the central authorities became aware of the importance of the second major department and, in particular, the development of agriculture.

Many scholars pointed out that people needed to put the development of agriculture on an important position because China had a huge population and weak economic foundation. During the First Five Year Plan, China’s average population growth rate was 2.2%, which was much larger than the growth rate of arable land. The development of agriculture in China could not meet the requirements in the development of the entire national economy and industry. Rural surplus labor was the material basis for the existence and development of all other sectors in national economy. The specific indication of such a situation was that agriculture supplied food, industrial materials, labor, fund and market to other sectors in national economy. So China had to further vigorously develop agriculture so as to guarantee the planned population growth and the improvement of the people’s living standard. Industry and agriculture formed a reciprocally dependent, supportive, promotive and developing relationship. People needed to guarantee the fundamental state of agriculture in national economy.¹⁶

Early in 1956, the central authorities proposed at the policy level the “Compendium on the Development of Agriculture from 1956 to 1967 (Draft)” and raised the development of agricultural production to a very important status. In the spring of 1957, the central authorities further proposed the guideline of concurrently developing industry and agriculture on the basis of prioritizing the development of heavy industry. However, these policies were all disrupted by the left-deviated thought from the period of 1958–1960. After the bitter and painful experience from the period of 1958–1960 and the Three Years of Difficult Time, various areas made deep and profound reflections on the limitations in developing heavy industry one-sidedly. In the early 1960s, the central authorities proposed that the arrangements in the plans of national economy should follow the order of agriculture, light industry and heavy industry. This order also represented the arrangements about the proportions of the two major departments in agriculture and industry.

¹⁵Editorial Office of Economic Research Journal (1986), p. 40, 338.

¹⁶Ji (1958), He (1958), Wang (1962), Xu (1962).

III. The Studies Related to Industrial Organization

(I) The Issue of Division of Work and Collaboration

The issue of division of work and collaboration on the basis of specialization was relatively close to the study of industrial organization. People mainly introduced the theories of the economists in the Soviet Union at the time to propose their theoretical framework and establish basic line of thought in research in the study on division of work and collaboration on the basis of specialization in China. The treatise introduced and translated in China the earliest in this area was the *Specialization and Collaboration of the Industry in the Soviet Union* written by L. Berri. The treatise written by Chinese scholars in this area in earlier time was *The Specialization and Collaboration of Socialist Industrial Production*¹⁷ written by Ji Ming.

Fei Wuwen et al. proposed that people needed to establish and complete enterprise responsibility system. They believed that enterprise responsibility system was the objective requirement in socialist socialized production. It reflected the mutual relations of people in production and work. And it was represented in certain regulations and systems. There were precise and strict relations of division of work and collaboration between various enterprises under the whole people ownership system. And each enterprise itself contained a complex system of division of work. Because of these, a strict enterprise responsibility system was necessary for guaranteeing the regular production in each enterprise and also the entire society. The substance of such system was to correctly handle in an enterprise the contradictions between productivity and productive relations and between economic foundation and superstructure. People should mobilize all positive factors to guarantee the systematical progression of production and ensure that enterprises constantly improved their labor productivity and completed in full scale and over-performed state plans.¹⁸

(II) The Issue about How to Treat Large Enterprises and Medium- and Small-Sized Enterprises

Enterprises of different sizes played different roles in economic life. In earlier time, some scholars proposed that China needed to have a sizable group of large enterprises and to develop medium- and small-sized enterprises. Large enterprises possessed the technological conditions for modernization and high production efficiency and they functioned as the “locomotive” that drove the great development and advancement of the entire Chinese national economy. And medium- and small-sized enterprises could easily have better combination in the areas of production, supply and distribution. Medium- and small-sized enterprises could promote the balance between the economies of various regions and speed up narrowing the gaps between the city and the countryside and between workers and peasants. Adopting the policy of

¹⁷Jiang Xiaojuan, “The Theories of Industrial Structure and Industrial Organization”, in Zhang (1999), p. 472.

¹⁸Fei et al. (1962).

combining large, medium- and small-sized enterprises was in fact to draw from each other's strengths to make up for their own weaknesses.¹⁹

However, the enterprises did not have the power to make decisions on planning. They lost the internal mechanism and motivation to handle well microscopic balance. They could not timely resolve a series of problems in their own production and operation and always rely on the central authorities and competent departments in everything. As a result, both large enterprises and medium- and small-sized enterprises were confronted with the problem of low efficiency.²⁰

2 The Progress in Study from the Beginning of the Reform and Opening Up to the Early 1990s

In the beginning of the reform and opening up, the imbalance of industrial or economic structure was one of the most important issues in Chinese economy in reality. The academic circle introduced and drew from western theories on industrial structure for the discussion of the issue. The most fundamental move in such practice was to introduce new analytical paradigm, namely the method to analyze economic structure with the Three Industries of primary, secondary and tertiary industries. In comparison with the original paradigm, the most prominent characteristic of this paradigm was to recognize the important status and role of non-material productive departments in economic activities. The specific theories that were introduced and drawn from included those about the division of the Three Industries, the relationship between the change of industrial structure and population employment structure, per capita income, and economic development, and the basis for changing the division of industrial structure. Chinese scholars used these theories to analyze the current situation in China, which included the current situation, characteristics, issues and directions of adjustment of China's industrial structure. Besides, because the industrial policy of Japan achieved success in practice, the introduction of the thoughts on industrial policy and their practice in China also became an important topic in discussion. During this period, Chinese scholars also started to introduce modern theories on industrial organization and discussed the issues on competition and monopoly under current situation, and the stimulations to change the low-standard operation of the enterprises.

I. The Introduction of Foreign Economic Thoughts

(I) About the Translation and Introduction of the Theories on Industrial Structure

In 1985, Yang Zhi used the term "industrial economics" in the title of his book in China for the first time and published *An Introduction to Industrial Economics*, which exerted large influence in China. During the same period, a large number of

¹⁹Chen (1958).

²⁰Editorial Office of Economic Research Journal (1986), p. 323.

foreign classical works on the theories of industrial structure were translated and introduced in the Chinese academic circle at the end of 1980s. Some works that had far-reaching influence included *Economic Growth of Nations: Total Output and Production Structure* and *Modern Economic Growth: Rate, Structure, and Spread*, written by Simon Smith Kuznets, *Industrialization and Growth: A Comparative Study*, written by Hollis B. Chenery, and *Structural Analysis of Japanese Economy*, written by Toshio Sanuki.

The theories of industrial structure translated and introduced mainly included the following several important thoughts:

1. The Introduction on the Classification of the Three Industries

In the book *An Introduction to Industrial Economics*, Yang Zhi systematically introduced the concepts and classification of the Three Industries and their performance in different stages of economic growth. In early 1980s, the introduction of the paradigm of the Three Industries once triggered intense argumentation in the academic circle in China. But after the middle of 1980s, the academic circle basically recognized the scientific nature and strong practical explanatory power of such classification. The introduction of the thought of the Three Industries broke the framework in original paradigm of the two major departments which only stressed the production of physical materials and recognized the importance of the tertiary industry which included service industry. It opened up a new horizon for Chinese scholars. The scholars applied the paradigm to carry out a large amount of research on the actual situation in China. It is worth mentioning that China's official sources started to publicize relevant data on the three industries in *China Statistical Yearbook 1988*. The data provided support to the academic circle so that people could use statistical data to further study the issues about China's three industries.

2. The Inherent Connections between the Evolution of Industrial Structure and the Indexes of Economic Development, Employment and Income

In the 17th century, British economist William Petty summarized on the basis of the actual situation in the UK at the time that the center of industry would gradually shift from the production of tangible properties to intangible service production as the economy developed constantly. In the 20th century, Colin Clark, another economist, expanded Petty's research. It was pointed out in Petty-Clark Theorem that labor was gradually transferred from the primary industry to the secondary industry and then to the tertiary industry as the economy developed.²¹ Simon S. Kuznets summarized the model of the evolution of industrial structure: In the stage of lower per capita output, the shares of agricultural department and non-agricultural department exhibited the change of the former decreasing while the latter increasing. The share of non-agricultural sectors increased largely but its internal structure, which involved industry and service industry, showed little change. When per capita output became larger, the shares of agricultural and non-agricultural departments showed

²¹Yang (1985).

little change but the proportion of service industry in non-agricultural department showed more noticeable rise.²² In Chenery's theory, it was believed that economic development could be divided into three stages and the structural evolution of the Three Industries accompanied the changes in these stages. The first stage was the stage of the production of primary product. The production of agricultural products and other primary products dominated but the production of primary products was slower than the production in manufacturing industry. The second stage was the stage of industrialization, the structure of production showed the quick shift from the production of primary products to manufacturing industry. The third stage was the stage of developed economy. The proportions of manufacturing industry lowered in economy and employment. Service industry gradually became the main department that drove economic growth.²³ Walther G. Hoffman believed that people had to pay more attention to the ratio of the net output of consumer goods industries and that of capital goods industry, namely the Hoffman Coefficient. In the process of industrialization, the value of such coefficient kept lowering; so the coefficient could also be used to judge the specific process of industrialization.²⁴

3. The Introduction about the Thoughts on Industrial Policy

The thought of the dominance of industrial policy believed that the government could play a positive role through industrial policy in the process of economic development on the basis of discovering the principle of the change of industrial structure. So the theory of industrial policy was the representation of the theory of industrial structure at the level of application. Toshio Sanuki discovered through analyzing the industrial development in Japan after the World War II that the development of the industry in Japan after the World War II experienced three successive stages, which were respectively the stage in which the electric power industry developed as a dominant industry, the stage in which the petroleum, petrochemical, steel and iron, and shipbuilding industries became dominant, and the stage in which high income elasticity industries such as automobile and house appliance industries became dominant industries. Toshio Sanuki believed that the replacements of dominant industries in the process of industrial development were in the following order: Light industry—raw material industry—processing and assembly industry. The dominant industries in different stages were textile industry, petroleum, petrochemical and steel and iron industries, and automobile and household appliance industries.²⁵

(II) The Introduction on the Theory of Industrial Organization

The basic theory on industrial organization appeared in some textbooks on microeconomics that were translated and introduced into China in earlier time. Yet *Market Power and Economic Welfare: An Introduction*, a treatise authored by William G.

²²Simon (1985), (1989).

²³Hollis (1989).

²⁴Yang (1985).

²⁵Toshio (1987).

Shepherd, might be a complete work translated and published in mainland China in earlier time. In 1985, the Economic Development Institute of the World Bank and the Tsinghua University School of Economics and Management jointly held an economic management workshop, in which a course on the theory of industrial organization was taught. This might be the earliest course on such theory taught systematically in China in record.²⁶ There was a special chapter that introduced industrial organization in *An Introduction to Industrial Economics* by Yang Zhi published in the same year. These works and courses played a positive promoting role in the dissemination of the theory of industrial organization in China. In late 1980s, the works of George J. Stigler and Kenneth W. Clarkson were translated and introduced into China. *Industrial Organization and Government Regulation* was a book of papers collected and translated from two books written by George J. Stigler, which included classical literature in the development of the theory of industrial organization, such as “The Economies of Scale” and “What Can Regulators Regulate? The Case of Electricity.” *Industrial Organization: Theory, Evidence and Public Policy* was a standard textbook authored by Kenneth W. Clarkson. It covered all important contents in the area of industrial organization at the time. An important feature of the book was the discussion on the legal issues concerning competition and monopoly.²⁷ These important works and translations exerted far-reaching influence on the scholars at the time.

II. The Study and Discussion on Industrial Structure

(I) The Study on the Issues Present in China's Industrial Structure

From the end of 1970s to early 1980s, the Chinese circle of economics carried out a research project on economic structure, or industrial structure, under the organization of the Finance and Economy Committee of the State Council, which was of very large scale and influence. A large number of research reports were published. The study on the issue of industrial structure at the time was to summarize the experiences and lessons during the 30 years after the founding of the People's Republic of China. The researchers pointed out that the irrationality of China's economic structure was mainly seen in the disproportions between agriculture, light industry and heavy industry and between basic industry and processing industry. The reasons that caused such structural irrationality included one-sidedly pursuing the prioritized development of heavy industry and one-sidedly stressing the principle of prioritizing the growth of the means of production and so on.²⁸ Some scholars believed that there were three lessons that could be learnt from the situation that China's light and heavy industries had irrational structures and did not achieve coordinated development: The first lesson was that heavy industry grew too fast and light industry became relatively backward. The second one was that light and heavy industries underwent large rises

²⁶Jiang Xiaojuan, “The Theories of Industrial Structure and Industrial Organization”, in Zhang (1999), p. 483.

²⁷William (1980), George (1989), Kenneth and Roger (1989).

²⁸Ma and Sun (1981).

and falls and became very unstable. The third one was that the internal structure of light and heavy industries were irrational, which was mainly seen in the facts that the proportion of self-service work was too large in heavy industry and that the proportion of work used to serve production was too large in light industry.²⁹

Yang Jianbai et al. also carried out in-depth study and discussion on the situations and issues of industrial structure during the 30 years after the founding of the People's Republic of China. Their article "On the Historical Experience of Our Country in the Relations between Agriculture, Light Industry and Heavy Industry" had larger influence. In the article, the scholars made basic judgment on the structure of China's national economy around 1980. They believed that China changed in the 1950s from an agriculture-industry country, in which agriculture dominated, to an industry-agriculture country, in which industry dominated. They studied the historical development processes of agriculture, light industry and heavy industry from the founding of the People's Republic of China by different time periods. They believed that the three were basically coordinated from 1949 to 1957 in the early period after the founding of the People's Republic of China, that the periods from 1958 to 1962 and from 1966 to 1976 were both periods of disproportion, and that the periods from 1963 to 1965 and from 1977 to early 1980s were both periods of adjustment. In the opinion of Yang Jianbai et al., the main reasons for the disproportion of agriculture, light industry and heavy industry included too high accumulation rate, deformed allocation of national investment, scissors differentials in the prices of agricultural and industrial products, and the direct damage to agricultural production caused by human reasons in China.³⁰ In their analysis on agricultural production from the early period after the founding of the People's Republic of China to 1984, some scholars pointed out that China still showed the most noticeable characteristic of a low-income country, namely too large share of agriculture in economy.³¹

(II) The Adjustment or Rationalization of Industrial Structure

As to the issue of how to correctly handle the relations between agriculture, light industry and heavy industry and to adhere to the Chinese industrialization road, Yang Jianbai et al. believed that people needed to take agriculture as the foundation, adhere to the Chinese industrialization road, change the structure of the production in heavy industry and make it adapt to the needs for developing agriculture and light industry, and adhere to following the order of agriculture, light industry and heavy industry in economic development.³² Some scholars proposed the countermeasures for rationalizing the structure of light and heavy industries: realizing the strategic change of the production in light industry and guaranteeing the steady growth of light industry; both guaranteeing the prioritized growth of heavy industry and properly controlling the scale and speed of heavy industry.³³ Song Zexing took Liaoning province

²⁹Sun (1984).

³⁰Yang and Li (1980).

³¹Research Group on Rural Development in China (1986).

³²Yang and Li (1980).

³³Sun (1984).

as an example in his discussion and believed that people should, in the adjustment of economic structure, pay attention to the proportions between accumulation and consumption, the weak links in economic structure, the coordinated development between various departments, and the coordination and cooperation between local and national economic structures.³⁴ Li Jingwen et al. proposed that people had to rely on technological progress in promoting the rationalization of industrial structure so as to realize the advanced development of industry. The basic principles in adjustment industrial structure included coordinated development, best benefits, consumption orientedness, technological progress, and employment demand. And among these, the first two were the most fundamental.³⁵

(III) The Study about the Tertiary Industry

With the translation, introduction and discussion of the classification of the Three Industries in Chinese academic circle, more and more scholars realized the scientific nature of using such classification. The study of Li Jiangfan was completed and published earlier and achieved greater influence. He proposed that people needed to consider the proportions not only between agriculture, light industry and heavy industry but also between material production sectors and consumer service sectors. In his treatise *Economics of the Tertiary Industry*, Li Jiangfan employed Marx's labor theory of value to analyze the tertiary industry and reveal the economic principles of the tertiary industry. The book also analyzed the sign, condition, time and approach of the formation of the tertiary industry and the issues about the distribution and consumption in the tertiary industry. In this book, he proposed that the faster rise of the magnitude of relative value of non-automated service industry and also the rise of the supply and demand of service would make the proportion of the tertiary industry in economy increasingly greater.³⁶

III. Industrial Policy

In the 1980s, Chinese scholars basically agreed with each other in their opinions on industrial policy. They believed that the implementation of industrial policy was an important reason that Japan and other countries achieved industrial structure upgrading and accelerated economic development in World War II. Hence, Chinese government also positively employed industrial policy.³⁷ Soon the view of the academic circle were valued and adopted by the government. The concept of industrial policy appeared and was given important status in the Seventh Five Year Plan formulated in 1986. In 1989, China promulgated its National Industrial Policy, which covered all major industry categories in agriculture and industry. The sub-industries in each industry category was classified into three types of those with support given for development, those with restriction imposed on development and those prohibited of development.

³⁴Song (1983).

³⁵Li et al. (1988a).

³⁶Li (1985), (1990).

³⁷Zhou et al. (1987), Yang (1989), Wang (1989).

Li Jingwen et al. summarized three types of industrial development models: skewed development model, evenly pushed development model, coordinated skewed development model. They believed that the third type should be a relative ideal development model suitable to China's reality that China should adopt during the period before 2000. Namely people should consider both the coordination development of national economy in general and the skewed development of different regions.³⁸ As to the development priority order of different industries, the academic circle suggested that China should prioritize the development of some leading or pillar industries with industrial policy. Some scholars took China's resource endowment as the starting point of their consideration and believed that China should prioritize the development of labor-intensive exporting industries.³⁹ Some other scholars believed that bottleneck industries were the main restraints of China's economic development and hence people should prioritize the development of basic industries such as energy industry.⁴⁰ As the discussion deepened, more and more factors were taken into account and more views about leading industry were formed in the academic circle. But people did not form any generally-accepted opinion.

IV. Initial Exploration on the Issue of China's Industrial Organization

The issue of enterprise organizational structure was one of the important issues in industrial organization. In early 1980s, Chinese scholars summarized the problems present in the organizational structure of China's enterprises although western theories on industrial organization were not yet introduced systematically. The main characteristics of the organizational structure of Chinese enterprises were being "large in size and universal in function" or "small in size and universal in function". These characteristics became the direct cause to the low standard of the economies of scale in China. Enterprises were of large absolute size but of small effective size. Besides, irrational economic system was also an important reason for irrational enterprise organizational structure. The structure of the sizes of Chinese enterprises reflected the underdeveloped characteristic of the country. Such characteristic was also seen in the unstable number and inferior economic efficiency of medium- and small-sized enterprises. The reasons that caused the above situation included undeveloped commodity economy, mistakes in economic development strategy, and current economic system, which included equalitarianism and irrational price system.⁴¹ In the middle of 1980s, the efforts to "delegating power" and "enlivening" in enterprise reform in the urban economic system reform caused another serious problem: The enterprises became lifeless once people imposed regulation and chaotic once people lifted it. Wei Xinhua et al. believed that, when improving the dynamism of the enterprises, people should

³⁸Li et al. (1988a).

³⁹Huang (1988).

⁴⁰Li et al. (1988b).

⁴¹Sun (1984).

include establishing and improving various restrictive mechanism to rectify the deviations that might occur in the process and to guide the dynamism of the enterprises onto the track of the plans of national economy.⁴²

Competition and Monopoly: An Analysis on Socialist Microscopic Economy written by Hu Ruyin was the treatise on the study of industrial organization that had greater influence in China in the 1980s. The book systematically examined the economic schools in the West and in Eastern Europe and also various theories on competition and monopoly in China proposed after the Third Plenary Session of the Eleventh CPC Central Committee and systematically studied the issue of competition in socialism. The author took Marx's framework in analyzing microscopic economy and examined the operation of socialist microscopic economy at the level of industrial organization from multiple angles. The book revealed the characteristics of the manifold splitting status in the operation of microscopic economy in China in the 1980s. It examined various restrictions to competition inside and between industrial sectors, spatial competition, and international competition and also the inappropriateness and low efficiency of resource allocation caused by these problems. The important conclusions in the book included the following: The monopoly in socialist economy was characterized by state monopoly and administrative monopoly. The competition in socialism had the characteristic of heterogeneous competition inside a sector. Various measures to give higher targets to units that achieved better performance and to take the resources of better units to help poorer ones, which were figuratively described as whipping the faster bull in the ploughing and taking from the fat to pad the lean, could refrain the imbalance in competition inside a sector. However, such measures also played a role of obstructing the growth of advanced enterprises and protecting backward ones so that the efficiency of resource allocation was lowered.⁴³

3 The Progress in Study in the 1990s

Through the exploration in the 1980s, China found the direction of its reform, namely establishing socialist market economic system. And such direction was officially established at the Fourteenth CPC National Congress in 1992. After a great wave of introducing the theories on industrial structure in the 1980s, the theories of industrial organization became the key area in the translation and introduction of economic thoughts in the 1990s. The study in the theories of industrial structure in China in this period included the evolution of industrial structure in reality, the rationalization of industrial structure, the development of industries related to new economy, and the influence of economic opening up to industrial structure. In the areas of industrial policy, exploration and discussion were made on the issues that people confronted in industrial structure at the time, such as bottleneck industry, declining industry,

⁴²Wei et al. (1986).

⁴³Hu (1988).

industry with excessive competition, and industrial protection. Some scholars made reflection on the effectiveness of industrial policy. The study in the area of industrial organization was mainly carried out under the structure-conduct-performance paradigm. Or a particular aspect in the area was taken out for special study. The application of industrial organization theories in policy was focused on the issue of the rationalization of industrial organization. Namely people realized proper concentration of dispersive industries and strengthened competition or implemented effective regulation in monopolized industries.

I. The Further Introduction of the Theory of Industrial Organization

1980s saw the climax of the introduction of the theories of industrial structure in China. After the start of 1990s, important thoughts on industrial organization in the West were comprehensively translated and introduced into China and quickly accepted by Chinese scholars. The textbooks on industrial organization that had greater influence in China included *The Theory of Industrial Organization* by Jean Tirole, *Modern Industrial Organization*, co-authored by Dennis W. Carlton and Jeffrey M. Perloff, and *Industrial Economics and Organization*, co-authored by Donald A. Hay and Derek J. Morris.⁴⁴ Jean Tirole put the discussion on industrial organization inside the analytical framework of game theory and information economics so that his textbook showed strong theoretical features. The most important feature of the textbook written by Dennis W. Carlton and Jeffrey M. Perloff was that they combined theory with a large number of practical cases and paid more attention to public policy. These three were textbooks that had greater influence in the academic circle of industrial organization in the West. The content of these textbooks covered all important schools and thoughts on industrial organization, such as the “Structure-Conduct-Performance” framework of the Harvard School, the tradition of the study on price theory of the Chicago School, and the perspective of studying through transaction expenses in the New Industrial Organization theory.

The competition trilogy of Michael E. Porter was also translated and introduced into China successively. He proposed the Five Forces Framework and the Three Generic Strategies of overall cost leadership, differentiation and focus in *Competitive Strategy*, value chain analysis in *Competitive Advantage*, and diamond framework in *The Competitive Advantage of Nations*. These analytical frameworks were quickly recognized and applied extensively by Chinese scholars.⁴⁵

After the start of 1990s, Chinese scholars started to pay attention to industrial organization policies, which included anti-monopoly, economic regulation and social regulation in foreign countries. *Regulation of Micro-Economics*, written by Masu Uekusa, was the first treatise translated in China that referred to the term “regulation economics” in its title. The thoughts on deregulation and reregulation were also introduced into China, such as *Regulation, Deregulation, Reregulation: The Future of Banking, Insurance, and Securities Industries*, written by Alan Gart. Some scholars,

⁴⁴Jean (1997), Dennis and Perloff (1998), Donald and Derek (2001).

⁴⁵Michael (2002).

such as Yu Hui and Wang Junhao, wrote papers to introduce regulation theories in particular.⁴⁶

II. The Study about Industrial Structure

(I) The Current Situation of China's Industrial Structure and the Direction of Its Adjustment

In the study on the current situation of China's industrialization, Liu Wei used the multiple country model of Chenery and Kuznets as reference and carried out comprehensive analysis on the entire structure of national economy. He calculated and analyzed the stage of industrialization that China was in. His work exerted greater influence.⁴⁷ Guo Kesha believed that the deviation in industrial structure and the slow upgrading of the structure of industry affected the continuous growth of economy in the process of industrialization and the improvement of the quality of such growth.⁴⁸

In the study of the direction of the adjustment of industrial structure, Guo Kesha drew the conclusion that there was greater deviation in China's industrial structure through comparing the general characteristics of the change of industrial structure in different countries. He believed that the model of pushing forward industrialization should be to accelerate the development of the tertiary industry so as to drive the transfer of rural surplus labor and the rise of the income of the peasants, to eliminate the demand restriction which came from the unharmonious proportions of the standard of per capita income and industrial output, and to support the evolution of different stages of industrialization and the high-speed steady growth of economy. Besides, people also should speed up the development of equipment manufacturing industry to drive the upgrading of industrial structure and promote the improvement of the quality of economic growth through accelerating system reform and promoting the coordinated development of marketization, urbanization and industrialization.⁴⁹ Zhang Shixian held different views about this issue. He believed that people needed to examine whether there was deviation in industrial structure from the particularities of China's national situation and its economic development. The changes in China's industrial structure did not follow the general model in the world. People should take the equality of the marginal efficiency of capital of industrial investments as the standard to judge the rationalization of industrial structure.⁵⁰

(II) The Development of the Industries Related to New Economy

In the 1990s, the USA achieved high-speed economic growth and some new features emerged in such growth. These attracted extensive attention in the circle of economics. Such economy was known as the new economy. The new economy

⁴⁶Masu (1992), Alan (1999), Yu (1995), Wang et al. (1998).

⁴⁷Liu (1995).

⁴⁸Guo (2000b).

⁴⁹Guo (1999).

⁵⁰Zhang (2000).

was based on information technology revolution. It not only boosted the rapid development of emerging industries but also profoundly affected traditional industries. The Chinese academic circle carried out extensive discussion on new economy and its relevant industries at the end of 20th century.

The Research Group of China's New Economy Development Strategy of the National Information Center believed that there was very large opportunity in the development of the industries in new economy although China faced a series of challenges. Such opportunity could be seen in such situation that China already formed certain industrial basis, huge market potential and comparative advantage, late-mover advantage in international division of work, and so on. The research group held more optimistic attitude toward the development of new economy in China.⁵¹ Xu Xiaonian believed that China still had a long way to go in developing high technology industries. People should focus on creating the conditions for the development of high technology industry. They should first provide a good environment for the development of high technology industry and should not hold the unrealistic fantasy of forming a situation of "catching up and surpassing the UK and the USA" through developing high technology.⁵²

(III) The Study on the Industrial Structure under the Condition of Opening Up

As foreign investment had increasingly larger influence in Chinese economy, many scholars considered the role of foreign investment on industrial structure. Some of them had optimistic views and others pessimistic ones. Wang Luolin et al. believed that many large transnational companies who owned advanced technologies came to invest in China and played a crucial driving role in the industrial structure upgrading of China's manufacturing industry. Song Hong and Chai Yu had opposite views. They made an empirical analysis on the status and role of overseas-funded enterprises in China's foreign trade from the trade between and inside different industries. They believed that overseas-funded enterprises already took up a dominant role in China's foreign trade and its adjustment of industrial structure while China's domestic enterprises were degrading into labor- and resource-intensive industries. Guo Kesha also believed that the structural inclination of foreign investments enlarged the structural deviation of the Three Industries in China and widened the gaps of the Three Industries in China in terms of development standard and international competitiveness.⁵³

III. Industrial Policies

(I) Bottleneck Industry and Declining Industry

China's infrastructure industry stayed in a tight operation status for a long time. The scholars proposed their policy positions from different angles with respect to how to

⁵¹Research Group of China's New Economy Development Strategy of the National Information Center (2001).

⁵²Xu (2000).

⁵³Wang et al. (2000a), Song and Chai (1999), Guo (2000a).

develop bottleneck industries. Some scholars believed that incomplete fundraising mechanism was the most fundamental difficulty among the reasons that caused the relative lagging behind of basic industries in China. They proposed the following ways to raise funds for infrastructure and basic industries: centralizing fiscal expenditure, raising funds for the development of infrastructure and basic industry through adjusting the structure of the stock of state-owned assets, utilizing foreign investments, acquiring effective financing through financial institutions, including building policy banks, utilizing the allocation or paid transfer of land resources, and so on.⁵⁴ Another scholar analyzed from the perspective of government regulation and believed that an effective approach to resolve the “bottleneck” issue was to reform the prevailing government regulation system in China’s infrastructure industries and improve the economic efficiency of infrastructure industry. Drawing from the experiences and lessons of the UK in reforming the government regulation system of infrastructure industry, the scholar believed that people had to implement the separation of administration and enterprise management and advocate competition in China’s infrastructure industry. When carrying out regulation, the government needed to take effective competition as the goal and set up regulatory price on the basis of economic principles.⁵⁵

After the start of 1990s, Chinese economy shifted from a supply-constrained situation to a demand-constrained one in general. In addition, the adjustment of industrial structure became inevitable as the economy developed. The reasons in these two aspects resulted in the situation that some industries met difficulties in operation and even an entire industry suffered loss. Jiang Xiaojuan believed that the declining of some industries were inevitable. It was caused by the increase of income and the structural change in consumption. Jiang Xiaojuan also believed that the difficulties of China’s state-owned enterprises were caused by both system problems and structural problems. Namely state-owned enterprises had larger distributive density in certain industries. Jiang Xiaojuan suggested that people should establish adjustment aid fund to provide exit assistance to state-owned enterprises. Those enterprises benefited should provide compensation to assist exiting enterprise. Special policies should be formulated on the dismissal and reemployment of the employees in these enterprises. Serial assistance measures should be taken for regional adjustment. The adjustments in traditional industries and the development of emerging industries should be combined. Assisting exiting enterprises should be a priority in China’s industrial policy within certain period of time in the future.⁵⁶

(II) Industry Protection in Open Economy

As the opening up of Chinese economy to the outside world kept deepening, scholars became aware of the issues of industry security and protection in China. Luo

⁵⁴Research Group on Fundraising in Basic Industries of the Economic Research Center of the State Development Planning Commission (1994).

⁵⁵Wang (1997).

⁵⁶Jiang (1995).

Yuanzheng believed that the introduction of foreign investment caused more competitive effect than supplementary effect in China's domestic economy from 1990s. "Exchanging market for technology" ended up in losing the market and failing to get technology. So people needed to pay attention to the relationship between expanding foreign investment and protecting national economy and should strengthen policy guidance, management and supervision on the introduction of foreign investment.⁵⁷ Wang Zhenzhong believed that there were no global companies that never cared about their citizenship. China still needed to face the issue of developing national industry. People needed to relax the control over market access in a limited degree and should not fully open up the market to foreign investments. People needed to implement limited "national treatment" and positively push forward "reciprocal treatment". They should strengthen the regulatory and monitoring measures over foreign companies.⁵⁸ Cheng Enfu believed that people needed to vigorously support several dozens of state-controlled group companies that could rival with transnational companies in China so as to ensure the security of national industry.⁵⁹

Some other scholars believed that China should face international competition with an open attitude. Li Yining believed that there was not at all too much foreign investment in China. The dominance of the products from joint ventures and foreign-funded enterprises in the market was a normal phenomenon resulted from market competition. Protecting backwardness could only hinder China's economic development and technological progress. Protecting backwardness was monopoly.⁶⁰ Xia Youfu and Ma Yu suggested that people should further improve the catalog and interim regulations for the guidance of industries for foreign investment. They should fully open up mature industries and general industries to foreign investors and vigorously encourage them to invest in infrastructure and basic industries. Even if there had to be industry protection, such protection had to conform to international practice and be implemented moderately. People should employ economic means to support domestic enterprises as much as possible.⁶¹

(III) The Evaluation of Industrial Policy

China was a country that implemented a larger number of industrial policies. These policies existed extensively in many areas for various reasons. But the actual effect of industrial policy was far from the effect that people expected from them for a long time. This indicated that there were factors between the two effects that had functioned and people failed to take into consideration. Jiang Xiaojuan applied the public choice theory to study government behavior in industrial policy. She believed that people would face two important changes when the government formulated industrial policy after the start of 1990s: As industries with general shortage decreased noticeably and the regulatory role of the market grew stronger, the objective criteria

⁵⁷Luo (1997).

⁵⁸Wang (1996).

⁵⁹Cheng (1998).

⁶⁰*Chinese Business Times* (1997).

⁶¹Xia and Ma (1997).

for formulating industrial policy reduced noticeably, the factors that influenced policy formulated increased, and the difficulty in policy formulation also increased. And as time passed, the influence of the factors related to the government's own interests showed a tendency of noticeable increase in the formulation of industrial policy. She believed that the formulation of industrial policy should meet such standard: People should select as much as possible those policy means that had consistent interests or less conflict with administrative system and the target entities of industrial policy under the premise that the policies were beneficial to realizing the goal of industrial policy. Only in this way could the industrial policies be effectively implemented. There were three thought-provoking points in her final conclusion: The presence of the issue of imbalance of industrial structure might not be the sufficient reason for implementing relevant industrial policy. Industrial policy might both resolve and cause industrial structure issues. In-depth study needed to be done with respect to the design, selection and matching of the means of industrial policy.⁶²

IV. Expanding the Study on Industrial Organization

(I) The Study about Market Structure and Enterprise Behavior

In the book *Industrial Organization and Its Effective Competition—An Initial Study on China's Industrial Organization* edited by Wang Huijiong, he made much pioneering study in the aspects of concentration ratio and minimal economies of scale in the area of market structure. In the book *Structure and Behavior—A Study on China's Industrial Organization* written by Ma Jiantang, he comprehensively examined the operation of the market in China at the time. He calculated the concentration ratio of three major industrial sectors in China, estimated the situation of the economies of scale in Chinese industrial enterprises, and ranked the barriers to entry in 40 industrial sectors. He pointed out that the barriers to entry the most unfavorable for the optimal resource allocation in China were some policy barriers and, in particular, the limitations on the entry of industry caused by the implementation of fragmented departmental and regional management system. Yang Huixin employed mathematical models and the methods in econometrics to examine and analyze the entry and exit of Chinese enterprises, taking automobile industry and durable goods manufacturing industry as examples. The scholar also made in-depth and systematic analysis on the excessive entry and exit barriers of enterprises in the process of re-tracking and the rigidity of their assets stock.⁶³

There was serious market segmentation in China. A unified domestic market was yet to form and a unique market structure with larger regional difference emerged. This had something to do with the imbalance between different regions in social and economic development. Some scholars believed that the uniqueness of regional market structure had very close relation with government behavior and, in particular, the behavior of local government. The behavior of local government came from the integration of administrative and economic management functions in Chinese

⁶²Jiang (1993).

⁶³Wang (1991), Ma (1993), Yang (2000b).

government over a long time and also from the unfulfilled decentralization reform between central and local authorities. Yin Wenquan and Cai Wanru used the theory of path dependence as the instrument in analysis and pointed out that local market segmentation was a particular phenomenon that only emerged in the process of economic re-tracking. The administrative decentralization, which had the basic characteristics of the major initiative of predetermined fixed payment from local fiscal revenue and the de facto local ownership of a large number of state-owned enterprises, was the deep-level system cause of such segmentation. Practical factors such as the distribution of industry left by traditional system and the performance evaluation of the leaders of local authorities intensified the tendency of local market segmentation.⁶⁴

In the study of enterprise behavior, most scholars followed the framework of property right structure-enterprise behavior-property right reform. Ma Jiantang's study also considered the influence of the internal structure of the enterprises and their external market structure and expanded the scope of the study of enterprise behavior. He pointed out that there was no definite correlational relation between concentration ratio and industry profitability in China. The main reason of this was that the state implemented relatively strict price control over the industries with high concentration ratio.⁶⁵ Chinese scholars noticed the issues of the enterprise behavior such as horizontal and vertical integration in the early 1990s.⁶⁶ Shen Zhiyu analyzed the price policy and price formation in the natural monopoly industries such as electric power, railway, civil aviation and telecommunications in China. He believed that it was typical administrative industrial monopoly and its behavioral pattern was an administrative one.⁶⁷

(II) The Study on the Issue of the Practical Industrial Operation Performance in China

Jiang Xiaojuan et al. examined the completely different industrial performance caused by competition during the re-tracking period. In some manufacturing industry, efficiency standard kept rising, product and technology were quickly upgraded, production concentrated toward a small number of advantageous enterprises, and international competitiveness showed noticeable improvement. However, in some other manufacturing industries, competition played an absolutely different role. The problems such as scattered production, repeated construction, lowering benefits, and a large number of enterprises or even an entire industry suffering loss, emerged and lasted for a long time. The cotton spinning industry was a typical case in which competition failed to improve industrial organization structure. Jiang Xiaojuan believed that the distortion of system environment and the characteristics of the industry in question were the causes of such problems. Here, she believed that people could not

⁶⁴Yang (2000a), Yin and Cai (2001).

⁶⁵Ma (1993).

⁶⁶Wang (1991).

⁶⁷Shen (1997).

just take concentration ratio as the index to measure whether industrial organization structure was deteriorating. They needed to pay attention to the influence of the expansion of market size at the same time.⁶⁸

In the study of the relation between concentration ratio and economic performance, Yin Xingmin examined the relationship between the concentration ratio and economic benefits of industry since 1980s and drew the following conclusion: The economic benefits of industry and the size of the enterprises were positively connected. The rapid establishment and expansion of small enterprises deteriorated China's resource allocation and restricted the improvement of the economic benefits of industry. The model of resource allocation in China's industrial economy indicated that Chinese economy still did not get out of the extensive development model of high speed and low efficiency.⁶⁹ Qi Yudong also believed that concentration ratio and industrial economic performance were positively correlated within certain range. But his explanation to such positive correlative relation was that it was the result of lowering unit cost and expense, which had little to do with price factors. And its deep-level determinants were technological progress and innovation.⁷⁰

Liu Xiaoxuan continued to use the approach of property right-performance in her study. She took the data of the national industrial census conducted in 1995 as the basis and used production function model and quantitative method to carry out a large scale measurement and comparison of the efficiencies of 170,000 enterprises that possessed competitive features. Her conclusion was that private and individual enterprises had the highest efficiency, overseas-funded enterprises the second highest, shareholding and collective enterprises, the third, and state-owned enterprises the lowest. The subordinate and hierarchical statuses in the old system were negative to the development of enterprises. Non-state-owned enterprises at lower subordination levels had higher efficiency than state-owned enterprises at higher hierarchical levels so that the advantage of scale of the latter was offset and lost.⁷¹

Some other scholars observed economic performance from the angle of industrial competition. Jin Bei discussed the theory and methodology on the international competitiveness of Chinese industry from the angle of the international competitiveness of industrial products, drawing from the research results of Michael E. Porter et al., and proposed the realization and factor indexes of the international competitiveness of industrial products. Pei Changhong carried out an empirical analysis on the industrial competitiveness of various industries such as electronics, automobile, clothing, cleaning products, tire and commercial retail and obtained the result on the influence of Chinese and foreign investments to China's industrial competitiveness in the industries of different natures. Lü Zheng and Cao Jianhai believed that there was excessive competition in China which resulted in too large intensity of competition and the loss of economic efficiency and welfare. The problem that excessive competition occurred in most industries in the re-tracking process was mainly caused

⁶⁸Jiang and Liu (1996), Jiang (1998).

⁶⁹Yin (1996).

⁷⁰Qi (1998).

⁷¹Liu (2000).

by institutional reasons. Jiang Xiaojuan believed that the reasons why China's state-owned industrial sectors had surplus capacities and excessive competition included that the sizes of state-owned enterprises failed to adapt to the supply that they needed and market conditions. The problems were also related to the industrial and regional distribution of state-owned enterprises and their exit barriers.⁷²

V. The Policies of the Government on Industrial Organization

(I) The Issue of the Moderate Concentration in Market Structure

In middle and late 1990s, Chinese economy shifted from a seller's market to a buyer's market. The industrial organizations of most industries were very unsatisfactory. The specific indications of such problem included that there were capacity excess in the entire industry, there were too many enterprises inside one industry, and the output of these enterprises were at very low absolute standard, which had a very large gap with the scale of internationally leading enterprises. Chinese scholars had relative consensus on such unsatisfactory market structure. They believed that people had to make advantageous enterprises bigger, eliminate backward production capacities, and realize the economies of scale and promote industrial concentration. Shen Lin believed that the extreme dispersion in market structure was caused by the situation that there was no separation between administration and enterprise management in China and that administrative power intervened in enterprise operation. Therefore, people had to separate administration from enterprise management, eliminate administrative barriers, and increase concentration through competition. Xie Di and Qiao Liang proposed the view that people needed to correct the name of monopoly and that pushing forward the moderate concentration of main industries was the objective requirement to achieve the fundamental transformation of the model of economic growth from an extensive one to an intensive one.⁷³

(II) Anti-Monopoly and Regulation Policy

Chinese scholars had relative consensus on anti-monopoly. The paper "Examining the Issue of Anti-Monopoly in China from the Telecommunications Industry", written by Zhang Weiying and Sheng Hong, had far-reaching influence as a specific analysis on anti-monopoly cases. The scholars made detailed analysis on the development process of China's telecommunications industry and proposed the basic thoughts on reforming China's telecommunications industry, such as forming a new "national telecommunications management commission", splitting China Telecom into several companies, and drafting the *Telecommunications Law*. They pointed out that the most important task in anti-monopoly in China currently was to fight against the monopoly of government departments and the behavior that limited fair competition. Such point was applicable to the industries of postal communication, electric power and railway as well as the telecommunications industry. Chen Xiaohong, Zhang Xinzhu and

⁷²Jin (1996), Pei (1998), Lü and Cao (2000), Cao (1999), Jiang (1995).

⁷³Shen (1993), Xie and Qiao (1997).

Wang Junhao also published important papers on the issue of monopoly in China's telecommunications industry.⁷⁴

In the study of regulation system and the application of regulation theory, Yu Hui examined in detail China's government regulation system. He believed that China's current government regulation system played certain promotive role in maintaining market order, guaranteeing the interests of consumers and the society, and promoting industrial development. However, because the problems of the mixing up of administration and enterprise management and of administrative units and institutional units, the phenomena still happened sometimes that certain government institutions abused the administrative power in their hands to maintain the interests of the departments or industries in their own charge.⁷⁵ Yang Huixin believed that people needed to form an atmosphere in which enterprises might enter and exit freely in China's regulation system. The government should set up different entry and exit barriers on the basis of the characteristics of different industries and guide the rationalization of industrial organization. The direction of the guidance of government in the industrial organization policies had to conform to the interests of the enterprises which were also guided by market signals. Only in this way would the policies be recognized and implemented.⁷⁶ In his treatise *An Introduction to Government Regulation Economics*, Wang Junhao systematically discussed various regulation theories and systematically studied the formation mechanism of the regulation prices of the three kinds of products under naturally monopolized operation of telecommunications service, electric power and tap water in China. Besides, he also construct relevant models to point out that the goal of the policy on the price regulation of China's naturally monopolized products had greater influence.⁷⁷

4 The Progress of Study from the Beginning of the New Century

After the beginning of the new century, important changes occurred to China's industrial structure. In 2010, the structural proportions of the primary, secondary and tertiary industries were respectively 10.2, 46.8 and 43.0%. When compared with the figures in 2000 of 15.1, 45.9 and 39.0%, these figures revealed the trend that the proportion of the primary industry decreased noticeably, that of the secondary industry remained roughly the same, and that of the tertiary industry continued to rise. While implementing structural optimization, people should also see the challenges that confronted the adjustment of China's industrial structure: After the accession to the WTO in 2001, China was confronted with international competition, the costs of production factors such as labor and land rose quickly. The growth rate of the

⁷⁴Zhang and Sheng (1997), Chen (1999), Zhang et al. ((2000), Wang (1998).

⁷⁵Yu (1998).

⁷⁶Yang (2000c).

⁷⁷Wang (2001).

supply of working-age population decreased, China's economy was about to reach the Lewis turning point and demographic dividend gradually disappeared. Resource and environment pressure grew larger and China faced the challenges in responding to climate change and the pressure in environment protection. New technological revolution was on the rise and global industrial structure adjustment was in progress. The price of bulk commodity had wide fluctuation in international financial crisis, and so on.

Confronted with various challenges, the CPC proposed in the report of the Sixteenth CPC National Congress in 2002 that China would take the road of new-type industrialization and informatization was the inevitable choice for speeding up the realization of industrialization. People should adhere to driving industrialization with informatization and promoting informatization with industrialization. They should take the road of new-type industrialization which had high scientific and technological content, good economic benefits, low resource consumption, and little environment pollution and brought China's human resource advantage into full play. It was further proposed in the Seventeenth CPC National Congress in 2007 that, in promoting economic growth, people should achieve the transformation from mainly relying on the secondary industry to relying on the synergic promotion of the primary, secondary and tertiary industries. They should speed up the development of modern service industry and raise the proportion of the tertiary industry in national economy. In 2010, the State Council adopted the decision on speeding up cultivating and developing strategic emerging industries, in which seven industries were selected, including energy conservation and environment protection, new generation information technology, biological technology, high-end equipment manufacturing, new energy, new material, and new energy automobile.

After the start of the 21st century, the focus of the study on industrial structure and industrial organization in China turned to open economy and to structural adjustment and monopoly and competition under global background. Such study mainly included structural adjustment, economic growth, road of new-type industrialization, anti-monopoly, and reform in natural monopoly industries.

I. The Study on Industrial Structure

(I) The Judgments on Industrial Structure, Development Stages, and Development Strategy

Wu Li and Wen Rui summarized China's industrialization process into three stages: In the stage of pursuing strength from 1949 to 1978, the relationship between light and heavy industries in industrialization was represented as "giving more weight to heavy industry and less to light industry". In the stage of pursuing wealth from 1979–1997, such relationship was represented as the synchronous development of agriculture, light industry and heavy industry. In the stage of exploring the road of new-type industrialization (1998–2005), such relationship was represented as the situation that

both the government and the enterprises were trying to find new economic growth points through structural adjustment so as to achieve rapid development.⁷⁸

After over thirty years of development in the reform and opening up, China transformed from an agricultural country to an industrial country. China's economic modernization entered a new stage in which the country transformed from a major industrial country to a powerful industrial country and took industrial modernization as the kernel task.⁷⁹ Lin Yifu and Liu Mingxing believed that the country should adopt a development strategy that conformed to its comparative advantage in the industrialization process of a developing country. Their empirical analysis indicated that the transformation of the Chinese government in development strategy was the key to the successful industrialization in the recent 20-odd years and more. Both state-owned and non-state-owned industries and both rural and urban industries should follow the principle of comparative advantage in their development.⁸⁰

(II) Adjustment of Industrial Structure and Economic Growth

Liu Wei et al. tried to take out technological progress and industrial structure evolution from factor productivity and measure the contribution of industrial structure evolution to China's economic growth. Their research indicated that the changes of industrial structure always had very remarkable contribution to economic growth from the beginning of the reform and opening up. However, as the degree of marketization increased, the contribution of industrial structure evolution to economic growth gradually became second to technological progress. Namely, the power of marketization manifested in industrial structure evolution would gradually be replaced by the power of technological progress.⁸¹ Zheng Ruogu et al. believed that industrial structure and system had direct influence on economic scale and they also played their role through the function of resource allocation with respect to productive factors and thus had indirect influence. The adjustment of industrial structure had direct influence to economic growth in both short and long terms. But its function of factor allocation only had short-term effect.⁸²

Huang Maoxing et al. analyzed the inherent relations between technological choice, industrial structure upgrading and promoting economic growth. They believed that people could promote the upgrading of industrial structure, improve labor productivity, and realize rapid economic growth through technological choice and reasonable capital deepening.⁸³ Jiang Xiaojuan believed that the optimization and upgrading of industrial structure was the driving power of continuous economic growth. Therefore, people needed to push forward the optimization and upgrading of industrial structure, which included improving the ability of independent innovation, strengthening the ability to integrate and utilize global technological

⁷⁸Wu and Wen (2006).

⁷⁹Chen and Huang (2005).

⁸⁰Lin and Liu (2004).

⁸¹Liu and Zhang (2008).

⁸²Zheng et al. (2010).

⁸³Huang and Li (2009).

resources, strengthening the construction of important basic industries and infrastructure, speeding up the development of the tertiary industry, and continuing to develop labor intensive industry.⁸⁴ Gan Chunhui et al. found that the growth of labor productivity mainly came from inside the industries and, particularly, the secondary industry. The flow of labor factors between different industries had the phenomenon of structural dividend but the flow of capital between the industries could not meet the hypothesis of structural dividend.⁸⁵

(III) Taking the Road of New-Type Industrialization

The road of new-type industrialization did not rely on capital accumulation but on the improvement of efficiency to achieve economic growth. This was generally accepted in the circle of economics. However, the circle had different views on how to proceed on the road of new-type industrialization and also on the relationship between the road of new-type industrialization and the phenomenon of heavy and chemical industrialization which emerged in China after the start of the new century.

Liu Shijin believed that industries of consumption nature, such as housing, automobile, electronic communication, and those of investment nature, such as steel and iron, nonferrous metal, machinery and chemical, became new leading industries in China after the beginning of the 21st century. The starting and end points of the growth of an industry were both based on resident consumption. This was a situation that never appeared in China in the past. As it was supported by resident consumption, it was impossible for bubbles to appear in Chinese economy in a large range and over a long time. He asserted that Chinese economy entered the stage of development of heavy and chemical industries which was based on the market and had gradually increasing technology content and added value and stronger sustainability. It was completely normal “within the scope of experience and commonsense” that China, as a large country, experienced a stage in which heavy industry grew at an accelerated pace and with increasing proportion in economy. The National Statistical Bureau also believed that China entered a period of the rapid development of heavy and chemical industries.⁸⁶

Wu Jinglian opposed the development toward the dominance of heavy industrial sector in economic structure. He believed that such development resulted in lowering overall efficiency of national economy, technological innovation lagging behind, slow development of service industry, damage of ecological environment, increasing difficulty in employment, and hidden financial risks. Therefore, people needed to build a system favorable to technological progress and efficiency improvement, speed up the development of service industry, and drive industrialization with informatization. He emphasized that China should not rely on high investment in economic development but should mainly rely on the improvement of efficiency.

⁸⁴Jiang (2005).

⁸⁵Gan and Zheng (2009).

⁸⁶Liu (2003a), (2004), (2005), The speeches of Li Deshui and Yao Jingyuan from the National Statistical Bureau at the press conference of the State Council Information Office on January 20, 2004.

This was the correct way to develop on the road of new-type industrialization.⁸⁷ Xu Zhaoyang et al. believed that, if the government prioritized the development of heavy industry, disregarding China's factor endowment structure, it would result in the distortion of resource allocation and the low efficiency in economic development. This was because industrial structure was endogenous to factor endowment structure and it would be upgraded with the upgrading of such structure. He believed that the kernel issue in economic development laid in the upgrading of factor endowment structure rather than in the upgrading of industrial structure. And with the efficiency of economic development taken into account, China should better not prioritize the development of heavy industry.⁸⁸ Lin Yifu believed that people should pay more attention to developing labor-intensive industries rather than capital-intensive industries as there was labor surplus in China. Zhao Lifen and Dong Jun believed that people should not judge China's industrialization process on the basis of the division of stages in industrialization in western countries. And the rapid growth of heavy and chemical industries in China in recent years was only a phenomenon particular to the period of economic ascent. People could not assert that China entered the stage of development of heavy and chemical industries on the basis of such phenomenon.⁸⁹

(IV) Inter-Regional Distribution of Industrial Structure: Convergence and Division of Work

The convergence of industrial structure occurred in many regions in China. For example, industrial isomorphism and vicious competition happened in the Yangtze River Delta region. The reason of industrial isomorphism laid in the influence of administrative decentralization and the system of predetermined fixed payment from fiscal revenue to superior authorities. Zhang Ye et al. believed that the economic performance competition system and risk aversion tendency that currently existed among local government officials were the radical causes of the convergence of local industrial structures.⁹⁰ Qiu Feng et al. also believed that industrial convergence was mainly seen in the areas where the government controlled investment. This was determined by the special government official promotion system in China. The forces of the market would promote the complementation and advancement of local industries. People needed to start with the transformation of supply systems when they tried to promote regional cooperation and optimize the spatial distribution of the industries.⁹¹ Hu Xiangting et al. further broke down the influence of the government to the isomorphism of industrial structure in two aspects: The government set up trade barriers, which would increase trade costs between different regions and increase the convergence of industrial structures between the regions. And the investment behavior of the

⁸⁷ Wu (2004), (2005).

⁸⁸ Xu and Lin (2010).

⁸⁹ Lin (2004), Zhao and Dong (2005).

⁹⁰ Zhang and Liu (2005).

⁹¹ Qiu et al. (2005).

government promoted the differentiation of industrial structures between the regions in general.⁹²

The inter-regional division of work among the industries was seen in industrial transfer. In China, such transfer was manifested noticeably as the transfer of the labor-intensive industries in the east into central and western China in recent years. Cai Fang et al. believed that China's northeastern and central regions had faster speed of the growth of total factor productivity and higher contribution rate in China after the start of the new century. People could realize the re-distribution of the industries in the three types regions of East China, Central China and Western China, namely the industrial upgrading and transfer in coastal areas and the industrial undertaking in central and western regions. Through such measure, people could let central and western regions to regain its comparative advantage of rich labor resource and, at the same time, retain the development of labor-intensive industries in China.⁹³ Chen Jianjun also believed that the factor flow and industrial transfer in the Yangtze River Delta region promoted the economic integration in the region. The industrial barycenter of manufacturing industry was transferred inside the region and then relatively reasonable industrial spatial structure and structure of industrial division of work was formed in the region. This caused the central region of Chinese economy with Shanghai as its regional focus to be expanded to cover the entire Yangtze River Delta.⁹⁴

Feng Genfu et al. was not very optimistic about China's large scale industrial transfer. Their judgment was that only partial and relative industrial transfer occurred between China's western, central and western regions by 2006 and absolute industrial transfer did not happen at all. At present, conditions were still not ripe for the large scale industrial transfer between China's eastern, central and western regions. Therefore, it was rather different within a very long period of time for people to, through the industrial transfer between these regions, try to realize coordinated regional development and to resolve the contradiction between China's industrial structure adjustment and employment expansion under the background of international financial crisis.⁹⁵

(V) The Development of Industrial Structure and Factor Market

The changes of industrial structure had close connection to the factors like population and land. On the one hand, the changes in industrial structure could promote the flow of factors between different industries and thus improve the productivity of factors. On the other hand, factors could react on the changes in industrial structure. Wang Dwen et al. believed that China's industrial structure conformed more and more to its resource and factor endowment and that the comparative advantage of cheap labor cost was constantly brought into play. They believed that the faster growth in light industry sectors and labor-intensive industries not only improved the

⁹²Hu and Zhang (2005).

⁹³Cai et al. (2009).

⁹⁴Chen (2007).

⁹⁵Feng et al. (2010).

general efficiency of China's industry but also played an important role in alleviating the increasingly serious unemployment issue at present.⁹⁶ Cheng Mingwang et al. believed that urban service industry was the main direction of the transfer of rural labor in China. Although regular industrial sectors and construction industry also played a promotive role in transferring China's rural labor, such role was relatively weak. Therefore, people should vigorously develop the tertiary industry. This was a strategic choice in resolving the issue of China's rural surplus labor.⁹⁷ The phenomenon of migrant worker shortage indicated that the conditions of China's rural surplus labor transformed from infinite supply to limited surplus. And this also meant that people needed to make use of national labor market to resolve the structural and regional issues at present. Cai Fang et al. believed that the adjustment of industrial structure did not achieve the goal of the optimal resource allocation because the growth and development of factor market was still at an incomplete level. The marginal return of physical capital showed smaller inter-regional difference, which converged with the development direction from the beginning of 1990s. The inter-regional difference in the marginal return of human capital and labor exhibited an enlarging tendency. So the acceleration of the adjustment of industrial structure and industrial transfer depended to a large extent on the situation of the growth and development of labor market.⁹⁸

The rise of land price in China in recent years triggered the study on the relationship between industrial structure and land. Kong Xiangbin et al. studied the relationship between the different stages of the development of the Three Industries and land use structure. In the stage of regional economic development in which the growth of the primary industry dominated, the driving mechanism of the changes in land use was mainly the competition between agricultural land and environmental land, which was mainly seen in the situation that the proportion of agricultural land increased, urban development land was at a stable level, and environmental and kept decreasing. In the stage of economic development in which the growth of the secondary and tertiary industries dominated, the main driving mechanism of the changes in land use was mainly seen in the situation that construction land and environmental land competed for taking up agricultural land. This resulted in the situation that the areas of construction land and environment land both increased while that of agricultural land decreased quickly.⁹⁹ Zhang Yin et al. also believed in their study that industrial structure and land use structure had close correlativity and showed the tendency of increasing or decreasing synchronously in change.¹⁰⁰

(VI) Industrial Structure and Resource Environment

One important content in the *Suggestion of the CPC Central Committee on Formulating the Eleventh Five Year Plan on National Economic and Social Development*

⁹⁶Wang et al. (2004).

⁹⁷Cheng and Shi (2007).

⁹⁸Cai and Wang (2002).

⁹⁹Kong et al. (2005).

¹⁰⁰Zhang et al. (2007).

was speeding up pushing forward the transformation of the intensive economic growth mode. It was a transformation from an intensive economic growth mode characterized by high investment, high consumption, high emission and low efficiency to a resource-saving one characterized by low investment, low consumption, low emission and high efficiency. However, after the beginning of the 21st century, China's energy intensity showed a trend of drastic growth. Liu Zaiqi et al. believed that the development of almost all industries would increase the emission of carbon dioxide. But such emission showed a descending order in the influence from the primary, secondary and tertiary industries. Therefore, in order to develop low-carbon economy, people needed to reasonably select leading industries and speed up the adjustment of industrial structure with China's national situation taken into account.¹⁰¹

(VII) Developing the Tertiary Industry and, Particularly, the Producer Service Industry

Li Jiangfan and Zeng Guojun analyzed the four levels inside the tertiary industry and carried out vertical and horizontal analyses on the evolution inside the tertiary industry in China using econometric regression. They believed that the lowering of the proportion of the first level and the rising of the proportion of the second level in the tertiary industry in China showed the direction of the structural upgrading of the tertiary industry in China. Li Jiangfan further pointed out that the structural upgrading inside the tertiary industry was seen in the decrease of the proportion of circulation sector and the increase of the proportion of life and production service sector and also in the decrease of the proportion of traditional service industry and the increase of the proportion of modern service industry. Under the circumstance of the advancement of industrial structure and the increasingly rising proportion of the tertiary industry in it, it was very necessary for China to comprehensively promote the modernization of the tertiary industry.¹⁰² Jiang Xiaojuan and Li Hui examined the development of China's service industry and the changes of its internal structure and analyzed the factors that influenced the development of service industry.¹⁰³

With the support of the constant innovation and extensive application of information technology, the relative statuses of the traditional distribution, social and personal service industries inside the tertiary industry lowered while that of producer service industry rose quickly. Producer service industry was the industry of the most dynamism and development potential in modern service industry. It not only formed mutual dependence and joint development with manufacturing industry but also could drive the upgrading and transformation of traditional service industry. Cheng Dazhong pointed out that, in comparison with other economies in the Organization of Economic Cooperation and Development, China's national economy and its three industries had relatively larger consumption of physical investment but smaller consumption of service investment, namely of producer service. The gap

¹⁰¹Liu and Chen (2010).

¹⁰²Li and Zeng (2003), Li (2005).

¹⁰³Cheng and Huang (2003), Jiang and Li (2004).

of the development of China's producer service industry was not just determined by economic development stages but caused to a large extent by the constraints in social integrity, system, mechanism, policy and regulations. He believed that breaking market monopoly, streamlining market mechanism, regulating market operation order and government behavior, and creating integrity economy were the priorities in developing producer service industry.¹⁰⁴ Lü Zheng et al. believed that people should speed up the development of China's producer service industry in the aspects of eliminating access barriers, enhancing the advantages in the division of work, promoting industrial linkage, pushing forward innovation in service industry, optimizing industrial distribution, and strengthening regional coordination.¹⁰⁵

(VIII) Industrial Structure and Foreign-Oriented Economy

After China's accession to the WTO, the connection of its national economy with foreign countries kept deepening and the study on industrial structure under the condition of opening up also became increasingly important. The influence of foreign capital and, particularly, transnational companies to China's industrial structure became one of the important research topics. Wang Luolin et al. believed that foreign-funded economy became an important component in Chinese economy and also a force to drive economic growth together with other economic sectors such as state-owned economy, collective economy and private economy. Foreign-funded economy made important and positive contribution to upgrading industrial structure, promoting technological progress, and enhancing the degree of internationalization of the economy.¹⁰⁶ Scholars who held such type of views believed that foreign-invested enterprises made contribution to expanding the scale of China's export and improving the structure of China's exported goods because these enterprises possessed the ability to flexibly making use of two markets and two kinds of resources and showed stronger ability in adjustment and adaptation.¹⁰⁷ Fu Qiang et al. believed that there was strong correlativity between the adjustment of China's domestic industrial structure and its introduction of foreign investment. The introduction of foreign investment promoted the advancement of China's industrial structure and improved the organic composition of industrial technology. And it also improved the qualities of various industries.¹⁰⁸ Huang Rifu et al. further pointed out that solely foreign-funded enterprises had the most prominent technology spillover effect and such effect produced noticeable positive action on industrial structure. Equity and contractual joint venture enterprises failed to produce noticeable action on industrial structure.¹⁰⁹

But people also needed to see the possible adverse effect of foreign direction investment on China's industrial structure. Liu Yu found that the serious skewed

¹⁰⁴Cheng (2008).

¹⁰⁵Lü et al. (2006).

¹⁰⁶Wang et al. (2000b), Jiang (2002b).

¹⁰⁷Jiang (2002a).

¹⁰⁸Fu and Zhou (2005).

¹⁰⁹Huang and Chen (2007).

distribution of foreign direct investment in industrial structure worsened the skewness of China's industrial structure.¹¹⁰ Wang Yanfei et al. believed that people needed to consider the role of FDI in a dialectical manner. FDI was beneficial to promoting employment in the secondary industry and the non-agricultural growth of employed population. However, FDI had inadequate influence on the tertiary industry and it was unfavorable to the transfer of rural surplus labor in China and the further optimization and upgrading of industrial structure.¹¹¹ Liu Zhibiao et al. indicated through studying the case in Suzhou that the processing trade model dominated by Chinese and foreign investment in the road of industrialization would quickly push forward the evolution of local industrial structure in the early period. But it could also result in very easily the imbalance in the advancement of local industrial structure, formed a dual development pattern caused by the squeezing of foreign investment, and further triggered the crisis of the hollowing and marginalization of Chinese enterprises.¹¹²

II. Industrial Policy

(I) The Selection of Development Strategy in State Industrial Policy

Jin Bei believed that the choice of state industrial development strategy was not just based on the principle of pure rational judgment. It would definitely contain strong factors beyond reason, which included the principles of racial, ethical and various other cultural values. The industrial development strategy currently viable to China had to be based on the outlook of scientific development. Its value embodiment should not only conform to objective principles but also satisfy the realization of certain social desirability goal.¹¹³ Xu Zhaoyang et al. had relatively conservative attitude toward the application of industrial policy. They believed that proper industrial policy could promote the upgrading of industrial structure. But its effectiveness was limited by factor endowment structure and it should be holistic, macroscopic and cross-industrial as much as possible.¹¹⁴

Cai Fang emphasized the importance of the balanced development of the industries. He believed that people should implement the strategy of rewarding agriculture and supporting the countryside, create good environment for the flow of labor, establish guaranteed mechanisms for funds to flow into agriculture and the countryside, and enhance the sustainability of the basic resources and production conditions of agriculture so as to form a harmonious and balanced pattern of urban-rural relationship.¹¹⁵

As to how to proceed on the road of new-type industrialization, Jiang Xiaojuan believed that China's road of new-type industrialization had the following several

¹¹⁰Liu (2007).

¹¹¹Wang and Zeng (2006).

¹¹²Liu and Zhang (2005).

¹¹³Jin (2004).

¹¹⁴Xu and Lin (2010).

¹¹⁵Cai (2006).

characteristics: First, people pushed forward industrialization in the time of the great development of information technology. Second, people pushed forward industrialization on the basis of the constantly deepening globalization. Third, people attached equal importance to economic development and environment protection. Fourth, industrialization should be favorable to the continuous transfer of rural labor and the improvement of the degree of urbanization. Guo Kesha believed that people needed to speed up industrial structure upgrading characterized by the rise of the proportion of technology-intensive industry.¹¹⁶

(II) The Choice of Leading Industry

The research group of China Input-Output Association believed that the influence and induction coefficients of the manufacturing industry were mostly larger than social average level and showed a rising trend. So manufacturing industry was the growth point in China's national economy. High and novel technology industry would become the leading industry in China's economic development.¹¹⁷

Guo Kesha believed that the automobile industry had very large promotive function to industry, service industry and employment and its indirect promotive function was far greater than direct promotive function. He believed that people should select automobile industry as China's leading industry in early the 21st century. It was favorable to alleviating the restriction of consumption demand on steady economic growth, to strengthening the driving role of investment demand to economic growth, and to adjusting and upgrading industrial structure.¹¹⁸

(III) Industrial Policy under an Open Environment after China's Accession to the WTO

Guo Kesha believed that the adjustment of industrial development policy should form a new situation which centered round the policy on industrial structure and matched the policy with the adjustment of the policies on foreign trade and use of foreign investment. It was the key of the industrial development policy in the new period to handle well the issue of the moderate and effective intervention of the government. Wang Ping and Qian Xuefeng examined the influence of the types and bias choices of technological progress to trade conditions. They believed that it already became the radical cause for the deterioration of China's trade conditions that the country took the path of export-biased technological progress for a long time. So China's policy for encouraging technological progress should give preference to import-biased medium- and advanced-leveled technologies. Ma Jie and Zhou Jidong believed that the optimization of policy intervention and whether it could offset the efficiency loss caused by asymmetric information depended on the type of competition rather than on information structure. Besides, after the deduction with the model under multiple international market oligarchs, Ma Jie believed that export

¹¹⁶Jiang (2002c), Guo (2004a).

¹¹⁷Research Group of China Input-Output Association (2006).

¹¹⁸Guo (2001).

tax rebate policy would compound the distortion of domestic market in reality and it might not improve the welfare of the country.¹¹⁹

(IV) The Adjustment of Industrial Structure in Backward Regions

There were a multitude of resource-exhausted state-owned enterprises in China and numerous enterprises faced the dual difficulties of resource exhaustion and system transformation. So the policy on resource-exhausted industries both posed theoretical questions and responded to China's urgent needs in reality. Yu Li et al. examined the practice of the city of Fuxin and systematically analyzed the types of exit barriers of resource-exhausted state-owned enterprises and the choices of exit routes.¹²⁰ Wang Dewen et al. believed that people should place vigorously developing light industry sectors and labor-intensive industries in a prominent position in the process of rejuvenating and transforming traditional old industrial bases.¹²¹

III. The Study on Industrial Organization

(I) Market Operation

Liu Xiaoxuan carried out the study on the behavior of China's state-owned enterprises under different market frameworks. He found that the goal of state-owned enterprises took the main form of the maximization of sales revenue in a market with monopolistic competition while it took the main form of the maximization of expenses payment in a market with regular competition.¹²² The strategic behavior that Chinese enterprises customarily had was price competition. An Tongliang et al. revealed, taking the colored television industry as an example, the industrial characteristics that could easily cause price competition in the six aspects of product features, stages of the product's life cycle, characteristics of the scale of industrial production, concentration ratio of the market, industrial exit barriers, and market power of downstream enterprises.¹²³

(II) The Study on Enterprise Competitiveness

Enterprise competitiveness referred to the comprehensive quality of an enterprise in a competitive market with which it could provide products or services to the market more effectively than other enterprises and achieve profits and its own development. Sun Luoping used marginal analysis to analyze and reveal the logical process in which the improvement of competitiveness was irrelevant to the size of an enterprise. He pointed out that the phenomenon of industrial clusters in a number of medium- and small-sized towns in China was a typical case of utilizing the division of work between market organizations to bring into play their competitive advantage.¹²⁴ Some scholars evaluated the competitiveness of medium- and small-sized

¹¹⁹Guo (2004b), Wang and Qian (2007), Ma and Zhou (2001), Ma (2002).

¹²⁰Yu et al. (2003).

¹²¹Wang et al. (2004).

¹²²Liu (2003b).

¹²³An and Yang (2002).

¹²⁴Sun (2004).

enterprises in different industries in China with the four leveled goals of competitiveness against external environment, strength of short-term survival, ability to achieve growth in medium-term, and long-term development potential. They believed that the order of the competitiveness of China's medium- and small-sized enterprises from the strongest to the weakest was as follows: electronic and electrical appliances industry; chemical, light industry and commercial service industries, food, machinery, metallurgy, construction and construction materials industry, and finally textile industry.¹²⁵

IV. The Government's Policy on Industrial Organization

(I) Natural Monopoly and Administrative Monopoly

A large part of China's monopoly was administrative monopoly. Such monopoly resulted in the high profits of state-owned enterprises, formed huge vested interest group, and became the largest institutional bottleneck in Chinese economy. Such issue caused both economic and political corruption. Liu Xiaoxuan analyzed enterprise behavior in the process of China's economic re-tracking. She believed that the primary task in a competitive market was to resolve the issue of property right and the most crucial task in a monopolistic competition market was to resolve the issue of administrative market monopoly. Anti-monopoly became an urgent long-term mission in China's economic re-tracking.¹²⁶ Zheng Jie et al. constructed a double-product dominant monopoly model on the basis of the characteristics of China's telecommunications industry. They believed that various conducts of dominant monopoly enterprises caused different effects and the forward and vertical control in such conducts would cause anti-competition effects which would cause the decrease of profits inside an industry.¹²⁷

Some scholars believed that it was necessary to retain a concentrated market structure in particular industries. Liu Wei and Huang Guitian believed that different countries had different modes to allocate financial assets. There were differences in the industrial organization structure in the banking industry. A relative concentrative industrial organization structure, which consisted of large-sized banks, might not result in decreasing degree of competition. Higher concentration ratio in China's banking industry might not be the reason that affected the degree of competition in the industry. Even if China's banking industry greatly improved its degree of commercialization, it was still not appropriate to make its industrial organization structure excessively dispersive. Retaining a relatively concentrative industrial structure might be more favorable to improving the efficiency of the allocation of financial assets.¹²⁸

¹²⁵Lin and Guan (2005).

¹²⁶Hu (2001), Liu (2003b).

¹²⁷Zheng et al. (2001).

¹²⁸Liu and Huang (2003).

(II) Anti-Monopoly Legislations

China's monopolistic areas mostly involved state-owned enterprises. Anti-monopoly and state-owned enterprise reform intertwined together, which resulted in great resistance and difficulty in work. But only when people deepened reform and introduced competition mechanism into monopolized industries could they effectively improve the efficiency of resource allocation in China.¹²⁹

Guo Yong et al. believed that China's accession to the WTO in 2001 brought a good opportunity for deepening China's economic system reform. People needed to make use of internationally accepted rules to regulate market behavior in China, break industrial monopoly and regional monopoly, re-examine and re-adjust existing laws, and gradually establish the framework of relevant legal system.¹³⁰ Anti-monopoly law was one of the legal cornerstones of a market economy country. It could guarantee the good operation of market mechanism and realize optimal resource allocation and improvement of economic efficiency. The organization of law enforcement with respect to anti-monopoly law in various countries could be divided into the judicial model represented by that of the USA and the administrative model represented by that of the EU. Wang Xiaoye believed that the administrative model was more suitable to China's law enforcement with respect to anti-monopoly law due to the considerations on China's actual conditions and the economic management functions of the government.¹³¹

Wang Xiaoye believed that people needed to be cautious of the monopoly of transnational companies because these companies could easily achieve dominant or even monopolistic status on China's market with their fund and technological advantages. She proposed that people needed to utilize anti-monopoly law to resist foreign monopolistic power. In particular, they should maintain the order of competition in the aspects of prohibiting international cartel, prohibiting transnational companies from abusing dominant market status, and limiting the external expansion of transnational companies.¹³²

(III) Privatization and Reform of Monopolized Industry

Wang Junhao believed that privatization could play a promotive role in truly realizing the separation of administration from enterprise management in natural monopoly industry. And privatization reform could effectively promote competition. Therefore, privatization reform was the necessary choice in deepening the reform of the government regulation system in natural monopoly industry.¹³³ Hu An'gang also accepted such a view. In the developed countries among the international community, their infrastructure and many public service departments were originally troubled by inferior public investment efficiency, high price, overstaffing, poor service quality and

¹²⁹Zhang (2007).

¹³⁰Guo and Hu (2003).

¹³¹Wang (2007).

¹³²Wang (1999).

¹³³Wang (2002).

serious loss. The government of these industrialized countries implemented privatization reform. On the one hand, the reform greatly saved government budget and obtained tax revenue. On the other hand, privatized institutions provided service at noticeably lower cost and higher efficiency in comparison with public institutions.¹³⁴ Luo Danglun et al. pointed out that some government-regulated industries gradually allowed the entry of private capital in China in recent years as marketization reform was pushed forward. Taking the private companies listed in the stock market in China from 2004 to 2006 as the sample in his study, he found, that private enterprises adopted effective political strategies to help themselves to enter government-regulated industries, which noticeably improved enterprise performance and promoted their own development.¹³⁵

(IV) The Study on Government Regulation

Wang Junhao et al. pointed out that there were both natural monopoly and administrative monopoly in China's monopolized industries under the current systems. Namely there was the duality of monopoly in China's monopolized industries. In order to radically break administrative monopoly, people needed to formulate effective classified regulation policy on the basis of the duality of monopoly in monopolized industries and the double-character characteristic of administrative monopoly.¹³⁶

The inappropriate regulation of the government on the market often brought efficiency loss. Liu Yuhui et al. believed, taking financial market as example, that the institutional arrangements in government regulation was one of the radical causes that resulted in extremely high IPO underpricing. Rent-seeking behavior resulted from government regulation increased the cost of the investors in the primary market and caused even higher IPO underpricing.¹³⁷ Zhu Hengpeng believed, taking medical industry as example, that the underpricing of the price of medical service resulted in the mechanism of "subsidizing doctors with drugs" and that the regulation policy of the rate of return further induced that hospitals purchased and sold drugs at higher prices. The government's regulation on medical service and drug price could not achieve their expected goal.¹³⁸

Some scholars reflected on regulation policy. Bai Rangrang and Yu Yihong proposed a new explanation on the initial cause of deregulation. Namely deregulation was an endogenous phenomenon caused by technological progress, demand structure change, and the product characteristics, industrial organization structure and power structure arrangement under original regulation. Deregulation triggered by marginal entry was a progressive "multi-win" result, which would not cause the regulation chaos or absence resulted from mandatory deregulation. Jiang Feitao et al. reflected on the regulation policy on the investments in China's steel and iron

¹³⁴Hu and Guo (2002).

¹³⁵Luo and Liu (2009).

¹³⁶Wang and Wang (2007).

¹³⁷Liu and Xiong (2005).

¹³⁸Zhu (2007).

industry purported to the prevention and control of “excessive production capacities” and implemented from 1994. They pointed out that there were three defects in the regulation policy on the investment in steel and iron industry: First, it could not radically regulate and control production capacity excessiveness. Second, relevant departments could not made accurate prediction and formulate desirable investment plans. Third, the policy would disturb market process and cause bad consequences. Regulation policy hampered the spontaneous adjustment of the market in infrastructure investment and resulted in some bad policy consequences. People should take a prudent attitude in adopting such policy.¹³⁹ Yuhui believed that there were institutional defects in regulated bureaucratic system. The current vertical configuration of administrative institutions, for example, the top-down vertical structure from the provincial level in drug administration and industrial and commercial administration, and also the horizontal integration of administrative institutions implemented in a vertical direction, such as the regional offices of banking, securities and insurance departments, were both very hard to implement in reality. This problem had something to do with the situation of the mixing up of party management and government administration, of enterprise management and government administration, and of state-owned property management and government administration and also the absence of public fiscal system. As a result, people found it very hard to achieve policy goals through regulation.¹⁴⁰

5 Several Comments

The most important characteristic that can be seen in the study on the theories of industrial structure and industrial organization in China during over 60 years from the founding of the People’s Republic of China was the close connection between theoretical study and economy in reality. This was first seen in the fact that the demand in reality was the basic driving force of theoretical research. The translation and introduction of foreign economic thoughts into China was a case in point. 1980s was a period of concentrated introduction of the theories on industrial structure while the introduction of most of the theories on industrial organization occurred in the 1990s. Such a situation could not be regarded as only being the result of the transfer of the interest of the scholars in study. It should be considered under the general background that changes occurred to social and economic conditions. It was new economic phenomena that generated the demand in theory. The combination between theory and practice was also seen in the influence of theory to practical policy. The studies in the theories of both industrial structure and industrial organization basically

¹³⁹Bai and Yu (2004), Jiang et al. (2007).

¹⁴⁰Yu (2003).

took reality as starting point and policy suggestions as ending point and showed rich pragmatic colors. Laws and regulations used to maintain market operation, such as *Anti-Unfair Competition Law* and *Anti-Monopoly Law*, and industrial development policies, such as *Automobile Industry Development Policy* and *Steel and Iron Industry Development Policy*, both received influence from the academic circle.

The progress of the study on the theories of industrial structure and industrial organization in over sixty years after the founding of the People's Republic of China was mainly seen in the following: (1) There was the transformation of research paradigms. The study on theory on industrial structure developed from the "Two Major Departments" and "Agriculture, Light Industry and Heavy Industry" before the reform and opening up to the "Three Industries". The study on the theory of industrial organization evolved from sporadic studies on particular issues to taking the "Structure-Conduct-Performance" framework or price theory as research paradigm. (2) Research methodology was enriched. The studies in earlier time were mainly carried out with qualitative analysis. As the study in relevant areas kept deepening, more and more quantitative studies were carried out. Besides, research methods used to compare static and dynamic situations emerged constantly. There were also studies made with pure deduction with models. (3) The depth and width of the studies kept expanding. The later in time a study was made, the more attention was paid to the diversity and complexity of variables, the more conditions were taken into account, and the broader the background was in which such studies were carried out. (4) The studies showed the spirit of self-examination. For example, in the earlier time of the reform and opening up, it was generally accepted in the study on policy application that the government could play a positive role in the rationalization of industrial structure or industrial organization. But gradually some scholars voiced different opinions. No matter which side was more reasonable, such disagreement indicated that scholars followed their spirit of independent thinking, which made their research containing more scientific attitude.

It should be seen that there were things that needed to be improved in the study on the theories of industrial structure and industrial organization in China. It was mainly that the degree of the division of work and specialization was inadequate in terms of research area. Researchers could not focus and track a relatively narrow area. This made it hard for their research results to form a system and for the research to become very profound and in-depth. Because of insufficient division of work and specialization, many research topics that the researchers chose were completely identical. This resulted in the situation that a hotspot issue caused the emergence of a large number of articles with similar views in a certain period. But there were little high-standard discussion on fundamental areas. Improving the degree of specialization in academic research was the trend of development in the future.

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Chapter 20

The Study on Price Theory and the Exploration on the Regularities in Price Reform



Xiaowei Chen

Price was the most sensitive lever in national economy. Under the condition of market economy, price was the most important and effective signal and the indicator for regulating production, circulation and consumption. The law of value regulated social and economic activities like an invisible hand. Even under the condition of planned economic system, the role of price still could not be overlooked as long as commodity production and exchange was retained. Administrative pricing caused price distortion which often caused negative influence to national economy or even serious imbalance of national economy. The scissors differential between the prices of industrial and agricultural production and its enlargement seriously refrained the development of agricultural production and resulted in the severe imbalance between industry and agriculture. The sensitivity, effectiveness and importance of price lever made a key area that the circle of economics paid great attention to after the founding of the People's Republic of China. One after another wave of heated discussion rose about it and many valuable innovation results were proposed.

Such a situation would be discussed in the following in the two periods of before and after the reform and opening up.

1 The Study and Exploration Before the Reform and Opening Up

China mainly implemented traditional planned economic system before the reform and opening up. The formation of prices was mainly the result of administrative pricing. The study, discussion and exploration on the issue of price was carried out

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under such a background. The main content of study and discussion roughly included the following several aspects.

I. Whether and How Should Planned Prices Embody the Requirement of the Law of Value

After the establishment of planned economic system, the formation of price was mainly the result of planned prices. Most economists held an affirmative opinion on whether planned prices should embody the requirement of the law of value. But they had different views on how should the prices embody such requirement.

Xue Muqiao believed that the price of commodity was determined by state plans under socialist system. But the state had to correctly utilize the law of value and meticulously considered the role of such law when it determined the prices. He pointed out that the following three objective factors were involved when prices were determined on the basis of the requirement of the law of value: (1) The price of commodity was mainly determined by its own value. (2) Currency was the rule to measure value. If change occurred to the value represented by currency, then commodity price changed with it. (3) The supply and demand relationship of commodity also affected commodity price to certain extent.¹

Yu Guangyuan had similar views. He believed that the restrictive role of the law of value to planned price was embodied in the following three aspects: (1) Although price was set by state stipulations, it could not completely depart from value. (2) When deviation occurred between price and value, the law of value would act on the basis of the situations present in such deviation and cause certain consequence. (3) Under socialist system, the general trend of price change in the long term was to advance toward the direction in which price approached value.²

Sun Yefang further believed that the principle of exchange at equal values had to be implemented. Price should be set according to the principle of not deviating from value. The CPC's price policy had to take the principle of exchange at equal values as the basis. He pointed out that the following three points were incorrect: (1) Price conforming to value was economic principle while price deviating from value was to have politics in command. Without the deviation of price from value, there would be no price policy. (2) In practice, people needed to consider policy when implementing the principle of exchange at equal values. (3) Price was the lever for the redistribution of national income and also the means of socialist accumulation. The purchase price of agricultural products should always be lower than their value while the sale price of industrial products should always be higher than their value.³ Sun Yefang's views in the above were consistent with his idea that, of all kinds of economic laws and principles, the law of value was the primary one.

The basis of price was value. The movement of price was subject to the regulation of the law of value. Price policy had to be formulated with due respect to the law of value. The mainstream view in the circle of economics at the time was correct.

¹See Xue (1963).

²See Zhong and Yu (1957).

³See Sun (1979, pp. 152–156).

II. Whether the Foundation of the Formation of Planned Price Under Socialist System Was Production Price or Not

This was a hotspot that caused extremely intense discussion. And during the time after 1964 and from 1966 to 1976, the academic argumentation turned into political issue. The scholars who advocated the theory of production practice was accused of preaching reactionary revisionism. Sun Yefang was the one who suffered the worst prosecution.

Some economists, represented by Sun Yefang, published papers intermittently from 1959 to 1964 and proposed that the transformation of value into production price had objective inevitability under socialist system. Production price was the basis of the formation of planned price of commodity. Namely, the profits, determined with departmental average cost plus average profit rate on funds, were taken as the basis. Recognizing production price was the inevitable and logical conclusion drawn from recognizing profit rate of funds. Only when recognizing production price could people implement the calculation on investment effect. The formation of production price in socialist economy was restricted by the situation that physical technological conditions and, mainly, the physical technological equipment of workers played an increasingly important role in the process of socialist production and that there was socialist socialized mass production. In order to recognize the role of the physical technological conditions in socialist economy, it was required that value be transformed into production price so that the surplus products created in various departments of national economy could be distributed on the basis of the amounts of funds occupied by various departments. Such practice had the following positive effects: (1) It was favorable to the smooth progression of extended reproduction. (2) It could integrate the economic effect of production units with that of the society so that it could help people to select production and investment plans reasonably. (3) It was favorable to promoting enterprises, departments and the entire national economy to adopt new technology and hence to achieving technological progress and improving labor productivity. (4) It was favorable to correctly handling the relationship between different departments and enterprises. (5) It was favorable for various departments and enterprises to try hard to save the funds that they occupied.⁴

The proposal of the proposition that there was production price in socialist economy immediately caused argumentation in the circle of economics. Some people disagreed with this point and believed that only value could be the basis for the formation of price in socialism. It did not require other forms of transformation. Some articles believed that the presence of production price was not determined by the physical condition of machine mass production but by the capitalist private ownership system of the means of production. And the substance of socialist economy did not allow the generation of production price. Under the physical condition of machine mass production, social value, rather than production price, still was the category that represented social labor. Using the categories of production price and average profit

⁴See Sun (1959), Yang (1963), He and Zhang (1964).

rate on funds could not play a positive role in socialist economic practice. On the opposite, it would cause some adverse impact.⁵ Some other articles believed that fund and profit did not have necessary connection between each other in socialist economy and that profit rate on funds was not the criterion to judge whether an enterprise was advanced or backward. Otherwise, people would have to expel socialist principles and the planned management of the state to enterprises. The profit earning of particular enterprises could not be equalized with the needs of the entire society. It was incompatible to the requirement of developing national economy in a planned manner to make average profit rate on funds an automated regulator.⁶

The voice criticizing the theory of production price became increasingly higher and, by and by, it was given a political label of preaching revisionism. As a result, regular academic discussion related to it was forced to halt in the period from 1965 to the end of 1976

III. The Issue of the Formation of the Prices of Agricultural Production

One question was whether the formation of the prices of agricultural products was determined by the expenses under the production condition of medium quality land or inferior land. Some scholars advocated that it was determined by the production condition of medium quality land and believed that false social value was not allowed to exist under the condition of socialist planned economy and hence price formation should not be determined by the consumption in the production condition of inferior land.⁷ Others advocated that the prices of agricultural products were determined by the production condition of inferior land and believed that it was caused by the natural and economic conditions that would generate differential rent. Therefore, it was an objective necessity to consider the factor of differential rent and to stipulate the purchase prices of agricultural products on the basis of the labor consumption, namely departmental cost, and reasonable profit in the production of agricultural products under the production condition of inferior land.⁸ At the time, a larger number of treatises supported the latter view, namely the famous opinion in the analysis on the formation of the value of agricultural products proposed by Carl Marx in the third volume of *On Capital*.

Sun Yefang proposed new opinions on the issue of the “scissors differential” between the prices of industrial and agricultural products. He advocated that people should change the method of accumulating funds in the form of differential profits and implement different forms of taxation. This was because that direct tax was a relatively reasonable and progressive form of tax burden in comparison with indirect tax. The “scissors differential” between the prices of industrial and agricultural products was a covert and indirect form of burden. Its defect laid in its covertness,

⁵See He et al. (1964).

⁶See Dai (1964).

⁷See Liu (1962).

⁸See Wang and Su (1962).

with which both the state and the peasants could not find out clearly how much accumulation the state had taken from the peasants.⁹

IV. Gu Zhun Proposed and Called for Carrying Out the Study on the Operation of Socialist Economy on the Basis of Market Price. This was the Brightest Result in the Discussion and Exploration on the Price Theory Before the Reform and Opening Up

In 1957, Gu Zhun wrote an article and pointed out that price would balance supply and demand and stimulate production when people let the law of value control the movement of price as long as socialism was still under the control of the law of value. When people cause the separation of value and price to reach the extent of violating the law of value, it would inevitably worsen the disconnection between supply and marketing and obstruct the development of production. Therefore, it was necessary to make the law of value control the movement of price whether people stipulated prices with plans or implemented economic accounting system to automatically regulate price. For the production of an enterprise, it was necessary to implement independent cost accounting. In the process of pursuing advantage and profit, the enterprises would naturally respond to price. Planning could not replace market. Planning should only give predictions rather than forming the “integration of particular plans”. He also inferred that the enterprises would spontaneously select and regulate production on the basis of profits and price would fluctuate spontaneously. Hence, the movement of price would actually send signals that required the increase or decrease of production.¹⁰ It can be seen from the above that Gu Zhun’s thinking on economic theory in the 1950s was greatly foresighted. It already approached the standard of the theory of socialist market economy and made remarkable contribution to economic theory.

2 The Argumentation and Innovation on Price Theory After the Reform and Opening up

After the beginning of the reform and opening up, the Chinese circle of economics achieved prominent results in the innovation of price theory. The innovated price theory played a promotive role and had remarkable effect in the practice of price reform. In the 1980 and 1990s, China’s price reform became an area of unique brilliance and developed faster than other reforms in China and, particularly, than enterprise reform and macroscopic management reform. It greatly promoted the re-tracking of China’s economic operation system and quickly made the market enlivened. The successful practice in price reform benefited to a very large extent from the extensive consensus in the circles of economic work and economics that

⁹See Sun (1965).

¹⁰See Gu (1957).

price needed to be formed in exchange under socialist system and that the theory of market price should replace the theory of administrative pricing. Of course, the success also benefited from the situation that the CPC and the Chinese government attached importance to price reform. It was specifically pointed out in the *Decision on Economic System Reform* at the Third Plenary Session of the Twelfth CPC Central Committee early in 1984 that “price is the most effective means of regulation. Reasonable price is the important condition to guarantee that national economy retains dynamism without falling into chaos. The reform of price system is the key to the success of the reform of entire economic system.” Such a situation greatly stimulated the attention and enthusiasm of various circles in the society about price reform. In the other way round, a series of successful practices in price reform provided rich materials and experiences to the innovation in price theory so that economists had the conditions to study the objective regularities of China’s price reform. At the same time, the *Price Law*, which regulated price behavior, took effect in May 1998 so that price reform was put onto the track of the rule of law.

Although substantial progress was achieved in China’s price reform, the reform was not finished yet. People still needed to improve price institution and price system. Therefore, people needed to continue to innovate in price theory and further explore the regularities in price reform. After the beginning of the twenty-first century, China’s economic growth accelerated. Its GDP achieved two-digit growth for five consecutive years since 2003. But people noticed at the same time that too heavy price in resource and environment was paid for such economic growth. Resource and environment capacities became the main “bottlenecks” in economic growth. This required that people earnestly put the outlook of scientific development into practice and speed up the mode of transforming economic development from mainly pursuing quantitative growth to mainly pursuing quality improvement. People should take good quality as the top priority and seek faster development on such basis. In this area, it became the most prominent and practical issue to rationalize price relations and, in particular, those of production factors and resource products. As it was pointed out in the report of the Seventeenth CPC National Congress, people needed to make those prices reflect the supply and demand relations on the market, the scarcity of resources, and environmental damage costs. The marketization reform of the prices of production factors and resource products already became the focus whether people could transform the mode of economic development and realize the sound and fast development of the economy. This urgently required further innovating in price theory so as to promote the further deepening of price reform and contribute to turning China’s economic and social development onto the track of scientific development.

First, let us review the argumentation and innovation of price theory under the great trend of reform.

Over thirty years passed until now from the time when the Third Plenary Session of the Eleventh CPC Central Committee made the important decision on reform and opening up in 1978 and decided that the purchase prices of agricultural products be raised largely first to stimulate the restoration and development of agricultural

production. In 1979, the purchase price of eighteen types of main agricultural products was raised by 24.8% on average. During these years, a great trend of reform and opening up unfolded on China's vast territory of 9.6 million km². Chinese economy achieved sustained fast development under the powerful impetus of the reform and opening up. China became the major country with the fastest economic growth in the world. And in 2010, it became the second largest economy on the globe. In the entire process of economic system re-tracking, price reform played a critical role in the radical transformation of economic operation mechanism from command economy to market economy. The great trend of the reform and opening up promoted and drove the exploration, argumentation and innovation of price theory and the innovation in price theory, in turn, pushed forward the deepening of price reform step by step. When viewed from certain aspect, the pioneering development of ideology and theory, the liberation of thought, and the innovation in theory played a decisive role in successfully pushing forward the practice of reform.

China's price reform was pushed forward in the process of constantly liberating the thought and breaking through the confines of traditional price theory. After the beginning of the reform and opening up, theoretical argumentation occurred roughly in the following several aspects in the study of the area of price.

I. Whether People Should Take Market Price System as the Goal of Price Reform

In the early period of reform, the CPC and the Chinese government took a series of price adjusting measures. For example, the purchase prices of grain and other agricultural products were greatly improved to encourage peasants to increase the output of agricultural products. The measures achieved good effect. Some comrades in the CPC believed on the basis of such achievement that people could rationalize price relations through the government's price adjustments. In the middle 1980s, the circle of theoretical study exaggerated the role of shadow price and attempted to rationalize price system through implementing a price system based on decision making.¹¹

Different from the above, many economists advocated that people should put price formation back into market exchange and take market price system as the target model of price reform. Adjusted price, shadow price and floating price could only be taken and used as transitional forms. They believed that there was serious distortion in price structure in the beginning of the reform. Such problem was manifested in concentration in the sharp gaps between the profit rates on funds in different industries. In 1979, state-operated industrial enterprises at the county level and above achieved an average profit rate on funds of 12.3%. But there were great differences between different industries: that of wristwatch was 61.1%, of industrial rubber 49.4%; of knitwear 41.1%, of bicycle 39.8%, of dye and paint 38.4%, of petroleum 37.7%, of oil field 34.1%, of sewing machine 33.1%, and of chemical drugs 33.1% but that of coal was only 2.1%, of fertilizers 1.4%, of iron ore 1.6%, of chemical ore 3.2%, of ships 2.8%, of cement 4.4%, of semi-mechanized agricultural implements

¹¹ See Research Group of Industrial Policy of the Economic (1987).

3.1%, of timber felling and selection 4.8%, and of agricultural machinery 5.1%.¹² Because of this, people needed to adopt the measures of adjusting prices, referring to shadow prices, and utilizing floating prices in the beginning of the reform so as to avoid the drastic change of interest relations caused by fully opening up price control at one go and to increase the controllability of price reform. But it needs to be seen that there was an inherent defect in adjusting price. Price adjustment might rationalize price relations for a moment. But because no change was made to price formation mechanism, the originally rational price relations became irrational again and new distortion occurred for not very long time because of the changes in supply and demand relations. Only through realizing the transformation of price formation mechanism, namely opening up price to market regulation and building market price system, could people guarantee with relevant mechanisms the rationalization of price relations and the formation of rational price structure.¹³

The practice of price reform in China proved that the position of building and improving market price system conformed to the direction of China's marketization reform.

II. Whether People Should Complete Price Reform at One Go or Push It Forward Step by Step

How should people implement price reform? There were different ideas about it. One opinion advocated pushing forward quickly or completing the reform at one go as the best way.¹⁴ Another one advocated pushing forward step by step. Namely people should not do it too rashly. In practice, the latter was adopted.

What laid behind the two different positions above was the discrepancy on whether people should push forward price reform under the condition of retaining roughly stable prices. The scholars who supported the first opinion believed that people needed to discard the slogan of stabilizing prices in the process of price reform. They said that "stabilizing prices" represented a kind of "price awareness of non-commodity outlook" and that stabilizing prices would restrain the action of the reformers and "might make China end up in a more and more adverse situation".¹⁵ The scholars who supported the second opinion believed that the prices of various commodities were artificially lowered because government pricing had been implemented over a long period of time. Implementing price reform, be it either adjusting or opening up prices, would cause price level to rise in certain extent. It was generally believed that there needed to be a one-time or more rise in price if people needed to achieve the purpose of rationalizing price relations. As a result, if people attempted to push forward price reform quickly or even completed it at one go so that the general price level experienced sharp rises, the reform could result in social turbulence and market chaos, including the panic buying of goods. So such measure was unadvisable. Adopting the method of gradually pushing forward price reform would have

¹²See He et al. (1981).

¹³See Zhang (1990).

¹⁴See Wu et al. (1988).

¹⁵Ibid.

smaller risk and hence represent a safer and more reliable approach. Although there would be price rises in the reform process, such rises could be broken down and taken away in a longer period, for example, a decade or more than a dozen years, so that annual price rise would not go beyond 10%. As a matter of fact, China's consumer price index showed an average increase of 5.6% from 1978 to 2010. The prices stayed in a steady state, which allowed China's price reform to be pushed forward smoothly.

III. **Whether the Double-Track Price System of the Means of Industrial Production Should be Unified into a Single-Track System of Market Prices or Planned Prices**

This issue caused large argumentation in the early 1990s. The implementation of double-track system with respect to the prices of the means of industrial production, namely planned price and market price, was the product of China's progressive reform. The system lasted for five to six years from 1985. In the early 1990s, the gap between the prices in the double-track system narrowed significantly so that conditions were ripe for unifying them. Some economists advocated that the double-track prices of the means of industrial production mainly be unified into planned single-track prices for the reason that the means of industrial production were mostly products that concerned national interest and people's livelihood and that they played an important role in social and economic activities and were troubled by imbalance of supply and demand or, in the case at the time, the situation that supply fell short of demand. Some comrades in the CPC specifically advocated that over 80% of the prices be turned into planned prices in the unification of the double-track system of the prices of the means of production. The comrades who supported such opinion also believed that people should work hard in studying and calculating the reasonable profit level of these products and use it as the basis for pricing.¹⁶

Different from the above, many economists believed that people should adhere to market-orientedness, focus on resolving the issue of price formation mechanism, and expand the role of market mechanism. The majority of the prices of consumer goods were opened up at the time with remarkable effect achieved. People just could not let the prices of the means of industrial production be turned into planned prices and form opposition to the price form of consumer goods. Moreover, the difference between the prices in the double-track system was greatly narrowed in the early 1990s. And market single-track price would not cause large rise in the general standard of prices. In the re-tracking process, people should not put most of their efforts on calculating the price and profit levels of various kinds of products but should open up prices to market regulation.¹⁷ The practice in later time indicated that the unification of the double-track system of the prices of the means of industrial production was successful. Some famous foreign economists spoke highly of China's practice in implementing double-track system in the prices of the means of industrial production. Polish economist Wlodzimierz Brus said at the famous "Bashan Tourist Ship" Conference held in

¹⁶See Wen (1989).

¹⁷See Zhang et al. (1990).

September 1985 that it was the invention of China to implement double-track prices on the means of production. It could be taken as a bridge, with which people could realize the transition from one price system into another price system. In other words, they could implement the transition from administratively or officially determined prices to market prices. The transition could be more stable with such a bridge.¹⁸ American economist Joseph E. Stiglitz believed that a genius solution had been adopted in the implementation of the double-track system of the prices of the means of production.¹⁹

IV. Whether the Disturbance of Inflation Should be Eliminated in Price Reform

After the beginning of the reform and opening up, several short-term medium-level inflations occurred with rapid economic development. The situation posed the question whether price reform could be pushed forward smoothly under the condition of inflation or whether the disturbance of inflation should be removed in price reform.

Some economists advocated that people should utilize inflation to support rapid economic development so as to make the cake bigger as quickly as possible. Price reform could only be pushed forward in inflation.

Some economists disapproved such position and believed that utilizing inflation to stimulate the rapid growth of economy could only achieve effect in short term but there was large aftermath resulted from such practice. So in the long run, the measure was unfavorable to the sustained rapid growth of the economy.²⁰

Under the condition of inflation, for example, the cases in 1988 and from 1993 to 1995, price reform could hardly make substantial steps, let alone making breakthroughs. In addition, people needed to impose regulation once again on some prices that had already been opened up so as to prevent prices from rising too sharp. This resulted in the reappearance of irrational price ratios and also the emergence of new price distortions. In order to successfully push forward price reform, which included the realization of the unification of the double-track system of the prices of the means of industrial production into the single-track market system, people had to first regulate inflation and stabilize economy and general price level. As pointed out by Xue Muqiao, a famous economist, the encouragement of inflation from 1985 to 1988 caused price system to become more and more distorted. The two tracks in the double-track price system did not converge gradually but diverge. Multileveled speculative reselling occurred in the middle of the two tracks. The double-track system evolved into a disorderly multitrack system. Under the circumstance of increasingly serious inflation, people attempted to speed up price reform through circumventing the step of controlling inflation. This triggered the problem of panic deposit withdrawal and purchasing in the summer of 1988. The government was forced to implement control and rectification after the punishment of the objective principles and laws of commodity economy.²¹

¹⁸See China Society of Economic Reform (1986, p. 51).

¹⁹Joseph (1998).

²⁰See Cheng (2006).

²¹See *The Memoir of Xue Muqiao* (1996).

The practice in China's price reform proved that the second position was practical and viable. The removal of the disturbance of inflation was beneficial to successfully pushing forward price reform.

3 The Exploration on the Regularities and Basic Experiences in Price Reform

As price reform unfolded and deepened and relevant experiences were accumulated, the circle of economics started to explore some regularities in China's price reform and proposed their own views. For example, some articles proposed that the following was the main regularities that people had found initially up to the present:

- (1) Price reform included the two major aspects of price system reform and price management reform. The reforms in these two aspects needed to be carried out in a complementary manner. And people needed to be good at pushing forward the rationalization of price system through the reform of price management system. The most fundamental thing in the reform of price management system was to realize the transition from the dominance of administrative pricing to that of pricing through market.
- (2) The new price model required that people controlled macroscopic prices in a planned manner, which included controlling the general price level, main price ratio relations, and strategic prices, and lifted control and enlivened microscopic prices, which mainly involved market price. Price reform needed to conform to such requirement in general.
- (3) People needed to implement price system reform step by step, which generally included the following three stages: Regulating prices so that various industries could achieve roughly the same profit standard; opening up prices so that price could fully reflect the supply and demand relations on the market; and linking with the prices on the international market.
- (4) The rationalization of price relations needed to be implemented in different steps and in a complementary manner. First, people needed to rationalize the prices of base products. Once these were rationalized, it would promote the rationalization of the entire price system.
- (5) The difficulty and main conflict of price reform laid in the task of addressing well the relationship between rationalizing and stabilizing prices. How large a step people could make in price reform and the progress and effect of such reform depended on the result of how high price rise ratio the reform would cause and whether the state, enterprises and the mass could accept such price rise.
- (6) People needed to create a good economic environment for price reform. The most important factors in it included the following: Economy developed in a coordinated manner. General supply, general demand and their main structure should be in balance. The growth of money supply should match with the

needs in economic development and economic marketization and it should be controlled within 5% even when there was hyper-growth.²²

Besides, some treatises proposed that the basic experiences of China's price reform were as follows:

- (1) People must handle well the relationship between reform, development and stability in price reform.
- (2) People should observe the law of value, transform price mechanism, and build a price mechanism dominated by formation through market.
- (3) People should push forward the reform progressively and deepen it step by step.
- (4) People should coordinate, match and orderly push forward various reforms.
- (5) People should strengthen the leadership of the CPC and the government on price reform so that the reform could advance along a correct path.²³

Some articles believed that the experiences of China's price reform in thirty years were the following:

- (1) Taking the theory of socialism with Chinese characteristics as guidance, starting from the reality of China, and adhering to the market orientedness of the reform was the fundamental guarantee with which people could succeed in implementing the reform.
- (2) Liberating the thought, courageously advancing and taking action, and being good at innovation was the powerful driving force for successfully pushing forward price reform.
- (3) Taking a positive, safe and reliable attitude, exploring earnestly, and implementing progressive reform was the road to the success of the price reform with Chinese characteristics.
- (4) Adhering to the principle of people-orientedness, paying attention to people's livelihood, properly coordinating and resolving various interests' relations and contradictions in the reform, and winning the understanding and support of the extensive community of the mass was where the driving power laid for the success in implementing the reform.
- (5) People should both adhere to the crucial status of price reform and carry out well the work to coordinate and complement with other reforms. They should win the support of various areas so that the reform could obtain reliable material guarantee.
- (6) People should strengthen the construction of price management and research institutions to provide theoretical instruction and organizational guarantee to the successful implementation of price reform.²⁴

Theory was the guide of practice. The discussion or argumentation on some important issues in the process of China's price reform manifested that people were constantly liberating their thought, deepening their understanding, and pushing

²²See Zhang (1987a).

²³See Li (2005).

²⁴See Wen (2008).

forward theoretical innovation. These discussions and argumentations played an important driving role to the practice of reform. For examples, the discussions that people had to respect the role of the law of value and bring price formation back into market exchange, how the double-track system of the prices of the means of industrial production could be unified, that people should adhere to marketization orientation in price reform were all crucial ones. In the other way around, the practical experience in price reform became increasingly richer and hence constantly contributed to the deepening and development of the theories on reform. For example, the exploration on the regularities of price reform was initially the summarization of the experiences furnished by the practice of reform. And the innovation in the theory of price reform, in turn, played a new driving role in deepening price reform.

4 Innovation in Price Theory Powerfully Drove Price Reform into an Area of Unique Brilliance

Driven by the incessant innovations in price theory, China's price reform could be said to have unique brilliance and advanced ahead of the reform of state-owned enterprises and other reforms in the 1980 and 90s. The gradual opening up of prices brought activity and vigor to the market so that national economy was full of dynamism. The "China Miracle" emerged. In different times in this period, some economists reviewed the journey of reform and carefully summarized successful experiences.

I. In the Very Beginning, China's Economic System Reform Specifically Followed Market Orientation. Market Mechanism was Introduced Gradually to Reform the Traditional Planned Economic Management System Which Repelled Commodity Production and Market Relation.

In 1992, people further determined that socialist market economic system should be taken as the target model of the reform. Moreover, China was a large country with a population of more than a dozen billion in which both social productivity and people's living standard were very low. In 1978, there were 250 million people nationwide still suffering subsistence issues. The development of different regions was rather imbalanced. Therefore, people needed to be resolute, relentless and very meticulous in reforming China's economic system. They should push it forward region by region and step by step, "crossing the river by feeling the stones". They should properly select the order and priorities of the reform and should not try to complete it at one go. The successful practice in China's price reform during over thirty years fully exhibited the necessity to implement a progressive marketized reform in China's economic system and the huge effect achieved in it.

The most important reason why China's price reform achieved huge success was that people both adhered to the market-orientedness of the reform and adopted a progressive guideline when pushing it forward. Specifically speaking, they first regulated and then loosened prices, combined regulation and loosening, gradually opened

up prices and connected with international market price. The reform mainly focused on adjusting irrational price ratio and price difference before 1984 so that various industries could have generally the same profit level. And some work was also done in opening up prices. The reform after 1984 mainly focused on opening up price and some work was also done in adjusting prices. Such practice allowed the reform to be pushed forward under the condition of generally stable general price level in which average annual rise was no more than 6 and 10% at the most. People also tried to take opportunities. Prices were boldly opened up in some regions wherever conditions allowed. The city of Guangzhou was the place where the prices of vegetables, fruits, aquatic products and pork were opened up the earliest during the period at the end of 1970s and in the beginning of 1980s. The result of such action was that the situation became enlivened wherever the prices were opened up. The prices rose a bit in the beginning when they were opened up. But soon sufficient supplies quickly brought down and stabilized them. The citizens all applauded the reform. The biggest change brought about by opening up prices was the cancelation of coupon-based supply. In the 1960–70s, there were once 118 kinds of coupons at the most in Guangzhou. Then as commodity prices were opened up one by one, market supply increased and the coupons were cancelled one by one. There were still 48 coupons in 1982. In 1988 only grain and sugar coupons were left. And soon these two were also cancelled.²⁵

Different places nationwide mostly took the road of the city of Guangzhou in opening up prices within several years. In 1985, the state opened up the purchase and sale prices of the majority of agricultural and sideline products except for a few types subject to state orders, such as grains, cotton, edible oils and sugar. The prices of industrial consumer products were gradually opened up. In 1985, the prices of sewing machine, radio and wristwatch were opened up. In 1986, the prices of several durable consumer products such as bicycle, refrigerator and washing machine were opened up. In 1988, the prices of 13 brand name cigarettes and liquors were opened up. Before these measures, the prices of 160 and 350 kinds of small commodities were opened up respectively in September 1982 and August 1983. In 1992, the government opened up the prices of a large group of commodities and the items in the catalog of the commodities whose prices were subject to the management of the central government were reduced largely. Among them, the number of the prices of the means of production in heavy industry and of communications and transportation were reduced from 737 to 89, that of agricultural products from 40 to 10, and that of light industry commodities from 41 to 9. Hence, China's market price system was initially formed.²⁶

The “magical power” of the market was fully exhibited in the process of China's efforts to open up prices. Namely, although there were rises for a moment after some prices were opened up, the products related to them would soon started to burst like from a fountain. These products increased supply and activated the market so that prices gradually became stable. Hence more and more commodities showed the change from the situation that the goods were always in shortage, people queued up to

²⁵Guangzhou (1988).

²⁶Ma (1999).

buy them, and black market became rampant to the situation that the products showed sufficient supply and great diversity. The public felt in person the practical benefits that the reform brought to them and thus the reform won the powerful support of the extensive community of the mass. In 2006, the proportions of market-regulated prices reached respectively 95.6, 97.7 and 91.9% with respect to total volume of retail sales, total value of the purchase of agricultural and sideline products, and the total volume of the sales of the means of production.²⁷ The opening up of the prices brought about the comprehensive activity of the market so that the entire national economy was filled with dynamism and vigor.

II. The Practice of Implementing the Double-Track Price System of the Means of Industrial Production in the Middle and Late Periods of 1980s and Its Unification into Market Single-Track System in the Early 1990s was a Vivid Example of a Progressive Market-Oriented Reform.

The prices inside and outside state plans of the same kind of means of industrial production present in the same place at the same time point in China started to emerge in 1984 and such merger covered all products after 1985. According to the statistics in 1988, the proportions of the products sold at state-set prices among the ex-factory prices of heavy industry products were respectively 95.1% for the products in extractive industry, 74.6% for raw material products, and 41.4% for the products of processing industries. The parts left out of these proportions were sold at prices outside state plans or market prices. The double-track system of the prices of the means of industrial production was the concentrative manifestation of the coexistence of dual economic systems and, particularly, dual economic operation systems under the environment of shortage economy and also that of dual production systems and material circulation systems. The prices in double-track system could stimulate the increase of the output of the materials in shortage, encourage the production that exceeded state plans, and satisfy the needs of raw materials in non-state-owned economies that state plans could not consider and take care of, including the needs of town and township industrial enterprises. It was favorable to adjusting surplus and shortage, to regulating circulation, and also to knowing the regular price ratio relations. These were the positive side of implementing double-track prices. On the other side, double-track prices often affected the performance of supply contracts when people were driven by interests. It would encourage speculation, illegal reselling, embezzlement, and malpractice to seek personal gains. These were its defects. Experiences indicated that the positive role of double-track prices could be brought into better play if the difference between the prices in the two tracks were not so large or if market price was not more than one time higher than planned price. But its negative effect would become prominent if the price difference was very large or if market price was over one time higher than planned price. In the middle of 1980s, namely the early period of the implementation of double-track prices, the price difference was not so large. It was estimated that the price difference was about one time at the end of 1985 and in early 1986, which was in normal range. But later,

²⁷See *People's Daily*, August 25, 2007.

market price, driven by too heated demand, often became over one time higher than planned prices or even twice or thrice higher. Such a situation caused market disorder. Speculative reselling of the means of production became rampant. The voice calling for the cancellation of double-track system prices became very loud. In 1990 and 1991, supply and demand relations tended to ease as macroeconomic environment improved. The difference of the prices in the two tracks lowered within one time or even 50%. The CPC and the Chinese government took the favorable opportunity to unify the prices in the double-track system, mainly turning them into market single-track prices. This also indicated that the double-track system of the prices of the means of industrial production and its transition to market single-track system was another successful practice in China's progressive market-oriented reform.

III. China's Economic System Reform Created a "Miracle" in Its Economy. The Remarkable Sign of Such Miracle was That, from 1996 and 1997 after the Reform had been Implemented for More than a Decade, China Said Goodbye to the Shortage Economy from Which the Whole Nation Suffered for Several Decades. The Market Throve in General and People's Living Standard Was Greatly Improved. The Buyer's Market Started to Take Shape, a Situation of Which All the People had Dreamed and in Which Supply Exceeded Demand. And the Direct Driving Power That Contributed to the Success of Such Important Transformation was the Marketized Price Reform.

With price reform, the prices of various products and services were not determined and adjusted by the government but returned to be formed in market exchange. Thus there was broad space for the law of value to fully play its regulatory role in the production and exchange of commodity. When commodity supply was in shortage, prices would rise and thus commodity producers were stimulated to increase output with their best efforts so as to add supply. On the opposite side, if there was too much supply of commodity, prices would drop and thus consumers were stimulated to consume more while producers would reduce their output and supply. Then there could be the situation that commodity supply became insufficient and prices rose. Hence, social production and social demand formed inherent connections with such cyclic situation. Before the reform and opening up, China practiced planned economic system for a long time and gradually fell into shortage economy in which there was tight market supply, the phenomena of coupon-based ration, queuing and panic purchase were very common, and the people had much inconvenience in their daily life. Commodity prices were gradually opened up after China implemented reform and opening up and, in particular, pushed forward price reform. After commodity price saw certain rise, the situation would immediately form powerful stimulation to commodity producers so that they would produce and supply more so as to speed up development and increase benefits in market competition. With the action of market mechanism, every market entity endeavored to expand its own

market share. This caused commodities to increase in large groups and amounts. New products emerged endlessly with more product types and quality improvements. Commodities that used to be in shortage for a long time, such as food, clothing, household appliance and construction materials, quickly became abundant. Radical change occurred to market situation, in which a seller's market was turned into a buyer's market. Namely, most commodities were in the balance of supply and demand or the situation that supply was slightly larger than demand. Consumer sovereignty started to take form and could be realized.

The formation of buyer's market resulted in change in the efforts to maintain fair competition in market environment. In the past, local authorities imposed market blockade mainly to prevent agricultural products and raw materials produced locally to be transported outside their own precinct. They even send militias to guard county or city boundaries. After the formation of buyer's market, local blockade mainly became market blockade. Namely, local authorities required that local products be sold in the market and obstructed products produced elsewhere to enter local market in competition. In sum, opening up prices and allowing market competition brought prosperity and development. This was also the reason why market economic system could liberate productivity and improve the efficiency of resource utilization and allocation.

Price reform not only directly resulted in China's transformation from shortage economy to buyer's market but also promoted the rapid growth of Chinese economy. Price was the kernel of resource allocation by market. Opening up prices and turning to implement market price system caused prices to better reflect value and market supply and demand relationship, to reflect the scarcity of resources, and to form relatively reasonable price structure. Thus, producers and operators were given accurate market signals so that they could know what commodities to produce and operate. In this way, people promoted the optimization of resource allocation, improved economic efficiency, and promoted sustained and rapid economic development. The World Bank once compared the economic growth rates of over thirty developing countries with different price deviations and discovered that the countries with higher price deviations or distortions achieved economic growth rates two percent lower than the average while those with lower price deviations or distortions had economic growth rates two percent higher than the average.²⁸ After the beginning of the reform and opening up, China's economic growth accelerated from 1978 to 2010. The average growth rate of 9.9% was twice higher than the 3% average growth rate of developed countries and the globe in the same period. One important reason about this was that price structure tended to become reasonable after the prices were opened up and in turn promoted the optimization of resource allocation.

²⁸World Bank (1983, p. 63).

5 The Proposal of the Theory of Price Reform in the Broad Sense and the Task of Deepening the Price Reform of Production Factors and Resource Products in the New Century

In the 1990s, the majority of the prices of physical products and services were gradually opened up in China and regulated by the market. Then the circle of economics started to discuss and explore the question of the connotation of price reform. Should it be the price reform in the narrow sense which was only limited to the reform of the prices of physical products and services? Or should it be the price reform in the broad sense which should include the reform of the prices both of physical products and services and of production factors and resources?

Some economists tended to limit price reform as the reform of the prices of physical products and services. Such idea was consistent with the situation that competent department in charge of prices was only responsible for regulating the prices of physical products and services. Starting from such understanding, the economists believed that China's price reform had completed the whole journey and basically arrived at its destination because the majority of the prices of commodity and service was opened up to market regulation and market price system was initially established in the early 1990s. However, many economists thought differently and believed that price reform should not be limited only to the reform of the prices of commodity and service. It should also include the reform of the prices of production factors, such as fund, land, labor and technology, and resources. It should evolve from the price reform of commodity and service in the narrow sense to the reform in the broad sense which included the prices of production factors and resources. This was exactly the inherent logic of deepening and developing price reform. With the progress in the theoretical studies on socialist commodity and market economy, it was confirmed that production factors and resources should be gradually commoditized and put into the market to find their prices. As a result, the importance of prices in the broad sense and its reform was proposed and given extensive attention. In fact, the practice in China's price reform already entered a new stage from 1990s. It was characterized by the adjustment and reform of prices in the broad sense with the linkage of price, wage, interest rate and exchange rate, and later with the prices of resources included, for example, those of land and other natural resources. The reform was expanded from the marketization of the prices of physical products and service to that of production factors and resources. Market mechanism could be formed and comprehensive progress could be achieved in market-oriented reform only after the reform went beyond such a stage. It can be seen that the unification of the process of the price reform in the broad sense and the exertion of the overall function of market mechanism was the prominent characteristic of the price reform in the twenty-first century. Such unification signified exactly the deepening of people's understanding on price reform and such understanding powerfully promoted the deepening of price reform. Some treatises proposed that commodity price system included the price system that reflected the reproduction of physical materials and the price system that

reflected the relatedness of production factors and physical materials. Specifically, it referred to the price system of price, interest rate, dividend, wage, exchange rate, information and scientific and technological transfer. Price reform was exactly meant to rationalize the price system above.²⁹

It was proposed in the report of the Seventeenth CPC National Congress that people should “speed up forming unified and open modern market system with orderly competition, develop various kinds of production factor market and improve the price formation mechanism of production factors and resources that reflects market supply and demand relation, resource scarcity, and environmental damage cost”. Such statement was of greatly important guidance meaning. The report not only specifically explained that price needed to reflect the scarcity of resources but also listed environmental damage cost as price formation factor for the first time. It also proposed and highlighted that people should improve the price formation mechanism of production factors and resources. In the process of comprehensively building a well-off society, deepening price reform meant to earnestly and carefully implement and thoroughly practice the spirit of the report of the Seventeenth CPC National Congress in the above.

Until now substantial progress had been achieved in China’s price reform. The prices of a large amount of commodity and service were already opened up and regulated by the market. Market price mechanism was already established initially. However, there needed to be further improvement in this respect. After the beginning of the twenty-first century, the restriction of the “bottlenecks” in production factors, which included land in particular, energy and resources became increasingly prominent as economy grew rapidly. The key area of price reform was already shifted to continuing to push forward the marketization reform of the prices of production factors and resource products.³⁰

Deepening the reform of the prices of production factors and resources and realizing the marketization of the prices of production factors and resources was the inherent requirement in improving socialist market economic system. The criterion of a socialist market economic system was that market played a fundamental role in resource allocation. And resources referred to various production factors, which included fund, labor, land, technology and some natural resources, such as mineral resources, water resource and environmental resource. The key to bringing into play the fundamental role of the market in resource allocation was developing factor market and implementing the marketization of the prices of production factors and resources. If production factors and resources could not enter the market and circulate freely and if they could not move freely from industries with lower benefits to those with higher benefits, resource allocation could not become optimal and more effective. The entry into market and free circulation of production factors and resources meant that the prices of production factors and resources were formed by the market. Only when the prices of production factors and resources were opened up could production factor market develop well.

²⁹See Xu (1991).

³⁰See Zhang (2008).

During the reform and opening up, the prices of production factors started to be opened up gradually from 1990s. But the progress in this respect was still not very fast until the present. Except that the prices of technology had higher degree of marketization, the prices of other factors were still subject to much government regulation and intervention. The main part of interest rate, the price of fund as the most important production factor, such as the interest rates of deposit and loan in current account and fixed term account, was still subject to government regulation. These were not opened up and regulated by the market. In recent years, interest rates became lower or even showed a status of negative rates. This became an important reason that caused too fast growth of investment. The price of land as an important production factor was also distorted. China's average per capita farmland was $<1.4 \mu$, only 40% of the world's average. In the process of industrialization and urbanization, people needed to strictly limit the transfer of agricultural land into non-agricultural land and use transferred land effectively. They should prevent the waste of the precious land resource. But the current land market still had some way to go to meet the requirement in relevant regulations. The return of the transfer of agricultural land into non-agricultural land was not distributed reasonably. Land-lost peasants did not get the compensation that they should have. After the beginning of the twenty-first century, a multitude of migrant workers came to work in the city and various labor markets and talent markets developed quickly. According to the statistics of competent departments, 145 million migrant workers came to work in the city. Abundant labor resource was one of China's major advantages. People needed build and complete uniform and standardized labor market, form the employment system with the equality of rural and urban workers, and gradually achieve the marketization of labor price. Thus, millions of rural surplus labor could steadily and orderly transfer into the city and into the secondary and tertiary industries and China's social labor productivity could be improved. According to relevant statistics, rural labor was transferred into the secondary and tertiary industries and labor productivity was raised by four to five times on average. It can be seen how important the marketization of labor price and the development of labor market were to the rapid growth of China's economy.

After the beginning of the twenty-first century, the issue of resource shortage became increasingly prominent. The issues of resource price reform and resource product price marketization became noticeable and also a priority in China's efforts to deepen price reform in the future. Some production factors, such as land, was also an important resource. The price reform of resources also included the reform of the prices of certain part of production factors.

After the beginning of the twenty-first century and, particularly, from 2003 when the economic growth rate reached round 10%, the extensive mode of economic growth caused more and more prominent resource "bottleneck" restrictions.

First, energy consumption increased largely in recent years. The elasticity coefficient of energy consumption rose from below 0.5 from the beginning of the reform and opening up to the year 2000 to over 1 from 2002 to 2004 during the Tenth Five

Year Plan. From 2005 to 2007, the figure still reached 0.93, 0.76 and 0.59 respectively. The elasticity coefficient of electric power exceeded 1 each year from 2000 to 2007. It was respectively 0.58, 0.78 and 1.27 from 2008 to 2010.

Second, China did not have a great abundance of energy and other important resources and the efficiency of resource utilization was low. Such resource consumption was unsustainable in the future. China's per capita resource reserves of petroleum, natural gas and coal were respectively 11, 4.5 and 79% of the world's average. The per capita quantity of 45 kinds of mineral resources was less than half of the world's average. The resource reserves of iron, copper and aluminum were respectively 1/6, 1/6 and 1/9 of the world's average. Per capita quantity of farmland was 40% of the world's average and that of fresh water 1/4 of the world's average.

On the other side, China's utilization efficiency of energy and resources were low. In 2005, China's 10,000 RMB GDP energy consumption was 1.22 t standard coal, 3.2 times of that of the USA and 8.7 times of that of Japan. In 2005, China's GDP accounted for 5% of the world's GDP. But its primary energy consumption accounted for 14.7% of the world consumption, coal consumption being 36.9% of the world's figure, steel consumption 27% of the world's figure, and cement consumption 50% of the world's total. In 2006, China's GDP accounted for 5.5% of the world's GDP. But its energy consumption was 15% of the world's consumption, that of steel was 30% of the world's figure, and that of cement was 54% of the world's total.³¹ In 2009, China manufactured 568 million ton crude steel and 1.65 billion ton cement, respectively accounting for 43 and 52% of the world's total outputs. The majority of these products were consumed in China. Primary energy consumption reached 3.1 billion ton standard coal, accounting for 17.5% of the world's total energy consumption. And China's GDP accounted for only 8.7% of the world's total. Excessive consumption of energy and resources over many years caused increasing shortages in energy and resources in China. China relied on more and more imported energy and resources so that its foreign dependency of main mineral products rose from 5% in 1990 to around 50% at present. 40% or even over 50% of crude oil, iron ore, aluminum dioxide, and copper concentrates depended on importing. China's strong demand on resource products on the international market drove the large rise of such products on the market. At the end of 1998, the price of crude oil on the international market was only a bit over USD 10 a barrel. In 2008, it once rose to USD 147 a barrel. In 2011, it was still around USD 100 a barrel.

Finally, as energy consumption grew rapidly, the discharges of main pollutants kept increasing and ecology and environment were also deteriorating. Coal was the main component in China's energy structure. High energy consumption often brought the aggravation of environment pollution and hence brought economic loss. According to the *Research Report on China's Green National Economic Accounting 2004*, published by the State Environmental Protection Administration and the National Statistical Bureau, environment pollution caused 511.8 billion RMB economic loss nationwide in 2004, accounting for 3.05% of the GDP in the current

³¹See *China Economic Times*, March 19, 2007.

year.³² It was also pointed out in the report that the figure was based on incomplete research and actual loss was even larger. A few years ago, an evaluation of the “environmental sustainability index” was published at the World Economic Forum in Davos, Switzerland and China ranked No. 133 among 144 countries and regions on the globe.

In order to help Chinese economy to retain sustained, rapid, coordinated and healthy development, it already became an urgent issue to transform the mode of economic growth and the mode of development and to establish resource-saving and environment-friendly production mode and consumption model.

One important reason why it was hard to radically transform China’s extensive mode economic growth troubled by high investment, high consumption, high pollution and low benefits laid in the situation that the prices of resource products were subject to government regulation in China for a long time so that they were obviously very low, which encouraged people to abuse and waste. This was already a consensus in the circle of economics.³³ The main indications of the problem were as follows:

- (1) Too low land price. Some local governments requisitioned land from peasants at low prices with administrative powers and then ran development zones and granted land at low prices to attract businesses and investments.
- (2) Low water price. The water price in cities in China did not include the price of water resource. And in some places, it did not include wastewater treatment fee or such fee was very low and lower than costs. Agricultural water was almost free. Water price was generally lower in all the cities. Low water price resulted in the overall loss of China’s water industry in certain years.
- (3) Low energy price, including the prices of coal, oil, natural gas and electricity. The reason why a large amount of high energy consumption products competed to export was because China’s energy price was at a low level for a long time.
- (4) Low price of mining products. For a long time, only 20,000 among over 100,000 mine enterprises in China needed to pay to get mining rights. The majority of them took the mines for free through administrative granting. Some years ago, the average rate of mineral resources compensation fee was 1.18% in China while it was 2% to 87% abroad. Resource taxes and fees were raised in the recent few years but they were still low.

If people wanted to build a resource-saving society and form the production mode and consumption model that saved energy, land, water and materials, they had to deepen the price reform of resource products so that their price could reflect resource scarcity in a very good way. The mining and use of main resource products often caused damages to environment and ecology, so their prices also needed to reflect the costs in environmental and ecological damages. In general, people should gradually raise prices and employ price lever to force production enterprises and consumers to practice conservation when using resources so that people could improve the

³²See *Guangming Daily*, September 9, 2006.

³³See Zhu and Zhou (2008).

efficiency of resource utilization and put the operation of the entire Chinese economy onto the track of resource-saving economy.

It was pointed out in a research report of the World Bank that some economists carried out a research project involving 2,500 companies in 2004 and found that 55% of the decrease in the amount of energy use could be attributed to price adjustment, 17% resulted from research and development, and the rest was the result of the change in the share of industry in economy.³⁴

Some cities in China were troubled by serious shortage of water. How should people distribute limited water resources among the enterprises? Should the government distribute according to plans or should water be sold to the highest bidder in public auction? Facts proved that the latter was the way to use water resource effectively. According to the introduction in an article published in *China Prices*,³⁵ the research results in the USA showed that water use decreased by 42% when water price rose from 7.9 cents per m³ to 13.2 cents per m³ and by 26% when it rose from 15.9 cents per m³ to 21.1 cents per m³. It can be seen that price lever played a very obvious role in this respect.

In sum, if people wanted to transform the mode of economic growth and the mode of development and improve the efficiency of resource utilization, they had to push forward price reform and rectify the distortive phenomenon that the prices of resource products were at a lower level for a long time.

In the process of rationalizing the prices of various resource products, the key area was to raise energy price, raise the prices of natural gas and gasoline, and also gradually adjust the prices of coal and electric power. Raising energy price was an effective approach to lower energy consumption coefficient.

In addition, people should raise main resource compensation fees. Water resource price and sewage treatment fee should be included into the calculation of water price so that water industry could make up for their cost and gain some profits. The prices of the lands for business operation should all be determined through public auction in accordance with relevant regulations. Black case work should be prevented strictly, and so on.

In sum, people needed to gradually raise the prices of resource products and took opportunities to open up these prices according to the requirements of the law of value and on the basis of the needs in economic development and the affordability of the society. Some economists pointed out that China's CPI rose respectively by 1.8 and 1.5% in 2005 and 2006, which was a great opportunity to adjust the prices of energy and resource products. It was a pity that people did not have proper understanding on the importance of the price reform of resource products at the time so that the opportunity was lost and China did not make large adjustments to the prices of resource products. In the future, people should pay special attention to taking favorable opportunities to speed up pushing forward the price reform of resource products. Economists generally believed that 2009 was a good chance to implement

³⁴World Bank (2004, p. 70).

³⁵See Duan (2003).

the price reform of resource products. They hoped that China did not miss the opportunity once again.³⁶ In addition, after the prices of water, electricity, oil and gas were raised, people needed to consider giving certain subsidies to peasants and low-income community, which included moderately raising the standard of subsistence allowances or giving temporary subsidies.

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³⁶See Dong (2009).

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Chapter 21

China's Fiscal Transition and the Route of the Formation of the Public Finance Theory After 1990s



Peiyong Gao and Zhiyong Yang

After the goal of the reform of socialist market economic system was determined in 1992, China's fiscal transition picked up speed and fiscal theory also experienced radical change. The most noticeable situation was that multiple forces facilitated the formation and development of China's theory of public finance.

1 The Preparations for the Formation of China's Theoretical System of Public Finance

China's theoretical system of public finance was not formed abruptly after the determination of the goal of market economic formation. Before this, the academic circle made preparations in various aspects. The term "public finance" was basically overlooked before and then it reappeared in academic study. This change itself was an important piece of work.

The employment of the term "public finance" in China was something after the determination of the goal of social market economic system. But strictly speaking, public finance was not a completely "new-born" concept to China.

Before 1949, there was already the formulation of "Gong Gong Cai Zheng", namely public finance, in China. The concept of public finance was used in the book *General Finance* written by Chen Qixiu who studied in Tokyo Imperial University in Japan and the book *Finance* written by Shaw Kinn-Wei, doctor of economics of

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the Columbia University (Chen 1924; Shaw 1926) in the 1920s. But under the background then, the term “public finance” did not have much difference from government finance. During the 30 years from 1949 to the time before the implementation of the reform and opening up, the term “public finance” was rarely seen in the circle of fiscal theory and in the area of fiscal practice. The term was used more and more in different occasions only after the beginning of 1980s. In 1983, the Chinese translation of *Public Finance* written by American economist Otto Eckstein was published. Its translator Zhang Yushan literally translated the title “Public Finance” as “Gong Gong Cai Zheng Xue”, namely the study of public finance (Eckstein 1983). The book was not of a great length. But it exerted larger influence under the economic and social environment then. Yet probably people at the time were not aware of the profound connotation in the concept of public finance and the profound change that it would brought to China’s economic and social life. The circle of the theoretical study of fiscal matters did not paid adequate attention to the translation of the term. They did not make much special discussion and exploration on it. Nor did they give it any special meaning.

According to the examination of Yang (2008), the occasions in which “public finance” was used from the founding of the People’s Republic of China in 1949 to the time before the proposal of the goal of the reform of socialist market economic system in 1992 roughly included the following: when the term was used in the translation and introduction of foreign fiscal theory and practice, when it was used to refer to fiscal matters in capitalism, when it was used to discuss the issues on Chinese economic system reform, when it was used to summarize the direction of fiscal reform, and when it was used in the same meaning as “fiscal”.

The marketization orientation of China’s reform was set up before the determination of the goal of market economic reform. At the time, economic reform was still in the stage of “crossing the river by feeling the stones” and, naturally, it was difficult to determine the goal of fiscal reform. Most of reform measures and research suggestions were proposed centering round the fiscal issues in reality. For example, various circles made in-depth discussion on “rejuvenating the fiscal area” in order to address China’s fiscal difficulty from the middle and late period of 1980s and early 1990s. But it was after 1992 that people truly carried out their study from the angle of transforming fiscal model and constructing China’s public finance theory.

2 The Practice of Marketization Reform Pushed Forward the Progress in the Practice of “Public Finance” Reform

I. Using the Term “Public Finance” to Scale Down Fiscal Expenditure

After the beginning of the 1990s, there was pressure from the difficulty in fiscal revenue and expenditure after China implemented economic system re-tracking. The proportion to fiscal revenue to GDP kept decreasing and there could hardly be any major change to the situation within a short period. Under such background, the

circle of the academic study on fiscal matters and the area of relevant practice tended more and more to find a way out from cutting down the scale of fiscal expenditure. (For example, Ye 1993; An and Peiyong 1993) As a result, there was the action of adjusting expenditure structure for the purpose of scaling down expenditure scale and also the formulation of “eliminating excess”, “making up absence” and “correcting misplacement”. The adjustment of expenditure structure involved the change in fiscal expenditure model that had been used for many years. It was very necessary to propose a goal with certain direction different from the past. The state finance of typical market economy countries had the characteristic of narrower function scope, which matched exactly with China's initial intent to cut down the scale of expenditure through adjusting expenditure structure. Besides, in that period, people were used to putting public finance together with the pattern of fiscal expenditure of typical market economy countries. They even used public finance as the synonym of the state finance of typical market economy countries. Therefore, with the fiscal system and mechanism of typical market economy countries as reference system, the term “public finance” was “borrowed” to discuss the practice in cutting down the scale of fiscal expenditure and easing the difficulty in fiscal revenue and expenditure.

II. Comprehensive Reform of Fiscal and Taxation Systems and Public Finance

Simply adjusting expenditure structure and not making change on the side of revenue at the same time could only relieve part of the financial difficulty at the most. In order to get out of the limitations of such “crippled” adjustment and radically get out of the difficult situation in fiscal revenue and expenditure, fiscal and taxation system reform was implemented in 1994. The tax distribution system in 1994 played an important role in regulating the fiscal relationship between central and local authorities. It also played a positive role in strengthening the macroscopic regulation of the central government and exerted decisive influence on the behavior choice of local government. The taxation system reform in 1994 was one such reform of the largest scale and the most far-reaching influence from the founding of the People's Republic of China. Its basic principle was defined as “unifying tax law, imposing fair tax burden, simplifying tax system, and implementing reasonable division of power”. This principle, which contained sixteen characters in Chinese and thus was known as a “sixteen-character” principle, exerted considerable impact under the general background at the time because it was, after all, rooted in the soil of socialist market economic system and based on the goal of constructing a taxation system adapted to socialist market economic system. The principle could only be explained with the philosophy of market economy (Xiang 2002). Therefore, when people summarized the theoretical basis and ideological source of tax system reform, the term “public finance” often appeared from time to time in relevant literature that discussed the issue of tax system reform.

III. The Determination of the Goal of the Public Finance Reform in Practice

Either adjusting on the side of expenditure or the change on the side of revenue, represented by reforming tax system, involved after all local issues rather than global ones in fiscal system and mechanism. Local adjustments done in a piecemeal approach

were indeed important but the issue of fiscal difficulty could not be resolved in its entirety without reconstructing fiscal system and mechanism as a whole and incorporating local adjustments into the framework of the whole fiscal system and mechanism. It was even impossible to truly establish a fiscal system and mechanism adapted to socialist market economy. People also found at the time that they could not find any other terms except for public finance to function as a concept that could command all the leads of fiscal reform and cover all the items in the reform. So taking the national fiscal work meeting held on December 15, 1998 as an opportunity, China's decision makers made an epoch-making important decision: to establish China's public finance framework (Li 1998).¹ Besides, from then on, public finance construction officially entered the work agenda of China's governmental departments as part of the specific positioning in the goal of China's fiscal reform and development.

Five years later, the Third Plenary Session of the Sixteenth CPC Central Committee was held in October 2003. The meeting adopted the *Decision of the CPC Central Committee on Several Issues on Improving Socialist Market Economic System*. At the meeting and also in the important document above, the strategic goal was proposed that people should further improve and complete public finance system on the basis of the judgment that the framework of public finance system was initially established (Li 2003). As people had recognized that a complete public finance system was an important component of a complete socialist market system, it naturally became part of China's development goal to put a complete public finance system onto the blueprint of a complete socialist market economic system and thus to design the plan for further pushing forward public finance construction, incorporating the close connection between the two. So it can be said that the meeting definitely brought new opportunities to China's public finance construction.

The Seventeenth CPC National Congress held in 2007 made comprehensive arrangements in the areas of economic, political, cultural and social constructions in China in the new period on the basis of comprehensively summarizing the historical process and precious experience in reform and opening up. In these arrangements, both the exposition on the issues involving economic and political constructions and the description of the picture of cultural and social constructions were incorporated with the philosophy of public finance and permeated with the spirit of public finance. The term "public finance" was even used directly in them. In particular, the formulation of "improving public finance system centering round the equalization of basic public service and the construction of development priority zone" (Hu 2007) signified in a more extensive scope and at a deeper level that the theory and practice of China's public finance was pushed onto a new stage.

It could be found in further examination that the term "public finance" could be found currently in China in a series of important documents of the departments of the CPC and the Chinese government, in the discussion of the academic circle on important economic and social issues, centering round the outlook of scientific

¹At the meeting, Li Lanqing, the then vice premier of the State Council and member of the Standing Committee of the Political Bureau of the CPC Central Committee, specifically proposed that people should "positively create conditions to gradually establish the basic framework of public finance".

development, the transformation of government functions, and the construction of public service system and social undertakings, and even in the topics about improving people's livelihood that common citizens talked about in their pastime chatting. All these involved the explanation on relevant contents with public finance as the main lead. It can be said in certain sense that it might not be exaggeration at all that China already entered a time of comprehensively building public finance with all its strength.

3 The Formation and Development of Public Finance Theory in China

I. "Dual Finance" and the Target Model of China's Fiscal Reform

There was once the formulation of "dual finance", which was used to name the target model of China's fiscal reform, in the construction of the system of public finance theory pushed forward centering round the exposition of the concept of public finance.

In 1993, Ye Zhenpeng and Zhang Xin proposed that the target model of China's fiscal reform should be a dual finance model or a dual structure finance model that included both public finance and state-owned assets finance or state-owned capital finance. Ye Zhenpeng published an article entitled "Adapting to the Requirements of Market Economy and Reconstructing Fiscal Functions" in the third issue of *Public Finance Research* in 1993. After that, he and Zhang Xin jointly submitted a paper "On Dual Finance" for the Seventh National Symposium on Basic Fiscal Theories held at Xiamen University in late June 1993. The paper contained a comprehensive introduction to the basic views in dual finance theory. In 1995, Ye Zhenpeng and Zhang Xin jointly wrote the book *Dual Structure Finance—A Study on China's Fiscal Model* and made systematic and comprehensive exposition and demonstration on dual finance theory. The second edition of the book was published in 1999.

The dual finance theory² believed that the fiscal administration under socialist market economy was "dual finance", a term as a shortened form for dual structure finance, which was an organic unity that consisted of relatively independent public finance and state-owned capital finance. In market economy and under the circumstances of the separation of administration from enterprise management, of administration from state-owned assets management, and of state-owned assets management and enterprise management, fiscal behavior was manifested objectively as the formation of public finance, in which the government carried out distribution in the identity of social management entity to meet public needs in the society, and also as the formation of state-owned capital finance, in which the government carried out the value management and distribution of returns of state-owned capital in the identity of the representative of the whole people ownership system of the means of production.

²The dual finance theory was jointly developed by Prof. Ye Zhenpeng and Prof. Zhang Xin. The section here mainly introduces the theory on the basis of Zhang (1999).

Whether dual finance model could become the target model of China's fiscal reform depended to a large extent on whom to consider the issue of socialist market economy. There were two understandings on socialist market economy in general: The first kind was "public ownership system or state ownership system + market economy" and the second kind "social justice + market economy". If the former was the case, then state-owned capital finance could coexist with public finance. If the latter was the case, state-owned capital finance lost its basis in reality to a large extent because the role of state ownership system was not stressed especially any more.

There were large amounts of operating state-owned assets in reality. The fiscal model in the transitional period could be a dual finance model but such model could only be used in certain stage. The State State-Owned Assets Administration established in 1988 and the State State-Owned Assets Supervision and Administration Commission in 2003 were to a large extent the organs that exercised the functions of state-owned capital finance.³ Of course, even though different fiscal components were defined in dual finance, they did not necessarily have corresponding organs in reality. As long as fiscal operation was carried out according to the philosophy in dual finance, it could be said that the dual finance model was established.

The dual finance theory was a theory that summarized the target model of fiscal reform and that was proposed after the authors above borrowed from western fiscal science and took into account the specific national conditions in China. Public finance was a study devoted to resolving market failure, an issue that western fiscal science also faced, while state-owned capital finance focused on preserving and increasing the value of state-owned capital or profitable or operating state-owned assets, an issue particular in China.

However, such outlook on fiscal administration, radically speaking, only adapted to the needs in transitional economy. It could not adapt itself to the fully-established socialist market economy. By dividing fiscal administration into public finance and state-owned capital finance, people could adapt it to the strengthening of state-owned capital administration during the transition period and promote the satisfaction of the requirements on preserving and increasing the value of state-owned capital because it achieved the personification of state-owned assets and resolved the issue of the vacancy of principal to a certain extent. But how to address the relationship between public finance and state-owned capital finance, which came up in such a situation, was an issue very hard or even basically impossible to solve.

II. How to Understand and Interpret "Public Finance"

Logically speaking, when "public" and "finance" were put together and formed the term "public finance", there would definitely be some special meaning different to the original concept "finance". So in the discussion carried out centering round public finance, there was a question that China's fiscal academic circle could never avoid or

³In reality, the function of state-owned capital management was broken down and exercised in multiple government departments, which were not limited to state-owned assets administration departments.

get round, namely what was the difference between “public finance” and the original term “finance”?

In the inference on the basis of the logic in the above, “public finance” naturally took the original “finance” as its object of transformation. It can be said that “public finance” was a new concept formed against the original concept of “finance” (Liu 2000). The problem was that, if there was some difference between “public finance” and the original concept “finance”, it was the highlighting of “publicness” and so the original concept “finance” certainly possessed some “non-public” characteristic. Or it lacked “public” characteristic at least in certain aspects.

In fact, no matter how people understood the concept subjectively, an important work item which consumed much energy in the Chinese circle of financial study from the very day the concept of public finance was proposed and taken as the goal of reform, namely to find the point of difference between “public finance” and the original term “finance”. In addition, there was a period of very dramatic experience in the circle in summarizing the “non-public” characteristics of the original “finance”.

In the beginning, many people, for example, An (1999) and Gao (2000), interpreted “non-publicness” as production and construction expenditure and hence defined public finance construction as the withdrawal of fiscal expenditure from the area of production and construction. However, as time passed and progress was achieved in practice, people quickly noticed that, although it conformed to the direction of reform of marketization to take the area of public service as the main direction of investment in fiscal administration and correspondingly reduce production and construction expenditure, reduction was not equal to withdrawal. What needed to be reduced was only limited to the part of expenditure in competitive areas. The public functions to be performed by the government could not exclude the production or provision of public utilities and infrastructure under any social form or economic system. The production or provision of public utilities and infrastructure definitely belonged to the series of production and construction expenditure and definitely did not exclude publicness.⁴ Therefore, it was necessary to reduce the investment in the area of production and construction in fiscal budget in the process of the reform. But it was absolutely not the substantive content in public finance construction to withdraw fiscal expenditure from the area of production and construction after such reduction or even to take the withdrawal as the direction of adjusting the structure of fiscal expenditure.

There were also many people, for example, Zhang (1999, 2004), regarded the fiscal administration during the time of planned economy as the typical cause of “non-publicness”. And they attempted to reveal the meaning of public finance construction from the institutional difference between planned economy finance and market economy finance and hence determined that public finance was the product of market economy or the fiscal type or model that adapted itself to market economy. They even regarded public finance as an equivalent to western finance.⁵ However, people could

⁴Many people based their criticism on public finance on such a point or attacked it in the criticism.

⁵A representative explanation was that public finance was the distributive activity or relationship with which the state provided public products or services under the condition of market economy. It

not explain many things starting from this point when they examined the entire history of the development of government finance. In the long history of human society during several millennia of pre-market economy times, there were many government expenditure items that possessed public features, such as the expenditures on water projects, building roads and bridges, disaster relief, sacrifice and even military matters. In addition, even in the pattern of fiscal expenditure dominated by production and construction expenditure during the time of planned economy in China, many expenditure items which could be classified as part of the production and construction domain, including urban infrastructure and social welfare facility construction, belonged to typical “public” expenditure. Therefore, if people took market economy finance as an equivalent to public finance and regarded all non-market economy finance as belonging to “non-public” finance, it would be impossible for them to explain the fiscal system under pre-market economy and its pattern of operation and the public expenditure items under planned economic system. Besides, it would be hard for them to clearly assort the motivation and model of the behavior of the government departments as the managing entities of the entire society and also that of other behavioral entities.

There were also people who simplified public finance subjectively and arbitrarily. The prominent manifestations of such treatment were seen in two extremes: either viewing “public finance” as a new category or discipline different from the original “finance” or regarding it as a faddish concept with the same connotation as the original “finance”. The former put public finance in opposition to the category and discipline of finance in the past and attempted to interpret it into a new category or discipline different from that in the past. Thus there were new terms such as the “study of public finance”, the “specialized field of public finance”, and the “research direction of public finance” in academic circle in China. The latter replaced the word “finance” with “public finance” everywhere when it was used without adding any substantial meaning to the term. Then there were new phrases like “budget of public finance”, “revenue of public finance”, “expenditure of public finance”, and “policy of public finance”. Some people even advocated renaming the Ministry of Finance as the “Ministry of Public Finance” and departments or bureaus of finance as departments or bureaus of public finance.⁶ However, when following such a line and giving it some more thinking, people could easily notice that it could hardly hold water either to take “public finance” as something new or to regard it as a remolding of an old concept. On the one hand, public finance needed, according to the logic of the former, to have new connotation and extension, new research object or new research approach different from those related to the original “finance”. But these elements did not appear in “public finance”. The connotation and extension, research

was the model of government revenue and expenditure or fiscal operation mechanism to satisfy social public needs. It was a kind of finance that adapted itself with market economy and the prevailing fiscal system and institution in market economy countries. Zhang (1999) carried out in-depth study on public finance from the three aspects of basic characteristics, theoretical summarization and the history of the theory of finance.

⁶There were more wordings of such kind in the media, such as “public finance pays the bill for normal education”, “public finance saves rural kids from dropping out of school”, and so on.

object and research approach of “public finance” did not show any difference from the original “finance”. On the other hand, the replacement of the original concept of “finance” with “public finance” became according to the logic of the latter the conduct to follow fashion or something redundant without any substantial meaning (Chen 1999). Thus people just needed to run the replacement function on word processing software to complete everything in the entire world about public finance through changing a term. Of course, this was something inconsistent with the reality. Therefore, the two manifestations above were two extremes but neither touched the substance of public finance. To certain extent, they represented the misinterpretation of the concept “public finance”.

In the great trend of paying attention to and improving people's livelihood, a new formulation about public finance emerged. Some people regarded public finance as the equivalent to livelihood finance. They even took whether finance focused on the matters related to people's livelihood as the measurement to distinguish “publicness” from “non-publicness”. However, it could be found easily when people observed a bit more that such understanding was incorrect. In the time of planned economy, large amounts of funds in fiscal administration were invested in production and construction. The improvement of people's livelihood was relatively overlooked. In the process of the transition from planned economy to market economy, people made the mistake of “throwing away the baby with the bathwater” and shifted the burden of a great number matters about people's livelihood to the market. So a large amount of financial work was left undone in the area of people's livelihood all the way along the development course of China. At present, it was certainly necessary to increase the investment of finance into the matters of people's livelihood and emphasize the urgency of improving people's livelihood. But after all, improving people's livelihood was not the sole function of finance. In addition to this, other typical public matters, such as national defense, diplomacy, environment protection and social management, were all “public” functions that finance had to perform. The current preferential policy on the area and matters of people's livelihood only indicated that the area became a bottleneck that needed to be taken as a priority in investment when it was compared with other functions and matters of finance. It did not mean that the functions and matters of finance only included improving people's livelihood. Neither did it mean that only matter of people's livelihood was of public nature. So when people misinterpreted the action to improve people's livelihood, which was somewhat to make up the past as all the content of public finance, overlooking the other while focusing on one thing and moving from one extreme to the other, their view was in fact biased and it failed to reveal the substance of public finance.

The difficulty that people encountered in finding the point of difference between “public finance” and the original “finance” in fact reflected the particularity of China's public finance issues.

Public finance developed along the course from the change of the translation of a term in English to being borrowed and used in the practice of fiscal reform and tax system reform and from constructing the frame work of public finance, to further improving and completing public finance system, and then to improving

public finance system. This basic course meant that public finance was not a pure academic concept that was tested in careful demonstration but more a product of the practice of reform.

Under the condition of traditional planned economy, fiscal system and mechanism could be summarized as “state ownership finance + urban finance + production and construction finance”. The activities about fiscal revenue and expenditure mainly involved state-owned departments and urban regions. And they were mainly carried out centering round production and construction matters. At the time, relevant conditions determined that state-owned departments were mostly located in cities while what the cities had in its concentrated areas were state-owned departments. The matters in production and construction expenditure were mostly operated in a closed manner inside the system of state-owned departments. So when viewed from ownership system, these three layers of state-owned departments, cities and production and construction were highly overlapped. Fiscal revenue and expenditure mainly manifested as the income and spending within the domain of state-owned departments. Now that it became the matter and choice of a single domain, its operation was rooted inside state-owned departments even though there were certain regulations. It did not need to be put onto the public track. Nor needed it to adapt itself to the public rules and philosophy of the entire society. Yet with the establishment of the goal of the reform of socialist market economic system and according to the practical requirement of building “finance of multiple ownership systems + finance of urban and rural integration + public service finance”, the activities of fiscal revenue and expenditure involved the departments of multiple ownership systems, including both state ownership and non-state ownership. It concerned all territories of China, including both the city and the countryside, and all its social members. Besides, it centered round the matters in the entire area of public service which focused on satisfying social public needs. At the moment, fiscal revenue and expenditure went out of the domain of state-owned departments and evolved into matters related to the income and spending of the entire society. Once fiscal revenue and expenditure needed to operate in the scope of the entire society and once it involved the personal interests of all social members and became a matter and choice of the mass, it had to be incorporated into the track of public matters and be placed on the basis of public rules and public philosophy of the entire society.

The coverage difference of the two concepts in system and mechanism and the conversion of the former into the latter brought China’s financial system and mechanism to a higher and broader platform of system transformation: Changing the rules of the game—old systems and regulations applicable state-owned departments among themselves were replaced by new “public” systems and rules applicable to the whole society. In fact, the proposal of the concept of public finance and the important change that occurred in China’s fiscal area centering round the concept was exactly a process of system transformation (Jia 2008). All the things that people had done under the slogan of public finance was to push forward the transformation of China’s fiscal system, which laid in taking China’s fiscal system and mechanism onto public track and operating according to public rules and philosophy.

Therefore, public finance was a kind of financial system arrangement in the end. But different from the past, it was a kind of fiscal system arrangement with an aim to satisfying social public needs rather than other needs. Corresponding to such arrangement, public finance construction was a transformation of fiscal system. It was a fiscal system transformation that took the transformation into publicness rather than other goals as its orientation.

4 Realizing the Inherent Characteristics of Public Finance into the Practice of System Construction

The understanding on the inherent characteristics of public finance had to finally end with system construction. Only in this way could the development of China's public finance theory have solid practical foundation.

It was very important to understand this point. It tells people that they could summarize the inherent characteristics of public finance with the word "publicness" and the process and direction of China's fiscal reform and development with the phrase "transformation into publicness". And they could actualize the substance of China's public finance construction with fiscal system transformation, which could manifest "publicness".

For such purpose, it was necessary for people to stand at the height of system transformation and profoundly understand and master the basic characteristics of public finance system in accordance with public rules and philosophy.

It obviously needed theoretical abstraction. In view of the particularity of the issue of China's public finance, people needed to draw from multiple areas to establish the ideological source of such theoretical abstraction. It should be both constructed on the basis of the general principles of public economics and rooted in the practice of reform and opening up. It should both extensively draw from all the achievements of civilization in the society of the mankind, including those in typical market economy countries, and take root in China's basic national situation.

If people gathered the ideological sources together and compared them with the situation in the time of planned economy, they could summarize the basic characteristics of public finance system into the following three properties.

The first property was publicness. Namely, public finance should satisfy the public needs of the entire society rather than the particular needs of any ownership system, region, social class or social group. It should take such a point as the rule to define its financial functions. Finance should not intervene in any matter that did not belong to or be incorporated in the area of social public needs. And it had to get involved in any matter that belonged to or could be incorporated in the area of social public needs.⁷

⁷Li (2002) once summarized the function of public finance as satisfying the functions of social public needs, legal regulations and macroscopic regulation and control. He also defined the function of

Different from traditional system and mechanism which focused on satisfying the needs of state-owned departments, urban regions, and production and construction, public finance system needed to satisfy the public needs of the entire society. The so-called social public needs were defined in comparison with private and particular needs. The term referred to the needs proposed with the society taken as a whole or with the entire society as a single unit. It did not refer to the needs of some people. Nor it referred to the needs of the majority, but those of all the people. The first one of the prominent characteristics of this concept was its wholeness. In other words, social public needs were proposed jointly by all social members as a whole rather than individually or separately by one member or some social members. The second one was its concentration. In other words, public finance should be organized and implemented in concentration by the entire society rather than by one social member or some of them through their own activities respectively. The third one was its compulsoriness. In other words, people should only rely on political power and employ compulsory means to realize it. They should not rely on personal will and realize it through the conduct of market exchange.

With these properties as the rule, the representative matters of fiscal functions that could be included in social public needs were as follows:

(1) Providing public service; (2) Regulating income distribution; (3) Implementing macroscopic regulation.

The second property was nonprofit. Namely public finance took the maximization of public interests as the starting and end points in arranging fiscal revenue and expenditure rather than the gaining of profits through investment or the pursuit of profit on operation.

Public finance system was rooted in its nonprofit nature, which was totally different from traditional system and mechanism plagued by the mixing up of administration and enterprise management and the full involvement in competitive areas. This was because government and enterprises played different roles under the condition of market economy and had radically different behavioral motivation and pattern.

As an entity of economic behavior, an enterprise took the maximization of profit as the motivation of its behavior. It needed to achieve the goal of making profit through participating in market competition. As the entity of social management, the government could not set the motivation of its behavior as getting corresponding reward or gaining profits. It could only take the pursuit of public interest as its responsibility. Its function and duty could only be to provide necessary system guarantee and material foundation for the orderly operation of the market through satisfying social public needs. Under special circumstance, the activities of providing public goods or service would generate profits in different amounts incidentally. Despite of such a situation, the basic starting or end point of public finance was still to satisfy social public needs rather than gaining profits. When such a situation was manifested in fiscal revenue and expenditure, it became the principle that the obtainment of fiscal

satisfying social public needs with “publicness” and regarded such function as the basic function of public finance.

revenue had to be based on raising funds to satisfy social public needs. The arrangements in fiscal expenditure should always take satisfying social public needs as its aim. Fiscal revenue and expenditure formed centering round the satisfaction of social public needs generally only focused on input and did not have output or had almost no output. The cycle of its movement was basically “only to put in and not to take out”.

In addition to the general reasons in the above for the great stress put on nonprofit nature, there were the following several considerations mainly made out of actual national situation:

- (1) As the entities of social management, government departments always needed to have corresponding political power. These departments with political power would naturally use such power to realize their desire to pursue profits once they entered competitive areas and attempted to gain profits. It was very likely that such a situation ended up in the disturbance or sabotage of the normal operation of the market because of power-for-money deal.
- (2) Once government departments entered the market as competitor for the purpose of gaining profits, the basic rules on the division of work between market and government would be broken. Because of the mixing up of administration and enterprise management, it was very likely that government behavior, which was supposed to focusing on satisfying social public needs, became alienated into enterprise behavior characterized by the pursuit of operating profits. In the end, government behavior deviated from the track of publicness on which it pursued public interests. Or “displacement” of fiscal funds emerged in the area of social public needs because they were used in profitable projects.
- (3) Once fiscal revenue and expenditure went beyond the boundary of satisfying social public needs and were extended to competitive area, it was inevitable that various entities of economic behavior were given differentiated treatment. In the end, the activities in fiscal revenue and expenditure which focused on satisfying social public needs would break the fairness in normal market and fair competition because of its preferential treatment to certain areas. It could even obstruct the orderly development of market economy.

The third property was regulation. Namely, public finance meant the management of fiscal matters in accordance with the law. The will of the administration or officials should not be taken as the behavioral code in the operation of fiscal revenue and expenditure.

Different from traditional system and mechanism which had strong color of randomness, public finance system was built on the basis of a series of strict regulations and standards. The fundamental reason for this laid in the fact that the fiscal revenue and expenditure which focused on satisfying social public needs was also closely related to the personal interests of all social members. Fiscal revenue needed to come from the contribution of the whole community of social members. Fiscal expenditure needed to be used in matters that concerned the well-being of all social members. And the cost and benefit brought about by the difference between fiscal revenue and expenditure would eventually end up on all social members. It was

of course necessary to establish and follow strict systems and regulations as fiscal revenue and expenditure operated within such an extensive range and involved such a multitude of social members.

In general, these systems and regulations included at least the following three features.

- (1) They should be based on the rule of law. In other words, the mode and quantity of fiscal revenue and the direction and scale of fiscal expenditure had to be established on the basis of the rule of law. People could not just collect and spend no matter what and how much they wanted.
- (2) All revenue and expenditure of the government should be included in the budget. Government budget was not only the plan for the annual fiscal revenue and expenditure of the government but also an important approach for the activities in fiscal revenue and expenditure to receive the supervision of the people's congress at various levels and all social members. The preparation, examination and approval, implementation and final accounting of government budget could put the behavior of the government related to revenue and expenditure under such supervision from the beginning to the end. And it could be inferred that all the revenue and expenditure of the government had to be put under such supervision. It was not permitted that there were certain government revenue and expenditure that were not subject to supervision and existed outside the budget.
- (3) Fiscal and taxation departments took charge of all the government revenue and expenditure in general. That is to say, all government revenue and expenditure was put under the centralized management of fiscal and taxation departments. Funds were raised from all social members and then given to various government functional departments as activity funds. Various government functional departments were not allowed to separately collect money from and spend money on the objects that they served or managed. Thus people could radically remove the soil for generating corruptive conducts of "embezzling money with power" and "exchange power for money" so that government departments could perform their functions with regulated conduct under a regulated institutional environment.

5 Conclusions and Revelations

When people looked back at the process of the evolution of the public finance theory in China and focused on the pattern of its development in reality, they could get the following several mutually related conclusions and revelations.

First, there were commonalities and differences between public finance and the original term "finance". When viewed from a purely academic perspective, public finance was not at all different from the category and discipline of "finance" in the general sense, both of which had very long history. Whether the word "public" was added to it or not, finance had always been referred to government revenue and

expenditure or the activities in it. The discipline of finance was always a science about government revenue and expenditure or the activities in it. Therefore, public finance was not a new category different from the original term "finance" or a new science different from the original discipline of "finance". But when people turned into the domain of practice and examined public finance with a reform perspective, it had substantive difference from the "finance" during the time of planned economy in China. There were the changes from local coverage to comprehensive coverage, from differentiated treatment to indiscriminate treatment, from focusing on production and construction to covering the entire area of public service, from the application of the particular regulations of state-owned departments to the application of the "public" regulations in the entire society. And these changes were the focal points of the reform against traditional fiscal system and mechanism. Therefore, public finance was a kind of fiscal system arrangement different from the original "finance".

Second, "publicness" was the inherent and intrinsic attribute of finance as an economic category. It existed in finance under any social form and economic system without exception. What was different under different situations was the sufficiency of its publicness and its form of manifestation. Either when it was called "public finance" or when it was called "finance", it meant no change to its public attribute. When examined on such basis, China's road of public finance construction was in essence a process to turn China's fiscal system and mechanism back onto the track of "publicness". It could also be recognized on the basis of the logical chain of practice-theory-practice and with attention paid to the link between traditional Chinese finance study and traditional Chinese fiscal system and mechanism that there was also a process of returning to the track of "publicness" for the traditional Chinese finance study, which was built on the foundation of traditional Chinese fiscal system and mechanism.

Third, the traditional fiscal system and mechanism with the characteristic of "non-publicness" was a special arrangement based on the special historical background of the time of planned economy. If this was the case, then it could be regarded as a special measure proposed on the basis of the historical background of system retracking that people proposed the concept of public finance and marked with it the direction of China's fiscal reform and development. Therefore, people should comprehensively push forward the fiscal system reform with the orientation of the "transformation into publicness" at the institutional level in accordance with the basic requirement of public finance system and then construct a fiscal institutional system that could highlight the feature of "publicness". Such task was both something inherent to public finance as an economic category and a necessary choice of China in a special historical background.

Fourth, public finance entered the view of Chinese scholars in certain sense in the process of learning and borrowing from the fiscal theory and system applied in typical market economy countries. When examined from an even broader view, public finance, as a banner in China's fiscal reform and development, burgeoned from the soil of reform and opening up, took root in China's basic national situation, and drew from all the achievements of civilization in human society. Therefore, the general principles in the science of public finance, the basis of practice of the reform and

opening up, China's basic national situation, and relevant fiscal philosophy, rules and institutional arrangements in the achievement of civilization of all human societies including those in typical market economy countries jointly formed the ideological basis of China's public finance system.

Fifth, when people examined the process of China's fiscal reform and development until the present on the basis of the basic characteristics of public finance system, they could see that China's public finance system only had an initial framework although it was already established. There was still a long way to go on the journey toward a complete public finance system. People still needed to do many important things before China could truly enter a new conception of public finance system. They needed to recognize that economic marketization and the transformation of fiscal administration into publicness were the two sides of the same coin. "Publicness" was an intrinsic attribute of finance as an economic category which existed from the very beginning. A very urgent task that people faced was that they needed to aim at the goal of public finance system and constantly advance toward this goal. In this way, they could build an institutional system of public finance which adapted itself to a complete socialist market economic system and connected itself with the intrinsic attribute of finance.

Sixth, China's public finance was a concept with rich Chinese characteristics which was proposed on the basis of China's own needs so as to resolve its own issues. The theory was rooted in the particular national situation in China and, in particular, its national situation of atypical market economy (Gao 2005). People needed to take their position at a height of the mutual mergence and permeation of theory and practice and give a definition of public finance specific to China with special thinking and perspective. And they should, on such basis, transform the disciplinary system of China's finance study and draw the blueprint for China's fiscal reform and development. This was a special mission that history had entrusted upon the scholars of this generation. The achievements obtained in such work would become important components to the theoretical system of socialism with Chinese characteristics.

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Chapter 22

The Evolution and Development of the Thoughts on Finance in China



Lei Zhang

The evolution of China's financial system after 1949 underwent three stages: (1) From 1949 to 1978, China formed during the period of planned economy a financial infrastructure which consisted of the separated management systems for fiscal and credit funds and a mono-bank system with the separation of deposit banking and loan banking as its kernel contents and which mainly served industrialization. It also formed a corresponding financial superstructure which could be said to be characterized by the comprehensive balance of fiscal administration, credit and materials. (2) From 1979 to 2008, China progressively formed a marketized financial infrastructure which had a two-leveled banking system with central bank and state-owned commercial banks as its foundation and mainly served industrialization. It also formed the current framework of macro-prudential financial regulation system as its corresponding financial superstructure. (3) The outbreak of global financial crisis in 2008 proposed new demands of the time to building a financial system that could match and support urbanization. In this chapter, the author would like to make a brief historical review on the thoughts on finance in China, centering round the evolution of its financial system.

1 Financial System and Financial Thoughts During the Period of Planned Economy

The financial infrastructure in planned economy could be analyzed with fund flow identity. The fund flow identity of planned economy could be summarized as $I = S + \Delta M$ s, in which I stood for enterprise fixed assets investment, S for national savings, and ΔM s for the increase of money supply. In planned economy, people constructed

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an enterprise investment and financing system which consisted of the so-called separated management system for fiscal and credit funds and a mono-bank system with the separation of deposit banking and loan banking as its kernel contents so that such system adapted to the situation that the government was almost the sole entity in saving and investment. The so-called separated management system for fiscal and credit funds referred to the system in which fiscal departments satisfied the needs of the enterprises for fixed asset investment funds and current funds with fixed quota. Such highly-centralized financial system was restricted to satisfy the temporary or seasonal needs of the enterprises for above-quota current fund only in the form of bank loans. Besides, a mono-bank system was established in order to prevent fiscal departments from shifting their tasks in supplying current funds to the banks and also because of the difficulty to determine current fund quotas. The kernel content of a mono-bank system was the separation of deposit banking and loan banking. Namely, the bank head office controlled all credit decision power and its branches only had the power to take in deposits and did not have the power to issue loans independently. Besides, the deposits that the branches took in could not be used to issue loans directly but had to be turned into bank head office. The credit volume of a branch was determined by the credit quota set up by and transmitted from the head office. So it can be seen that it was impossible for a branch to issue loans independently and carry out credit expansion. As shown in the identity above, the banking system in China was deprived of the right to turn savings (S) into investment (I) and directly provide fixed asset investment loans in planned economy because of the combination of the separated management system of fiscal and credit funds and a mono-bank system. Besides, people imposed effective control on the indirect participation of the banking system in fixed asset investment in which it provided current fund loans through credit expansion, namely the increase of money supply (ΔM_s). It was very obvious that debt financing, represented by bank credit, was in principle excluded from the investment activities of an enterprise in planned economy. State equity investment in the form of fiscal appropriations became almost the sole form of enterprise investment and financing.

During the period of planned economy, China also formed a financial superstructure characterized by the so-called comprehensive balance of fiscal administration, credit and materials. Ge Zhida believed that, first of all, people had to realize the internal balance of fiscal administration and credit matters respectively before achieving the comprehensive balance of fiscal administration, credit and materials. Here, fiscal balance entailed the principle in socialist fiscal work of adhering to the balance of fiscal revenue and expenditure with some surplus. And credit balance required that the use of credit fund had to follow the principle of “taking loans according to plans, having material guarantee, and repaying when they were due” so as to maintain the regular currency supply and withdrawal on the market and keep the adaptation of currency circulation to commodity circulation.¹ Second, people needed to form the mutual combination, unification and balance of fiscal funds and credit funds. When people arranged fiscal budget each year, they needed to take the balance

¹Ge (1963).

of credit receipts and payments into consideration and increase the allocation of credit funds in addition to increasing the allocation of current funds. When determining the scope and quantity of making up the balance in credit in fiscal budget, people needed to take the nature of its formation as the basis. If such balance was caused by economic loans, such as those for the expansion of commodity circulation and the increase of the purchase of agricultural and sideline products, the needed increase of money supply should be effected through issuing currency. If such balance was caused by fiscal loans, for example, the balance formed with the funds often occupied in the form of commodity fund loans and agricultural loans, the funds needed should be provided in fiscal budget. It can be seen here that the most important function of a bank during the period of planned economy was to realize the use of the funds in fiscal budget in the form of credit in addition to its functions of accepting idle funds in the society and issuing loans with them. It was very obvious that there was certain necessity to have certain balance in the credit receipts and payments of the banks under such financial system in order to adapt them to the needs in economic development. And such balance needed to be made up through budgetary allocations and economic currency issuance. In other words, fiscal balance played a role more important in the comprehensive balance of fiscal administration and credit. Finally, after establishing the balance between fiscal budget and the credit funds of banks, people also had to realize the balance between fiscal administration, credit and the supply and demand of materials. In particular, they needed to realize the compositional balance between fiscal revenue and expenditure, credit receipts and payments, and the supply and demand of materials. People needed to address well the relationship between accumulation and consumption and promote the production in the first department and the second department, namely the proportional coordination of the production of capital and consumer goods, and realize the internal balance of supply and demand of different commodities and product categories. Only in this way could they provide reliable guarantee to realizing the prior balance between fiscal revenue and expenditure and credit receipts and payments and avoid the occurrence of deficit concealed in false balance in fiscal administration.

It can be seen here that Chinese scholars already realized the difference between the prior and post balance of fiscal revenue and expenditure and credit receipts and payments during the period of planned economy. And they positively explored the cause of the phenomenon of the deficit concealed in false fiscal balance and its countermeasures. Lin Jiken believed that people did not verify and allocate current funds adequately during the period of planned economy. In particular, they arranged too large scale capital construction. These resulted in the misappropriation of current funds. On the one hand, it caused the problem of fiscal expenditure exceeded budget plans. On the other hand, it might hamper the timely formation of production capacity in investment projects, which would result in the decrease of the economic benefits of the enterprises and the generation of nominal fiscal revenues. Therefore, one of the reasons for the formation of deficit concealed in false fiscal balance was that “capital construction takes from fiscal budget, fiscal budget takes from banks, and

banks issue money” and this caused the issuance of money out of fiscal reasons.² Lin Jiken further proposed that people could calculate the volume of needed money on the market through calculating the ratio between the volume of social cash transaction and velocity of money under socialist system on the basis of the formula for Marx’s law of currency circulation. This volume in turn was helpful to promoting the issuance of currency out of economic reasons.³ Here, the total volume of social cash transaction included the five elements of the volume of social commodity sales, the volume of purchase of agricultural and sideline products, labor service supply, the volume of savings increase or decrease, and residents’ tax payment. With respect to the determination of the velocity of money, people needed to adopt a historical research approach. First, they needed to study and analyze the normal velocities of money in history. The so-called normal velocity of money was that under the circumstance of stable finance and prices and solid currency circulation. Second, they needed to study and compare the situations of economy and currency circulation at present and in history. They should analyze the differences present between the current velocity of money and the current economy and those in history and determine what are the normal factors or abnormal ones that affected the increases and decreases of the velocity of money. Thus, they could find out the normal velocity of money for certain period of planning. It was on the basis of such research method that Lin Jiken proposed the very influential empirical value of currency issuance of 1:8 during the period of planned economy in China. Namely, people needed to increase the issuance of RMB one more yuan for fund turnover for each RMB eight yuan increment in the volume of cash transaction. Yang Jianbai and Huang Da explored the countermeasures to realize the comprehensive balance of national economy respectively from the angles of setting reasonable prices of products on the basis of social production price and of realizing the planning of bank credit. Yang Jianbai proposed that products should be priced on the basis of the production price approach in socialist economy. Specifically speaking, people needed to set prices according to fund profitability. Namely price should be product cost plus profit calculated according to advanced fund profitability.⁴ Only when people set prices according to production prices could they relatively accurately determine the scale, standard, speed and proportions of the development of national economy, verify and determine economic effect and correctly handle various economic relations. It can be seen that Yang Jianbai already realized that reasonable pricing played an important role in improving resource allocation. Huang Da proposed that people should utilize bank credit to improve resource allocation. Huang Da believed that there were the following connections between currency circulation and bank credit: (1) The organization of the entire currency circulation in socialist economy was based on bank credit; (2) The redistribution of bank loans and the expansion and contraction of such loans directly regulated the volume of money in circulation.⁵ Therefore, it was the

²Lin (1981).

³Lin (1963).

⁴Yang (1963).

⁵Huang (1962).

key to realize normal currency circulation to organize well bank credit so that credit business could adapt itself to material turnover plans in a planned manner. Huang Da emphasized in particular that planned currency circulation required not only that currency circulation had to consciously adapt itself to the turnover requirements in material plans but also that currency circulation became the active factor to promote planned turnover of materials. For such reasons, people had to make arrangements in advance on the range of the increase and decrease of the volume of money during certain period of planning and the distribution and direction of flow of the volume of money between different departments, regions and seasons. Only in this way could people consciously guarantee normal currency circulation. After all, if the movement of materials was irrational, the provision of loans only on the basis of the principle of material guarantee would definitely cause irrational credit distribution and, in turn, irrational currency circulation. Nevertheless, the conceptions of Yang Jianbai and Huang Da about improving resource allocation respectively through reasonable pricing and through utilizing bank credit were destined to be impractical during the period of planned economy. In the former, pricing according to the production price approach only involved the reasonable adjustment of planned prices. But it still met severe attack. In the latter, because bank credit funds mostly came from allocations in fiscal budget and hence fiscal balance was always the key to comprehensive balance, the effect of utilizing bank credit to allocate resources would definitely be very limited. Moreover, under the circumstance that the prices of the products were seriously distorted, it was impossible for resource allocation through utilizing bank credit to really have a role to play in the area.

In sum, China's financial infrastructure and superstructure during the period of planned economy was favorable to the maximization of the rate of capital accumulation and the acceleration of industrialization in theory. However, such institutional arrangement in which investment and savings functions were centralized in government planning departments had low savings-investment conversion efficiency in general. Such problem was not just seen in inferior capital allocation efficiency. In the 1970s, China's economic growth slowed down noticeably and excessive investment occurred frequently, which in the end caused serious famine during the period from 1960 to 1962.

2 Marketization Financial System and Thought Mainly to Serve Industrialization

As marketization reform was launched in China and, in particular, the scope of market pricing kept increasing, profound change occurred to the pattern of national income distribution in China and its corresponding savings and investment structure early from 1981. In such transformation, the savings of government departments could not cover its expenditure for a long time. The savings of the enterprise sector also could not cover its own investment demand after part of its retained profits was

deducted as the income of the employees in redistribution. Hence, the shortage in savings and investment could only be made up with the savings in family sector. It was very obvious that the increasingly widening gap between savings and investment required that people deepen the reform of enterprise investment and financing system. As a result, the finance industry became an indispensable “match-maker” between depositor and investor in savings-investment conversion process who would promote the evolution in China from fiscal-administration-led economy, which centered round centralized government investment, to finance-led economy, which was characterized by dispersive enterprise investment.

In addition to system reform, the choice of economic growth mode also exerted important influence on the development of financial system. In the beginning of the reform and opening up, China seized the historical opportunity of international industrial transfer and element reorganization. It took full advantage of the preferential policies for bonded areas to develop export-oriented industrialization mainly characterized by processing trade and resolve the issues of release of surplus labor and insufficient capital on international market. The growth mode of export-oriented industrialization was highly adapted to the situation of the development of productivity in the beginning of the reform and opening up. Inspired by the ring theory about the spatial distribution of productivity proposed by Johann Heinrich Von Thünen in his book *The Isolated State* (Johann Heinrich 1966), some scholars proposed that the world’s economic system could be divided into three parts of central, semi-marginal and marginal areas in certain order, each of which could be more than one in number.⁶ Among them, the centers of the world’s economic system could be the centers both of productivity and of purchasing power and market. They possessed the ultimate power to determine the market price of commodity. In the beginning of the reform and opening up, the situation of the development of productivity in China that its per capita income was extremely low determined that it was no rival with developed economies as the centers of the world’s economic system at the time. This was the radical reason that China once selected the growth mode of export-oriented industrialization. It should be said that China very successfully and indirectly exported labor to the international market in a very long period of time through developing export-oriented industrialization. It accumulated tremendous wealth and capital and finally broke poverty trap, namely the per capita income below USD 1,000. It was in order to match and support the growth mode of export-oriented industrialization that China developed financial infrastructure and superstructure corresponding. The financial infrastructure mainly served export-oriented industrialization and took a two-leveled banking system with central bank and state-owned commercial banks as its kernel. Its corresponding financial superstructure was represented by the current framework of macro-prudential financial regulation system. These two parts formed the marketization financial system which mainly provided service to export-oriented industrialization. In the chapter, the author will introduce them respectively while taking into account the relevant evolution of financial thoughts.

⁶Johann Heinrich (1966).

I. The Establishment of Two-Leveled Banking System of Central Bank and State-Owned Commercial Banks and Relevant Financial Thoughts

Financial thoughts always played an important role in the financial reform and development in China. Among them, there was a type of thought which analyzed the statistical identity calculated mainly with national income and fund flow. It discussed from a macroscopic view the promotive role of the changes in savings structure and investment structure after the beginning of the reform and opening up to the formation of marketization financial system. Bei Duoguang analyzed the impact of the changes in savings structure and investment structure to financial structure.⁷ He pointed out that profound change occurred to China's savings structure from 1978 to 1981 mainly because of the impact of the change in the pattern of national income distribution. As savings-investment difference expanded increasingly, China was evolving from a fiscal-administration-lead economy, which centered round centralized government investment, to a finance-led economy, which was characterized by dispersive enterprise investment. Guo Shuqing also pointed out that the sectoral structure of aggregate savings experienced an obvious shift between two extremes. Government and enterprises were originally main savings entities, their savings accounting for 75.6% in 1979. But now residents became the main savings entity, their savings accounting for 65.9% in 1989. The sum of the savings of government and enterprises was more than thrice of the residents' savings but now it was only more than half of the residents' savings. The source of investment funds changed structurally from mainly coming from fiscal budget to mainly coming from bank. Financial market grew rapidly. All these were closely related to the profound shift in the structure of aggregate savings.⁸ Xie Ping analyzed the process of the deepening of finance industry in China from 1978 to 1991 and the characteristics of the assets and liabilities structure of China's government, enterprises, individuals and state-owned banks at the end of 1991. His work highlighted the role of state-owned banks in the investment and financing of the enterprises.⁹

It was very obvious that the changes of savings structure and investment structure after the beginning of the reform and opening up only implied that the realization of the smooth savings-investment conversion urgently required the development of financial intermediation and financial market. The specific form of China's financial structure was still an impending question. In general, China's mainstream financial thoughts developed along the direction of affirming a financial system dominated by bank credit. One type of analysis among them focused on discussing the necessity and rationality of restoring the banks' function in providing investment and financing to enterprises. Liu Guangdi analyzed the necessity to restore the banks' function of capital allocation.¹⁰ He suggested that bank loans should be provided to supply not only all the operating funds that enterprises needed in the future but also the capital construction investment and long-term fund that the enterprises needed so

⁷Bei (1986).

⁸Guo et al. (1991).

⁹Xie (1992).

¹⁰Liu (1979).

as to strengthen the banks' promotive and supervisory role to the enterprises. Yang Peixin made very original interpretation on the separated management of fiscal and credit funds and believed that the issuance of medium- and short-term equipment loans did not violate the principles of the separated management of fiscal and credit funds.¹¹ This was because the difference between fiscal budget and banks laid in that fiscal revenue and expenditure involved no charges while bank receipts and payments involved charges. If people believed that such difference represented the fundamental principle of the separated management of fiscal and credit funds, it was completely reasonable and normal for the banks to issue medium- and short-term equipment loans because people could take new paths to improve the effect of investment in a microscopic perspective and strengthen comprehensive balance in a macroscopic perspective. Huang Da expounded on the necessity and feasibility of allowing banks to provide full loans for operating funds and fixed assets investment to enterprises so as to accelerate economic growth from the perspectives of the nature of currency as transaction medium and the process of credit expansion in which loans created savings. Cao Erjie, Li Minxin and Wang Guoqiang and Shang Ming, Wu Xiaoling and Luo Lanbo also described the process of institutional transformation in which state-owned banks became the dominant entity in providing full loans of operating funds and fixed assets investment to enterprises.^{12,13}

The financial system dominated by bank credit won more extensive recognition and some important achievements were achieved centering round building a two-leveled banking system of central bank and state-owned commercial banks. With the establishment of the reform goal of socialist market economy, Dong Fureng proposed the reform direction of building a two-leveled system of central bank and commercial banks. In such a direction, it was required that fiscal organs issue bonds to make up for fiscal deficits and that the central bank assist fiscal organs by purchasing government bonds through its open market business so as to improve the independency of the People's Bank and make it China's central bank in the real sense. In addition to this, people had to make the central bank independent of the government. In order to reform specialized banks into commercial banks in market economy so that they could operate independently and assume sole responsibility for their profit or loss, people also needed to implement shareholding system reform among specialized banks and strip off their policy-related businesses. Besides, the paper also cover the issues like building more commercial banks, including regional commercial banks, to break the monopolistic structure of specialized banks and realizing the single-level legal person management of banks under shareholding system.¹⁴ Hui Xiaobing and Li Xiaoxi made similar analysis on the direction of banking system reform.^{15,16} Xie Ping analyzed the reason why the reform of specialized banks lagged behind and the

¹¹Yang (1981).

¹²Cao et al. (1992).

¹³Shang et al. (1992).

¹⁴Dong (1994).

¹⁵Hui (1994).

¹⁶Li (1994).

challenges that people were confronted in the reform. He also proposed the goal of the reform and the countermeasures in the reform, including adjusting organizational structure.¹⁷ Xie Ping believed that the reason for the lagging behind of the reform laid in the situation that the specialized bank system still had “positive return” effect during certain period to the four interests entities of specialized banks themselves, central government, local government and enterprises. In fact, such “positive return” came from the huge loan increment of specialized banks each year. And in turn, such increment came from the increase of loans, or monetary base, of central bank or from the increase of the balance of social necessary cash in the process of the monetization of economy. It was the income of currency issuance.

There were also some scholars who discussed the necessity to develop capital market. They attempted to introduce more factors of financial market into a financial system dominated by bank credit. This type of analysis mainly developed centering round two theoretical directions.

First, some scholars hoped to develop capital market and, in particular, stock market to improve the governance structure of state-owned enterprises. Huang Fanzhang demonstrated that shareholding system was the best form of industry organization to realize socialist whole people ownership system and, on such basis, discussed the important meaning of developing stock market.¹⁸ Zhang Yichun and Zhou Yinggang proposed, employing the analytical methods in information economics, that the shareholding system and contracting system reform of the enterprises were more effective in forming stimulation mechanism but they failed in forming effective supervision mechanism. Therefore, people should produce more adequate enterprise operation information through developing securities market so as to reduce the information asymmetry between investors and operations and promote the formation of effective enterprise supervision mechanism.¹⁹ Wang Jinbin and Liu Yuanchun proposed that limited markets or products on China’s capital market increased the opportunity cost when investors exited stock market and caused serious information distortion and terrible infirmity of the basis of stock valuation. It was very obvious that inadequate development of capital market seriously restricted the options of investors and reduced the efficiency of pricing and corresponding enterprise governance function.²⁰

Second, some scholars hoped to improve the proportion of direct financing through developing capital market so as to realize the socialized sharing of financial risks and to avoid the over-concentration of financial risks in state-owned banks. Yi Gang analyzed the structure of China’s financial assets in 1978, 1986, 1991 and 1995. On such basis, he summarized the characteristic that the proportion of direct financing was lower in China’s enterprises and the harm brought about by such characteristic. And he proposed that the most important financial reform measure to correct such

¹⁷Xie (1994).

¹⁸Huang (1989).

¹⁹Zhang and Zhou (1997).

²⁰Wang and Liu (2000).

deviation was to positively yet prudently develop China's stock market and bond market for direct financing.²¹

Zhang Chunlin proposed that the radical cause of the problems that state-owned enterprises faced was the financing system with the state as the sole intermediary as the legacy of the planned economy. The solution to radically resolve the issues of state-owned enterprises laid in the replacement of the financing system of planned economy with that of market economy, namely the replacement of state financing with competitive capital market. Besides, people should resolve the historical arrears left by state financing system as quickly as possible. These included both the implicit state debt burdens embodied as the arrears in social insurance and explicit state debt burdens embodied as bank bad debts.²²

Zhou Tianyong proposed that important change occurred to the pattern of the distribution of national income in China from the beginning of the reform and opening up. There was the transition from the situation that the direct capital injection from fiscal budget dominated the operation of national economy to that of the capital-loan-type economic operation in which state banks centralized the supply of loans to operate enterprises. Such capital-loan-type economy resulted in inflation pressure and financial risks related to the bad debts accumulated in the banks. And such accumulation was caused by the low efficiency of state-owned enterprises. The radical solution laid in the measure that people should open up the assets structure of the enterprises horizontally to the society. In this way, people could form capital demand, streamline the channels of direct financing, and form capital supply so as to realize the socialization of the capital and risks in investment, production and operation in national economy.²³

Wang Jinbin proposed a development path different from those described in traditional financial repression, or liberalization, or restraint theory. In the 1990s, China adopted a policy of both development and control in financial reform when addressing the relationship between financial reform, risks solution and economic growth. Financial control provided the capital needed in the reform and, at the same time, it permitted individual residents to participate in the transactions on the government-led capital market so as to socialize risks. China's financial control during the period of transition eased the fund relations between state-owned banks and state-owned enterprises. It also reduced the proportion of anticipated bad assets of the banks as much as possible. While state-owned banks were allowed to continue to function as main creditors of large- and medium-sized state-owned enterprises, people bought time to solve risks within relevant system and, in particular, among state-owned commercial banks.²⁴ Therefore, according to Wang Jinbin's analysis, a financial system dominated by bank credit came more from strategic institutional arrangement.

²¹ Yi (1996).

²² Zhang (1997).

²³ Zhou (1997).

²⁴ Wang (2000).

But the theoretical position that people should realize the improvement of enterprise governance mechanism and the socialized sharing of financial risks still met extensive criticism from relevant research results that took the design of the rational structure of financial market as its main research content. Liu Guangdi proposed specifically that the strategy for developing China's stock market should include the following: (1) People should take indirect financing as the dominant form and direct financing as the auxiliary form. When examined from the historical evolution of the way of financing, a development process existed between direct financing and indirect financing. During the time when and in a region where commodity economy was undeveloped, the direct loan between individuals enjoyed an important status. During the time when and in a region where commodity economy was relatively developed, indirect financing through the intermediation of financial institutions enjoyed a dominant status. During the time when and in a region where commodity economy was very developed and high efficiency was pursued in fund procurement, the status of indirect financing became even more important. Considering the restriction of the standard of the development of commodity economy, people should draw from the experience in Japan during its economic takeoff in the beginning of the development of the stock market in China and adopted the model of taking indirect financing as the dominant form and direct financing as the auxiliary form. (2) People should take bond market as the main target area and positively develop stock market at the same time. (3) People should combine the development of state-owned shareholding enterprises with that of non-state-owned shareholding enterprises. (4) People should realize the mutual promotion and combination between improving market conditions and regulating shareholding system.²⁵ Liu Biao and Yang Haiqun discussed the special role of banks in enterprise investment and financing and enterprise governance.^{26,27}

Zhang Wenkui proposed that enterprise debt could also play a role in improving enterprise governance through debt repayment guarantee mechanisms. Debt repayment mechanisms were divided into the two categories of prior guarantee and post guarantee and included automatic obligation fulfilment, creditor's prudence and credit rationing, liquidity and convertibility, and piercing the corporate veil. Improving debt repayment guarantee mechanism in China could be more effective than simplistically developing stock market for the supervision of enterprise operation under the current enterprise financing structure.²⁸

Lin Yifu, Sun Xifang and Jiang Ye proposed the theory of optimal financial structure from the perspective that development stage and financial structure should match with each other. They emphasized in particular that regional medium- and small-sized banks should become the main components of the financial system of developing countries. Specifically speaking, labor-intensive industries had comparative advantage in developing countries. And the enterprises in these industries were generally of smaller size and smaller fund demand. The product market of the enterprises

²⁵Liu (1993).

²⁶Liu (1994).

²⁷Yang (1994).

²⁸Zhang (2000).

and the technologies that they owned were relatively mature. The risks of these enterprises mainly came from entrepreneurial risk. Because the medium- and small-sized enterprises were relatively opaque and their scale of financing was smaller, their financing through financial market involved very high fixed transaction costs. These labor-intensive medium- and small-sized enterprises generally did not have very high rate of return and hence could hardly acquire funds through issuing stocks or bonds publicly. But banks and other financial intermediaries and, particularly, regional medium- and small-sized banks possessed the comparative advantage in saving information costs in handling the business of labor-intensive medium- and small-sized enterprises and providing financing service to them. So it was natural that these banks should become the center of the financing system of developing countries.²⁹

In summary, the financial system dominated by bank credit won more extensive recognition and it exerted important influence to the practice in building a two-leveled banking system of central bank and state-owned commercial banks. From 1979 to 1984, China's original mono-bank system was transformed into a hybrid banking system through the reform of bank credit system in which people restored the banks' function in providing loans to enterprise fixed assets investment. Different from the mono-bank system, various specialized banks already became independent economic entities under the hybrid banking system and possessed corresponding credit functions. They were not just specialized institutions that implemented state credit plans. In 1985, people implemented the reform of the credit fund management system in which people adopted the measure of providing actual loans in actual deposit accounts to specialized banks, established central bank system in management, and formed the two-leveled banking system of central bank and state-owned specialized banks. From 1990s, China further carried out the reform of building a two-leveled banking system of central bank and state-owned commercial banks. On the one hand, the degree of commercialization of state-owned banks were raised obviously through a series of reforms in operational and financial restructuring of state-owned specialized banks, unified legal person management, financial supervision, property right and governance structure, and introduction of credit market competition. State-owned commercial banks shifted from originally focusing more on providing full credit support to enterprise investment to stressing the balance between providing such support and stabilizing credit quality and controlling credit risks. On the other hand, the independence of the central bank was improved from 1993 through such reforms as establishing the goal of monetary policy as "maintaining monetary stability and promoting economic development with it", prohibiting the making up of fiscal deficits through overdrawing from the central bank, and transforming the operation of the macroscopic regulation system of the central bank from implementing multileveled regulation to stressing the centralization of regulatory power. The reform of the financial and accounting system related to profit retentions in 1993 also eliminated the profit-gaining motivation of the central bank, which promoted the central bank to

²⁹Lin et al. (2009).

become more specialized in macroscopic regulation. The increase of the independence of the central bank and the elimination of its profit-gaining motivation were combined with the improvement of the degree of commercialization of state-owned banks. This changed the original nature of the central bank as a wholesale bank so that the two-leveled banking system of central bank and state-owned commercial banks were established.

II. Two-Levelled Banking System of Central Bank and State-Owned Commercial Banks, Imbalanced Financial Development and Loss of Balance in Foreign-Related Economy

The establishment of the two-leveled banking system of central bank and state-owned commercial banks gave state-owned commercial banks a kernel position in savings-investment conversion. On the one hand, state-owned commercial banks mainly provided financing to the production and investment of the enterprises through providing industrial and commercial loans. On the other hand, these banks took in domestic savings through various types of deposits. Such financial system dominated by the credit service of state-owned banks resulted in imbalanced financial development, namely that the process of monetization “throve like forever” while the process of capitalization underwent constant twists and turns, which was seen in the market value of shares, which fluctuated drastically, and the development of bond market, which seriously lagged behind. From the beginning of the reform and opening up and, in particular, after the middle of 1990s, China’s monetization index (M2/GDP) went up quickly. It not only became greatly higher than that in major developed countries but also exceeded that of the developing countries at the level of development similar to China’s. Yi Gang (1995) believed that China’s monetization process was basically completed in 1985 and regained its impetus in 1992. M2/GDP was 0.9 in 1992 and its kept rising after that. In 1997, it reached 1.22. According to the figure of the GDP that China published after revision, the ratio between M2 and GDP in China already reached 1.66 at the end of 2006. In 2009, monetization index regained its rising trend, driven by unprecedented easy monetary policy, and reached 1.8. In 2010, it reached a new high of 2. It was very obvious that, under such financial infrastructure and imbalanced financial development, savings vehicles were of relatively monotonous options. They were mainly concentrated in various types of bank loans. Because the projects involved in financing were generally of smaller size, the enterprise industrial and commercial loans issued by the banks were mainly of medium- and short-term ones. Its higher liquidity could indirectly provide better protection to savers who faced serious information asymmetry and promote the smooth conversion between savings and investment. However, such monotonous types of savings vehicles still caused the difficulty of the insufficiency of savings vehicles to China in its high growth. People had to use domestic savings surplus and capital obtained correspondingly through current account surplus to purchase the financial assets portfolios of developed economies and, in particular, of the USA. Only in this way could they promote the smooth conversion between savings and investment and realize sustained economic growth. Christopher D and David N (1994) proved that

high growth could bring high savings but not necessarily vice versa.³⁰ Michael et al. (1997) further emphasized the importance of such effect in the economy of East Asia.³¹ China was no exception to the point that high growth brought high savings. Because domestic finance was underdeveloped, which was particularly seen in the insufficiency of savings vehicles provided by the financial market, China could not fully absorb its own high savings. Only after the high savings became the fund source of the USA's currency and debt expansion and were converted into its current account deficit could they once again become the driving power of economic growth. Therefore, the two-leveled banking system of central bank and state-owned commercial banks, in this sense, became the kernel of financial infrastructure under the condition of open economy, which mainly served export-oriented industrialization.

It can be seen here that it was exactly the mismatch between high economic growth and the lagging behind of the development of domestic financial market that caused China's dependence on the financial market of the USA and the corresponding imbalance in foreign-related economy. Only from such an angle could people propose the countermeasures to correct such imbalance in a better way. Regrettably, most of China's domestic research in the area underestimated the influence of domestic financial underdevelopment to the imbalance in foreign-related economy. The scholars mainly focused their energy on analyzing the negative effect of the imbalance^{32,33} (Yao 2007; Zhang and He 2006). Shi Jianhuai's research reflected such a point prominently. He challenged the theory of the syndrome of "conflicted virtue" related to high savings proposed by Ronald I. McKinnon in his article. The article analyzed the problem present in the demonstration of two key propositions behind such theory, namely that the changes in exchange rate failed to adjust current account and that the risk premium of local currency assets became negative to attract the holding of USD assets. He believed that McKinnon's statement that China might fall into deflationary spiral and zero interest rate liquidity trap was incorrect. Therefore, the moderate appreciation of Renminbi had feasibility.³⁴ However, the empirical research that Shi Jianhuai carried out himself proved McKinnon's judgment on the deflationary effect of Renminbi's appreciation.³⁵ The reason why conflict occurred between model deduction and empirical research results in Shi Jianhuai's study was because he overlooked the endogenous demand of domestic financial underdevelopment for international financial market and corresponding imbalance of foreign-related imbalance. It was very obvious that Renminbi's appreciation and deflation could coexist without conflict when international economic and financial market was in the status of expansion. Only in this way could China retain its dependence on international financial market. And the imbalance of its foreign-related economy would then be generated correspondingly.

³⁰Christopher D and David N (1994).

³¹Michael et al. (1997).

³²Yao (2007).

³³Zhang and He (2006).

³⁴Shi (2005).

³⁵Shi (2007).

Of course, some research results concerned the importance of developing capital market in exchange rate reform. After the pressure of Renminbi's appreciation rose abruptly, Li Yang and Yu Weibin proposed that it was crucial to determine the priority order between the reform of exchange rate formation mechanism and the change of the standard of exchange rate in the process of the reform of Renminbi exchange rate system. The article believed that the mechanism reform should be prioritized and that people should always pay great attention to the stability of exchange rate in the process of the reform. This should be the basic strategy for the reform of the Renminbi exchange rate system. Returning to managed floating exchange rate system was a proper choice for implementing such a strategy. In the process of returning to managed floating exchange rate system, currency mismatch constituted main risk. In order to manage such risk effectively, people should retain higher level of foreign exchange reserve. It should strengthen the prudential regulation on the issue of currency mismatch, implement sound macroeconomic policy, and promote the development of capital market in the process of steadily pushing forward the relaxation of the control over capital items.³⁶

III. The Characteristic of Government Dominance in the Two-Level Banking System of Central Bank and State-Owned Commercial Banks and Its Influence to Economic Stability and Growth

When compared with the mono-bank system during the period of planned economy, the system of central bank and state-owned commercial banks contained more marketization factors. However, its obvious characteristic of government dominance and the accompanying financial distortion still brought uncertainties to certain extent to China's economic stability and growth, which caused extensive attention. Zhang Lei summarized the financial system with government dominance as one in which the state provided implicit guarantee to prevent financial intermediaries from bankruptcy and replicated the concentrative equilibrium of low interest rate credit through credit interest rate regulation combined with credit interest rate subsidy. The financial system with government dominance was a phasal optimal financial institutional arrangement jointly determined by financial underdevelopment and learning-by-doing economic growth, which was embodied as export-oriented industrialization with processing trade as its main part under open economic conditions. Its effect would keep weakening with economic growth and corresponding financial development so that people needed to realize marketization transformation at proper timing after they broke the bottleneck of demand restraint in financial development.³⁷ (1) The purpose of the financial system operation with government dominance laid in breaking the bottleneck of demand restraint in financial development. At such moment, because marketization financial system, or in essence the separating equilibrium of credit, could not guarantee the inclusion of all eligible borrowers, it was necessary to have government intervention and to stimulate financial intermediaries or the banks to carry out loan issuance and credit expansion. (2) The financial

³⁶Li and Yu (2005).

³⁷Zhang 2010.

system with government dominance had better operation effect in learning-by-doing economic growth. Learning-by-doing economic growth provided the growth mechanism that matched the best with the financial system with government dominance. It was helpful to alleviating the issue of the adverse selection of concentrative credit equilibrium and improving capital allocation through bringing into play the function of indicating the post signal on the quality of the investment projects on the market of competitive products, fostering borrower or entrepreneur reputation mechanism, and controlling the credit size of investment projects. (3) The operation of the financial system with government dominance would encounter the dilemma of resource mobilization and systemic risk control. This was the inevitable result caused by the situation that concentrative credit equilibrium could not realize the differentiated pricing of the financing cost of venture investment projects in advance. It can be seen here that the characteristic of government dominance of the system of central bank and state-owned commercial banks exerted the function of development finance to certain extent.

It was exactly because of the characteristic of government dominance of the system of central bank and state-owned commercial banks and the financial distortion that it brought that the academic circle had larger controversy on the influence of the financial system dominated by the credit business of state-owned banks to the influence of the stability and growth of Chinese economy. First, the circle of economics in China mostly recognized that the financial system dominated by the credit business of state-owned banks played the role of accelerating investment-driven economic growth. With his empirical analysis on the financial development and economic growth in China's reform during seventeen years, Wang Guangqian demonstrated that the quantitative expansion of finance had a promotive role to the economy while its lower efficiency had negative impact on economy.³⁸ Zhang Jie and Zhang Xingsheng both affirmed the extreme importance of subsidizing in-system growth through financial repression, which mainly involved state-owned enterprises, to promoting macroeconomic growth and stability.^{39,40} Zhang Jie also analyzed the possible mechanism for subsidizing in-system growth through financial repression, namely the special capital structure of state-owned banks. State reputation, as manifested in the situation that the state provided implicit guarantee to state-owned banks for their immunity to bankruptcy and their deposits, was the most important component of the capital of state-owned banks.⁴¹ The research group of economic growth and macroscopic stability of the Institute of Economics of the Chinese Academy of Social Sciences further summarized China's financial system from the beginning of the reform and opening up as a triad of bank credit expansion under the implicit guarantee of the state, monetary policy with both economic growth and inflation control taken into account, and Renminbi fixed exchange rate system based on capital

³⁸Wang (1996).

³⁹Zhang (1998).

⁴⁰Zhang (2002).

⁴¹Zhang 2003.

control. The research group also gave a more systematic demonstration on the feasibility of accelerating investment and growth through currency and financial distortion in the stage of learning-by-doing economic development.⁴² However, there were also numerous research results that tended to negate China's financial development or even the promotive role of the development of the banking industry to economic growth. Boyreau-Debray (2003) examined the influence of the development of the banking industry in China to the economic growth in different provinces with province level panel data from 1990–1999. He found in the paper that the scale of savings in China's banking system and the credit scale of state-owned banks was negatively correlated to economic growth.⁴³ Wang Jinbin divided different financial regions on the basis of the long-term correlativity between regional bank deposit volume and regional credit volume. And he found that financial development did not play a conspicuous promotive role to economic growth in regions of strong financial control. Financial development was not an explanatory factor to economic growth but played a negative role. And there might be a "neutral" interaction between financial development and economic growth in the regions of weak financial control.⁴⁴ Chen Yulu and Ma Yong introduced control factors like social credit culture, legal tradition, government governance and management ability and found that the more the structure of the financial system of an emerging market country tended to be of a "bank-led" type, the higher its operating costs and the lower its efficiency became.⁴⁵ Wang Dingxiang, Li Lingli and Ran Guanghe gave a second proof that China's government-led financial development had negative influence to economic growth.⁴⁶ However, as Rioja and Valev pointed out, the relationship between financial development and economic growth had different forms of manifestation in different stages: Financial development promoted economic growth mainly through influencing productivity in developed countries while it promoted economic growth mainly through capital accumulation in developing countries.⁴⁷ Yang Shenggang and Zhu Hong verified such a point to certain extent with the data on the financial development in the central regions in China.⁴⁸ But when people took into account the investment-driven characteristic of China's economic growth, it could be seen that the empirical research results in the above were not sufficient to overthrow the judgment that China's financial development and, in particular, the development of the banking industry played a promotive role to economic growth.

Second, the Chinese circle of economics showed high attention to the credit inflation and economic fluctuation that might be caused by the financial system dominated by the credit business of state-owned banks. Huang Da and Zhou Shengye defined

⁴²The Research Group of Economic Growth and Macroscopic Stability of the Institute of economics of the Chinese Academy of Social Sciences (2007).

⁴³Boyreau-Debray (2003).

⁴⁴Wang (2007).

⁴⁵Chen and Ma (2008).

⁴⁶Wang et al. (2009).

⁴⁷Felix and Neven (2004).

⁴⁸Yang and Zhu (2007).

in earlier time the concept of credit inflation and pointed out that credit inflation would eventually cause inflation. The loans that would cause money supply had to be determined on the basis of the increment of the volume of necessary currency in the circulation of the current period. When such a limit was exceeded, there would be excessive money supply, namely credit inflation.⁴⁹ The institutional cause to excessive credit supply and inflation could be specifically summarized as the following: Because of inadequate system reform, enterprises and various investment entities allocated too much funds to fixed assets investment. The scale of the bank loans to fixed assets investment grew at a high speed, which fueled the inflation in fixed assets investment. As a result, people were forced to adopt credit expansion to ease the problem of insufficient operating funds in enterprises. Jiang Yue proposed in earlier time that excessive fixed assets investment could cause credit inflation and regular inflation. With a series of hypotheses such as that the government pursued output maximization, the government participated in enterprise resource allocation, and that there was information asymmetry present between the government and the enterprises, Wang Yijiang demonstrated the possibility of such theory in a stricter manner.^{50,51} From the perspective of the lagging behind of enterprise property right reform and the corresponding issue of insider control, Qian Yanmin demonstrated, the mechanism that the output of representative state-owned enterprises rose higher than optimal social standard so that it forced excessive credit investment and money supply.⁵² Zhong Wei and Yuan Yuanyuan constructed the microscopic basis of the credit distortion and inflation in financial crisis through introducing soft budget. And they proposed that people had to start from reducing policy burdens, weakening implicit government guarantee and introducing competitive financial system so as to prevent financial crisis of this kind.⁵³ Yi Gang and Ling Ming proposed that the post expense maximization and prior investment maximization of state-owned enterprises was the main driving power of the scale expansion of Chinese economy. But such growth mode involved very high costs and its direct consequence was the formation of huge bad assets in banks.⁵⁴

IV. China's Exploration on Macro-Prudential Financial Regulation

According to the analysis in the above, the two-leveled banking system of central bank and state-owned commercial banks constituted the kernel of China's financial infrastructure which mainly served export-oriented industrialization and it had obvious characteristics of government dominance. Besides, China also developed financial superstructure which matched the growth mode of export-oriented industrialization, namely the current framework of macro-prudential financial regulation system. As a

⁴⁹Huang and Zhou (1981, Issue 1).

⁵⁰Jiang (1986).

⁵¹Wang (1994).

⁵²Qian (1996).

⁵³Zhong and Yuan (2001).

⁵⁴Yi and Ling (2003).

major developing country in the process of re-tracking, China faced huge uncertainties in economic growth and system re-tracking. In order to restrain the over-optimism about economic growth and financial development, which was brought about by the overlapping of the uncertainties, and corresponding credit and debt expansion, China was forced to implement macro-prudential financial regulation. The main content of macro-prudential financial regulation was that people directly or indirectly control the scale of credit and debt expansion at the price of spontaneously slowing down economic growth during economic boom so as to timely release the excessive accumulation of system risks, represented by inflation and assets price inflation and thus achieve financial and economic stability. Macro-prudential financial regulation included a series of kernel mechanisms, such as controlling investment scale and structure, retaining monetary policy instruments for controlling credit scale, implementing the strategy of both developing and controlling capital market, and adding the macroscopic regulation goal in monetary policy, so as to increase the stability of capital market. These mechanisms were explained in detail as follows:

- (1) The control over investment scale and structure was always an important component of China's macro-prudential financial regulation. Although the monopoly of the state on investment already became history as marketization reform was pushed forward, its powerful influence on investment scale and structure was always retained. Such a situation was noticeably shown in the fact that the National Development and Reform Commission, which evolved from the National Development Planning Commission, still could effectively regulate and control investment scale and structure with the investment industry access policy and the examination and approval power based on investment scale
- (2) Although the indirect regulation instrument system of the central bank based on price signals (in the broad sense) was more and more complete, the direct regulation instruments in monetary policy, represented by credit scale ceiling management, which was in essence quantitative regulation means, was already retained and they played a very important role in macroscopic regulation. At the end of 1997, the People's Bank promulgated the *Notice on Changing and Improving the Control over the Lending Ceiling of State-Owned Commercial Banks* and decided that the control over the lending ceiling of state-owned commercial banks would be removed on January 1, 1998 and that a new management system with "plan guidance, self-retained balance, proportional management, and indirect regulation" would be implemented on the basis of implementing asset-liability ratio management and risk management. No mandatory loan plans would be transmitted to state-owned commercial banks. Relevant measure would be changed to transmitting guidance plans by quarter or year. Such guidance plans would be taken as monitoring indicators in the macroscopic regulation of central bank and given as reference to various banks when they prepared their own fund plans. Nonetheless, credit scale control, once again, became one of the most important policy instruments in the macroscopic regulation from 2004 to 2007 and the latest round of macroscopic regulation in 2008 and 2009.

- (3) China always adopted a strategy of both developing and controlling capital market and endeavored to restrain the accumulation of system risks. One important characteristic of the development of China's capital market was the presence of obvious rigid regulation over a long time. Such characteristic was, first of all, seen in the long lagging behind of the marketization reform of bank credit interest rates. However, such a situation did not completely restrict the development of the banking industry because the repression of other capital markets and, in particular, bond market ensured the monopolistic status of state-owned banks. What is as important as the above characteristic was that the central bank indirectly controlled the credit scale of the banks through credit spread. And it implemented macroscopic regulation on bank credit scale through credit scale ceiling management when necessary and thus achieved the policy purpose of both developing and controlling bank credit market. Second, the development of enterprise bond market lagged behind for the purpose of adapting to bank interest rate regulation and also because of the disturbance of the multiple-agency regulation of enterprise bonds. In March 1987, the State Council promulgated the *Interim Regulations on the Management of Enterprise Bonds*, which stipulated that the issuance of enterprise bonds should be subject to the examination and approval of the People's Bank of China and that the People's Bank of China should set down the total quota of enterprise bonds nationwide each year in conjunction with the National Development Planning Commission and the Ministry of Finance. Finally, China's stock market regulatory system also had noticeable color of rigid regulation. Such characteristic was shown from share floatation and issue, share allotment right, and the confirmation of delisting qualification. Stock issuance could be taken as an example. From 1990 to 2000, regulatory institutions adopted the examination and approval system in quota management with respect to stock issuance. Namely, quotas were transmitted to provincial governments or competent industrial departments, these authorities recommended enterprises within the limit of their quota, and then the China Securities Regulatory Commission examined and approved these enterprises to issue stocks. In March 2001, approval system was officially implemented in new stock issuing, which established the responsibility mechanism that included prior accountability, disclosure in accordance with the law, and post traceability and took mandatory information disclosure as the kernel. Compared with quota examination and approval system, the main advancement in approval system laid in the situation that it improved the degree of routinization and standardization of the issuance examination and approval work. But no radical change was made to the substance of quota examination and approval in the system. Besides, stock issuance pricing system was also changed from administration dominance to market dominance. So it can be seen that China adopted the strategy of both developing and controlling in all capital markets (in the broad sense) such as bank credit business, bond and stock. The kernel content of the strategy was to impose necessary scale control over various forms of financing and gradually realize the marketized pricing in financing.

- (4) China constantly adjusts the goal of macroscopic regulation on the basis of the new changes in economic situation and system transformation. Take the goal of the macroscopic regulation of monetary policy as the example. As stipulated in the *Law of the People's Bank of China*, the goal of monetary policy was to retain the stability of currency value and promote economic growth with it. Price stability should naturally be the primary goal of monetary policy. However, China's monetary policy seemed to focus more on output goals in practice^{55,56,57} (Xie and Luo 2002; Fan 2004; Zhao and Huang 2006). From 2005, the steady operation of asset market attracted extensive attention once again and became a new goal in macroscopic regulation, which also covered monetary policy, as financial marketization accelerated and assets price inflation emerged.

Macro-prudential financial regulation was mainly implemented as in necessary capital flow control and floating exchange rate regime in Renminbi management in the area of opening up to the outside world in China. Among the two, capital flow control included two aspects: The first one was foreign debt scale and term control and the second one was portfolio investment regulation under the framework of qualified foreign institutional investor (QFII) system. And differently, the capital control in foreign direct investment was always the loosest. From 2001, China experienced the reforms in the foreign exchange settlement of the capital of foreign-invested enterprises and the foreign exchange management of foreign direct investment. At present, there was basically no limit to foreign direct investment in China except for in strategic industries. Besides, similar to the majority of developing economies who worried about currency mismatch, China always regarded retaining the stability of the exchange rate of Renminbi as one of the goals in China's monetary policy. After the Renminbi exchange rate system reforms in 1994, 2001 and, particularly, 2005, the foreign exchange management system reform in China mainly advanced along the direction of forming more flexible Renminbi exchange rate determination mechanism. On July 21, 2005, the People's Bank of China published an announcement that China started from the date to implement a managed floating exchange rate regime based on market demand and supply and adjusted with reference to a basket of currencies. The exchange rate of Renminbi would not follow the dollar peg no more so that a more flexible Renminbi exchange rate mechanism would be formed. But it was still an undisputable fact that the current floating exchange rate system in Renminbi management stressed more on retaining the stability of Renminbi exchange rate.

It can be seen here that the current macro-prudential financial regulation system in China had its duality. On the one hand, the four major kernel mechanisms in macro-prudential financial regulation in the above mutually complemented between each other and highly effectively regulated and controlled credit and debt expansion. Among such effect, the control over investment scale and structure lowered the over-optimistic expectation on investment and growth and weakened the stimulation

⁵⁵Xie and Luo (2002).

⁵⁶Fan (2004).

⁵⁷Zhao and Huang (2006).

to credit and debt expansion. Implementing the strategy of both developing and controlling capital market meant imposing necessary scale control on various forms of financing. The monetary policy instruments which retained credit scale control and the monetary policy goals which increased the stability of the capital market improved the efficiency of monetary policy and restrained credit and debt expansion from the source. On the other hand, the framework of the current macro-prudential financial regulation system also had the characteristic of facilitating one-way capital outflow. It was very obvious that one-way capital outflow was easier under such framework. And one purpose of such easiness was to promote the reinvestment in American financial market so as to make up for the insufficiency of the supply of savings vehicles in China. In sum, the current framework of macro-prudential financial regulation system was helpful to regulating and controlling credit and debt expansion and the corresponding economic and savings growth so as to create good conditions for smooth savings-investment conversion. And it could absorb surplus savings by means of the capital export on the American financial market. However, such financial superstructure that served export-led industrialization was designed for the world's economic system centering round developed economies and, in particular, the USA. Such strategy to make up for China's inadequate domestic financial development in reliance to external developed finance and in the manner of imbalance in foreign-related economies had to take the prosperity and stability of the American financial market as its premise.

The outbreak of global financial crisis in 2008 resulted in the extensive attention on macro-prudential financial regulation. The debate about macro-prudential financial regulation was carried out centering round the phenomenon of speculative growth. According to the analysis of Ricardo J et al. (2006), the so-called speculative growth referred to an economic phenomenon that high economic growth and assets price inflation could coexist in a long period of time when there was huge uncertainty in technological progress or financial development.⁵⁸ The article proposed on the basis of rational expectation hypothesis that assets price bubble was a result that people had no other choice but accept, which accompanied technological progress, financial development and economic growth. Logically, macro-prudential financial regulation did not work in economics. Differently, Emine and Enrique G (2010) abandoned rational expectation hypothesis and studied with Bayesian learning process the economic fluctuation that might be caused by the uncertainty of financial development. They proposed that macro-prudential financial regulation was feasible.⁵⁹ Boz and Mendoza divided financial development into the two stages of high leverage stage and low leverage stage and obtained its transitional probability through Bayesian learning process. Simply put, the post status of the leverage of the first period directly affected the prior belief about the leverage of the second period. For example, high leverage occurred in the first period, investors would be more likely to expect that high leverage would remain in the second period. Hence, investors would simply follow extrapolate expectation within a fairly long period and only return to rational

⁵⁸Ricardo J et al. (2006).

⁵⁹Emine and Enrique G (2010).

expectation in the end. This, in turn, created the possibility for credit overexpansion and capital mismatch. Boz and Mendoza found that people could better simulate the economic and financial fluctuations in the USA from late 1990s when employing a model which contained the above learning effect and Irving Fisher's debt-deflation mechanism, which in essence was the financial accelerator effect. And the results were much larger than when they simply used rational expectation hypothesis and Irving Fisher's debt-deflation mechanism. Chinese scholars also carried out extensive research on speculative growth. Lin (2007) and Gong and Lin (2007) related to speculative growth respectively from the angles of the wave phenomena in investment in developing countries and the mystery of the "deflationary high growth" of Chinese economy, which was in essence the phenomenon of understated inflation which accompanied high growth.^{60,61} Lin et al. (2010) further constructed the microscopic model of the wave phenomenon, starting from the hypothesis of the "indetermination of the total number of enterprises in the industry".⁶² The research group of China's economic growth and macroscopic stability (2010) started from the reality that the uncertainty faced by capital accumulation was lower than that by technological innovation and discussed the path dependency of assets revaluation process to the technological progress in capital accumulation and its consequence.⁶³ But this kind of literature had the weaknesses of not having specific analysis on capital market and only having indirect connection with macro-prudential financial regulation. So the study on macro-prudential financial regulation at present was more of the summarization of practical experience and people needed to make further theoretical exploration in this respect.

Summary

In the beginning of the reform and opening up, China selected the growth mode of export-led industrialization, which was suitable to its development standard of productivity at the time, and gradually formed a financial system that matched the growth mode, namely the financial infrastructure with the two-leveled banking system of central bank and state-owned commercial banks and the financial superstructure embodied as the current framework of macro-prudential financial regulation. As such financial system that mainly served export-led industrialization and had obvious characteristic of government dominance, China improved capital allocation and accelerated economic growth. Besides, it also effectively promoted smooth savings-investment conversion, realized economic stability, and eventually successfully broke poverty trap. And the Chinese academic circle also achieved a series of research results as discussed in the above centering round the development of the financial system that matched and supported the growth mode of export-led industrialization.

⁶⁰Lin (2007).

⁶¹Gong and Lin (2007).

⁶²Lin et al. 2010.

⁶³Research Group of China's Economic Growth and Macroscopic Stability (2010).

3 Global Financial Crisis, Building the Financial System that Matched and Supported Urbanization, and New Challenges in the Study of Financial Theories in China

Although China successfully broke poverty trap, its growth mode of export-led industrialization caused at the same time the situation that urbanization seriously lagged behind industrialization. And a series of problems emerged so that China was confronted with the difficulty that its development showed inadequate potential and could face great difficulty in carrying on. (1) The development in urbanization lagged behind so that land use showed inferior efficiency, resource and environment constraints became prominent, and the potential of economic growth decreased. (2) The development in urbanization lagged behind so that the leading role of central cities were weakened, which resulted in the imbalance in development between different regions and between the city and the countryside and increased the difficulty of the spatial expansion of industrialization. (3) The development in urbanization lagged behind and, as a result, China could not form purchasing power and market center in itself so that it seriously depended on foreign trade and its economic growth was confronted with the restraint of the demand on the international market and, particularly, developed economies. And there was no other way to improve the sustainability of economic growth than vigorously raising the level of urbanization, promoting the coordinated development of urbanization and industrialization, and realizing the transformation of the economic growth mode of export-oriented industrialization. Specifically speaking, it meant to realize the spatial concentration of production factors and, in particular, human capital through urbanization, drive technological progress and industrial upgrading, promote industrialization from a high starting point, and relax the resource and environmental restraints of economic growth. The key reason why such new growth mode was advisable laid in the fact that the spatial concentration of production factors and, in particular, human capital realized through leading industrialization with urbanization could generate traditional learning effect in the production of products and it could also generate the learning effect in technological innovation, which was in essence knowledge production, so as to ensure that industrialization could have constant support of technological progress.

The outbreak of global financial crisis in 2008 increased the urgency in transforming the growth mode of export-oriented industrialization. As pointed out in the analysis above, the rationality of the growth mode of export-oriented industrialization and its supporting financial infrastructure and superstructure was built on the basis of the world's economic system centering round developed economies and, in particular, the USA. But as technological progress spread in the world, the economic growth of developed economies showed stagnation while emerging market economies, represented by China, achieved steadily rising productivity standards. Such a situation powerfully shook the rational basis of the growth mode of export-oriented industrialization and the supporting financial system of this mode. The outbreak of global financial crisis reflected the overestimation of the economic

growth and financial development potential of developed economies and, in particular, the USA. More importantly, the situation that developing economies recovered earlier than developed ones, for the first time in history since the end of the World War II, after the outbreak of global financial crisis, driven by the mutual direct investment between emerging market economies. This indicated exactly that emerging market economies had to look for new international markets, including turning and developing themselves into new centers of the world's economic system, because of the stagnation and even shrinkage of the markets of developed economies. As the largest emerging market economy, China naturally should participate in the competition to become a new center of the world's economic system. It was under such a general background that the pressure rose to an unprecedented level in transforming the economic growth mode of export-oriented industrialization and promoting the coordinated development of urbanization and industrialization.

According to the analysis in the above, a center of the world's economic system was both a productivity center and a purchasing power and market center. It could only be formed with the impetus from industrialization led by urbanization. This was because people needed to improve the standard of urbanization development and realize the spatial concentration of production factors and, in particular, human capital. Besides, they needed to realize the effects in product manufacturing and technological innovation and thus push forward industrialization at a higher starting point. Only in this way could a productivity center be formed eventually. Besides, the spatial concentration of human capital and, in particular, the emergence of socialized urban life and mode of consumption promoted the formation of purchasing power and market center.

Because the investments for industrialization and urbanization had obvious structural difference, it was required that people should build new financial infrastructure and superstructure needed for adapting to pushing forward urbanization process and realizing the coordinated development of urbanization and industrialization. As shown in Fig. 22.1, obvious change occurred to the key areas in financial intermediation and market investment and financing in the process of urbanization. (1) People added new financing related to urbanization, which included the financing for both the construction of urban infrastructure and the capital accumulation for service industry and human capital needed to support urbanization development. When compared with industrialization investment projects, urbanization investment projects needed to realize the spatial concentration of factors. Its financing might be of larger scale and longer term. (2) New content was added to the financing related to industrialization. Different from export-led industrialization, the industrialization led by urbanization had the characteristic of more intensively concentrated factors and capitals. The financing for industrialization investment projects became larger in scale and longer in term. Only in this way could China's development further obtain the learning effect of product manufacturing. (3) In order to adapt to the formation of purchasing power and market center, people also needed to add the financing of housing mortgage loan and consumption credit to the financial system. The financing for urbanization and industrialization in the above was only helpful to the formation of productivity center. People needed to provide necessary financing for housing

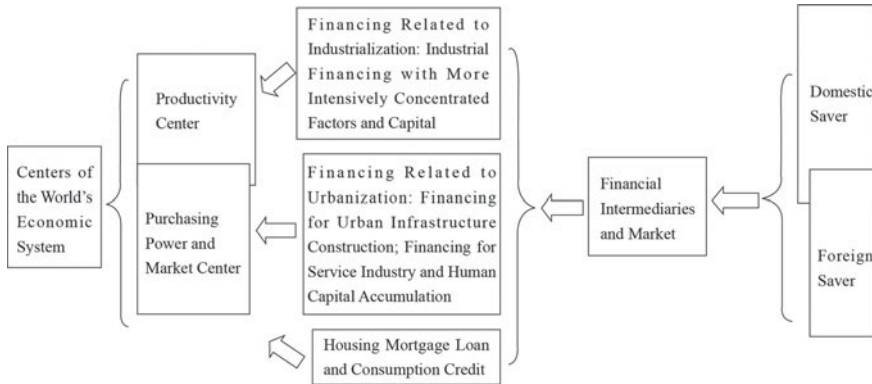


Fig. 22.1 Fund flow to build new centers of the world’s economic system *Note* Arrows indicate the direction of fund flow

mortgage loan and consumption credit to human capital which would realize spatial consumption so that it could obtain socialized urban life and consumption mode. Only in this way could purchasing power and market center be truly formed. It was very obvious that both the financing related to urbanization and industrialization and housing mortgage loan belonged to large-scale long-term investment and financing which had the characteristic of insufficient liquidity. On the one hand, it was required, in relation to such characteristic, that domestic financial intermediaries and market adopted the principle of proximity service in the financing related to urbanization and industrialization and to the primary securities related to housing mortgage loan and consumption credit so as to improve the information production related to the investment and financing of relevant projects. On the other hand, more urgent requirement was made about raising the liquidity of investment project, supplying qualified savings instruments, and absorbing domestic and foreign savings funds. This was because savers were confronted with serious information asymmetry. Only savings instruments with high liquidity could provide better protection so as to mobilize savings. This was particularly important for absorbing foreign savings funds. If domestic financing was underdevelopment and there were no adequate qualified savings instruments, the task of leading industrialization with urbanization and building new centers of the world’s economic system would definitely meet the difficulty that domestic savings-investment conversion could not be made smoothly and in turn investment would become inadequate. Therefore, different from the case in export-oriented industrialization, providing sufficient qualified savings instruments on the basis of improving long-term investment projects became the key to the financial infrastructure centering round urbanization. Specifically speaking, it meant that people should, centering round the process of urbanization, focus on pushing forward the asset securitization of investment projects and the development of growth enterprise market that were related to urbanization. On the one hand, because urban infrastructure construction and human capital accumulation both belonged to large-scale long-term investment, people urgently needed to develop municipal debt market,

implement moderate asset securitization, and improve the liquidity of investment projects. On the other hand, because the urbanization process also involved industrial upgrading and technological progress, broad space was created for developing growth enterprise market, which in essence was the asset securitization of venture capital investment. And even existing stock and enterprise bond markets also had great development potential. These could further improve the standard of asset securitization of the long-term investment projects related to industrialization. Theoretically, housing mortgage loan and consumption credit could also be put into asset securitization. But considering that they were limited by the standard of urbanization in general and involved larger uncertainty, the large-scale securitization of these should be put off for the moment so as to control system risk more easily.

The task of leading industrialization with urbanization and building new centers of the world's economic system also entailed requirements on reforming the financial superstructure that served export-oriented industrialization, namely the current framework of macro-prudential financial regulation. According to the analysis in the above, such framework took facilitating one-way capital outflow as main characteristic and it was designed centering round the USA as the center of the world's economic system. Contrary to the situation above, building new centers of the world's economic system needed at least to gradually realize the two-way free flow of international capital. Only in this way could China effectively absorb domestic and foreign savings fund and realize the smooth savings-investment conversion in the country.

To sum up, the key to building a financial infrastructure that matched urbanization laid in proving adequate qualified savings instruments on the basis of improving the liquidity of long-term investment projects. Moreover, the key to building a corresponding financial superstructure laid in progressively reforming the current framework of macro-prudential financial regulation and gradually realizing the two-way free flow of international capital. From 2005, China's financial marketization reform and financial foreign opening up accelerated obviously. Their main contents included accelerating the marketization reform of credit interest rates, relaxing Renminbi foreign exchange management system, strengthening the opening up in the area of capital business, and launching equity division reform. However, current financial marketization reform and opening up to the outside world still mainly centered round industrialization. Relevant work was still at a large distance away from building a financial system that matched and supported urbanization. Wang Guogang proposed that the transformation of China's mode of economic development was a process of shifting from taking industrial economy as main driving power to taking industrial economy and urban economy as joint driving power. Its inherent basis was that people should effectively resolve the issue of serious shortage in the areas of "housing, transportation and education" after they resolved the issues in "food, clothing and other daily supplies" through industrialization. They should speed up developing urban economy. In the process, financial products and services that directly served the wealth management of the residents would increase obviously. The differentiation

of financial products and services would become the focal point in financial innovation.⁶⁴ Yet generally speaking, there were fewer research results in urbanization finance. The *Suggestion of the CPC Central Committee on Formulating the Twelfth Five Year Plan of National Economic and Social Development* already published had two points that involved financial reform and development: One was deepening financial system reform and constructing a counter-cyclical framework of macro-prudential financial management. The other was speeding up the construction of multileveled capital market system and obviously increasing the proportion of direct finance. People should positively develop debt market and steadily develop over-the-counter market and futures market. It was very obvious that these two were both closely related to the financial system that matched and supported urbanization. The Chinese academic circle needed to further carry out in-depth study on them.

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⁶⁴Wang (2010).

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Chapter 23

The Important Breakthrough in the Theory of Socialist Residents’ Income Distribution—The Participation in Distribution According to Production Factors and the Debate on the Issue of the Relationship Between Fairness and Efficiency



Wenmin Zhang

After the conclusion of the special period, people started to take some actions in theory and rectify and clear the mistakes of left-deviation. And at the same time, they sent the clarion call for China’s reform. Under the guidance of the Deng Xiaoping theory, the study of distribution theory in China entered new realms. In 1981, the *Resolution on Several Historical Issues of the Party after the Founding of the People’s Republic of China* was formulated under the presiding of Deng Xiaoping. It was proposed specifically that “our socialist system is still in the primary stage”. “Our socialist system will definitely experience a long process from being relatively incomplete to being relatively complete. This requires that we work hard to reform those systems that are not fit for the needs of developing productivity and the people’s interest under the premise of adhering to the basic system of socialism”.¹ These statements provided solid foundation for reforming and adjusting productive relations beyond current development stage. In September 1982, the *Sixth Plenary Session of the Twelfth CPC Central Committee adopted the Resolution on the Guidelines for the Construction of Socialist Spiritual Civilization*. It was pointed out that “China is still in the primary stage of socialism. It must implement distribution according to performance and develop socialist commodity economy and competition. Besides, it also needs, with a considerably long historical period, to develop

¹*Resolution of the Central Committee of the Communist Party of China on Several Historical Issues of the Party after the Founding of the People’s Republic of China*, People’s Publishing House (1981, p. 53).

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multiple economic sectors under the premise of the dominance of public ownership system and to encourage some people to become rich first under the goal of common prosperity. Under such historical condition, people need to recognize the reasonable difference in the area of distribution caused by such policy in the moral construction among the whole people. Besides, they should encourage people to carry forward the spirit of socialist collectivism that advocates the combination of the interests of the state, the collective and the individual”² Here, the document pointed out the specific content of the reform. It was emphasized that distribution according to performance was not equalitarianism and that it coexisted with reasonable difference. It was also emphasized that the primary stage of socialism entailed the development of multiple economic sectors under the premise of the dominance of public ownership system. Because ownership system as well as the standard of productivity development determined the specific form of distribution, the proposal of “developing multiple economist sectors” would definitely result in multiple forms of distribution. Socialist public ownership system was already realized before the reform and opening up but it was impossible to truly realize distribution according to performance because of inferior productivity standard. Only low-standard equalitarianism could be implemented. According to the estimation of the World Bank, the Gini coefficient of China’s urban residents’ income in 1980 was 0.16.³ A Gini Coefficient of 0.3 was normal but 0.16 was extremely equalitarian. Deng Xiaoping pointed out that “the issue of left-deviation from 1957 to 1978 caused China to lag behind in development by nearly 20 years. China did develop in this period but the whole society was in standstill. During the period, the average annual income of peasants was RMB 60 yuan and that of urban workers RMB 60 yuan. The situation stayed unchanged for nearly 20 years. China was always under the poverty line according to international standard.”⁴ Deng Xiaoping pointed out that “people must achieve advanced productivity when building socialism. Poverty is not socialism. When adhering to socialism, we need to build the socialism that has superiority against capitalism. First, people must get rid of poverty. Although we are building socialism right now, we are in fact not qualified for it”.⁵ “We adhere to taking the road of socialism. Its fundamental goal is to achieve common prosperity. But it is impossible to develop in complete parallel. In the past, people practiced equalitarianism like everybody eating from a big rice pot. This was in fact common backwardness and common poverty. We lost much because of it. In the reform, people need to first break equalitarianism and the ‘big rice pot’.” “Our policy is to allow some people and regions to become rich first so as to urge and help backward regions. It is their obligation for advanced regions to

²“The Resolution of the CPC Central Committee on the Guidelines for the Construction of Socialist Spiritual Civilization, “Library of the Documents of the National Congresses of the Communist Party of China”, PEOPLE.COM.CN.

³World Bank, *China: Socialist Economic Development*, Vol. 1, English Edition, Washington (1983).

⁴“The Talk of Deng Xiaoping When Goh Chok Tong, the First Deputy Prime Minister of Singapore” (May 29, 1987), *People’s Daily*, May 30, 1987.

⁵*Selected Works of Deng Xiaoping*, Vol. 3, People’s Publishing House, 1993, p. 225.

help backward regions.”⁶ Under the guidance of Deng Xiaoping theory, China made world-shocking achievements in its reform. With the reform, people enriched and developed China’s distribution theory and established socialist income distribution theory with Chinese characteristics.

As China’s economic system reform was pushed forward, its income distribution theory also developed in practice with breakthroughs achieved in it. After the reform and opening up, the channel of income distribution was expanded and the research area of distribution theory was enlarged correspondingly. Three major transformations occurred: The first one was the transformation in direction from complete distribution according to performance to the dominance of distribution according to performance and the coexistence of multiple forms of distribution. The second was the transformation from consumer goods distribution to income distribution. And the third was the transformation in direction from normative research to empirical research. These transformations reflected the new picture in the development of distribution theory after the beginning of the reform and opening up. And in the end the socialist income distribution theoretical system with Chinese characteristics emerged.

1 New Income Distribution Theory Gradually Formed After the Beginning of the Reform and Opening up

I. The Transformation in Direction from the Single Form of Distribution According to Performance to the Dominance of Distribution According to Performance and the Coexistence of Multiple Forms of Distribution

The theory of the primary stage of socialism úformed after the beginning of the reform and opening up resulted in the adjustment from public ownership system to the dominance of public ownership system and the coexistence of multiple economic sectors. The distribution form of the coexistence of multiple forms of distribution with the dominance of public ownership system emerged in adaptation to such adjustment. Such change in turn caused changes in the content of China’s distribution theory.

(I) The Challenge on Traditional Theory of Distribution According to Performance

First, there were four premises in Marx’s conception on practicing distribution according to performance in future society: The first one was the single form of public ownership system. The second was the implementation of distribution by the society among workers. The third was that commodity production and currency exchange already disappeared. And the fourth was that the particular labor of workers did not form social labor via a route full of twists and turns any more. Rather, it

⁶Selected Works of Deng Xiaoping, Vol. 3, People’s Publishing House, 1993, p. 155.

became the component of aggregate social labor directly. Then specific basis was provided on the basis of these four basic premises for understanding what distribution according to performance was. Was the mode of distribution of personal consumer goods in China after its foundation distribution according to performance? It was basically the realization of the form of distribution according to performance. This was because China's practice only satisfied the first two of the four premises in the above. Namely, centralized distribution was carried out by the society under public ownership system and there were certain grades and differences. But the third and fourth premises, which followed the two above, still did not exist in China. But why was it called the form of distribution according to performance? It was because the problems of inferiority, equalitarianism, chaos and rigidity occurred in the realization of distribution in economic units under whole people ownership system. The practice could not embody the principle of distribution according to performance, namely whoever worked more got more, workedless got less, and did not work got nothing. In rural collective economic units, people got extremely low labor points, which could hardly meet the needs in labor reproduction. Although China practiced "complete" distribution according to performance in the theories before the reform, it was in fact equalitarian distribution with slight differences among people.

Over a long time, the Chinese circle of economics put distribution according to production factors and distribution according to performance in opposition. It was believed that distribution according to production factors was the capitalist form for distribution according to labor value. Under socialist condition, people realized the public ownership system of the means of production and distribution according to performance became the sole form of distribution. Because of the development of multiple economic sectors from the beginning of the reform and opening up, there was the reality that multiple forms of distribution coexisted objectively. And distribution theories, guidelines and policies changed correspondingly.

Second, the traditional theory of distribution according to performance, as examined from the development of the distribution theory, referred to the principle that the income of a worker was determined by the quantity and quality of the labor that he contributed under the public ownership system. But the theory and practice of distribution according to performance was detached from each other in real life. In other words, distribution according to performance was in fact not implemented thoroughly although it was said to be the sole principle of distribution in socialism. The practices in real life, such as implementing equalitarian distribution, opposing material incentives in ideology, and breaking bourgeoisie legal right, all departed from the requirements of distribution according to performance and restricted the development of productivity. Besides, people did not have a generally-accepted definition on what distribution according to performance was in real life. Take the discussion before 1990s as example. In the 1960s, people believed that differential rent belonged to the production team, which "was the foundation of the three-tiered ownership system". And this principle represented the principle of distribution according to performance in socialism characterized by more pay for more

work.⁷ But some people commented that it was more pay for more output and hence not distribution according to performance.⁸ In 1980, some people said that the profit retentions of the enterprises came from the distribution according to performance by the state among the collective of enterprises.⁹ Some said that the object of distribution according to performance was only individual worker rather than collective of workers.¹⁰ In early 1980s, some people said that rural household contracted responsibility system could more adequately realize the principle of distribution according to performance.¹¹ But others opposed such point and objected that rural household contracted responsibility system was merely a kind of household economy in which people assumed the sole responsibility for their profit and loss. It was radically not distribution according to performance at all.¹² The reason why controversy arose from these issues was that some people took as their basis the conception about distribution according to performance that Marx made in his works such as *Critique of the Gotha Program* while others gave new definitions to distribution according to performance. Because their definitions about distribution according to performance were different from each other, they naturally could not have conclusions consistent with each other. In sum, traditional theory on distribution according to performance already faced challenges. The so-called traditional theory on distribution according to performance included two parts: One was the conception on distribution according to performance made by classical writers and the other was the definition on distribution according to performance in the textbooks on political economics in the Soviet Union. In the conception of classical writers, the condition for practicing the conception of distribution according to performance was the public ownership system of the means of production and the elimination of commodity production. In the textbooks on political economics in the Soviet Union, distribution according to performance was taken as the principle of distribution and also the sole principle of distribution. The Soviet Union practiced planned economy. It emphasized equal pay for equal work. It practiced uniform wage system in units under the whole people ownership system. And the units under collective ownership system implemented their own distribution standard. These practices caused controversy after they were introduced into China. For example, some people believed in the 1950s on the basis of the statements of Marx that distribution according to performance was practiced among the workers in the area of production. But the wage principle was the Paris Commune was practiced among the workers in state organs because their labor remuneration came from the deduction part that the workers in the area of production provided to the society. Hence, distribution according to performance was not the sole principle of socialist distribution.¹³ For another example, Luo Gengmo pointed out when

⁷Yan (1961).

⁸Zhang (1962).

⁹Jiang (1980).

¹⁰Xiao and Xiang (1981).

¹¹Lin (1982).

¹²Zhang (1982).

¹³Zhong (1957).

analyzing the economy under collective ownership system that collective economy was “public in the outside and private in the inside”. Namely, it was public to its inside. And it was part of the relationship between private and public sectors in its commodity exchange with the state. The commodity exchange relationship among state-operated enterprises included the relations of the “big public one” to the “small public one” or of the “small public one” to the “big public one”. It was the same as the relationship of distribution according to performance between the state and the individual.¹⁴ Such a point proposed in fact the idea that production factors participated objectively in distribution. These views were not the mainstream but they were thought-provoking.

Then what is on earth the definition of distribution according to performance? One kind of view believed that, examined from the form of distribution that China practiced over a long time, the so-called distribution according to performance that China implemented for long was not based on the principle of distributing consumer goods on the basis of the quantity and quality of labor and that it was not the sole principle of distribution practiced in its distribution of consumer goods. This was because what people got from the economic units under public ownership system was not only wages but also collective welfare. The latter was distributed equally. Hence, the distribution according to performance in China became giving some kind of labor income not measured by labor.¹⁵

(II) Main Thought Proposed in the Process of Distribution System Reform

1. Two-Leveled Distribution According to Performance

In 1980, Jiang Yiwei proposed the theory of “two-leveled distribution according to performance” in response to the problem that equalitarianism was practiced among the enterprises under whole people ownership system like that they were eating from a big rice pot given by the state. He believed that “the biggest weakness in the current economic system was that the ‘big rice pot’ of equalitarianism is put among the enterprises. If people do not resolve this issue of distribution according performance in a larger scope and only practice distribution according performance among individuals inside an enterprise, it is putting the cart before the horse. The reason for this is because people only simply understand distribution according to performance as distributing according to the amount of personal contribution. They do not consider that personal labor can be turned into social labor only through enterprise products or labor services. And hence they did not consider that distribution according to performance is first of all the issue of distributing according to the amount of collective contribution of enterprises.” So people had to follow the principle that “the society practices distribution according to performance among the collective of enterprises and the enterprises practice distribution according to performance inside themselves so that workers care about the results of labor of the collective and the individual

¹⁴Luo (1957).

¹⁵Zhang (1987).

because of material interests”.¹⁶ This view triggered heated discussion as it was an important issue that people needed to resolve in state-owned enterprise reform. Facts proved that the “two-leveled distribution according to performance” was helpful to resolving the issue of serious equalitarianism that state-owned enterprises were fed with the “big rice pot” given by the state. It was one of the thoughts for realizing the transition from planned management system to market economy management system. However, the concept of “two-leveled distribution according to performance” was insufficiently rigorous because distribution according to performance, according to Marx, referred to the distribution of personal consumer goods, which took individuals as object. “Two-level distribution according to performance” included the first step that “the society practice distribution according to performance among the collective of enterprises”. Here, the object of distribution according to performance was changed from individual to “collective”. Obviously, this was inaccurate.

2. The System of Sharing Profits after Deducting Costs

The so-called sharing profits after deducting costs meant that an enterprise deducted the means of production from sales revenue, which was namely deducting costs; then deducted all costs except for wages from net output value, which included administrative charges paid to superior competent departments and industrial and commercial taxes; and took the rest as its net income and shared it between the enterprise and its employees according to stipulated proportions. The practice had two theoretical bases: One was the principle of distribution according to performance in socialism, namely what Marx pointed out in *Critique of the Gotha Program* that “Accordingly, the individual producer receives back from society—after the deductions have been made—exactly what he gives to it.” The other was that the means of production was collective property and workers were owners of the enterprise in an enterprise under collective ownership system under the condition of socialism. Labor was commodity no more. Because of the combination of the means of production, there were no people who paid or received “wages”. The income from the collective labor of the workers was sales revenue. After the cost of the means of production was deducted, the residual was the net income created by collective labor. It was distributed reasonably between state, enterprise and individual workers. The part that individual workers got was personal income. It was the labor remuneration that a worker got according to the principle of distribution according to performance. It was not a converted form of labor value or price. Thus, the category “wage”, which reflected capitalist hiring and exploitive relationship, did not exist in a socialist collective enterprise. It was replaced by “personal income”, a category that reflected the socialist relationship of the distribution of the means of consumption. The personal income of a worker was then exactly the payment of new value after an enterprise deducted the cost of the means of production from sales revenue. And naturally product costs did not include wages and an enterprise needed not to use its funds to

¹⁶Jiang (1980).

pay wages to its employees.¹⁷ This method of distribution was first practiced in handicraft production cooperatives and rural collective economy early in the 1950s. Then in 1981, it was practiced in some collective enterprises in Chengdu. It was called the system of sharing profits after deducting costs. Later it was known as two-levelled distribution according to performance and net output value distribution according to Jiang Yiwei's concept of "two-levelled distribution according to performance". It became a hotspot in discussion in the 1980s because of the discussion on expanding the autonomy of the enterprises which started to rise in 1979. This method of distribution was only suitable to small joint equity partnership enterprises. The concept of costs in it was only limited to the means of production. This was not consistent to the requirements of market economy. So the discussion did not raise a greater debate and ended completely soon.

II. Practice Promoted the Proposal of the Theory of Distribution According to Production Factors

After the beginning of the reform and opening up, distribution theory broke the constraints of various kinds of "dogmatisms" and experienced leap-forwards and developments. And among them, distribution according to production factors was the most outstanding example. Before the reform and opening up, distribution according to performance was regarded as the sole principle of distribution of socialism in distribution theory because of the implementation of the complete public ownership system of the means of production. Distribution according to production was regarded as part of the value theory of three basic production factors proposed by Jean-Baptiste Say and connected with and criticized as the source of value creation. But distribution according to production factors emerged as objective reality after the emergence of rural household contracted responsibility system. For example, it was proposed in some articles at the Fifth National Symposium on Distribution According to Performance that investment and land factors also participated in distribution in the distributive relations in the rural household contracted responsibility system. It was said in these articles that "The lands of various contracting households, calculated on the basis of contracting output, and their quality are generally the same. But because the households put different investment into the lands, their outputs are different and the differential earnings formed out of them are also different. So under the principle of 'taking the rest for themselves', the quantities of products and income of the contracting households are determined by the quantities of labor and fund that they has put into production. In other words, investment in production participates in the distribution of products." "Besides, because of the difference in the contracting method, there will be differences in the quantities of land that each worker in labor possesses. Under such circumstance, the quantity and quality of the means of production determine more noticeably the quantity of products that a contractor could obtain. The proportion of the output of each worker in labor to the amount of labor input will vary in different households."¹⁸ Then with the

¹⁷Zhang (1985).

¹⁸Zhang and Yu (1984).

existence and development of multiple economic sectors, distribution according to production factors already emerged objectively and conspicuously. This was because when people admitted the existence of private economy, they admitted distribution according to production factors. Besides, after shareholding transformation system was practiced in public ownership economy, the principle of distribution according to production factors would definitely emerge as distribution was made according to the ownership right of production factors. Under such circumstance, some people in the academic circle made the theoretical demonstration on the view that people needed to practice distribution according to production factors as well as distribution according to performance in the area of distribution. For example, Gu Shutang and Cai Jiming believed that there were multiple ownership system components in the primary stage of socialism and there were also commodity production and exchange. The state, enterprises, individuals all had relatively independent economic interests. It was not possible for the state to completely stipulate in a centralized manner on the proportions of accumulation and consumption in national income and the choices between the practical and long-term interests of the workers and between personal needs and public needs. Enterprises and individuals possessed autonomy in different degrees in income distribution and accumulation. Therefore, people could not fully practice distribution according to performance. The principle of distribution in the primary stage of socialism was distribution according to contribution. Namely people carried out distribution according to the actual contributions made by various production factors during the creation of social wealth. In the primary stage of socialism, various kinds of incomes all were the forms of distribution according to contribution—Wages were remuneration given to workers on the basis of the contribution of labor; salaries were the remuneration given to entrepreneurs on the basis of their contribution in operation and management; and interests, dividends and bonuses were remuneration given to asset owners on the basis of the contribution of funds or capital. The contribution of various kinds of production factors were determined by the marginal revenues of various production factors. And the determination of various revenues was realized through market mechanism.¹⁹

III. Economic Policies Provided Guidance to the Improvement of the Theory of Distribution According to Production Factors

The theory of distribution according to production factors were improved and completed gradually. In 1987, the political report of the Thirteenth CPC National Congress entitled *Advancing along the Road of Socialism with Chinese Characteristics* stated that “the reforms that we have made, including taking public ownership system as the main part and developing the economy with multiple ownership systems and even allowing the existence and development of private ownership economy, are all determined by the actual conditions of productivity in the primary stage of socialism.” The report also proposed that “the principle that we must adhere to is taking distribution according to performance as the main part and other forms of

¹⁹See Gu and Cai (1988).

distribution as supplementation. Distribution according to performance brings forth personal labor income as a main form of distribution. In addition to this, there will be interests acquired through creditors' right when an enterprise issues bonds to raise fund. There will be dividends obtained from shares with the emergence of share economy. The income of enterprise operators includes some risk compensation. When a private enterprise hires certain amount of labor, it would bring its owner non-labor income. All these incomes should be permitted as long as they are legal."²⁰ Here, the idea and content about distribution according to production factors were in fact recognized. From then on, the documents of the CPC Central Committee more specifically declared the necessity to implement distribution according to production factors. For example, Jiang Zemin said in the report at the Fifteenth National Congress of the Communist Party of China in 1997 that "people should permit and encourage factors of production such as capital and technology to participate in distribution".²¹ Here, the theoretical term of distribution according to production factors were used specifically. Then in 2002, Jiang Zemin said in the report at the Sixteenth National Congress of the Communist Party of China that "people should establish the principle that factors of production such as labor, capital, technology and management participate in distribution according to contribution and improve the distribution system in which distribution according to performance dominates and multiple modes of distribution coexist".²² As the CPC and the Chinese government recognized distribution according to production factors, state-owned enterprises implemented shareholding system transformation and multiple economic sectors achieved development, the proportion of distribution according to production factors grew larger. This broke the pattern that distribution according to performance was the sole mode of distribution.

IV. The Issues that Needed to Be Studied Further in the Theory of Distribution According to Production Factors

(I) The Relationship between Distribution According to Production Factors and Distribution According to Performance

There were different views at present on whether distribution according to production factors and distribution according to performance were the same as concepts. One of these views regarded the two as one category, seeing them as different forms of manifestation. For example, some people believed that "distribution according to performance in the present stage of development in China is included in the distribution according to production factors in the present stage. The relationship between the two is of including and being included."²³ Some people said that "the relationship between distribution according to performance and distribution according to

²⁰A *Collection of the Documents of the Thirteenth National Congress of the People's Republic of China*, People's Publishing House, 1987, p. 29, pp. 38–39.

²¹A *Collection of the Documents of the Fifteenth National Congress of the People's Republic of China*, People's Publishing House, 1997, p. 25.

²²A *Collection of the Documents of the Sixteenth National Congress of the People's Republic of China*, People's Publishing House, 2002, p. 27.

²³Yang (2004).

production factors is that between essence and phenomenon or between content and form. It is distribution according to performance that is converted into or manifested as distribution according to performance.”²⁴

Some people did not agree with the views in the above. They believed that “people should not identify distribution according to performance with the participation of labor in distribution as production factor”. This was because “distribution according to performance only exists in public ownership economy. A worker can participate in production and distribution as owner rather than merely as a provider of labor factor. Distribution according to production factor takes the existence of private ownership economy as premise. In a private or foreign-funded enterprise, workers are not its owner. Their labor only participates in production and distribution as one of the production factors. Therefore, people should not include distribution according to performance in distribution according to the contribution of production factors.”²⁵

According to Marx’s theory on distribution according to performance, distribution according to performance and distribution according to production factors were not of the relationship between content and form.

First, what was distribution according to performance? Distribution according to performance referred to distribution according to the contribution of labor. The labor factor in distribution according to production factors also meant distribution according to the contribution of labor. These two were the same. But could people say that distribution according to performance and distribution according to production factors were of the same concept. This was obviously wrong. It was because that Marx believed that the reason why private ownership system caused exploitation was because of the inequality of the possession of the means of production. So after the public ownership system of the means of production was realized, labor was taken as the measure of distribution and factors of production did not participate in distribution. Lenin summarized the conception on distribution according to performance proposed by Marx as the principle of distribution according to performance. Namely, “the mankind could only directly transform from capitalism to socialism, namely to the public ownership system of the means of production and distribution according to performance”.²⁶ In addition, the limiting wording of “the socialist principle of ‘He who does not work shall not eat’”²⁷ was added to this principle of distribution of socialism. Ever since, people took the principle of “He who does not work shall not eat” as a synonym of distribution according to performance when they talked about the principle of distribution of socialism. Therefore, distribution according to performance only recognized “labor” as the basis of distribution and took not recognizing the participation of production factors in distribution as its premise. But distribution according production factors recognized the participation of production factors in distribution. This was the distinction between the two in essence.

²⁴Zhou and Lu (2002).

²⁵Wei (2003).

²⁶Vladimir I. Lenin, *The Task of the Proletariat in the Present Revolution, Selected Works of Lenin*, Vol. 3, p. 63.

²⁷Vladimir I. Lenin, *The State and Revolution, Selected Works of Lenin*, Vol. 3, p. 252.

Second, the so-called distribution according to production factors referred to the situation that the owners of various production factors participated in the distribution of newly created value on the strength of the shares of the production factors that they owned respectively. The object of such distribution could be either individual or collective. This was different from distribution according to performance. The object of distribution according to performance was limited to individual. Besides, distribution according to production factors was not merely determined by the nature of ownership system or of private ownership system. It was determined by the mode of resource allocation. Under the condition of public ownership system, people could implement both distribution according to performance and distribution according to production factors. For example, solely state-owned enterprises could adopt the mode of distribution according to performance. In a shareholding enterprise in which public ownership system dominated or different share owners were different entities with public ownership system, its form of distribution was the participation of non-labor production factors in distribution and the purpose of such form was to effectively utilize resources and reward the used resources. This was a method generally applied in market economy. For another example, labor point system was implemented in rural collective economy before the reform and opening up. It was a typical form of distribution in Marx's conception on distribution according to performance. After the household contracted responsibility system was implemented, distribution according to production factors was implemented in substance because of the separation of the rights of operation and use from ownership right although the form of collective economy still remained. And of course, people could only implement distribution according to production factors under the condition of market economy with private ownership system as the ownership right of production factors was privately owned. In sum, people should not identify distribution according to performance with distribution according to production factors although distribution according to performance did mean to distribute according to labor factor.

(II) The Relationship between Distribution According to Production Factor and Exploitation

The core issue of distribution according to performance was that exploitation was eliminated after the means of production was publicly owned. But according to the labor theory of value and the theory of residual value, there would be exploitation when distribution according to production factors recognized that non-labor factors such as capital and land participated in distribution. Then it became an unavoidable question whether there was exploitation when distribution according to production factors was implemented in the primary stage of socialism. Those who supported the presence of exploitation believed that, "in the eyes of Marx, factors other than labor do not create value because he regarded value as the manifestation of the productive relations in human society and as the contribution indicator of individuals to the society and thus the natural world and other factors were naturally irrelevant to the contribution of individuals to the society. When examined with such a view as starting point, the income obtained not through one's own labor, including the income

that purely came from the ownership right of non-labor production factors, was all ‘exploitation’ of the labor of other people.” They also believed that “the efforts to modify the labor theory of value with the ‘theory of factor remuneration’ have been popular in China’s circle of economics around the recent 20 years. It did its best to preach ‘capital and land also participate in production and create value’. And on such basis, it advocated that ‘income be distributed according to production factors’. Such ‘theory of factor remuneration’ was inconsistent with Marx’s labor theory of value. Its negation of the theory of exploitation does not hold water, either.”²⁸

People who supported the view in the theory of no exploitation in distribution according to production factors believed that “people should confidently discard the formulation of ‘exploitation income’ and replace it with the new outlook of ‘capital income’.”²⁹ Some people explained that, “according to our research, capital is no longer the factor that plays a dominant role in many aspects. It could be utilized or hired by other factors rather than hiring other factors.” “The income obtained in the occasions where capital hires labor can be defined as exploitation income.” “The income obtained from the capital hired by other factors cannot be recognized in general as exploitation income”. “The larger share of the returns is given to human capital or knowledge capital rather than material capital. This is a manifestation of the progress in the society.”³⁰

Other people believed that “people should not solely take the labor theory of value as the only basis of income distribution. Whoever creates value owns the value. ... In fact, labor must create use value at the same time if it is to create value. And the creation of use value, namely material wealth, needs objective factors such as capital and land in addition to labor. Without these investments of non-labor factors, labor cannot create value. In other words, although production factors such as capital and land do not create value, they are the necessary conditions for creating value. They help labor to create value through participating in the creation of use value. Therefore, they also need to participate in value distribution and get the reward that they deserve. As long as they get their due share, it cannot be called exploitation or ‘reasonable exploitation’. Marx’s proposal on the exploitation theory of residual value was of particular social background. Today people cannot only give weight to value creation and not to wealth creation. They need to combine the creation of value and wealth and also give weight to the investment of production factors.” “Now people all recognize distribution according to production factors. The income of distribution under normal conditions is reasonable and legal. There is no depriver and hence not the question of deprivation-depriver.”³¹

At present, all views about “exploitation” believed that it was objective existence and had its inevitability. The focus still laid in the old question of whether to recognize “the monism of labor creating value”. However, those who supported the view that non-labor production factors did not create value criticized and negated the view

²⁸Zuo (2003).

²⁹Yang (2003).

³⁰Hong (2002).

³¹Hu (2007).

that non-labor production factors should participate in distribution. They believed that the labor theory of value did not negate the historical inevitability that non-labor production factors should participate in distribution. People should permit the right to acquire proper rewards and earnings on the basis of assets for the purpose of saving the use of resources and stimulating the preservation and increase of value. As long as a system of distribution was favorable to the development of productivity, there was the reason for its existence. Traditional theory believed that labor created value and hence only labor had the right to participate in distribution. It negated the participation of all non-labor factors in distribution. This was a view of historical idealism that departed from the basic conditionality of material interests.³² It should be said that this was the largest part in seeking common ground while reserving differences. It was also the biggest progress in the discussion on the theory of distribution according to production factors and the issue of exploitation.

V. The Socialist Income Distribution Theoretical System with Chinese Characteristics Was Gradually Formed

When looking back at the theories of income distribution during the 60 years from the founding of the People's Republic of China, people could see the following in general. China mainly digested and absorbed the theories of distribution according to performance introduced from abroad in the first 30 years. People realized that the theories were basically unfit for China's reality. And two completely different attitudes emerged: One was the sect of cancellation in the extreme left-deviated thought trend and the other was the sect of exploration. Later, the sect of exploration found that the planned management system introduced from abroad was unfit for China's reality and it changed into the sect of reformation. In the second 30 years, China carried out economic system reform under the guidance of Deng Xiaoping theory. It developed multiple economic sectors, established socialist market economy, and gradually formed the distribution system with distribution according to performance as the main part and the coexistence of multiple modes of distribution. Namely, people established the principle that factors of production such as labor, capital, technology and management participated in distribution according to their contribution. And the principle developed into the theoretical system of socialist income distribution with Chinese characteristics. This theoretical system broke the prejudice in traditional socialist political economics. It applied the categories that had been believed to be of capitalism in the past in socialist market economy on the basis of the inherent requirements in the development of market economy and it gave scientific interpretations to these categories. The categories, such as the development of non-public ownership economy and the participation of non-labor factor factors into distribution, injected vigor into the market economy in the primary stage of socialism. They contributed to the development of economy and the improvement of the standard of income distribution of the people. Practice proved that this distribution theoretical system was suitable to the development of productivity. It was correct.

³²Yu (1997, pp. 48–49).

2 The Transformation from Consumer Goods Distribution to Income Distribution

When conceiving that the future society would implement distribution according to performance, Marx pointed out that “Within the co-operative society based on common ownership of the means of production”, “nothing can pass to the ownership of individuals, except individual means of consumption. But as far as the distribution of the latter among the individual producers is concerned, the same principle prevails as in the exchange of commodity equivalents: a given amount of labor in one form is exchanged for an equal amount of labor in another form.”³³ Obviously, distribution according to performance involved the distribution of consumer goods and the content of distribution was limited to the means of consumption. In the distribution theory in China before the reform and opening up, the so-called distribution mainly involved the distribution of consumer goods through distribution according to performance and did not include that of non-labor income. Then China’s ownership system developed from two kinds of public ownership systems to a system adapted to the dominance of public ownership and the coexistence of multiple economic sectors. With the establishment of such system, various kinds of production factors such as labor, land, capital, technology and management jointly participated in distribution under the condition of the dominance of distribution according to performance and the coexistence of various kinds of distribution modes. The content of distribution was not limited to the means of consumption. It involved the income of various owners and the distribution became income distribution. Such a change was not just a change in the quantity of income. Income could be converted into capital to provide conditions for further expanding production and operation.

“Income distribution” emerged the earliest in distribution system in the implementation of the rural household contracted responsibility system in 1981. Its basic characteristic was that the collective contracted land and other means of production to rural households while retaining the necessary centralized operation of collective economy. The contracting households made operation decisions independently according to the authorizations as provided in their contracting contracts and shared the fruits of operation under the premise of fulfilling the tasks of the state and the collective. The general practice in this system was to divide land according to population or proportions of manpower and also according to the combination of responsibility, right and interests and give to rural households for operation. Rural households used the land and other means of production of the collective to carry out independent operation. The method of distribution of this system was “fully submitting the quota of the state, leaving enough for the collective, and taking the rest for themselves”. Here the so-called “taking the rest for themselves” included not only the means of production but also the expenses of seeds and other means of production and of reproduction. So the system basically created a household economy characterized

³³*Selections of Karl Marx and Friedrich Engels* Vol.3, People’s Publishing House, 1972, pp. 10–11. https://www.marxists.org/archive/marx/works/download/Marx_Critique_of_the_Gotha_Programme.pdf.

by the assumption of the sole responsibility for profit or loss. And the so-called distribution meant to distribute the income in the system. In the *Decision on Several Issues on Building Socialist Market Economic System* adopted at the Third Plenary Session of the Fourteenth CPC Central Committee in 1993, there was the decision on “building reasonable personal income distribution and social insurance system”, which officially recognized the formulation of income distribution.

The transformation from consumer goods distribution to income distribution promoted the development from single income source to income diversification. The income of urban and rural residents was increased in general. The people personally experienced the superiority of socialism. This achievement realized what Deng Xiaoping said: The superiority of socialism should be embodied radically in “constantly improving the material and cultural life of the people on the basis of developing productivity.”³⁴ Besides, it also enriched and developed the theory of distribution of the primary stage of socialism.

3 The Development from Normative Analysis to Normative Analysis and Empirical Analysis

The studies on distribution theory before the reform and opening up mainly employed normative analysis and repelled empirical analysis. But there was empirical analysis in the classical works of Marxism and there was normative analysis in western classical economics. So as research methods, normative analysis and empirical analysis did not repel each other. But people preferred to use normative analysis in the studies in Marxist economics in China during the period after the founding of the People’s Republic of China.

The characteristic of normative analysis was to take value judgment as basis and focus on logical reasoning. People first established the premise of economic theory and formulated some criteria as the measure for analyzing economic policies and economic matters. Second, they studied how to make economic policies and economic matters conform to theoretical premises and criteria. And lastly, they answered what the result should be and they needed not to consider how to test their conclusion. Empirical analysis mainly referred to quantitative analysis. People mainly proved whether a hypothesis was true or false through handling statistical data. Its characteristic was that the study goes beyond all value judgments and only considers the inherent connections between economic matters so as to analyze and predict the results of people’s economic behavior. It answered what the result was and endeavored to test the conclusion that they got against experiential facts.³⁵

In the 1980s, Chinese scholars basically carried out normative study. For example, the issue of the measurement of the standard and difference of income was only limited to calculating the multiple relations of the magnitude and difference of income

³⁴*Selected Works of Deng Xiaoping*, Vol. 3, People’s Publishing House, 1985, p. 63.

³⁵Hu et al. (1997).

changes in the normative study in the past. There was little accurate measurement. As China's reform and opening up deepened, the standard and channel of the residents' income both experienced growth. Correspondingly, people needed to carry out quantitative analysis to adapt to new situation. In addition, as western economics was spread extensively in China in the middle of 1980s, empirical analysis which was the strength of western economics, started to have increasingly larger influence in China. Chinese economists started to use the method of empirical analysis in the study in the area of distribution. First, they used some concepts and then they gradually started to employ mathematical methods to carry out empirical analysis. The literature that used the method of empirical analysis the earliest was that Lorenz curve and Gini coefficient were employed in the fifteenth chapter "The Issues of China's Consumption Fund and Personal Income Distribution" in the book *A Study on the Strategic Issues in China's Economic Development* edited by Liu Guoguang et al. and published by Shanghai People's Publishing House in 1984. From then on, people started to use empirical methods extensively. This promoted the study on the issue of the unfairness in income distribution in China and totally changed the picture of such study. Representative works in this respect included *A Study on China's Residents' Income Distribution* edited by Zhao Renwei et al. and published by China Social Sciences Press in 1994 and *Income Distribution in Economic Development* written by Chen Zongsheng and published by Shanghai SDX Joint Publishing Company in 1991.

In the area of distribution, normative study mainly discussed the basic theory on the fairness of income distribution and analyzed income source and how to distribute while empirical study mainly focused on relevant countermeasures to resolve the contradictions in distribution relations and design ideal distribution modes. So these two were complementary and they should not repel each other in modern economic study. It was gratifying that the scholars give more and more weight to empirical study in the area of income distribution. The combination of empirical study and normative study became a general trend. The combination of the two could help China's income distribution theory to combine closely with practice and achieve healthier development.

4 The Evolution of the Forms of Distribution Determined the Emergence of the Explorations on the Issue of the Relationship Between Fairness and Efficiency

The Chinese circle of economics explored twice the issue of the relationship between fairness and efficiency: The first exploration occurred in the 1980s and the second in early 21st century. The background of the first exploration was that China started to implement the development strategy of reform and opening up and that distribution was in a status of inferior efficiency and serious presence of equalitarianism. People were thinking about how to get out of such difficulty. For example, China's Gini

coefficient was 0.16 in early 1980s. It was a standard of absolute equalitarianism and China's productivity was of an extremely low standard. Under such a circumstance, the Chinese circle of economic theoretical study proposed the views such as the theory of prioritizing efficiency, the theory of prioritizing equality and reciprocity, and the theory of balancing fairness and efficiency.³⁶ The Third Plenary Session of the Fourteenth CPC Central Committee proposed the guiding thought of "prioritizing efficiency with due consideration on fairness", targeting the weakness of traditional system that equalitarianism, which was compared to the "big rice pot", resulted in inferior efficiency. In early 21st century, income gap grew while the standard of residents' income kept rising. The issue of fairness and efficiency once again attracted people's attention and hence the second major discussion on fairness and efficiency occurred. The focus of the argumentation was whether the principle of "prioritizing efficiency with due consideration on fairness" could continue to be applied.

Ying Yixun believed that there was obvious theoretical defect in the theory of "prioritization" which advocated "the prioritizing efficiency with due consideration to fairness". The theory of "prioritization" only paid attention to the aspect that efficiency and fairness were mutually contradictory. It did not pay attention to the aspects that they were in unity and complementation, which were more important. In particular, it failed to pay attention to the situation that the imbalance in fairness would cause harm to efficiency. So it was inconsistent with the requirement of market economy. It should discard the theory of "prioritization" and change to the "theory" of "parallelism". The specific representation of it could be "to endeavor to realize the optimal combination of efficiency and fairness". Namely, people should maintain proper social fairness to promote efficiency and further improve social fairness through improving efficiency.³⁷

Xiao Liang said that some people proposed to change the formulation of "prioritizing efficiency with due consideration on fairness" in response to the tendency of enlarging income gap in the city and the countryside and advocated paying equal attention to efficiency and fairness. But he believed that the original formulation should not be changed. This was because (1) Production determined distribution. The formulation of "prioritizing efficiency with due consideration to fairness" was proposed with the equalitarianism before the reform and opening up as the target. It contained the intention to improve production. In order to improve production, people had to adhere to prioritizing efficiency in distribution system so as to mobilize the initiative of the extensive community of producers and operators. Changing the original formulation looked like turning back to the old path and it was unfavorable to improving production. (2) In the present stage of the market economy in China, the enlargement of income gap was an irreversible tendency. Such income gap could only be "adjusted moderately". It should not be overstressed. ... Besides, enlarged income gap might not necessarily be something bad. It could be a good thing. (3) The current enlarging income gap in China was the enlargement under the circumstance

³⁶See *China Economic Science Yearbook (1988)*, pp. 133–134.

³⁷Ying (2002).

of the improvement of income in general. Namely, some people had more improvement while other had less in such enlargement. It was not income polarization. (4) Common prosperity was a long-term goal. Namely the enlarged income gap could narrow gradually only after great achievement was made in economic development. Besides, even when common prosperity was achieved in the future, it still would not be that everybody had the same standard of income.³⁸

Zhao Renwei also believed that it was advisable to implement the principle of “prioritizing efficiency with due consideration on fairness”. In the process of economic transition, economy developed faster due to the reasons like the rapid transformation of industrial structure. This required that there should be large improvement of efficiency and certain enlargement of income gap. Implementing the principle of prioritizing efficiency with due consideration on fairness conformed to objective economic principles.³⁹

At present there was indeed the tendency of enlarging residents’ income gap and the standard of income was kept rising. This resulted from China’s reform and opening up and the implementation of the principle of “prioritizing efficiency with due consideration on fairness”. This was also the inevitable result of implementing the principle of “prioritizing efficiency with due consideration on fairness”. It needed to be pointed out that the formulation of “prioritizing efficiency with due consideration on fairness” was not mentioned in the document of the CPC from the decision of the Fourth Plenary Session of the Sixteenth CPC Central Committee in 2004 to the report of the Seventeenth CPC National Congress. Under such background, Liu Guoguang made another proposal of implementing the principle of “giving equal weight to fairness and efficiency” so as to resolve the contradiction between fairness and efficiency. He said that “I approved of the formulation of prioritizing efficiency in the early period of the reform and opening up under the general background of giving more weight to fairness and less to efficiency so that people could change with it the pattern of interests characterized by equalitarianism like ‘everybody eating from a big rice pot’. After the reform has been implemented for thirty years, the issue of efficiency is not as prominent as that of fairness now. Under the new situation that the issue of fairness increasingly appears to affecting efficiency and stability, I call emphatically for giving equal weight to efficiency and fairness and pay more attention to social fairness.”⁴⁰

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³⁸Xiao (2003).

³⁹Zhao (2002).

⁴⁰Liu (2010).

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Chapter 24

The Formation and Development of a Brand New Social Security Theoretical System



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The study on traditional social security theory mainly came from the discussion on welfare in classical theories such as Marxism, Leninism and Mao Zedong Thought. Marx's thought about "product deduction", Lenin's thought about "state insurance", and Mao Zedong's thought about "promoting development with welfare" all provided theoretical basis for the establishment of social security system in The People's Republic of China. The "state insurance" of the Soviet Union provided system template for China directly and became the object that The People's Republic of China learned from in social security. Under the guidance of these theories and systems, the People's Republic of China established "state/enterprise insurance system". This system made great contribution to the economic construction of The People's Republic of China.

After the beginning of the reform and opening up, the Chinese circle of economics studied the theory of social security under the guidance of the ideological line of "liberating thought and seeking truth from facts". They took China's actual national situation as the basis of study and started with introducing and drawing from foreign social security theory and discussed the gains and losses in foreign experience. And they gradually formed the social security theory and system with Chinese characteristics. People summarized the experiences in labor insurance system which was reinstated after the beginning of the reform and opening up. And on such basis, they made comparison between the traditional social collection and personal account model and the emerging personal account model. After such comparison, China

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finally established through implementing pilot projects its unique pension security and medical care systems on the basis of the social collection and personal account model.

Around the turn of the century, China reflected once again on social collection and personal account model for the purpose of improving its social security system. After that, it further expanded the coverage of pension insurance and improved the accrual and issuance method of the benefits of pension insurance. It constructed a rudimentary framework for a medical care insurance system that covered both the city and the countryside and officially established unemployment insurance system and subsistence allowance system. After the beginning of the new period of the 21st century, the construction of harmonious society and the outlook of scientific development became the new theoretical basis for China's social security system. In this new period, there were still very serious tasks and numerous problems that people had to face in the construction of social security. The issues such as the social security of peasant workers and the direction of development of the social collection and personal account system were all areas that needed to be improved in the new period.

1 The Theoretical Basis and Development of Traditional Society Insurance System (Before 1992)

I. The Theoretical Basis of China's Social Security System Before the Reform and Opening Up

In the early period after the founding of the People's Republic of China, there were three theoretical bases for China's social security system: The first one was Marx's "production deduction" theory. According to Marx's explanation, the "gross social product" created by workers was the basis to build a social security system and social security was a necessary condition for man to carry out "reproduction". Therefore, when examined from the perspective of "reproduction", it was necessary to make welfare deduction from "gross social product".¹ The second one was Lenin's "state insurance" theory. Lenin developed Marx's "product deduction" theory into "state insurance theory" and the responsibility of the state in social security.² The social security model of the Soviet Union, established on the basis of such theory, exerted overwhelming influence on the Chinese circle of economics and China's selection of the model of its social security system. The third one was Mao Zedong's theory of "promoting development with welfare", which advocated giving "visible welfare" to workers and mobilizing the initiative of investors on the basis of guaranteeing the

¹*Selections of Karl Marx and Friedrich Engels* Vol. 3, People's Publishing House, 1995, pp. 302–303.

²*Complete Works of Lenin*, Vol. 29, People's Publishing House, 1985, p. 489.

welfare of the people.³ This was of important meaning to restoring national economy. In the process of revolution and construction, Chinese communists summarized their own practice and experience in social security. They followed the basic thought of Marx in “product deduction”, incorporated the basic principles in Lenin’s thought of “state insurance”, and further extended the model of “state insurance” of the Soviet Union. And in this way, they established the model of “state/enterprise insurance” with the features of the welfare thought of Chinese communists and the Communist Party of China.

Specifically speaking, the model of “state/enterprise insurance” referred to the social security model with the combination of the state and enterprises in which the state functioned as the entity of implementation and management and the state and enterprises jointly bore expenses.⁴ Its features mainly included the following three aspects: First, the model of “state/enterprise insurance” provided urban residents with the protection “from cradle to tomb” and became relative good supplementation to low wage system under planned economy. Second, the state dominated and enterprises implemented. Social security policy was implemented by various enterprise units but what stood behind this was the unlimited responsibility of the fiscal organs of the state. “Unit” became the medium for the specific implementation of various social security policies of the state. Third, “state/enterprise insurance” was in fact the system dominated by the trade union system in which “the central planning of the state and the provision of insurance of the state” were combined. It was mainly manifested as the graded management and use of insurance fund by the trade union. With the developments in economic construction, the superiority of the three features of the social security system of The People’s Republic of China in the above became conspicuous increasingly and provided positive guaranteeing functions in the economic construction of The People’s Republic of China.

Later, three problems were exposed in the model of “state/enterprise insurance” with the system took shape and developed. First, there was only one channel of fund raising. Employees did not participate in fund payment personally. State fiscal organs found it hard to shoulder the burden so that social security system became another “big rice pot”. Second, the coverage was narrow and imbalanced between the city and the countryside, which worsened the characteristic of dual structure in China. In general, it was unfavorable to the long-term development of economy that the standard of social security in the countryside was lower than the city. Third, traditional “state/enterprise insurance” suffered extremely large impact during the ten years from 1966 to 1976. The “state/enterprise insurance” degraded into “enterprise insurance” and labor insurance system became a matter inside an enterprise from then on. And the situation lasted until the reform and opening up began. The degradation of the “state/enterprise insurance system” into “enterprise insurance system” resulted in the further decrease of the degree of socialization in traditional social security system. The situation that different units took care of the matter on their own seriously affected the normal flow of labor between enterprises under different ownership systems,

³ *Selected Readings of Mao Zedong*, Vol. 2, People’s Publishing House, pp. 563–564.

⁴ Ma and Zheng (2005).

between different departments, and within certain regions. Examined from the angle of sustainability in finance, “enterprise insurance” caused such heavy burden that the enterprises could hardly bear. In particular, old state-owned enterprises faced growing payment risks coming from insurance benefits. As China’s economic system underwent transition, labor insurance benefits became an increasingly conspicuous burden that hindered the system transformation of the enterprises.

II. The Study and Development of Social Security Theory Under the Conditions of the Reform and Opening Up

The new issues that emerged in the practice of social security under the background of system transformation after the convening of the Third Plenary Session of the Eleventh CPC Central Committee at the end of 1978 could not be resolved with the theory of “product deduction” in Marxism. And then the circle of the area of social security in China welcomed the spring of theoretical study and embarked on the journey of study and learning. First, fundamental and classical theories in social security, such as welfare economics, started or resumed to be introduced into China.⁵ Among them, there were welfare economics, state intervention theory and theories of neo-liberalism.⁶ These theories laid the theoretical foundations for people to explore the social security system with Chinese characteristics in the new period of development. Second, works that introduced the social security system in various countries were also published successively.⁷ Moreover, works on social security were written and published in China on the basis of reflecting on the current situation of social security in the country. The publishing of these works further improved the depth of the theories on social security in China. They also laid the theoretical foundation for cultivating talents who specialized in social security in China.

In addition to theoretical study, the Chinese circle of theoretical study carried out heated discussion on the issues such as the nature and role of China’s social security work, the raising of insurance funds and its management system, centering round the theme how to build a social security system with Chinese characteristics and targeting numerous problems that newly emerged in the process of economic system transformation, in the academic study and discussion on China’s labor insurance/social security system and relevant theories and also in the study and discussion on relevant policies. At the time, the discussion mainly focused on three aspects: First, defects present in the prevailing labor insurance/social security, second, the nature and role

⁵The translation and introduction of some classical works started before 1966. These works were reprinted successively after the beginning of the reform and opening up, such as *A Review of Welfare Economics*.

⁶The works on welfare economics included *A Review of Welfare Economics* and *Theoretical Welfare Economics* reprinted by The Commercial Press in 1980. The works on Keynesian theories included *Monetarism and Keynesianism* (1984) and *Democracy and Deficit: The Political Legacy of Lord Keynes* (1988). The works on the theories of neo-liberalism included *Free to Choose: A Personal Statement* (1982) and *Individualism and Economic Order* (1989).

⁷For example, *Social Security Systems in Fifty Countries* (1985), *Economic Welfare System in Various Countries* (1986) and *A Survey of Foreign Social Security Systems* (1989) and *Social Security Systems in the Soviet Union and Eastern Europe* (1991).

of labor insurance/social security, and third, the choice of the model of social security. Although there were many controversies in the discussion, the Chinese circle of economics still had consensus on the following: The terms of “labor insurance” and “social insurance” did not have substantial difference.⁸ China in fact implemented “employment insurance”, which should be transformed into “social security” in the future.⁹ Social security system should be adapted to the standard of productivity development. Social security system should have wide coverage, low standard and multiple levels. The spending on social security should be borne by the three parties of state, enterprise and individual. The raising of the funds of social security and the services in social security should be socialized. Later, these theoretical research results were successively integrated and manifested in various social security policies formulated by the CPC and the state.

The achievements made in theoretical study and policy making in this period were mainly seen in the following several aspects: First, people sought advancement in steady development and constantly expanded the scope of coverage. The coverage of labor insurance system was expanded from only including government organs, institutions and state-owned enterprises to also including collective economy. The establishment of rural pension insurance system started to be put into the agenda of various meetings. Second, people clearly defined the system framework of pension insurance with the dominance of centralized social planning. They established the principle that state, enterprise and individual bore the expenses and proposed the goals of further expanding the coverage of pension insurance and establishing multileveled pension insurance system. Third, people proposed the direction of medical system reform: to establish step by step an employee medical care insurance system suitable to China’s national situation with multiple forms and levels and higher degree of socialization, in which state, enterprise and individual reasonably bore relevant expenses. Fourth, “employment-pending insurance” was established from scratches.¹⁰ People established for the first time employment-pending insurance system for the employees in urban state-owned enterprises in the form of laws and regulations. This laid the foundation for establishing unemployment insurance system at the end of 1990s. Fifth, the circle of the theoretical study on social security, in this period, still regarded social security as “an indispensable supportive project in socialist market economy and socialized mass production”.¹¹ So they mostly carried out discussion and exploration from the angles of year-on-year economy, state-owned enterprises, and labor distribution system reform. These could be seen from the formulations such as “benefiting production and guaranteeing life”.

⁸Secretariat of the China Association for Labor Studies, “A Theoretical Discussion on Reforming Social Security and Welfare System—An Account of the Symposium on the Issue of Social Security and Welfare”, *China Labor*, Issue 18, 1983.

⁹Chen and Zhao (1986).

¹⁰For the discussion on the terms of “unemployment insurance” and “employment-pending insurance”, see Chen (1991), Zhao (1992).

¹¹Dorje (1995).

2 The Exploration and Development of the Theory of Social Security: The Selection of the Target Model of China's Social Security (1992–1998)

Deng Xiaoping's South Tour Speech in 1992 signified that China's reform and opening up entered a new historical period. The Third Plenary Session of the Fourteenth CPC Central Committee held in 1993 adopted the *Decision of the CPC Central Committee on Several Issues on Building Socialist Market Economic System* (or the Decision for short). It proposed "building socialist market economic system" and, "in personal income distribution, adhering to the system of taking distribution according to performance as the main part and achieving the coexistence of multiple modes of distribution and manifesting the principle of prioritizing efficiency with due consideration to fairness". It also proposed the goals in system construction, such as "building multileveled social security system" and "implementing the combination of centralized social planning and collection and personal account". It was pointed out in the discussion on the reform of social security system in the Decision of the Third Plenary Session of the Fourteenth CPC Central Committee that "to build a multileveled social security system is of important meaning to deepening the reform in enterprises and institutions, maintaining social stability, and successfully building socialist market system". The development from planned commodity economy to building market economy meant a great leap-forward in China's economic system transformation. In this period, Chinese economy faced two difficulties: serious inflation and state-owned enterprises' operation difficulty. Economic system transformation, difficulties present in practical work, and reform of labor distribution system, these changes in external environment exerted profound influence on the research and exploration on social security theory in new period.

I. Developing the Theories of Social Security and Borrowing from International Experience

In the early and middle periods of 1990s, there were a great abundance of books on the theories of social security. The contents of these works showed development in both depth and width and formed contrast with the situation in the last decade when there were only a small number of college textbooks on social security. These works could roughly be divided into several types: The first type was college textbooks. A considerable amount of new college textbooks were published during this period.¹² These books guaranteed the teaching work in the new specialty of social security that emerged in the area of social work and management. The second type was works that summarized experiences. These included not only those summarizing the experiences in pilot projects¹³ but also those summarizing the theories and practices

¹²For example, *An Introduction to Social Security* (1992, 1995, 1996); *Modern Social Security System* (1994); *Theory of Social Security* (1995); *An Introduction to Medical Care Insurance* (1995); *Social Security* (1996).

¹³For example, *The Zigong Model: An Exploration on Building New Pension Insurance System of Urban Collective Enterprise Employees* (1992).

of the reform of social security system.¹⁴ The third type was works about theoretical research. These works were of great importance to constructing the theories of social security and analyzing the interactive relations between social security and other disciplines.¹⁵ The fourth type was works that discussed special topics. These works mainly contained special research and discussion on certain them within the area of social security.¹⁶ The fifth type was the works of rural social security. These works contained theoretical analysis and discussion on the actual situation of social security in the countryside in China.¹⁷ The sixth type included working manuals and reference books. A considerable amount of reference books emerged in this period.¹⁸ The publishing of these works created great convenience for the spreading of the theories on social security and the conducting of the operational practice of social security.

In this period, the works that borrowed from foreign experiences in social security covered more extensive scope in discussion and contained more in-depth research. A large number of foreign works on social security were also published in this period.¹⁹ A multitude of articles on the social security systems in different countries were published in various academic periodicals. In the past, people mainly introduced the social security systems in developed countries in western and northern Europe and in the USA. Different from this, people made comparison and drew from foreign studies in a broader perspective in this period. They introduced in a large number of works the social security systems in Singapore and in the economics in East Asia and also the personal account system in the countries in Latin America in addition to those in developed countries. It needs to be pointed out that the paradigms for comparative

¹⁴For example, *Social Security System Reform* (1995); *Social Security System Reform* (1996); *A New Theory of Social Security System Reform* (1997), *Pension Insurance System Reform* (1997), *Medical Care Insurance System Reform—A Transformation Concerning Life, Old Age, Disease and Death* (1999).

¹⁵For example, *Social Security and Insurance* (1994); *Social Security System* (1994), *Theories and Policies on Pension Insurance System* (1995); *Economic Theories on Social Security* (Cong Shuhai, 1996); *Policy and Management on China's Medical Care Insurance System Reform* (1999).

¹⁶For example, *Social Security Index System* (1993); *Fiscal Management in Social Security* (1996); *An Analysis on the Structure and Operation of Social Security System* (1997); *Social Security Law* (1997); *A Complete Collection of Basic Medical Care Insurance System for Urban Employees* (1998).

¹⁷For example, *A Manual on Rural Social Pension Insurance* (1993); *A Summary of China's Rural Social Security* (1993); *A Survey of China's Rural Social Pension Insurance* (1993); *A Report on the Demonstration of the Basic Plan for Rural Social Pension Insurance* (1995); *Rural Social Pension Insurance* (1996); *Rural Social Pension Insurance Work* (1996).

¹⁸For example, *An Encyclopedia of Social Security* (1994); *A Guide of Pension Insurance* (1995), *617 Questions and Answers on Pension Insurance* (1996); *A Guiding Manual on the Reform of Employee Medical Care Insurance System* (1996); *Questions and Answers on Medical Care Insurance Policies* (1999).

¹⁹For example, *Social Welfare System in Northern Europe and China's Reform of Social Security System* (1993); *Social Security Systems in Various Countries in the World* (1994); *A Survey of Social Security System in Major Countries in the World* (1995); *Social Security in the United States* (1995); *Global Social Security 1995* (1996); *An International comparison of Social Security and Tax System* (1996).

study were mostly adopted in the research on the social security systems in various countries in the world in the 1990s. People paid more attention to introducing new developments and changes in the social security systems in various countries rather than simply introducing social security systems. These comparative studies played an important referential role in the selection and determination of the model of social security in China.

Under the historical conditions at the time, the international comparative research on social security system sustained unavoidable impact in general international environment like all other studies. Oil crisis and population ageing caused to certain extent the occurrence of payment crisis in traditional DB-type²⁰ pay-as-you-go system. In contrast, the DC-type²¹ full-funded system reform, led by neoliberalism and pioneered in Chile, achieved the results that attracted the attention of the world. The introduction of personal account and its role in social security system attracted increasing attention of relevant circles and triggered a discussion on the comparison on the superiority of the models of social security system worldwide. For a moment, the debate on models became extremely intense. The traditional DB-type pay-as-you-go system, represented by that in Sweden, faced growing fiscal pressure while the DC-type full-funded system, represented by Chile, achieved relatively ideal market returns. Because of this, Chile's full-funded system and Singapore's Central Provident Fund model, which also introduced personal accounts, became a focal area that attracted great attention in China's circle of economic study and work. A large part of Chinese economists had great interest on the applied studies on personal account and DC-type funded system.²²

II. The Discussion and Exploration on the Selection of the Model of Social Security System and Other Issues

The main tasks of China's economic system reform in the 1990s were implementing state-owned enterprise reform and building modern enterprise system. The main risk that confronted the reform was inflation. The main task of social security reform was to establish the basic framework of modern social security system and its main risk was population ageing. The main issues that the Chinese circle of theoretical study generally recognized in social security system included the following: Its coverage was too narrow. Enterprises under different ownership systems had different burdens. The lack of incentive effect resulted in the phenomenon of the waste of social security resources. Policies were made by multiple policy-makers and decision making and fund use were not well-regulated because of the lack of supervision. Besides, issues like unemployment insurance issue, lowering social security collection rate and value preservation and increase of social security funds also attracted the attention of various circles.

1990s was the key period for the construction of social security system in China. To be accurate, the rudiments of the social security systems for pension and medical

²⁰Defined Benefit type.

²¹Defined Contribution type.

²²Zheng (2008).

care were created at the end of 1990s. In this important historical moment, the Chinese circle of theoretical study gradually achieved consensus on some important theoretical issues. These “social consensus” played an important and positive role in establishing the general framework of the social security system in the 1990s. First, the definitions on the concept of social security gradually converged into the same one: After several decades of discussion, the circle of theoretical study gradually believed that social security was a concept of security in the society in general. It included four aspects of social insurance, social welfare, social relief and veteran benefit and placement. Among them, social insurance was the kernel of this system.²³ In terms of verbal representation, the definition of social security given by the International Labor Organization gradually took the dominant status.²⁴ Second, the Chinese circle of theoretical study achieved consensus on the general principle of social insurance: People should strengthen the functions and duties of the government in the undertakings of social security. They should build a multileveled social security system and gradually realize a social security system that combined basic insurance, supplementary insurance and personal savings. And they should implement a mode of fund raising with multiple channels and practiced centralized social planning and collection. Third, the Chinese circle of theoretical study generally believed that people should enlarge the scope of the personnel eligible for participating in social insurance in China’s social security system. They should increase the factors of income redistribution. Enterprises under different ownership systems should bear the expenses on social security fairly. They should strengthen the construction of the laws and systems on social security.

1990s was both the period when the general framework of social security system was formed in China and the period when there was very intense contention on the theory of social security. These debates emerged in the 1990s and exerted important influence on the choice of the model of the social security system in China at the time. And some issues in the debate still existed today and the debates on them continued. The issue of the model of fund raising for pension insurance caused the largest controversy at the time. This issue caused great attention because it concerned the sustainability and prospects of the system. There were mainly three different views then.²⁵ The first view supported funded system. It was believed that the direction of China’s reform should mainly be the Singaporean model. This model could stimulate on-job employees to work hard to create welfare and guarantee for themselves. It could also promote saving, reduce state expenditure, and reasonably allocate resources. The second view supported the pay-as-you-go system. It was believed that social security should take fairness as the main principle with due consideration to efficiency. The per capita income of the Chinese people was very low. In particular, some enterprises were in difficulty in their production and operation so that it was impossible

²³Zhang (1994).

²⁴International Labor Organization Convention No. 102: *Social Security (Minimum Standards) Convention*.

²⁵Zhang (1994).

for China to implement personal account system and it could only implement pay-as-you-go system. The last one believed that people should combine the two models and establish partial-funded system. Thus, people could both guarantee the subsistence of the majority through pay-as-you-go system and satisfy the requirements for further improving and bettering life standard through personal account funded system. Namely people should implement social mutual aid on the basis of self-guaranteeing through establishing social collection and personal account system so as to realize fairness on the basis of achieving efficiency.²⁶

In general, the discussion in this period was influenced by China's domestic economic situation and the international development of social security. In the international community, various countries that practiced the traditional pay-as-you-go system generally adopted the measures such as lowering benefit payment standards, increasing social insurance contribution rates, and extending retirement age to respond to payment crisis. The achievements that Chile and other countries made through practicing personal account system in the same period caused the circle of theoretical study concentrate their eyes more on funded system. The operation difficulties of state-owned enterprises caused uneven burdens in social security among these enterprises and contribution payment difficulty and unemployment became increasingly prominent. Inflation exposed the original social security funds to the risks in value preservation and increase. This rang the alarm for the optimistic supporters of funded system. The realization of funded system needed conditions. And the discussion on such conditions occurred at the end of this period.²⁷

III. Policy Achievements and Theoretical Developments

1990s was also the period when China determined the target model of its social security system. At the time, the theories of social security were more mature. The circle of theoretical study already achieved certain understanding on the advantages and disadvantages of the social security systems of various countries in the world. Theoretical analysis and discussion related more closely to the actual situation in China. Under the background that China faced the challenges of state-owned enterprise reform and serious inflation, the circle of theoretical study started to pay more attention to the financial balance of social security system. The line of theoretical development in this period was like this: People started to reflect on the weaknesses of traditional pay-as-you-go system through international comparison and drew from the successful experience of some countries in implementing personal account system. Then people reflected on and summarized the issues that occurred in the process of the operation of social security system and also summarized the experiences in resolving the issues. And then people determined the principle, goal and system model choice of China's social security. Under the influence of such line of theoretical development, various policies and regulations on social security in China drew from and absorbed largely the results of theoretical discussion at the time. Such a situation was mainly manifested in the following aspects:

²⁶Liu (1995).

²⁷Li (1997).

(I) Establishing the Social Collection and Personal Account Model of Pension Insurance System

In 1997, the State Council promulgated the *Decision of the State Council on Establishing Unified Basic Pension Insurance System for Enterprise Employees*. The Decision was an important milestone for the final establishment of the social collection and personal account system for urban employee pension insurance in China. It laid down the basic pattern of China's basic social security system in the future. It is noteworthy that the time when China determined the social collection and personal account model for its pension insurance system was also the period when the trend of neo-liberalism became greatly popular in the international community. But in the end, China eventually was not influenced by the radical trend of neo-liberalism. It chose a reasonable partial-funded model suitable to China's reality. The original intent and philosophy of the design of this system was praiseworthy even until today. In theory, this model could combine the characteristics of centralized social planning and collection and personal account. It could both realize social mutual aid and enhance personal responsibility. But many issues remained unsolved in this period. The circle of theoretical study already reached consensus on the issue that "pension adjustment mechanism is absent and management system is not well-calibrated" for a long time. But this issue still was not resolved. The complexity of pension insurance system and some specific regulations also foreshadowed new issues that occurred later. Regulations such as acquiring "transitional pension" from pension insurance funds resulted in the situation that one generation of people shouldered the burdens of more than one generation. This was the radical cause in the system why the problems of empty account and insurance withdrawal occurred later.

(II) The Pilot Projects for the Combination of Social Collection and Personal Account in Medical Care Insurance System and the Establishment of the System

In 1998, the *Decision of the State Council on Building Basic Medical Care Insurance System for Urban Employees* was promulgated. This signified that the medical care insurance system characterized by the combination of social collection and personal account was established in China. The opinion of some scholars on the social collection and personal account system was that implementing the combination of social collection and personal account meant practicing social mutual aid on the basis of guaranteeing and realizing fairness on the basis of efficiency. ... Solely implementing centralized social planning and collection had the problems of weak incentive effect and too much equalitarian elements. So the existence of personal account was very necessary.²⁸ From this perspective, the social collection and personal account system gave equal weight to fairness and efficiency in medical care insurance. It was a system that effectively combined the responsibilities of state, enterprise and individual. Besides, many issues existed in the area of medical care insurance, such as that medical care and health system did not match the insurance system, that medical expenses rose quickly, and that the insurance had too narrow

²⁸Liu (1995).

coverage, and there was also the issue how personal account and social collection account should be combined. Resolving these issues would directly influence the next stage of the reform of China's medical care insurance system.

(III) The Development of the "Employment-Pending Insurance" System of the State-Owned Enterprises

The *Interim Regulations on the Employment-Pending Insurance for the Employees of State-Owned Enterprises* promulgated in 1993 expanded the coverage of employment-pending insurance. And it also clearly defined the management institution of employment-pending insurance and its functions and adjusted the benefits standard of the insurance. The emergence of the "employment-pending" system was a special stage in the process of establishing unemployment insurance system in China. It was an epitomizing example of the progressive strategy of the reform and opening up that China adopted. It was also a special product of the overall environment at the time. Similar to the issues in other insurance types in social security that occurred in the same period, there were issues in several aspects in the "employment-pending" system at the time. For example, the coverage of employment-pending insurance was too narrow. The level of its centralized planning and collection was too low. Insurance benefits were also too low. And supervision and management systems were not well-regulated.

(IV) Implementation of the Pilot Projects for Urban Residents Subsistence Allowance System and Its Promotion

In the second half of 1995, the Chinese circle of academic study established on the basis of summarizing the experience in pilot projects the system framework with Chinese characteristics for urban residents subsistence allowance system, which included the determination of the security line of minimum subsistence, the qualifications and conditions for the receivers of subsistence allowance, fund source of the system and mode of bearing expense burdens, and institutions and modes of aid of the system.²⁹ In 1997, the State Council issued the *Notice on Establishing Urban Residents Subsistence Allowance System Nationwide*. It was stipulated that various places should gradually give minimum subsistence security to the residents in non-rural residence registration on the basis of actual local conditions. By the end of September 1999 when the *Regulations on Urban Residents Subsistence Allowance* took effect, subsistence allowance system was established in 668 cities and 1,638 designated towns which were the seats of county governments nationwide.³⁰

²⁹See Research Group of the "Study on the Reform of Urban Social Relief System in China", "A Research Report on Building the System of Security Line of Minimum Subsistence for Chinese Urban Residents", *Social Work Research*, Issue 6, 1995.

³⁰Yang (2008).

3 The Prosperity of the Theories on Social Security and the Improvement of the Systems: The Initial Establishment of China's Society Security Model (1998–2007)

Around the time when the social collection and personal account model was established in pension security and medical care insurance systems, state-owned enterprises had operation difficulty once again and the impact of Asian financial crisis affected China. The changes in external environment quickly turned the inflation in China into deflation. The percentage of loss-incurring state-owned enterprises and their loss rate increased year by year. Under such background, the central government made the arrangements for the goal of “letting state-owned enterprises getting out of difficulty in three years” in 1998. State-owned enterprises made industrial structure adjustments. A large number of redirected personnel, namely laid-off and retired employees, brought huge pressure to the operation of social security system. This was the general external environment that the circle of the theory of social security faced in the early period of this stage.

I. The Development of the Theory of Social Security and the Borrowing from Other Systems

This period was one of the periods when the theoretical study on social security was the most active. There was an immense number and also a great variety of theoretical works. The representative works among them could be roughly divided into seven major types: The first type discussed the theory of social security from the angle of economics and income distribution.³¹ These works examined the functions of social security in realizing redistribution and promoting social fairness from the angle of economics. They also discussed the Pareto efficiency in the retracking of social security system. The second type were the works that summarized and reflected the construction of China's social security system.³² These works reviewed the journey of the reform of social security system in China, summarized the experiences and lessons in the reform, and constructed the theoretical framework for the construction of social security system in the future. The third type of works were about social security law.³³ These works discussed the legal theory and construction of social security and other contents. Other types of works were mostly domestic ones but

³¹For example, *Social Security System and Economic Development* (1998); *Social Security Economics* (1999, 2003); *National Wealth and Income Redistribution in Social Security* (2003); *Social Insurance and Economic Guarantee* (2005); *An Economic Analysis on Deepening Social Security Reform* (2006); *China in Transition—Social Security and Social Justice* (2007).

³²For example, *The Construction of Social Security System in China in Twenty Years* (1998), *Reform and Improvement of Social Security System in China* (2000), *A Report on the Reform and Development of Social Security System in China* (2001), *Transformation and Evaluation of Social Security System in China* (2002); *Tackling and Cracking the Key Difficulties in the Reform of Social Security System* (2005); *Social Security Reform: Where to Go* (2006).

³³For example, *Philosophy, Practice and Innovation of Social Security Law* (2002); *Social Security Law* (2002, 2003, 2006); *On Social Security Law* (2003).

this type was different. Large amount of foreign works on social security law were introduced in this period. The fourth type was works about rural social security.³⁴ These works summarized the experiences and lessons in developing the undertakings of social security in the countryside in China and proposed the theoretical framework of system construction. The fifth type of the works were the theories on the practical work in social security and those on the social security of special groups that emerged in this period.³⁵ The sixth type included several dozens of college textbooks. And the seventh type of works was book series and book published periodically in the manner of magazines that emerged in this period.³⁶

Also in this period, the Chinese circle of theoretical study made more in-depth introduction and comparison on international social security systems. Domestic scholars achieved a myriad of research results in their study on the social security systems in particular countries and regions. These results could be roughly divided into two types on the basis of research objects: The first type of these results was the study and analysis on the social security systems of specific countries and regions. In comparison with the past, the study on the systems became more in-depth and often included a number of time spans. The study also had more abundant contents and often included a large amount of contents on the backgrounds of the construction of social security systems and relevant theoretical discussions.³⁷ The second type of these results was comparative studies and analyses on special topics. The themes of these studies showed extensive distribution in research areas, from fund management to social security law, from privatization reform to comparisons in rural social security, and from the collection and selection of various regional social security systems to the transformation of social security under the background of globalization. The contents of these comparative studies were unmatched by those in the past in terms of depth and width.³⁸

³⁴These works included *A Study on China's Agricultural Insurance and Rural Social Security System* (2002); *Reform and Development of the Social Security for the Peasants in Underdeveloped Regions in the 21st Century* (2004); *Centralized Planning and Collection of Urban and Rural Social Security: Theory, Mechanism and Practice* (2005); *Structure and Transformation of China's Rural Social Security System: 1949–2002* (2006).

³⁵For example, *Operation Management of China's Social Security Funds* (1999), *Actuarial Principles of Social Security* (2000); *Social Security Funds and Enterprise Annuity Management* (2007); *A Study on Social Security Policies and Measures for Urban Impoverished Groups* (2006).

³⁶For example, *A Series of Contemporary Studies on Social Security System* (2001); *A Study on Social Security Issues, China Social Security Development Report, Insurance and Social Security*.

³⁷For example, *A Study on the Social Security System in the United States* (1999); *Contemporary Social Security Systems in the United Kingdoms and Sweden* (2000); *International Comparison of Social Security System* (2001); *The Selection of Social Security System in Canada and Its Revelation to China* (2003); *The Development of Social Security System in Sweden* (2004).

³⁸For example, *Social Security System Reform and Its Fund Management: A Common Topic on the Globe—A Collection of Papers of the International Symposium on Social Security Fund Management* (1998); *Contemporary Social Security Systems in African and West Asian Countries* (2001); *A Study on the Social Security Systems in the Countries in the European Union* (2003); *A Comparative Study on Chinese and Foreign Social Security Theories and Systems* (2004); *An International Comparative Study on Rural Social Security and Its Revelations* (2006).

II. Social Security Theory with Chinese Characteristics and the Discussion on System Issues

(I) Issues Present in Social Security System in This Period

The circle of theoretical study believed that there were some prominent issues present in the operation process of social security system in China in the first ten years. In summary, these issues occurred in the following five aspects: First, the issues present in the area of pension insurance included the operation of personal accounts for pension insurance with many empty accounts, too narrow coverage, too heavy charge payment burdens, highly fragmented departmental and regional management system, and low-level centralized planning and collection. Second, the issues present in the area of medical care insurance included too narrow coverage of the system, increasingly serious problem of “too difficult and expensive access to medical service” in China, and the rise of medical expenses exceeding the speed of economic growth. Third, the acceleration of population ageing worsened the contradiction between receipts and expenses in social security fund. Fourth, all funds faced the difficulty of preserving and increasing their value under the circumstance that wage growth rate exceeded 10%. Fifth, the legislative work in social security lagged behind.

(II) The Discussion on the Pension Insurance System

The discussion and argumentation on pension insurance system mainly concentrated on the three issues of empty account and hidden debt, comparison of pension insurance models, and rural social security and migrant workers’ participation in social security.

First, various circles basically reached consensus on the issue of empty account. “Employ account is nothing but another form of manifestation of hidden debt.”³⁹ The circle of theoretical study discussed the cause, scale and approach of solution of hidden debt. The consensus that various circles achieved on the cause of hidden debt was that it was the issue brought about by the method of resolving the deficient amounts in the personal accounts of the personnel who belonged to the old system and who stood in between the old and new systems. Various circles also measured the size of such amount. Because of the differences in the methods and scopes of measurement and calculation, the results ranged from RMB 1.8 trillion yuan to RMB 11 trillion yuan.⁴⁰ There were roughly the following suggestions on the approach to resolve such issue, which included fiscal payment transfer, fund raising inside the system, state-owned assets allocation, value increase of pension insurance fund, establishment of sovereignty pension fund, and extension of retirement age.

Second, economic analyses and judgments based on neoclassical economics started to emerge in the comparison of the models of pension insurance in this stage.⁴¹

³⁹Zhao (2001).

⁴⁰World Bank (1997), Yvonne (2005), Fang (1998), The Institute of Social Insurance of the Ministry of Labor and Social Security (2000), Wang (2000), Song (2001), Wang et al. (2001).

⁴¹Yuan and Song (2000), Yuan (2001), Bo (2000), Feng (2004).

The scholars mostly utilized the methods and analytical instruments in neoclassical economics, such as overlapping-generations model, to demonstrate the determining conditions between pay-as-you-go system and full-funded system and to discuss the relationship between China's social security model and its savings rate and welfare. In the decade, average wage growth rate exceeded 10% and the actual rate of return of pension insurance was too low. Under such a circumstance, the conclusion of these analyses and judgments was closer to the Aaron condition based on biological rate of return. Namely, only when the sum of population growth rate and wage increase rate was smaller than the rate of return of fund could full-funded system have its superiority and advantages. But the actual situation in China was just the opposite. The debate on the models in the period also included the discussion and exploration on notional defined contribution system.⁴²

Third, the Chinese circle of theoretical study reached consensus on many issues present in the operation of rural social security system, such as small coverage, poor sustainability, low standard of social security, instability in the system, and difficulty in value preservation and increase of the fund. But there was much contention in evaluating rural social security system, such as that "rural social security insurance does not have the substance that matches its name".⁴³ Some people even believed that "there are important mistakes in theory and practice" in it.⁴⁴ People also argued endlessly on the three schemes for the future social security model of migrant workers:⁴⁵ The first one tended to incorporate them into urban social security system. The second one wanted to establish a new social security system for migrant workers. And the third one tended to incorporate migrant workers into rural social security system.

(III) Discussion on Medical Care Insurance System

The discussion on medical care insurance system mainly concentrated in the following two aspects: the marketization reform of medical care and health system and the maintenance or removal of personal accounts.

The first aspect was the marketization reform of medical care and health system. In 2005, the research group of the Development Research Center of the State Council pointed out that China's reform in medical care and health system was basically unsuccessful. The main reason was the emergence of the tendency of marketization and commercialization in medical care and health system. This opinion stirred up a big wave of responses. The academic circle started the discussion on the marketization reform of the medical care and health system. One type of view believed that the commercialization and marketization of the medical care and health system violated in its orientation the basic principles of the development of medical care and health undertakings so that the accessibility of medical care and health service was greatly

⁴²Zheng (2003), Wang (2005).

⁴³Liu (2001).

⁴⁴Wang (2000).

⁴⁵Yang (2003).

lowered.⁴⁶ Other scholars believed that marketization and commercialization were not the causes of the failure of reform. The government's monopolization of medical care resources and the hospitals' monopolization of patients in the past were the radical causes.⁴⁷ China's medical care reform was unsuccessful because the government did not fully shoulder its responsibilities, medical care insurance system was not fully established, or, it could be said, the subsidization system for low-income group from state fiscal budget was not established. And these were the source of the issue.⁴⁸

The second aspect was the maintenance or removal of personal accounts. The view that supported the maintenance of personal accounts mainly focused on the points of controlling too fast growth of medical care expenses, buffering payment risks in the fund under centralized planning and collection, and increasing the medical care funds disposable for participants in the insurance.⁴⁹ The view that opposed personal accounts mainly focused on the following several aspects: Personal accounts did not conform to the principle of "risks under the law of large numbers" in medical care insurance. Personal accounts caused low efficiency in management. The "private" attribute of the accounts would indulge the emergence of the moral hazard of "payment for third party".⁵⁰

III. Policy Achievements and Theoretical Developments

(I) Making Personal Accounts Real and Improving Retirement Benefits when Improving Pension Insurance System

The CPC Central Committee and the State Council attached great importance to many issues present in pension insurance system and promulgated a series of documents and adopted a series of measures to improve China's social security system. These documents and measures mainly included those in the following several aspects: First, people streamlined the relations between regions and departments and cancelled industrial management. The measure was mainly embodied as the *Notice on the Issues about Implementing the Centralized Planning and Collection at Provincial Level of the Basic Pension Insurance of Enterprise Employees and Transferring Industrial Centralizing Planning and Collection to Local Management* published by the State Council in 1998. Second, people established collection and payment system and expanded coverage. By 2005, the coverage of pension insurance system further expanded to flexible employment personnel who worked on non-full-time, temporary and flexible working bases. Third, people built personal accounts into a real system

⁴⁶Research Group of the Development Research Center of the State Council, *Evaluation and Suggestions on China's Medical Care and Health System Reform*, 2005.

⁴⁷Song (2006).

⁴⁸"Views of Several Experts on Medical Care Reform", Speeches at the Colloquium on China's Macroscopic Economy and Trend of Reform in 2006, March 2006.

⁴⁹Wang (2005), Fu (2005).

⁵⁰Research Group of the Study of China's Social Security System (2000), Zheng (2007b), Chapter 8; Zheng (2007a).

and expanded the range of pilot projects. This indicated the determination of the Chinese government to build personal accounts into a real system and realize partial-funded system. In this way, people could further clearly define the responsibilities undertaken by state and individual so as to give social collection and personal account system the substance that matched its name and promote the virtuous development of pension insurance system. Fourth, people reduced the proportion of contribution of personal account and adjust the relationship between social collection and personal account. The proportion of contribution of social collection account was raised from 17 to 20% while that of personal account from 11 to 8%. Besides, the connection between pension and payment was raised. Fifth, people established the trust DC-type enterprise annuity system and clearly defined its status as the second pillar in social security.

In retrospect, people found that relevant policies and regulations in social security system in the decade had hidden defects that resulted in the emergence of issues in the future although they did make great achievement. The government adopted the financial management model of separated accounts for “social collection and personal account” but it did not radically resolve the issues related to employ accounts. Besides, people started with the system design created from resolving the issues left in historical conditions within the system. This resulted in disproportionately heavy burdens of one generation so that the contribution payment observation rate was unsatisfactory in the operation of the pension insurance system when people were faced with a personal contribution payment proportion of 28%. Moreover, although people strengthened the connection with income in pension insurance system, the returns of the part from social collection was also unsatisfactory. And people could not guarantee that pension insurance fund could achieve satisfactory rate of return under the premise of the current standard of fund management and the maturity of the capital market.⁵¹ All these caused the problems of the chaotic situation related to the target replacement rate of pension and the pension insurance participants selecting to retire earlier or withdraw from the insurance.

(II) Initially Establishing the Medical Care Security System That Covered the City and the Countryside

Upon the beginning of the 21st century, the reform and constant exploration in the medical care insurance system became the main theme of this historical period.

The first area was the reform of the medical care and health system. It was pointed out in the *Report of the State Council on the Situation in Implementing Urban and Rural Medical Care and Health System Reform and Strengthening Food and Drug Security Supervision* (2007) that the general goal in deepening medical care and health reform was to build a basic medical care and health system that covered the residents in both the city and the countryside. And first of all, people needed to

⁵¹ At the 3rd Annual Meeting of the China Social Security Forum held in 1998, Yu Xiaoming, deputy auditor general of the National Audit Office of the People’s Republic of China, indicated that the annual rates of return of the five kinds of social security funds were less than 2%. <http://finance.sina.com.cn/g/20081107/02402502198.shtml>.

strengthen the responsibilities and investments of the government and establish the leading role of the government in providing public health and basic medical care service.

The second area was the exploration in multileveled urban medical care security system. The first thing included in the area was to expand the coverage of medical care insurance. From 1999 to 2006, medical care insurance was gradually extended to the groups such as flexible employment personnel who worked on non-full-time, temporary and flexible working bases and migrant workers.⁵² The second thing was to implement medical care aid system. In July 2005, the General Office of the State Council published the *Opinion on the Work of the Pilot Projects in Establishing Urban Medical Care Aid System*. The general goal of the work was to establish nationwide an urban medical care aid system with institutionalized management and standardized operation. The third thing was to develop supplementary medical care insurance system. In 1998, the State Council pointed out specifically in the *Decision on Building Basic Medical Care Insurance System for Urban Employees* that “the expenses in medical care insurance that exceeds maximum payment limit can be acquired by means of commercial medical care insurance and other channels”.

The third area was the establishment of urban resident medical care insurance system. In 2007, the State Council promulgated the *Guiding Opinions on Carrying Out the Pilot Projects on the Basic Medical Care Insurance for Urban Residents*. It was pointed out that urban resident basic medical care insurance should be focused on guaranteeing the payment of the medical care expenses on major diseases of the participating residents in out- and in-patient medical service. And the regions with proper conditions might gradually implement pilot projects on the centralized social planning and collection for the payment of the expenses on out-patient medical care service. By the end of 2007, the number of people who participated in urban resident medical care insurance reached 42.91 million.⁵³

The fourth area was the establishment of new-type rural cooperative medical care insurance. Traditional rural cooperative medical care system gradually declined in the reform of the economic system. In 2002, the coverage of rural cooperative medical care in China reached a low of 9.5%.⁵⁴ In 2003, the General Office of the State Council transmitted the *Opinions on Building the New-Type Rural Cooperative Medical Care System*. This signified that China’s rural cooperative medical care

⁵²These measures included that employees in the railway system were included in the social medical care insurance system in 1999 and that flexible employment personnel who worked on non-full-time, temporary and flexible working bases, employees in enterprises under mixed ownership system and non-public ownership economic organizations, and also personnel who migrated from the countryside into the city to work were included in the coverage of medical care insurance in 2003. In May 2006, the Ministry of Labor and Social Security published the *Notice on Taking Action to Turn the Work in the Participation of Migrant Workers in Medical Care Insurance into the Expansion of Coverage* and proposed to comprehensively push forward the work in the participation of migrant workers in medical care insurance.

⁵³Statistical Database of INFOBANK.CN.

⁵⁴Zou (2008).

insurance system reached a new development period. By the end of 2007, the number of peasants who participated in the new insurance nationwide reached 726 million and the participation rate exceeded 86%.⁵⁵

(III) Building Urban Employee Unemployment Insurance System

In 1997, state-owned enterprise reform entered the stage of tackling and cracking key difficulties and laid-off workers and unemployment became the most prominent problem that people encountered in the reform at the time. Under such background, the State Council promulgated in 1999 *Unemployment Insurance Regulations*, which officially renamed “employment-pending insurance” as “unemployment insurance”. This signified that the development of unemployment insurance regulation entered a new period. In the implementation of the *Unemployment Insurance Regulations*, the circle of theoretical study discussed the issues present in the process as new ones had emerged.⁵⁶ These included that the scope of insurance needed to be further expanded, such as to employees in township and town enterprises and migrant workers, that unemployment insurance funds were hard to collect and there was the problem of misappropriation and unwarranted diversion, and that the examination and review of the qualifications for the application and reception of unemployment insurance was not strict enough. In addition, the circle of theoretical study also started to pay attention to the issue of “unregistered employment” and unemployment statistical index system.

(IV) Improving Urban and Rural Resident Subsistence Allowance System

In 1999, the State Council promulgated the *Regulations on Urban Residents Subsistence Allowance*, which signified the official establishment of the subsistence allowance system. Upon the start of the 21st century, China’s urban subsistence allowance system entered the stage of development and consolidation. Breakthroughs were achieved in its development. The coverage of the system was gradually enlarged. The population covered by the allowance rose from 2.659 million in 1999 to 22.721 million in 2007.⁵⁷ The spending on allowance funds increased greatly. The payment of subsistence allowance nationwide increased from RMB 4.574 billion yuan in 2001 to RMB 24.101 billion yuan in 2006.⁵⁸ The allowance played an important role in alleviating poverty and guaranteeing the basic life rights and interests of urban residents. While certain achievements were made in the system, there were also a series of problems present in the process of its implementation. For example, the standard of subsistence allowance was low so that it could not realize effective guarantee. The structure of the system was too simple so that the existence of some special cases was overlooked. The system failed to effectively distinguish between people eligible

⁵⁵Chen and Wang (2010).

⁵⁶Feng and Zhao (2000), Liu and He (2004), Ding (2005).

⁵⁷The website of the Ministry of Civil Affairs of the People’s Republic of China, *2008 Statistical Report on the Development of Civil Affairs Undertakings*.

⁵⁸Statistical Database of INFOBANK.CN.

to subsistence allowance and those not. And it was not connected with other social security policies in a good way.⁵⁹

While implementing the urban resident subsistence allowance system, China also started the exploration on rural subsistence allowance system. In order to practically carry out and implement the spirit of the Sixth Plenary Session of the Sixteenth CPC Central Committee and practically resolve the life difficulty of rural impoverished population, the State Council decided that rural subsistence allowance system be established nationwide in 2007. By the end of 2007, 35.663 million people in 16.085 million households had received rural subsistence allowance, showing a year-on-year increase of 19.732 million. RMB 10.91 billion yuan rural subsistence allowance funds were issued in the whole year in 2007 and per capita allowance subsidies amounted to RMB 38.8 yuan per month, showing a year-on-year increase of 12.5%.⁶⁰

4 Constructing Harmonious Society and Building Social Security System: Important Theoretical Breakthroughs in the New Period (2007–The Present)

As the system was basically established and fixed, the development of China's social security undertakings entered a new stage. In the new period, the country not only pursued economic development but also tried to accomplish more than satisfying basic life needs in the constructions related to people's livelihood. Improving the living quality of the people and paying attention to the future development of individual under the guidance of the concept of people-orientedness became the goal that China pursued in the new period. Establishing a social security system that covered the entire people was indispensable to realizing such a goal. And the complete proposal of the goal of constructing a socialist harmonious society and the outlook of scientific development provided theoretical basis and development opportunity for building social security system.

I. Guiding Thought and Policy Achievement for Building China's Social Security System in the New Period

(I) Improving Social Security—An Important Means for Building a Harmonious Society

Examined from the construction and study on social security system, there were two highlights in the communique of the Sixth Plenary Session of the Sixteenth CPC Central Committee:

First, social security enjoyed more prominent status. Firstly, improving social security was an important area in promoting social construction. If people

⁵⁹For relevant references, see Mao and Liu (2007), Kang (2007), Yang (2008), Cheng (2008).

⁶⁰The website of the Ministry of Civil Affairs of the People's Republic of China, *2007 Statistical Report on the Development of Civil Affairs Undertakings*.

only stressed on economic construction and omitted social construction, “Latin-Americanization” and “social diseases” would emerge and spread so that these problems would cause great negative influence on economic construction. Secondly, social security system was a specific manifestation of the development of social undertakings. If social security was incomplete and social undertakings were undeveloped, there was no way to realize social harmony. Thirdly, social security was a means and purpose to promote social fairness and justice. Social security was an important means to promote social fairness and justice for socialism with Chinese characteristics.

Second, people drew the blueprint for the prospects of social security by 2020. The communique of the Sixth Plenary Session of the Sixteenth CPC Central Committee officially drew the blueprint and prospect for social security in China: “to basically complete establishing a social security system that covers urban and rural residents”. It was the first time that a plenary session of the CPC Central Committee specifically proposed the prospective goal of improving social security system by 2020. It was also the first time that it was specifically pointed out at a plenary session of the CPC Central Committee that China wanted to basically complete establishing a social security system that included both the city and the countryside in its coverage. This was an important strategic arrangement for improving the construction of social security system.⁶¹

(II) Building a Social Security System That Covered Urban and Rural Residents—With the Outlook of Scientific Development as Guidance

It was pointed out in the report of the Seventeenth CPC National Congress with the outlook of scientific development as its theme that “social security is an important guarantee of social stability”. This was the highest evaluation on improving social security system. Building a social security system that covered urban and rural residents was an important guarantee for constructing a harmonious society. A society without a complete social security system that covered both the city and the countryside was definitely not a harmonious society. A social security system with narrow coverage or a fragmented system that separated the city and the countryside was unfavorable to the construction of harmonious society. It was even equal to shovel the difficulties at present into the future.

In addition to pointing out the general direction of the development of social security system, the report of the Seventeenth CPC National Congress also summarized the specific targets of the development of the system and its development road. For example, the proposal of “taking social insurance, social aid and social welfare as the basis” in the report was in fact a description of the blueprint of the social security system with Chinese characteristics. The proposal of “taking basic pension, basic medical care and subsistence allowance systems as priorities” in the report, in

⁶¹The main references of the contents above included Zheng Bingwen, “Improving Social Security: An Important Means to Building a Harmonious Society”, *China Securities Journal*, October 17, 2006, p. A04. “Social Security: New Requirements in Building a Harmonious Society”, *Chinese Academy of Social Sciences Semiweekly*, November 2, 2006, p. 1.

fact, pointed out the three important areas that urgently needed to be improved in the construction of social security system at present. The discussion on “comprehensively pushing forward the construction of urban employee basic medical care insurance system, urban resident basic medical care insurance system and new-type rural cooperative medical care system”, in fact, was the important judgment and basic summarization on the general pattern of the medical care insurance system. It was also the important guidance for China to build a medical care security system with the centralized social planning and collection for both the city and the countryside.⁶²

(III) Achievements Made in China’s Social Security System in China in the New Period

Under the guidance of the “people-oriented” principle and the outlook of scientific development, China made great achievements in social security system in the new period, which included those in the following several aspects:

First, the *Social Insurance Law* was promulgated. As a legal pillar in China’s legal system for social security, the law embodied the following several legislative principles: Firstly, the people could share the fruits of reform and development. The goal of this area was to achieve the effect that there was no absence in system, no omission in coverage and no seam in connection so that the whole people could have basic guarantee and become free of concerns in pension and medical care. Secondly, there were the combination between fairness and efficiency and the correspondence between right and obligation. As the social security system led by the government, social insurance needed, first of all, to embody the principle of fairness and prevent and eliminate polarization. But at the same time, it should also embody the principles of incentive and guidance and adhere to the mutual adaptation between right and obligation. Thirdly, people should establish relevant framework and advance progressively in the area. The *Social Insurance Law* was still in the process of development. Its present legislative work presented some flexible or right-vesting provisions so as to leave room for improving systems and innovating mechanism in the future.⁶³

Second, the coverage of various kinds of social insurance systems continued to expand and their number of participants and sizes of funds also grew constantly. By the end of September 2010, the covered populations of China’s urban employee pension insurance and urban resident medical care, unemployment, employment injury and maternity insurances reached respectively 250 million, 420 million, 130 million, 160 million and 120 million. These figures all exceeded the targets specified in the Eleventh Five Year Plan.⁶⁴ In the area of the receipts and payments of funds,

⁶²The main reference of the content above was Zheng Bingwen, “Giving Weight to Social Construction and Endeavoring to Improve People’s Livelihood—Understandings from Studying the Report of the Seventeenth CPC National Congress”, *Chinese Academy of Social Sciences Semiweekly*, October 23, 2007, p. 3.

⁶³*China Daily*, “Endeavoring to Guarantee and Improving People’s Livelihood—Hu Xiaoyi’s Detailed Interpretation of the *Social Insurance Law*”, http://www.chinadaily.com.cn/hqgj/jryw/2010-11-24/content_1271940.html.

⁶⁴Yin Weimin, “Completing the Social Security System That Covered Urban and Rural Residents”, see the website of the Ministry of Human Resources and Social Security,

the receipts of the funds of five kinds of social insurances, not including rural social insurance, in the whole year totaled 1.6 trillion RMB at the end of 2009, showing an increase of 242 billion RMB and a growth rate of 17.7% in comparison with the figure in 2008. The payments of funds totaled 1.2 trillion RMB, showing an increase of 237.8 billion RMB and a growth rate of 24.0% in comparison with the last year. Moreover, the thirteen provinces nationwide in the pilot projects to build the personal accounts of enterprise employee basic pension insurance into a real system accumulated a total of 156.9 billion RMB funds in the personal accounts of basic pension insurance by the end of 2009.⁶⁵

Third, the pilot projects on new-type rural pension insurance were pushed forward quickly. In September 2009, the State Council printed and transmitted the *Guiding Opinions on Carrying out the Pilot Projects on New-Type Rural Social Pension Insurance* and officially launched the pilot projects on the insurance. The coverage of the first batch of the pilot projects reached 11.8%. The insurance was another important preferential policy for the peasants implemented by the central authorities in addition to the cancellation of agricultural tax and the implementation of agricultural direct subsidy and new-type agricultural cooperative medical care system. It was also another important breakthrough in China's efforts to establish the social security system that covered urban and rural residents. By the end of 2009, the population of the participants of rural pension insurance nationwide amounted to 86.91 million, showing an increase of 30.96 million in comparison with the figure at the end of 2008. A total of 15.56 million peasants received their pensions in the whole year. The total payment of pension amounted to 7.6 billion RMB, increasing by 33.8% in comparison with the last year. The accumulative balance of funds in rural pension insurance reached 68.1 billion RMB at the end of the year.⁶⁶

II. Several Discussions on the Issue of Social Security System in the New Period

When reflecting on China's social security system, people would find that there was much work to do in the new period as China was still far from the goal of constructing "the social security system that covered urban and rural residents". At present, China's social security system was still incomplete and it still had many issues. For example, the social security of migrant workers became a problem. How should people determine the guiding thought on medical care reform? What was the road that people should take in the pension insurance reform of government organs and institutional units? What should people do in China's social security system to respond to global financial crisis? Were there opportunities or challenges in it, and so on? All these questions were worth thinking over. And in these years, people never stopped discussing these questions.

December 17, 2010, http://www.mohrss.gov.cn/Desktop.aspx?path=mohrss/mohrss/InfoView&gid=204ea610-2845-40d2-8e68-394a7d68ac3a&tid=Cms_Info.

⁶⁵The website of the Ministry of Human Resources and Social Security, "2009 Statistical Bulletin on the Development of Human Resources and Social Security Undertakings", http://wl.mohrss.gov.cn/gb/zwxx/2010-05/21/content_382330.htm.

⁶⁶Ibid.

(I) The Choices in Migrant Worker Social Security System—Fragmentation or Unification

The views on the issue of the social security of migrant workers could be summarized into those of the “unification sect” and those of the “fragmentation sect”. The “fragmentation sect” believed that the present urban basic social security system was not suitable to migrant workers. So they advocated that a separate system be established for these workers. This was a typical “fragmentized” pension insurance system. The “unification sect” advocated another way in which people should reconstruct the present social pension insurance system. They should break the boundaries between the city and the countryside and between various occupations, went beyond the confines of the household registration system, and built a single basic pension insurance system on the basis of the identity of citizenship. Namely, one single system and one single set of rules should be used in the whole country. This was the “generally-unified” basic pension insurance system. Some scholars believed that the separate system proposed in the view of the “fragmentation sect” had many defects. For example, creating a separate system for peasant workers was to legalize the poverty of migrant workers. This would result in the distortion of labor market nationwide. Different benefits would cause the unrealistic comparison between different groups so that the society would become unharmonious. Therefore, establishing a separate pension insurance system for migrant workers was a kind of “short-sighted” behavior.⁶⁷

The Measures for Migrant Workers’ Participation in Basic Pension Insurance (Draft for Comment) promulgated in February 2009 was a transitional policy. It was very obvious that the Measures had some problems. For example, low fund base, low fund contribution requirement, and low contribution density would definitely result in the retirement benefit standard of migrant workers far lower than average social pension standard. But it resolved the most urgent portability issue of the insurance. This indicated that the decision makers eventually dropped the idea of creating separate pension insurance for migrant workers, which was great progress that made China’s social security advance a step forward in the direction of general unification.

(II) Pension Insurance Reform in Government Organs and Institutional Units—Three Linkages

As an important component of administrative management system reform and social security system reform, the pilot projects on institutional unit pension reform attracted extensive attention nationwide after the provinces and municipalities participating in the projects were determined. In fact, the plan for the pilot projects of institutional unit pension reform was determined in January 2008. But the projects met huge resistance that people had never seen before. There were two reasons for this: First, people panicked that pension was expected to lower. If the pension insurance system of institutional units were reformed to form resemblance to that of the enterprises, the

⁶⁷Zhang (2008).

pension for institutional units would undoubtedly lower under the circumstance that there was no other supplementary pension. Second, the reform was a “fragmentized” reform among institutional units. The main entities involved in the reform were medical care and health sector and colleges and universities. Such pilot projects of a “fragmentized” reform would certainly result in unrealistic comparison and cause panic out of human reasons. It would definitely make it hard for people to push forward the reform. This obviously increased the political cost of the reform and prolonged the historical process of the reform out of human reasons.

The first author of this chapter once pointed out⁶⁸ that the key to whether the reform could succeed that institutional units participated in basic pension insurance reform laid in “Three Linkages” from the long-term and global angle. The first linkage referred to that the reforms related to institutional units and public servants should be implemented together so as to avoid mutual unrealistic comparison and mutual impediment. The second linkage was that the three categories of institutional units should implement the reform together.⁶⁹ They should not be divided into different grades in pension insurance. The third linkage was to implement synchronously the reform in institutional units and the establishment of occupational annuity so as to make up for the part lost in lowering after people participated in the reform. This aimed to provide proper expectation, reduce resistance in reform, maintain living standard and keep it from lowering, and give all the people a “pill of reassurance”.

The lesson from the “fragmentized” system in France indicated that multiple retirement systems would definitely cause unrealistic comparison. Reform would certainly encounter objection. The longer the system operated, the larger the gaps became, the larger welfare rigidity became, and the more difficult the reform was. Reform could even trigger social turbulence. Moreover, many fragments already formed in China’s pension insurance system because of its lower standard of centralized planning. If the fragments of institutional units and public servants were added to it, China’s pension system would become irremediable because of the accumulation of serious problems. It would face the difficulty of unsustainability in the long term. Radically speaking, the people paid more attention to the fairness of pension insurance system and also to whether general unification could be realized in the “fragmentized” system. Such view believed that it was not advisable to build separate pension insurance systems for government organs and institutional units in the process of building the social security system that covered the city and the countryside. This was also consistent with the requirements in building a harmonious society.

⁶⁸See relevant articles of Zheng Bingwen, such as “The Key in the Pension Reform of Institutional Units Lies in Three ‘Linkages’”, *China Securities Journal*, February 23, 2009, p. A12; “The Legislation of the *Social Security Law* Faces Three Major Difficulties”, *Shanghai Securities News*, May 27, 2009, p. B06.

⁶⁹China’s institutional units could be divided into three major categories. The first category was those that fulfilled administrative functions. The second was those that engaged in public interests activities. And the third was those that engaged in profitable operation.

(III) New Medical Care Reform—Advancing toward the Medical Care for the Whole People

The Opinions of the CPC Central Committee and the State Council on Deepening the Reform of Medical Care and Health System published in 2009 stipulated on China's medical care insurance system that people should speed up building and improving a multileveled medical care insurance system that covered both the city and the countryside, in which basic medical care security dominated and various other forms of supplementary medical care insurance and commercial health insurance supplemented. In this system, basic medical care security system included urban employee basic medical care insurance, urban resident basic medical care insurance, new-type rural cooperative medical care and urban, and rural medical care aid system. When examined from the coverages of various systems, the new medical care plan in fact established a medical care system for the whole people.

After the new medical care reform plan was promulgated, the circle of theoretical study interpreted the whole people medical care system from the following several aspects:

First, the whole people medical care was the breakthrough point of China's medical care system reform. It could radically change the absence of the access to medical treatment for diseases. Under the whole people medical care system, all the residents in the city and the countryside were included in the basic medical care security system. The residents could spread risks in a large extent and achieve the goal of "finding medical treatment for diseases".⁷⁰

Second, there was the issue of selecting China's medical care security model under the whole people medical care security system. The scholars believed that there were two choices for the whole people medical care security dominated by the government: One was free public medical care and the other was mandatory medical care insurance. Naturally, the fairness of the free public medical care was unquestionable. But such system caused larger pressure to fiscal budget. So it was unfeasible to implement the model of free public medical service under the constraints of the current fiscal system and fiscal resources.⁷¹ The only way was that the state continued to play the role of insurer and realized the whole people medical care through adjustments in the current system architecture.

Third, there was the issue whether the whole people medical care had sufficient funds. Some scholar estimated the receipts and payments of medical care insurance funds under the whole people medical care system and believed that the urban and rural medical care insurance institutions could hopefully raise at least RMB 565 billion annually from 2010. The revenue of medical treatment in medical care institutions was about RMB 500 billion at present. The medical care insurance system

⁷⁰Gu Xin, "The Whole People Medical Care Is the Breakthrough Point of Medical Care Reform", http://news.xinhuanet.com/politics/2008-02/14/con-tent_7602104. Wang Shan, "The Whole People Medical Care Will Change the Absence of Access to Medical Care for Diseases", http://old.jfdaily.com/news/hot/200904/t20090407_595228.htm.

⁷¹Gu Xin, "The Whole People Medical Care Is the Breakthrough Point of Medical Care Reform", http://news.xinhuanet.com/politics/2008-02/14/con-tent_7602104_1.htm.

could afford the residents' expenses on medical treatment and thus no funding gap would occur.⁷²

(IV) The Solution to the Reform of Social Collection and Personal Account System—"Hybrid" Combination of Social Collection and Personal Account

The combination of social collection and personal account was a kind of partial-funded system. From its establishment until now, the system had operated in China for 12 years. People did make many achievements with it. But now the implementation of the combination of social collection and personal accounts met more and more challenges among the people. The first author of this chapter once pointed out⁷³ that one of the most important signs of the combination of social collection and personal account in partial-funded system was to make personal accounts a real system. But in specific operation, personal accounts were used as "empty accounts" in China. In 2001, people started the pilot projects in Liaoning on making personal accounts a real system and downsized the contribution proportion from 11% to 8%. Three issues were identified in pilot projects: First, current payment under social collection faced funding gap. Fiscal subsidies between one to two billion RMB were needed each year. Second, the funds accumulated in the accounts exceeded 50 billion RMB at the end of 2008. Should people give fiscal subsidies forever or approve of the application of Liaoning province on borrowing the funds in the accounts to make up for the gap in social collection? Once people approved of using the funds in the accounts, it meant that the pilot projects on making personal accounts a real system ended up in complete abortion and also that the combination between social collection and personal account only existed in form. Third, how to preserve and increase the value of the funds in the accounts became an important issue that the decision makers needed to consider as the funds in personal accounts were to be made into a real system. In addition to the issues present in the system of social collection and personal account itself, the lowering trend of the standard of pension benefits were unable to be contained and made up for within the pension system itself. From 2005, the central government raised pension for five consecutive years. This was because the gap of the standard of pension with average social wage and the pension standard of public servants kept enlarging. The calculation formulas in the social insurance system could do nothing to mend it.

When issues occurred to both the mode of financing and the formula of payment to a pension system, it meant that the system had reasons to make necessary reform as it failed to the extent that reform was inevitable. Nominal Defined Contribution system was an important system solution that people could choose at present. People could get out of the dilemma in making personal accounts a real system with it. It could

⁷²Gu Xin, "Three New Major Challenges in New Medical Care Reform", http://www.yewb.com/news/2009-04/13/content_2107040.htm.

⁷³Zheng Bingwen, "Translator's Epilogue: New Thought on the Reform of 'Nominal Defined Contribution' System in China's Social Security—"Hybrid" Combination of Social Collection and Personal Account", *Theory and Practice of Nominal Defined Contribution System—New Thought on Social Security Reform*, China Labor and Social Security Publishing House, 2009.

also help to drop the “external intervention” in adjusting benefits standard for many consecutive years. It could also solve many issues such as low standard centralized planning and collection, seriously unreasonable investment system, lower rate of return, and fund supervision difficulty caused by fragmented local separation.⁷⁴

(V) The Revelation That the Global Financial Crisis Brought to China’s Social Security System—Opportunity to Challenge

The global financial crisis triggered by the subprime mortgage crisis in the USA undoubtedly delivered huge impact on China’s real economy and, particularly, its exported-oriented manufacturing industry. It was pointed out at the Central Economic Working Conference in December 2008 that people should focus on securing economic growth. They should take expanding domestic demand as the radical approach to secure economic growth and accelerating the transformation of development mode and adjusting structure as the main direction of work in ensuring economic growth. When considered in the long term, an important system guarantee for stimulating domestic demand was accelerating the construction of social security system. Domestic demand would not start to grow without the safety net of social security system. Insufficient domestic demand was always the Sword of Damocles over the radical transformation of the mode of economic growth in China.

There were three reasons why China’s social security system could not make greater contribution to stimulating domestic demand. First, its coverage was too small. China’s social security system was created as an auxiliary system to economic system reform. People did not make comprehensive consideration when it was established in the beginning. Only employees in state-owned enterprises were included in the system while the extensive communities of rural residents and migrant workers were excluded. Besides, the current system had poor portability. So under such a circumstance, it was very hard to provide social security to all the people that should enjoy such welfare.

Second, the benefits of the basic social insurance in urban enterprises were not linked to the growth rate of average social wages. The income replacement rate of such retirement benefits decreased year by year and their gap with the pension of government organs and institutional units increased gradually so that the central government had to raise pension each year. Multiple retirement systems resulted in poor benefits, unrealistic comparison, discord between various units, fiscal risks, weakening consumer confidence of the people, and lowering public trust of social security system.

Third, the social security system was fragmented. At present, the spreading and expansion of China’s social security system was carried out in a fragmented way.

⁷⁴The main reference of this part was Zheng Bingwen, “Translator’s Epilogue: New Thought on the Reform of ‘Nominal Defined Contribution’ System in China’s Social Security—‘Hybrid’ Combination of Social Collection and Personal Account”, *Theory and Practice of Nominal Defined Contribution System—New Thought on Social Security Reform*, China Labor and Social Security Publishing House, 2009.

The so-called fragmented way of expansion meant that the existing social security system was unsuitable for the groups other than those in state-owned enterprises to participate in so that separate social security systems were established for different groups. Such systems were unfavorable for forming a general labor market nationwide. It could easily cause occupational segregation and weaken the consumption ability of the participants at the current period. It was also unfavorable to improve the general risk pooling ability of social security funds and bring into play the law of large numbers. To establish a unified national social security system was the requirement in the long-term interests of the society in the future. It was also a substantial requirement in promoting economic growth and defending external economic fluctuation and impact.

In order to respond to financial crisis, people should promote reforms in the following several aspects in social security system: First, they should increase the coverage of social security. The target groups in expanding coverage included three kinds of people: urban flexible employment personnel who worked on non-full-time, temporary and flexible working bases, migrant workers and peasants engaging in agricultural work in the countryside. Second, they should raise the standard of basic social insurance properly and timely and lower the standard of fund contribution at the same time. Third, the standard of some non-contribution welfare items should be raised properly, such as the social aid targeting subsistence allowance receivers in China at present. Fourth, they should establish some new welfare items. An urgent one at present was the pension subsidy system to be established nationwide, also known as “national annuity” or “social pension”. For China, improving social security system and speeding up the transformation of the mode of economic growth were both the result of responding to the changes in external environment and the inexorable demand of its internal development. It was also a very urgent strategic task given by the history. As long as people could achieve consensus, gather forces and resources nationwide, and form a combined force through coordinated action, they could take advantage of the current situation and establish a “win-win” social security system which could “guarantee both harmony and growth”.⁷⁵

⁷⁵The main references of this part are the following articles written by Zheng Bingwen: “Expanding the Coverage of Social Security System: International Experiences and Lessons”, *Red Flag Papers*, Issue 8, 2009; “Social Security Reform under Financial Crisis”, *Chinese Social Sciences Today*, June 16, 2009, p. 3; “Financial Crisis Resulted in the Constant Deepening of the Reform of Social Security System”, *China Securities Journal*, July 6, 2009, p. A14; “Social Security: Anti-Crisis Measures and Anti-Cyclical Means”, *China Labor and Social Security News*, July 10, 2009, p. 3; “Financial Crisis, Transformation of Growth Mode and Establishment of Unified Social Security System”, a speech at the Symposium of “Reform and Opening Up and Social Security” held in commemoration of the 10th anniversary of the establishment of the Zhejiang Provincial (and Zhejiang University) Social Security Development Research Center on December 18, 2008, see Zheng Bingwen’s personal homepage, <http://ilias.cass.cn/zhengbingwen>.

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Chapter 25

The Deepening and Development of the Theory on Opening Up to the Outside World in China after Its Accession to the WTO in 2000



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In December 2001, China officially acceded to the World Trade Organization. This was a major event of historic meaning in China's modernization process. It signified that China's opening up to the outside world entered a new stage.¹ Since its accession to the WTO, China successfully came in line with the multilateral economic and trade regime of the world and relevant international rules and practices. It initially established socialist market economic system, successfully defended international financial crisis, and continued to retain the sustained and rapid development of national economy. And it basically completed the transformations from the opening up in limited areas and scopes to all-round, multileveled and wide-ranging opening up, from stressing on policy-related opening up to system-related opening up, and from unilateral opening up to multilateral and interactive opening up. Moreover, China also vigorously pushed forward the transformations from domestic economic equilibrium to comprehensive balance between internal and external economies, from the participant and implementer of international rules to the legislator and formulator of international rules, and from emphasizing the attribute of a developing country to both emphasizing the status of a developing country to attaching importance to major power responsibility. In 2010, China exceeded Japan and ranked the second place in terms of economic aggregate. Its foreign trade volume exceeded USD 2.9 trillion and China kept the ranking of the third place in the world and became a true world trade power. Practice proved that China's opening up to the outside world in the decade after its accession to the WTO established a successful paradigm for emerging economies on the globe to exert their late-comer advantage, merge into globally open economic system, and take internationally open development road. It

¹Wei (2002).

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was also one of the most distinctive and important signs of the China model and the China road.

Within the decade, the workers on economic theories carried out abundant discussions and heated debates, which were not limited to any particular area or field, centering round one after another hotspot, focal and difficult issues. These activities promoted the attainment of new progress and achievements in the theory on opening up to the outside world in China.

1 New Progress in the Theory on Foreign Trade

I. The Discussion on Transforming the Growth Mode of Foreign Trade and Its Development

Within over twenty years after the beginning of the reform and opening up, the growth mode of foreign trade which tended to form advantages through quantitative expansion, labor intensiveness and low price made huge contribution to China's high-speed economic growth. After its accession to the WTO, the defect of such growth mode became strongly prominent as China gradually faced increasing foreign trade friction, too large foreign trade surplus, too much resource consumption, aggravating environment pressure, low economic benefits, and increasingly weak internal demand. Because of this situation, the circle of theoretical study carried out heated discussion centering round the transformation of the growth mode of foreign trade during the time of formulating the Eleventh Five Year Plan of the state four years after China's accession to the WTO.

Before the formulation of the Eleventh Five Year Plan of the state, the circle of theoretical study tended more to discuss the necessity of transforming the growth mode of foreign trade. People had different understandings on transforming the growth mode of foreign trade. Some scholars believed that the growth mode of foreign trade could also be divided between extensive and intensive types and also between intension and extension types, just like the growth mode of economy. Chai (2004) believed that the defects became increasingly noticeable in the growth mode of foreign trade that purely relied on quantitative scale and price advantage.² Wen (2005) proposed that the growth mode of foreign trade were contained in the growth mode of economy. The transformation of the growth mode of economy naturally included the transformation of the growth mode of foreign trade. The two were closely connected and mutually promotive.³

After the transformation of the growth mode of foreign trade was written into the Eleventh Five Year Plan of the state, domestic scholars turned the focus of their discussion to the basic approach, basic goal and operational strategy of the transformation of the growth mode of China's foreign trade. One type of view on the basic

²Chai (2004).

³Wen (2005).

approach of transforming the growth mode of foreign trade advocated “leap-forward transformation”. Namely, China should transform the growth mode of foreign trade as quickly as possible and thoroughly discard extensive growth mode. Another type of view advocated “progressive transformation”. Namely, the transformation of the growth mode of foreign trade needed to undergo a long and arduous process. Pei (2005) believed that the transformation of the growth mode of foreign trade in China was a long-term process.⁴ In this process, people needed to retain the international competitiveness of China’s low- and medium-end products and relevant production processes and retain the quantitative growth of foreign trade. Moreover, they needed to improve the international competitiveness of medium- and high-end process and relevant production processes so as to achieve the goal of improving trade structure and bettering trade quality. Under the premise of advocating “progressive transformation”, people had different views on the priorities and breakthrough points of the growth mode of foreign trade.

As far as the basic goal of the transformation of the growth mode of foreign trade was concerned, the circle of theoretical study generally believed that people needed to achieve the objectives of technological upgrading, quality improvement, structure optimization and increase of benefits. Jiang (2006) believed that the growth mode of China’s foreign trade would experience a “turning point” change in which the structure of exported commodity would become more optimized.⁵ Lu (2006) believed that people need to implement the transformation from quantitative increase to quality improvement and change “Made in China” into “Created in China”.⁶ Long Guoqiang believed that the transformation of the growth mode of foreign trade meant to transform from a quantitative growth mode to a qualitative one and from an extensive one to a benefit-oriented one and that it was mainly intended to elevate China’s status in global industrial value chain.⁷ Jian Xinhua believed that the new growth mode of foreign trade should be a sustainable one with the optimization of the structure of imported and exported commodity and the diversification of the market, in which China mainly relied on independent innovation and self-owned brand, in which China achieved prosperity in trade with science and technology and gained advantage with quality, and in which its products had reasonable structure, high degree of working, large added value and high benefits.⁸

As to how to realize the transformation of the growth mode of China’s foreign trade, Liu Wei and Huang Guitian believed that people needed to first improve the ability of innovation and promote the transformation of the growth mode of foreign trade with the transformation of the growth mode of economy.⁹ Gao (2006) believed that the key to the transformation laid in encouraging technological innovation and

⁴Pei (2005).

⁵Jiang (2006).

⁶Lu (2006).

⁷Long (2007b).

⁸Jian (2007).

⁹Liu and Huang (2006).

product upgrading and vigorously developing service industry.¹⁰ Liu (2006) advocated that people should adopt the four major measures of promoting system reform, optimizing export structure, improving import quality and pushing forward the transformation and upgrading of processing trade to achieve the transformation of the growth mode of foreign trade.¹¹ Chen (2007) believed that people should start the transformation with the five aspects of supporting the exporting of the products that possessed self-owned brands and high added value, controlling the exporting of resource products and the products that caused high energy consumption and pollution, increasing the importing of energy, raw material, advanced technological equipment, and key parts and components, endeavoring to expand service trade, and promoting the transformation and upgrading of processing trade.¹²

II. The Thoughts and Views on Vigorously Developing Service Trade

After the beginning of the 21st century, the world's economy quickly transformed from industrial economy into knowledge economy. The Third Technological Revolution promoted and sped up the prosperity and development of service industry. The areas in China's opening up to the outside world in service trade kept expanding. Service trade accounted for increasingly larger proportion in the entire foreign trade and showed increasingly conspicuous economic vitality. By 2009, China opened up 104 among the over 160 service trade sectors in the classification of the WTO, which accounted for 62.5% of the total. The figure was close to the average standard of 108 sectors of the developed WTO members. Among these, 54 sectors allowed the establishment of solely foreign-funded enterprises and 23 more allowed the establishment of foreign-controlled joint venture enterprises.

As to the role of service trade in China, some scholars measured on the basis of comparative advantage index that the primary comparative advantage in China's service industry laid in labor-intensive industry. But part of its technology- and knowledge-intensive industries, such as information service industry and advertising, also showed a rising trend. Therefore, they advocated that China's service industry should gradually achieve the dynamic accumulation of comparative advantage and make the pie of its comparative advantage bigger.¹³ Some other scholars believed that the improvement of the degree of opening up of service trade promoted the development of service trade in China and strengthened its driving role in national economy. In order to turn around the situation of trade imbalance, people had to further promote the system reform of service trade and bring into play the role of service trade in building China into a trade power.¹⁴

As the global service outsourcing market kept expanding and the service outsourcing industry achieved successful experiences in Tianjin, Nanjing and

¹⁰Gao (2006).

¹¹Liu (2006).

¹²Chen (2007).

¹³Wang and Gui (2004).

¹⁴Wang (2007).

Hangzhou in China, developing service outsourcing became a hotspot in the theoretical discussion and exploration after 2005. Long Guoqiang specifically proposed that service outsourcing industry should be taken as the breakthrough point in expanding service export and people should work hard to cultivate a group of leading export enterprises and qualified foreign trade talents.¹⁵ Wang Zixian believed that the strategic positioning of China's undertaking of international service outsourcing should be that people should take the outlook of scientific development as guidance and take positively participating in the globalization of service industry and vigorously undertaking international service outsourcing as the kernel contents of the new round of opening up to the outside world. They should place such kernel contents at the strategic height of transforming the growth mode of economy and enhancing the development standard of modernization and practically transform the outlook of development and innovate the approach of development.¹⁶ Huo Jingdong analyzed the characteristics of service outsourcing and believed that service outsourcing had many advantages such as low resource consumption, large added value, high information technology carrying capacity, and strong capacity to create jobs and, particularly, create jobs for college graduates. According to certain estimations, the increase of service outsourcing was 6–20 times of that of manufacturing industry but its energy consumption was 20% of that of manufacturing industry. If China could seize the opportunity of service outsourcing transfer, it could speed up its pace in adjusting economic structure and improving the competitiveness of service industry.¹⁷

III. Debate and Development on the Issue of International Trade Friction

In recent years, China faced more and more international trade frictions. “Tire war”, “toy war”, “car parts war”, “iron ore battle” and “oil war” occurred one after another. More and more of China's exported products were restricted or punished with trade remedy measures such as anti-dumping measures, anti-subsidization measures, safeguard measures and special safeguard measures. China became the largest victim of the abuse of trade remedy in the current world. China were confronted with a lastingly great number of anti-dumping investigation cases, which were 51 in 2002, 52 in 2003 and 51 in 2005, all accounting for over 20% of the number of anti-dumping cases in the world in the same year. And the amount of money involved in the case kept growing. By 2006, China had become the country that involved in the largest number of anti-dumping investigation cases in the world for 12 years consecutively.

The scholars had different views on the reasons why international trade frictions with China increased. Feng Lei believed that the factors and areas that affected China's trade friction were mainly the appreciation pressure of Renminbi, the industries under generalized system of preference, the pattern of general trade, the trading of products of which the transfer of production process was hard to implement, bulk

¹⁵Long (2006).

¹⁶Wang (2008).

¹⁷Huo (2007).

products, domestic politics of importing countries, and key areas in the WTO negotiations, and import friction.¹⁸ Some scholars believed that the friction was caused by international trade protectionism. They held that the deep-rooted trade protectionism was the radical cause of the escalation of trade friction. When economic depression occurred in developed countries, such protectionist tendency would become particularly serious.¹⁹ Other believed that the friction was caused by the imperfections in international trade rules. Many areas on the protection of intellectual property rights in TRIPS exceeded the standard of protection in prevailing international conventions. These provisions were made by some developed countries to protect their own economic interests. Such over-protection could easily cause right abuse and result in implicit trade friction.²⁰

The issue of the trade frictions between China and the USA and between China and the EU became a focal one under constant attention. The academic circle generally believed that the issue involved comprehensive factors in many areas such as politics and economy. The research group of the Ministry of Foreign Economy and Trade on the medium-term outlook of the Sino-US economic and trade relations summarized the main reasons of the trade friction between China and the USA as import and export statistical errors, entrepot trade via Hong Kong and the US import restrictions against China.²¹ Some scholars believed that the increasing trade frictions between China and developed countries was the result of the natural evolution in the rise of a major nation, which was similar to the paradox of harmony between chaos and order, although there was the influence of political factors. Zhao Xiao²² believed that China already entered a period of international economic friction which would last at least 20 years. The reasons for this were in three aspects: The world's economy was entering a period on its collision orbit. China was on the rise. And there were a series of issues present in the process of China's economic development.

Relevant personages also expressed their own views on how to respond to international trade friction. Wei Liqun pointed out that people needed to be good at borrowing from the internationally prevailing practice of "open protection".²³ They needed to learn to protect themselves within the framework of the WTO rules and protect domestic industries and, particularly, infant industries with various legal means that conformed to international practices. Long Yongtu proposed when analyzing the response to the international frictions in textile industries that people needed to control exporting rhythms well and safely pass the key periods.²⁴ They should not be too anxious to export but should observe calmly, handle carefully, and act

¹⁸Feng (2003).

¹⁹Jiang (2005).

²⁰Cai (2006).

²¹Research group of the Ministry of Foreign Economy and Trade on the medium-term outlook of the Sino-US economic and trade relations (2001).

²²Zhao (2003).

²³Wei (2002).

²⁴Long (2005).

prudently. They should take an attitude of positive cooperation, adopt powerful self-disciplinary measures, transform the growth mode of foreign trade, and optimize the structure of exported products. Wang Shichun believed that responding to trade barriers through exercising the rights vested in China by the WTO was an important subject that Chinese government and enterprises faced. When responding to trade barriers, people should not adopt a negative attitude of “waiting for windfalls”. They should positively and spontaneously collect information and learn about the development trends of foreign trade policies against China and the measures related to trade in effect or in the process of formulation. They should build and improve trade barrier notification and quick response mechanism and adopt timely adjustment and adaptation measures.²⁵ Sang Baichuan²⁶ believed that, as the products that involved in anti-dumping investigation were mostly labor-intensive products, accelerating the adjustment of economic structure was the radical solution for China to respond to other countries’ abuse of trade remedy measures such as anti-dumping measures, anti-subsidization measures, safeguard measures and special safeguard measures. Moreover, people needed to speed up independent innovation, master core technology, and pursue entering the high end of the industrial value chain.

IV. Theoretical Research Results on Requiring the Recognition of China’s Market Economy Status

The issue of China’s market economy status was closely related to measuring China’s degree of marketization. From 1990s, many researchers in China measured the degree of marketization of China from different angles for the purpose of promoting economic reform. Lu Zhongyuan and Hu An’gang measured and determined from the four aspects of investment, price, production and commerce that China’s degree of marketization in 1992 was 62.2%. The research group of the State Development Planning Commission divided economic marketization into the marketization of commodity flow and that of factor flow and measured and determined that China’s degree of marketization in 1994 was 65%. Chen Zongsheng et al. carried out comprehensive study on the degrees of marketization of different economic entities, industries and regions and that of the Chinese economy in general and measured and determined that the overall degree of marketization of China in 1997 was 60%. Jinping (2001) examined the comprehensive factors of the degree of marketization of agricultural products and agricultural factors, the degree of development of rural market system, the degree of the peasants’ adaptation to market economy, the situation of rural market operation mechanism and government regulatory capacity and concluded that the degree of marketization of China’s rural economy reached 49% in 1998. Gang et al. (2001, 2003) measured and determined the ranking of marketization of various provinces, autonomous regions and municipalities directly under the central government in China in 1997 from the five aspects of the relationship between government and market, the development of non-state-owned economy,

²⁵Wang (2004).

²⁶Sang (2009).

product markets, and factor markets, and the development of intermediary organization and the environment of legal system. These measurement results further enriched people's understanding on China's marketization reform process and contributed to completing economic retracking as quickly as possible and establishing socialist market economic system.

After China's accession to the WTO, trade environment was greatly improved, government behavior became more regulated, and international rules were adopted generally in various economic areas. The circle of theoretical study got a completely new perspective in the study on the degree of marketization, namely connecting global trade to the issue of China's market economy status. The USA and European countries still regarded China as "non-market economy country" after China's accession to the WTO. They adopted discriminatory policies in anti-dumping measures against China and built the most serious non-tariff barriers. Because of this, the index system for the measurement of marketization in this period paid attention to not only the role of price and resource allocation mechanism but also the transformation of government functions and the environment of legal system. Such index system not only stressed on reflecting the latest results in the development of market economy in China but also fully drew from the legislative standards on market economy status in international anti-dumping practice and relevant indexes for the measurement of economic freedom. Besides, large innovation was achieved in measurement methods and indexes.

The School of Economics and Resource Management of the Beijing Normal University carried out from 2001 marketization measurement for eight consecutive years, which was presided over by Li Xiaoxi, centering round the issue of China's market economy status, and formulated multiple volumes of annual *Reports on the Development of China's Market Economy*. The reports proposed five criteria and 33 indexes for marketization measurement and determined that China's degrees of marketization in the years from 2001 to 2008 were respectively 64.26%, 64.76%, 67.07%, 70.53%, 76.03%, 75.19%, 76.19% and 76.40%. The reports also summarized the basic stages and characteristics of the development of China's market economy from these data. The marketization indexes published in the reports won extensive recognition in the society.²⁷

The year 2011 marked the tenth anniversary of China's accession to the WTO. At present, nearly 100 WTO members recognized China's market economy status. But the USA, the EU and Japan refused to recognize until today. Such a situation involved complex factors in the political and economic games of major countries.

V. The Study on the Countermeasures for Constructing Foreign Trade Management System More Adapted to International Rules and Practices

The accession to the WTO brought both historic opportunities to China's foreign trade undertakings and austere challenges to China's foreign trade management system. The circle of theoretical study generally believed that China needed to establish an

²⁷School of Economics and Resource Management of the Beijing Normal University (2003, 2005, and 2008).

overall new foreign trade management system that operated in line with international rules, adapted itself to international practices, conformed more to the requirements of market economy, and paid more attention to the coordination between domestic and foreign business. Thus people could constantly improve the standard of trade liberalization and facilitation, reasonably regulate the balance of import and export aggregates, promote the optimization of trade structure, ensure the steady operation of foreign trade, and support the needs in the development of national economy in a better way.

Around the time of China's accession to the WTO, the circle of theoretical study paid more attention to how China's foreign trade management system should get in line with international practices. Yang Shengming pointed out that China's foreign trade system reform were mainly implemented in four aspects after its accession to the WTO²⁸: People accelerated the diversification of foreign trade entities and completed as quickly as possible the transition from the approval and examination system for foreign trade operation right to the registration and record system. People promoted the integration of scientific research, industry and trade. They strengthened the coordination and cooperation of relevant competent administrative departments of the state at the macroscopic level and granted foreign trade operation autonomy to large production enterprises at the microscopic level. They promoted the innovation of foreign trade intermediary organizations and sped up the innovations in outlook, content, function and system. And they established and improved effective protection mechanism and adopted more technological and environmental protection measures. Several years after China's accession to the WTO, Chen Deming emphasized that people needed to always keep an open mind. They should promote the basic balance in import and export trade and international balance of payments, speed up implementing the free trade zone strategy, properly handle economic and trade disputes, drive the expansion of domestic demand with opening up to the outside world, and resolutely take the road of peaceful development.²⁹

After 2005, the circle of theoretical study was confronted with the urgent requirements in China concerning important reform in exchange rate system, increasing international trade frictions, and transformation of the growth mode of foreign trade. So it paid more attention to how China's foreign trade management system could bring into better play its function in optimizing structure and achieving the balance between internal and external business and to how it could maintain the legal rights and interests of China's foreign trade operation on the basis of respecting the WTO rules. Shen Danyang proposed that people needed to strengthen macroscopic management functions and weaken administrative management instruments in China's foreign trade management system reform during the Eleventh Five Year Plan.³⁰ They needed to strengthen the management of export industrial policies and form the mechanism for such management. They needed to improve the market and social intermediary service systems related to foreign trade activities. They needed to

²⁸Yang (2000).

²⁹Chen (2009).

³⁰Shen (2005).

improve foreign trade promotion mechanism and form highly efficient foreign trade service system network. And they should improve foreign trade agent system and establish a common mechanism for the tax exemption, deduction and refunding of exported goods applicable to all kinds of exporting enterprises. Zhang Xiaoji pointed out that China's trade surplus was mainly caused by international factors and it was determined by the division of work in the market under globalization. Now, a large number of transnational companies were transferring their industries into China. The majority of their import and export business was intra-corporation trade. So trade surplus was not to be resolved by the Chinese government through unilateral macroscopic regulation. The purpose of the government's macroscopic regulation was always to prevent large economic fluctuations rather than limiting export.³¹ Zhang Yansheng pointed out that reducing surplus mainly included reducing trade surplus, reducing capital surplus and reducing the scale of foreign exchange reserve. The key area for China to realize the basic international balance of payments in foreign-related economy laid in improving the competitiveness of exported products rather than simply reducing export and expanding import. The adjustment of international payments and the reduction of surplus were not just issues to be resolved through macroscopic regulation. They also involved the improvement of competitiveness and the adjustment of structure.³² Other scholars proposed that people needed to establish and complete fair trade management system that involved anti-dumping, anti-subsidization and safeguard measures. They should speed up building import early warning system and timely prevent the serious damage caused by excessive importing to domestic industries. They should adopt the means permitted by the WTO against the importing that involved repeated construction and caused serious impact on domestic market so as to impose reasonable regulation and reduce adverse influence.³³

There were many theoretical views in this area, which not only caused extensive social influence but also forcefully pushed forward the practice of China's foreign trade management system reform. These views also played a promotive role in the aspects of promoting the reform of the organization structuring of foreign trade, revising the basic laws in foreign trade, and fulfilling the commitments upon the accession to the WTO on reducing tariff step by step. With the joint efforts of the government, the society and the circle of theoretical study in China, a new foreign trade management system was formed initially, which was regulated by the market, operated in line with international practice, and practiced free trade.

³¹Zhang (2006, p. 5).

³²Zhang (2007).

³³Han and Zhou (2009).

2 New Progress in the Theories on Using Foreign Investment

After its accession to the WTO, China moved up to a new level in absorbing foreign investment. Up to the end of 2010, China had approved the establishment of 710,000 foreign-invested enterprises and actually used USD 1,051.2 billion foreign investments, ranking the top place among developing countries. Foreign-invested enterprises already became an important component of Chinese economy. Whether China needed foreign investment and what the scale of using foreign investment should be were not questions that caused a great number of debates like in the 20th century any more. The hotspot under the attention of the academic circle turned onto even deeper questions such as how to treat foreign investment under the environment of fully merging into globalization and how to improve the quality of China's using of foreign investment.

I. New Understandings on the Issue of the “National Treatment” of Foreign Businesses

The accession to the WTO made China gradually opening up some areas for the entry of foreign investment and relaxing relevant conditions. Foreign investment enjoyed “national treatment” in more and more industries. But over a long period, China established a preferential policy system with income tax as the kernel for foreign-invested enterprises. Various local governments implemented a great variety of preferential treatments for the purpose of attracting businesses and investments. These efforts resulted in the “super-national treatment” of foreign investment. How people should consider the different treatments between domestically- and foreign-invested enterprises and with what attitude they should treat foreign investment after the accession to the WTO became a hotspot in the discussion and exploration of the academic circle. And mainstream views all showed a rational attitude in this respect in general.

Wu Yi pointed out that China would unswervingly implement the opening up strategy of mutual benefit and win-win result and comprehensively improve the standard of open economic development. China would not only work hard on the development of the country itself but also spontaneously undertake its responsibilities as a member of the international community. It would strengthen international development cooperation and respond to the challenges such as environmental and climate changes jointly with other countries. China's development would continue to benefit from extensive and in-depth international economic and trade cooperation. And in turn, its development would create wider space for expanding international economic and trade cooperation.³⁴

³⁴Wu (2007).

Li Xiaoxi proposed that people should consider the introduction of foreign investment with an unbiased mind. First, they should consider the market without bias. They should respect the regulatory role of the market when the amount of introduced foreign investments fluctuated. Second, they should treat domestically- and foreign-invested enterprises without bias. They should properly handle the matters concerning foreign-invested companies and, particularly, transnational companies in accordance with relevant laws and regulations. They should give equal treatment to domestically-funded enterprises in relevant matters and should not give more preferential treatment to foreign-invested enterprises and less to domestically-invested ones. Third, they should treat foreign businessmen without bias. They should create not only good investment and operation environment but also good living environment for them. Fourth, they should view market competition without bias. Chinese enterprises needed to learn and grow in competition and the government needed to work hard on creating an environment for fair competition. And fifth, they should organize activities to attract investments and businesses without bias. They needed to pay more attention to the long-term effect of attracting investments and businesses rather than pursuing short-term performance of the government in this respect excessively.³⁵

Sang Baichuan et al. believed that the high-speed growth of foreign investments in China had close relation to its preferential policies. The national situation of China's economic system retracking made it necessary for giving certain preferential policies to foreign investments. The preferential policies to foreign investments were also the means for China to win over high quality foreign investment in the game with other countries. But when considered in the long run, the direction of development should be the arrangement and implementation of investment preferential policies by industry and region on the basis of the requirements of the market economy rather than implementing different investment policies and treatments on the basis of economic ownership sectors. Such policy adjustment could be feasible only when people organically combined granting national treatment to foreign-invested enterprises with unifying the policy treatment of domestically-invested enterprises such as state-owned, private and individually-operated ones, hardening the budget restriction on state-owned enterprises, and reducing the chances for government officials to abuse administrative power to influence resource allocation.³⁶

II. Theoretical Progress in Expanding the Areas and Innovating the Modes of Using Foreign Investment

In the 21st century, transnational companies laid their eyes on China's service industry and some technology-intensive industries. The accession to the WTO provided conditions for transnational companies to implement expansion strategy in certain areas. In accordance with the commitments upon the accession to the WTO, China expanded market access for foreign investment. The areas opened up to the outside world gradually expanded from manufacturing industry to service industry.

³⁵Li (2009b, pp. 286–287).

³⁶Sang et al. (2006, pp. 14–15).

In addition, new modes of using foreign investment also emerged. These changes promoted the progress in relevant economic theories.

Pei Changhong et al. studied the investment mode and capital structure of foreign-invested enterprises over many years. Their research indicated that solely foreign-funded operation already became the primary mode of investment of foreign-invested enterprises. The proportion of foreign investment in the registered capital of foreign-invested enterprises showed a rising trend. And the tendency that foreign-invested enterprises became solely foreign-funded would further expand. In response to such a situation, domestically-invested enterprises should positively form strategic alliance with foreign-invested enterprises. People should maintain fair market competition environment and prevent transnational companies from forming monopoly in China market. They should strengthen intellectual property right protection and further increase the proportion of capital contribution with intellectual property right in foreign-invested enterprises.³⁷ Besides, they pointed out that the accession to the WTO became a dividing line in the attraction of foreign investment in China's service industry. Service industry became the area with the fastest growth in attracting foreign investment in China. At present, China's service industry was still of relatively low standard. People should start with the following two aspects in improving China's ability to receive international direct investment in service industry: One was to fully develop knowledge- and technology-intensive service industries and form modern structural system of service industry with high standard and reasonable structure. The other was to fully utilize various forms of industrial transfer in service industry.³⁸

He Dexu analyzed the influence of the entry of foreign investment in China's banking industry after the accession to the WTO and relevant countermeasures. Foreign-funded banks brought advanced technology, financial innovation methods, and advanced management philosophy and operation mode. They supplied examples to learn, reference systems to compare, and opponents to compete with for China's banking industry. Such a situation was favorable for China's commercial banks to raise their operation and management standard and improve their systems. However, foreign-funded banks had absolute advantages in the areas of operation and management, assets quality, human resources, and product innovation. China's banking industry faced obvious challenges. China's banking industry had to raise its comprehensive competitiveness in an all-round manner and adopt such measures as progressively promoting the opening up to the outside world in the banking industry, reforming the ownership system of state-owned commercial banks, improving the internal organizational structure of commercial banks, intensifying the efforts in handling the bad assets of state-owned commercial banks, enhancing the ability of medium- and small-sized banks in resisting external impact, establishing deposit insurance system, and strengthening the supervision on foreign-funded financial institutions.³⁹

³⁷Pei et al. (2010, pp. 39–42).

³⁸Ibid, pp. 45, 46.

³⁹He (2004).

III. Views on Improving the Quality and Standard of Using Foreign Investment under the New Situation

Improving the quality and standard of using foreign investment was an important issue that the researchers and decision-makers paid great attention in the area of absorbing foreign investment after China's accession to the WTO. It was officially proposed in the Sixteenth CPC National Congress that people should "further attract foreign direction investments and improve the quality and standard of using foreign investment". And it was further required in the Seventeenth CPC National Congress that people should "bring into play the positive role of using foreign investment in the areas of promoting independent innovation, industrial upgrading and regional coordinated development". These representations, which were later elevated into national strategy, also reflected the fruits of academic discussion. A large amount of literature was published on the quality and standard of using foreign investment. The authors would like to give a brief summary on it in the following.

Jiang Xiaojuan believed that one important role that the investments of transnational companies in China had played was greatly accelerating the structural upgrading of China's domestic industries. A considerable number of transnational companies supplied the technologies to fill up the blanks in China. Besides, the technologies introduced by foreign-invested enterprises generated obvious spillover effect.⁴⁰ Yu Yongding believed that FDI played a positive role in creating jobs and increasing export. It had very complicated influence on technological progress in China. Nonetheless, transnational companies would definitely bring some technological transfer and spillover as they possessed advantages in manufacturing technology, management and marketing network. The influence of FDI on economic growth was realized through the two channels of capital accumulation and total factor productivity. Considering crowding out effect and China's high savings rate, the scholar believed that FDI only had limited contribution to capital accumulation and that its contribution to economic growth was exhibited more in the area of raising total factor productivity.⁴¹ Wang Linsheng believed that foreign direct investment would continue to play a very positive role in China's industrial upgrading, which was still in process, after its accession to the WTO. In the policy on using foreign investment, the guideline of "exchanging market for technology" could only play a limited role. People needed a strategy of "promoting innovation with competition". Its basic connotation was that people should build a market environment which was open and in line with international practice and which advocated fair competition so that domestically- and foreign-funded enterprises could constantly improve their technological contents and innovate their technologies in competition.⁴²

⁴⁰Jiang (2004).

⁴¹Yu (2004).

⁴²Wang (2002).

IV. In-Depth Analysis on the Influence of Foreign Investment to National Security

After China's accession to the WTO, the several merger and acquisition events between transnational companies and China's important industry leading enterprises triggered extensive attention on the influence of the mergers and acquisitions of foreign investors to national security. The academic circle had large controversy on this issue.

Cheng Enfu and Li Bingyan believed that the investment strategy of transnational companies in China experienced important change. One of the prominent features in such change was that these companies sped up their merger and acquisition of Chinese domestically-funded industry leading enterprises. Key enterprises that originally had good development impetus were controlled by foreign capital so that they lost their right to independent innovation and also lost their quality assets, technical forces, brands and markets. As a result, their technical teams and capacities, which were cultivated through many years of independent research and development, were controlled, utilized or even eliminated by foreign capital. Huge amounts of profits flew outside China with such change and the value of their own brands were taken by foreign businesses. These facts proved that it was unrealistic to develop national economy through integrating national enterprises with foreign capital. Without the development and powerful presence of national enterprises, it was impossible to realize the goal of making China powerful and the Chinese people wealthy as quickly as possible.⁴³

Wu Cailin and Li Xin believed that people had to impose limitations on the merger and acquisition with foreign capital in some important industries, such as equipment manufacturing industry, financial industry, energy industry and mineral exploitation industry. Only when the state firmly took these key industries in hands and improved relevant laws, regulations, rules and systems could China stabilize and develop national economy under any circumstance and reduce the influence of foreign capital on the lifeline of Chinese economy.⁴⁴

Long Guoqiang believed that foreign direct investment could play a role like a "double-edged sword" to national economy security. If FDI was well-channeled, it could promote China's economic development. If it was managed improperly, there could be the risks that foreign capital monopolized domestic market and controlled strategic industries and hence FDI could threaten national economic security. Therefore, people needed to prevent the over-exaggeration of the threat of foreign capital to national economic security, which might cause China to lose development opportunities. On the other side, they also needed to practically improve the quality and standard of using foreign investment and prevent the over-dependency on foreign trade in strategic industries. For such purpose, people needed to renew their outlooks and guide the work related to foreign investment with new philosophy on economic

⁴³Cheng and Li (2007).

⁴⁴Wu and Li (2007).

security that was suitable to the age of globalization. They should improve and complete laws and regulations, strictly enforce laws and guard against risks.⁴⁵

3 New Developments in the Theory on “Going Global”

One of the important breakthroughs in China’s opening up to the outside world after its accession to the WTO was the transformation from focusing on “bringing in” to giving equal weight to “bringing in” and “going global”. The strategy of “going global” was the basic national policy in the new stage of opening up to the outside world. It mainly included going outside China in various ways such as investing in foreign countries, contracting projects in foreign countries and carrying out labor service cooperation with foreign countries and fully utilizing “two markets and two resources”.⁴⁶ In a broader sense, it also included various processes in utilizing comparative advantages to go into the international market, gain development conditions, and retain competitive advantages, such as economic and technical aids to foreign countries, foreign trade and exporting, and using foreign investments overseas. In 2001, the *Compendium of the Tenth Five Year Plan* listed “going global” together with foreign trade and using foreign investment as the three pillars to support the open economic development during the Tenth Five Year Plan. It was specifically proposed in the report of the Sixteenth CPC National Congress in 2002 that people should “adhere to the combination between ‘bringing in’ and ‘going global’ and comprehensively improve the standard of opening up to the outside world”. In this period, the academic study on “going global” also thrived.

I. Conditions and Motivations

Chinese economy developed rapidly and the comprehensive strength of Chinese enterprises grew more powerful. These laid the foundation for allocating resources on a global basis. After the accession to the WTO, Chinese economy became more globalized. Chinese enterprises expanded their international view. And there were more mature conditions and motivations for “going global”.

Lu Jinyong believed that implementing the strategy of “going global” was the requirement of China’s development after the accession to the WTO and the necessary requirement to adapt to the developments in economic globalization. It was favorable to adjusting economic structure and optimizing industrial structure and also to improving China’s international status. It also responded to the demand in developing China’s own transnational companies and the requirement in development high and novel technology industries.⁴⁷

Guo Hong and Zhao Chunming believed that people should develop outward foreign direct investment in the dynamic interaction between economic development

⁴⁵Long (2007a).

⁴⁶Chen (2008).

⁴⁷Lu (2003, pp. 91–94).

and investment development. According to the theory of investment development path, China would gradually meet the climax of foreign direct investment after the peak time of introducing foreign direct investment in large scale and over a long period of time. Although China was still a developing country, some large domestic enterprises fully possessed the capital strength to invest outside China. At present, the main purpose of the outward foreign investment of China's domestic enterprises was to pursue strategic assets, namely natural resources, technology resources and market resources, to enhance the resource basis of domestic enterprises and hence improve the international competitive advantages of these enterprises and, in particular, the international competitive advantages in domestic market. Thus, domestic enterprises could effectively resist the competition pressure brought by globalization through the synergy effect between domestic and foreign environment.⁴⁸

II. New Developments in the Ways and Areas of “Going Global”

After the development in nearly ten years after the accession to the WTO, “going global” initiative, such as outward foreign investment, foreign project contracting, foreign labor service cooperation, and foreign economic aid, showed increasingly diverse ways and gradually improving standards. China's “going global” initiative established businesses covering over 170 countries and regions in the world. It gradually developed from mainly engaging in trade service and small-scale processing in the past to engaging in the areas of energy, mineral resource exploitation, communications and logistics, processing and manufacturing, and high and novel technology industries. The study of the academic circle in this respect reflected the trends of development and changed in the ways and areas of “going global”.

Zhang Youwen et al. summarized the several new characteristics of the ways of “going global”: Outward foreign direct investment gradually developed from “green-field investment” to transnational merger and acquisition and other ways. Foreign project contracting constantly developed toward higher levels such as EPC general contract and BOT. The number of large projects constantly grew and the technological contents of the project also improved increasingly. In foreign labor service cooperation, people gradually explored and established such ways as whole team unit designation, designation after training in base-county, and designation on the basis of inter-governmental agreement. High-level labor service designation such as engineer designation increased constantly.⁴⁹ Yang Hongxi pointed out that the specific forms of China's foreign aid experienced constant development and improvement in recent time. Foreign economic aid became increasingly flexible and mature in the process of reform and adjustment. Material aid and current exchange aid reduced, the proportion of complete-set project aid rose, and technology and intelligence aid achieved larger development. There was also the transformation from bilateral aid into multi-lateral aid cooperation.⁵⁰ Lu Liping proposed that China's foreign direct investment should take resource exploitation ones and export-oriented ones as the main types

⁴⁸Guo and Zhao (2005).

⁴⁹Zhang et al. (2008, p. 359).

⁵⁰Yang (2009).

and people should also seize proper opportunities to supplement them with foreign investments of the types of market seeking and high and novel technology research and development. In addition to carrying out production-type outward foreign direct investment, people should also pay attention to fully bringing into play the role of foreign investments in service industry that already existed overseas such as those of the types of trade, post-sale service and financial enterprises. Moreover, people should positively encourage Chinese enterprises to carry out investment activities overseas by means of international financing and its outward foreign indirect investment. They should further expand the scope of China's outward foreign investment and utilize foreign resources well. These efforts would play a role of protection and service to the enterprises that carried out direct investment.⁵¹

III. Analysis on the Issues and Risks in “Going Global”

China's “going global” initiative started later and was still in a fledging period in general. Therefore, it was an important task in academic study to clearly identify the issues and risks in “going global” and find relevant solutions. There were many research results in this aspect.

Xu Dansong believed that the issues of “going global” were mainly exhibited in five aspects: Legislation work lagged behind. Examination and approval system was not suitable to the requirements of socialist market economy. Foreign exchange system was not suitable to the needs in the current situation. The overseas investment strategies of the enterprises were not clearly defined and their management system could hardly adapt itself to the needs on the international market. And inadequate information acquisition restricted the transnational operation of medium- and small-sized enterprises. The countermeasures to resolve these issues included improving the construction of legal system and speeding up legislation work; reforming relevant management systems to adapt to the requirements in market economy; creating better bilateral and multilateral international environments; strengthening the guidance and promotion of the “going global” initiative; speeding up the construction of financial service system; building foreign exchange management system that adapted to the needs on the international market; encouraging private enterprises to “go abroad”, and so on.⁵²

Nie Minghua analyzed in detail the risks in seven aspects that Chinese enterprises faced in outward foreign direction investment: (1) National political risks, including risks of “discriminative intervention” of political forces, creeping expropriation, war or civil strife; (2) Terrorism and nationalism risks; (3) Risks of policy and law changes; (4) Exchange rate change and exchange risks; (5) Investment decision making and operation risks; (6) Cultural conflict risks; (7) Management system and moral risks. In addition, there were also host country default risk, interest rate risk, financing risk, and technology risk. Chinese enterprises in outward foreign direct investment should bring into their spontaneity and initiative into full play to improving and complete their risk prevention and control mechanism and effectively

⁵¹Lu (2010, p. 190).

⁵²Xu (2002).

exerted their functions. The Chinese government should take scientific, well-targeted and operable policy measures to help the enterprises to avoid risks and enhance economic benefits in the process of “going global”.⁵³

Li Dawei believed that the “going global” process of Chinese enterprises could be divided into preparation stage, implementation stage and operation stage. Each stage faced different main risks and the losses caused by the risks were also greatly different. Political risk, policy risk and law risk were present in the entire process of the “going global” of the enterprises. These risks were highly irresistible and might trigger other risks. The periods when the risks caused the most serious loss were the ending period of the implementation stage and the early period of the operation stage. Technology risk and fund risk became explicit in the implementation stage and belonged to the area of business. Operation and management risk, environment protection risk and cost risk became explicit mainly in the operation stage. Environment protection risk might be caused by the policies of the host country. But the rest two types of risk basically belonged to the area of business and had much similarity with domestic investment risks. In addition, people also needed to pay attention to the operation and management risk caused by cultural difference. People needed to strengthen the tracking, monitoring and early warning related to investment receiving countries and lower political, policy and law risks. They needed to further expand financing channels and lower financial risk. They also needed to strengthen the construction of modern corporate system and culture to reduce operation and management risk.⁵⁴

IV. Discussion on the System Guarantee of the “Going Global” Initiative

The rapid development of the “going global” initiative posed higher requirements to system guarantee. It could not work without national system guarantee at the macroscopic level and it also needed enterprise system guarantee at the microscopic level.

Shi Guangsheng pointed out that people needed to speed up transforming government functions and vigorously promote the facilitation of outward foreign investment cooperation. They needed to improve promotive measures and enhance the international competitiveness of Chinese enterprises. They needed to build guarantee mechanism and maintain the legal rights and interests of the enterprises. Competent departments in charge of foreign economy and trade at various levels should follow the principle of “promoting vigorously, guaranteeing effectively and supervising with proper methods”. They should spontaneously strengthen the cooperation with relevant departments, establish good collaborative mechanism, and form a joint force to support the “going global” of the enterprises.⁵⁵

Pei Changhong and Fan Ying pointed out country-specific advantages provided system guarantee for the formation of the microscopic competitive advantages of the enterprises. The system arrangement of the government to promote the outward

⁵³Nie (2009).

⁵⁴Li (2009, pp. 246–268).

⁵⁵Shi (2002).

foreign direct investment behavior of the enterprises had to take the maximization of the interests of the home country as the premise. Under such a premise, the Chinese government could realize domestic investment policies and public services through specific measures like formulation of laws and regulations, fiscal and taxation encouragement policies, preferential policies on the financing in the financial area and foreign exchange use, and information service and talent training. In its overseas investment policies and public services, it could guarantee the safety and interest of the outward foreign direct investment of Chinese enterprises through signing bilateral or multilateral investment agreements with host countries. It could also promote the going global of a large group of enterprises through establishing the industrial clusters for foreign direct investment in various forms. These would form the country-specific advantages of the home country.⁵⁶

4 New Progress in Foreign Exchange Theory

From the beginning of the 21st century and, in particular, from the accession to the WTO, China sped up the process of integrating into economic globalization. The opening up to the outside world further expanded, socialist market economic system further improved, and radical change occurred to the situation in the foreign exchange market. China's foreign exchange management transformed from "tolerant entry and strict exit control" to balance management. People further brought into play the role of interest rate and exchange rate, orderly pushed forward the realization of capital account convertibility, paid great attention to preventing and defusing international financial risks, and worked hard to promote the balance of international payments.

1. Path Selection of the Reform of RMB Exchange Rate Formation Mechanism

As Chinese economy integrated into the broader stream of the world's economy after 2001, the original compulsory foreign exchange settlement and sale system could not correctly reflect the supply and demand relations on the foreign exchange market. The RMB exchange rate formation mechanism faced the necessity to have new reform. There were two key points in the RMB exchange rate system reform: First, people should establish a marketized RMB exchange rate formation mechanism that could adapt to the needs of China's economic development. Second, people needed to reduce as much as possible the risks of macroeconomic fluctuations and, in particular, of the unhealthy speculation on Renminbi or large fluctuations of the level of output within a short period, which might be brought about by exchange rate adjustment.

In response to these, the circle of theoretical study carried out heated discussion on whether the goal of exchange rate system reform was to continue to implement fixed or pegged exchange rate system or floating exchange rate system. Even some internationally-renowned economists gave unprecedented attention to such discussion.

⁵⁶Pei and Fan (2010).

Robert (2003) believed that changing current fixed exchange rate system involved great risk.⁵⁷ It was not helpful for China to absorb direct investment. Moreover, China's financial system was very vulnerable. China was not prepared for flexible exchange rate mechanism. Therefore, China should retain its current exchange rate system within foreseeable future.

Ronald (2004) also believed that people should keep the current central rate unchanged in RMB exchange rate management and carry out exchange rate fine-tuning around it within a floating range of 1–2%.⁵⁸ Thus, people could let more international participants join in China's current exchange settlement market. And in this way, they could reduce the exchange settlement pressure of the central bank and promote China's economic development. But many domestic scholars disapproved of their views. They believed that the current fixed exchange rate system would cause great restriction to China's monetary policy and damage its independence. In addition, it could easily cause the "moral risk" that private sectors did not have the initiative to make hedging operation.

Gang (2000) believed that it was impossible to realize a marketized exchange rate system which was truly elastic, completely floating, and flexibly adjusted in a developing country which still did not open up capital account.⁵⁹ Before the developing country realized the complete convertibility of its money, it was impossible to have market exchange rate in the true sense. What the developing country implemented was a managed floating exchange rate system controlled with policy parameters and based on market supply and demand.

Yongding (2001) pointed out that the characteristics of China's current open economy were quasi-fixed exchange rate system, capital control and continuous "double surpluses".⁶⁰ The combination of these three characteristics resulted in the complexity of the macroscopic management in China under open economy. Under fixed exchange rate system, continuous "double surpluses" would definitely require the central bank to constantly inject money into monetary base to increase money supply. This would cause instability in domestic economy. Therefore, continuing to retain fixed exchange rate system would definitely result in the fluctuation of money supply and economic instability.

Hu (2004) believed that people in fact overlooked the inherent contradiction between fixed exchange rate system and monetary policy autonomy and the progressive liberalization of capital account when they implemented the policy of keeping the current RMB exchange rate unchanged.⁶¹ This was because flexible exchange rate system could better reflect the ever-changing market situation and economic foundation. It would also allow China to coordinate freer capital flow on the one hand

⁵⁷Robert (2003).

⁵⁸Ronald (2004).

⁵⁹Yi Gang, "The Selection of Exchange Rate System and the Estimation of Effective RMB Exchange Rate", *Papers of the Employees in the People's Bank of China*, Issue 2.

⁶⁰Yu Yongding, "A Review of China's Macroeconomic Development and Policies in the 1990s", *China & World Economy*, Vol. 9, No. 6.

⁶¹Hu (2004).

and more effectively implement independent monetary policy on the other hand so as to control the risk of economic overheating and respond to various impacts from both inside and outside.

The scholars also carried out in-depth discussion and exploration centering round the basic path and opportunity to reform exchange rate formation mechanism. Xu (2003) pointed out that people should first realize interest rate marketization.⁶² They should change the current compulsory foreign exchange settlement and sale system and gradually implement voluntary foreign exchange settlement and sale system. They should improve the mechanism for the central bank to manipulate and intervene foreign exchange market and gradually lower the frequency of the central bank's intervention on the market. They should implement foreign exchange target zone, consider establishing foreign exchange equilibrium fund, realize the diversification and marketization of regulation, and speed up the development and improvement of foreign exchange market itself.

Sun (2004) pointed out that people needed to select a nominal anchor for monetary policy when a country exited fixed exchange rate system so as to ensure the credibility of low inflation commitment.⁶³ The time when money strengthened should be selected as the ideal opportunity for exiting the fixed exchange rate system. Smooth exit needed prudent risk exposure management with some effective risk avoiding instruments provided.

Zuliu (2005) pointed out that China needed to change its current fixed exchange rate system immediately and adopt managed floating exchange rate system. The implementation of exchange rate adjustment did not need to wait for the completion of banking reform. But China had to retain the control over capital account. The opening up of capital account should never come before the implementation of floating exchange rate system.

Guozhong (2005) believed that China could implement the transition from fixed exchange rate system to floating exchange rate system only after the reforms in investment system and financial system were relatively complete. He also believed that the current exchange rate was low to the Yangtze River Delta and the Pearl River Delta but it was high to other regions.

On July 21, 2005, the People's Bank of China declared the implementation of a managed RMB exchange rate floating system. China started to implement a managed floating exchange rate system based on market supply and demand and regulated in reference to a basket of currencies. RMB exchange rate was not solely pegged to US dollar. A RMB exchange rate formation mechanism with more elasticity was formed. Besides, it was proposed that people had to adhere to the principles of spontaneity, controllability and progressiveness in RMB exchange rate reform. From then on, the fundamental role of market in exchange rate formation was further strengthened, the elasticity of exchange rate was further expanded, and the regulatory role of international receipts and payments was further brought into play. RMB exchange rate reform entered the new stage of establishing and completing the managed floating

⁶²Xu (2003).

⁶³Sun (2004).

exchange rate system based on market supply and demand and retaining the basic stability of RMB exchange rate at a reasonable and balanced level. Yu (2005) believed that “exchange rate system reform increases the elasticity of RMB exchange rate, leaves sufficient space for the Central Bank to intervene in foreign exchange market, and hence guarantees the stability of RMB exchange rate. The Central Bank has to control well the stability and flexibility of exchange rate. It should neither overlook nor overstress the stability of exchange rate. Otherwise, the exchange rate system in reference to a basket of currencies will return to the exchange rate system pegged to the US dollar so that China will fail in achieving reform goals.”⁶⁴

II. Theoretical Contentions on RMB Appreciation

After the beginning of the 21st century, global economy fell into depression and economic imbalance became increasing serious. In particular, the outbreak of international financial crisis further deteriorated global economic situation. Some developed economies in the west fell into stagnation or even recession in economic development. In contrast, Chinese economy not only continued to retain high growth but also successfully resisted international financial crisis. Because of this, the United States and other developed countries constantly imposed pressure on China and required China to allow Renminbi to appreciate for the purposes of maintaining their own interests and turning around the situation of their trade deficit. Some even maliciously accused China of being an “exchange rate manipulator”. Confronted with such complex situation in reality, the Chinese circle of theoretical study had exceptionally intense discussion on the advantages and disadvantages, pressure and path of RMB appreciation.

As to whether Renminbi should appreciate or not, most scholars agreed that Renminbi could appreciate to a small extent in a controllable range. This was because Renminbi appreciation was an unavoidable trend under the situation that Chinese economy retained rapid growth, labor productivity raised constantly, and China’s foreign exchange reserve increased largely. The long pegging of Renminbi to US dollar and the undervaluation of its currency value resulted in deteriorating trade conditions, inappropriate resource allocation, and aggravating trade friction in China. Besides, China’s constantly growing foreign exchange reserve caused increasingly larger pressure in injecting money into monetary base. It also weakened the independence of China’s monetary policy. Such a situation could easily cause serious inflation and damage the overall stability of macroscopic economy. According to the analysis of some scholars, the total factor productivity of the department of trade goods grew faster than that in non-trade goods department under the policy combination of retaining unchanged real exchange rate and stable price level. But such a situation would cause a series of problems such as distorted industrial structure, enlarging trade balance, and lowering wage standards. Therefore, people needed to realize the rise of real exchange rate through revaluing RMB nominal exchange rate so that the relative prices of trade goods and non-trade goods could adjust reasonably. Only in this way could they optimize the structure of national economy, change

⁶⁴Yu (2005).

external imbalance, and promote the transfer of labor from the countryside to the city.⁶⁵ The scholars who disapproved of RMB appreciation were mainly Robert A. Mundell, Ronald I. McKinnon and Zhang Wuchang. They believed that RMB appreciation could not resolve the issue of China's huge trade surplus. It would also result in decreasing foreign trade export and foreign investment, deteriorating employment situation, and lowering price of agricultural products in China. It would cause deflation, give rise to new appreciation expectation, and stimulate the large influx of international fluid money.

The Chinese circle of theoretical study mostly believed that the pressure of Renminbi appreciation mainly came from global economic imbalance. Its main manifestations were the following: First, the issuance of US dollar was not restricted. Global fluidity increased greatly so that real economy and virtual economy became more deviated from each other. Second, the United States continued to have high consumption and low savings rates, which resulted in double huge deficits in its financial budget and international payments. On the opposite, China's high savings, high investment, high export and low consumption resulted in production capacity expansion and huge surplus in international payments. These structural conflicts caused huge risks to global economy, which needed to be adjusted gradually. So USD depreciation and RMB appreciation were both inherently-required factors in such adjustment. Some scholar believed that the pressure of RMB appreciation could be divided into the two types of short-term and long-term ones.⁶⁶ Short-term pressure was caused by internal and external economic imbalance. It was manifested as large amounts of surplus continuously present in international payments. Long-term pressure was brought about by rapid growth of Chinese economy over long time, constantly rising labor productivity, and constantly strengthening international competitiveness. Other scholars pointed that exchange rate fluctuation was the result of the gaming between various international forces after the disintegration of the Bretton Woods Regime. It was basically caused by financial transactions. In the RMB appreciation pressure, the speculation of international fluid capital, namely financial factors, played a role far larger than that of the factors in real economy. In addition, some scholar carried out cointegration test on the monthly data of the payments in Sino-US trade and RMB exchange rate from 1998 to 2003 through analyzing the annual data from 1994 to 2002 and applying the Engle-Granger two-step method.⁶⁷ He believed that there was no long-term stable cointegration relation between these two categories of data. So people could not resolve the trade deficit between the United States and China only through changing RMB exchange rate. Another scholar believed that the appreciation of RMB nominal exchange rate was not the only way for China to adjust trade imbalance.⁶⁸ Even if RMB exchange rate was still pegged to the US dollar, China still could utilize inflation to adjust the comparative prices of its products against American ones.

⁶⁵Zhang and He (2006).

⁶⁶Zhang (2005).

⁶⁷Shen (2005).

⁶⁸Xiao (2010).

There were always two kinds of views on the path of RMB appreciation in the academic circle. One kind of view believed that RMB appreciation should be completed at one go. Thus people could restrain the influx of speculative capital to the maximal extent. This was favorable to China's national strategic industrial distribution and macroeconomic regulation. And it conformed to China's own economic interests. But such measure caused too heavy impact on export and thus could easily cause domestic production capacity excess and assets bubbles. Another kind of view believed that people should adopt a steady and progressive mode in RMB appreciation and make decisions at proper timing on the basis of macroeconomic operation and rational expectations. Lin Yifu believed that the RMB exchange rate appreciation at present did not occur at a fast speed and raising exchange rate too fast was unfavorable to China's economic stability.⁶⁹ Yu Yongding believed that China could adopt the method of "graded leaps" to effect the appreciation of Renminbi.⁷⁰ Fan Gang pointed out that Renminbi was still very far from entering its depreciation zone and thus its appreciation should not be made at one go.⁷¹ Xia Bin believed that the appreciation at present should adopt the strategies of varying between dense and scattered distributions and between high and low differences so as to break the expectations on RMB appreciation.⁷²

In fact, RMB appreciation picked up speed from the exchange rate reform in 2005. Its accumulated appreciation already exceeded 20%. The central parity of RMB exchange rate went beyond eight in July 2006, seven in April 2008 and 6.6 in January 2011. Even under such a circumstance, international trade protectionism kept aggravating. In March 2010, 130 US senators jointly called for identifying China as an "exchange rate manipulator". It can be seen that the issue of RMB appreciation became increasingly complicated and difficult. Both the circle of theoretical study and the policy makers needed to be more clear-minded. They should draw from the lesson of the effect of the Plaza Accord between the United States and Japan and should not succumb to external pressure. They should adhere to the principles of spontaneity, controllability and progressiveness. They should endeavor to keep the value of Renminbi at a reasonable and balanced standard and maintain the general stability of China's macroscopic economy.

III. Discussion and Exploration on Speeding up the Process of RMB Internationalization

In recent years, China's central bank signed currency swap agreements with some countries and the Chinese government proposed to make preparations on implementing RMB international settlement and intended to build Shanghai into the "two centers" of international financial center and international shipping center. The

⁶⁹"Experts Argued on the Rhythm of RMB Appreciation: It Should Not Be Done at One Go", *China Securities Journal*, July 30, 2007.

⁷⁰Chen (2007).

⁷¹*China Times*, June 7, 2008.

⁷²"Experts Argued on the Rhythm of RMB Appreciation: It Should Not Be Done at One Go", *China Securities Journal*, July 30, 2007.

thought on promoting RMB internationalization at the policy level became increasingly clear. On the one hand, the circle of theoretical study achieved basic consensus on RMB internationalization. People generally recognized that the internationalization of a currency was the choice of the market. It could bring in international seigniorage revenue, reduce foreign exchange price risks in foreign-related economic activities and acquire “asymmetric” policy advantage. However, it could also cause China to face the dilemmas in monetary policy and fiscal policy and to become susceptible to speculative attacks and impacts of fake money. On the other hand, the scholars also carried out heated discussion centering round the practical feasibility and specific path of RMB internationalization from different angles.

There were mainly two types of views on whether China possessed the conditions for RMB internationalization.

One type of view believed that conditions were already ripe at present. Luo Xi believed that the constant growth of Chinese economy provided the strong driving power for RMB internationalization.⁷³ The world’s currency system reform provided a broad stage for RMB internationalization. The stability of China’s financial system provided the basic guarantee for RMB internationalization. Zhao Haikuan believed that there were four ready conditions for RMB internationalization, namely that China’s GDP already rose to the second place in the world, that China enjoyed very high credit status in international community that China had a very stable financial system, and that Chinese economy had increasingly higher degree of internationalization.⁷⁴ Liu Yihui believed that practical conditions were already in place when viewed from the medium term because China formed the advantages of huge deficit, large influence and strong international status in comparison with many developing countries.⁷⁵

The second kind of view believed that conditions were not fully in place. Ding Zhijie believed that the path of RMB internationalization extended from regional currency to international currency.⁷⁶ The influence of Renminbi was mainly present in Asia at present. Besides, there was not a complete, developed and open financial market for Renminbi. The capital could not flow completely freely. As an alternative choice, people could develop offshore financial market in Hong Kong and open up investment channel for overseas RMB investors. Wei Shangjin referred to the historical experience that US dollar became an international currency only 100 years after the United States achieved economic prosperity and pointed out that there was still some way to go before Renminbi became a mainstream international currency.⁷⁷ Chen Bingcai pointed out that RMB internationalization did not start at all and it was still uncertain whether the banks and enterprises of other countries would like to accept RMB settlement.⁷⁸

⁷³Luo (2009).

⁷⁴Wang (2009).

⁷⁵Liu (2009).

⁷⁶Ding (2009).

⁷⁷Wei (2009).

⁷⁸Chen (2009).

Zhao Haikuan believed that the Chinese government should adopt clear attitude and positive policy with respect to how to push forward RMB internationalization. People needed to support the initiative in the areas of politics, economy and diplomacy. They should positively push forward the full RMB convertibility under capital accounts and encourage RMB pricing and accounting. They should further improve domestic financial market and, in particular, bond market. Yu Yongding believed that current international financial crisis provided impetus for RMB internationalization. RMB internationalization was a progressive process mutually connected with the liberalization of capital accounts. But capital account liberalization was the necessary condition of currency internationalization but not a sufficient condition. Ren Zhigang pointed out that the development history of currency indicated that the importance of main currencies in international trade and finance would evolve gradually. But such evolution would be a relatively slow process. The extensive use of Renminbi in its present region and other places would be a progressive development process, which would ensure that various possible risks could be managed properly. Hong Kong could provide an ideal place of experimentation for RMB internationalization. This would contribute to the steady and successful implementation of relevant opening up measures. Luo Xi believed that RMB internationalization should follow a three-step strategy of currency use in adjacencies, regionalization and internationalization. People should further improve RMB exchange rate mechanism reform, strengthen financial reform and opening up, and build offshore financial market.

5 New Progress in the Theory of International Economic Cooperation

The accession to the WTO provided a broader stage for China to participate in international economic matters. There were very rich academic research that discussed international economic cooperation in combination with the influence of the accession to the WTO. These research pushed China to utilize multilateral trade systems and regional economic cooperation platforms, to participate in global governance and seek comprehensive interests maximization in globalized group gaming.

I. The Influence of the Accession to the WTO to the Transformation of the Economic Functions of the Chinese Government Was an Important Condition to Promoting International Economic Cooperation

One of the biggest challenges that China faced after its accession to the WTO was to transform government functions. The participation in the multilateral trade system of the WTO resulted in the changes in the inherent mechanism of the evolution of the systems in China. And the connotation of government system evolution was exactly the transformation of government functions. Such transformation was the key to pursue benefits and avoid harm in international economic relations after China's

accession to the WTO. And it also provided important conditions for expanding multilateral and regional economic cooperation.

The scholars of the Development Research Center of the State Council summarized the transformation of government functions into nine aspects: (1) China should support its own economy in the ways that conformed to the WTO rules. (2) The government changed from the sole formulator to one of the cooperators in policy formulation. And industrial organizations and market entities played an increasingly stronger role in policy formulation. (3) The target scope of policies extended from inside China to the regional areas and even to the whole world. (4) Part of the government powers were transferred to regional or international organizations. (5) Government functions were turned more to social policies. (6) Policies at state level were restricted by international rules more and more and the tendency of local decentralization reform grew stronger. (7) China showed widened view in policy making and external resources were attracted to resolve domestic issues. (8) China attached increasingly greater importance to the issue of economic security brought about by its opening up. (9) International cooperation in policy implementation became more and more important. Regional and international organizations had increasingly stronger functions and more and more complicated capacities.⁷⁹

Liu Guangxi summarized five basic rules through abstraction from the contents of the WTO agreements: All members were treated as the same and engaged in fair competition. Centralized management was implemented with openness and transparency. Enterprise-based principles were followed in open market. Intervention on market entities was reduced. And reasonable guarantee was provided flexibly with exceptions. These rules applied universally to the governments of WTO members. And China's WTO accession commitments had more concrete requirements on government function transformation. There were many special commitments related to the operation of macroeconomic environment at the policy and system level. And the economic system reform and government function transformation required by the WTO accession commitments at this level entailed radical transformation.⁸⁰

II. Explorations on Utilizing Multilateral Trade System to Create Favorable External Environment

The World Trade Organization was the most authoritative international organization in the world's multilateral trade system. Its influence was far larger than the economic capacity of the United Nations. After the accession to the WTO, China was always positively participating in and endeavoring to build a more reasonable global multilateral trade system.

Xue Rongjiu believed that China's accession to the WTO would promote the development of multilateral trade system in the following several aspects. First, the accession would make the World Trade Organization into the world's trade organization in the true sense. Second, China's opening up to the outside world would change from a unilateral, independent narrow-area one into a reciprocal, multilateral

⁷⁹Search group of the Development Research Center of the State Council (2002).

⁸⁰Liu (2003).

and all-round one. China would carry out open, fair and undistorted competition and cooperation with WTO members on the basis of the WTO multilateral trade system. Third, after its accession to WTO, China would provide more business opportunities to the WTO members in the world and promote mutual development and prosperity. Fourth, after its accession to the WTO, China would maintain the basic principles in multilateral trade system and earnestly and truthfully perform the commitments in the Accession Protocol to the WTO. It would work hard together with other WTO members to resolve difficulties that the multilateral trade system encountered and contain the aggravation of the bad trends so as to truly make the WTO into an integral more workable and enduring multilateral trade system.⁸¹

Wang Xinkui believed that to play a constructive role in multilateral trade system was the inevitable requirement and strategic choice for China to continue to unwaveringly adhere to opening up and to seize the right opportunity to push forward reform. Therefore, China needed to apply various rules fairly and reasonably and adapt itself to economic globalization so as to promote its own social and economic development. China needed to positively participate in the formulation of new rules. It should push forward the improvement of international economic order while maintaining its own interests. It should cooperate with developed country members, on the one hand, and with developing country members, on the other hand, so as to change the image of multilateral trade system as the rich club. China should fully consider the effect and impact of the development of Chinese economy to the outside world while enjoying the fruits of the accession to the WTO. It should respect and consider the interests of other countries so as to truly realize mutual benefit, win-win result, and joint development.⁸²

III. Discussion on Positively and Steadily Participating in Regional Economic Cooperation

From the beginning of the 21st century, regional economic cooperation with free trade zone as the main form exhibited a thriving trend. It increasingly became an important way for various countries to speed up realizing trade and investment liberalization and facilitation. The launch of China-ASEAN free trade zone in 2002 signified that China's regional economic cooperation entered the stage of accelerated development. The report of the Seventeenth CPC National Congress officially proposed positively implementing free trade zone strategy. At present, the rudiment of China's foreign economic cooperation framework was formed initially, which took the mainland China, Taiwan, Hong Kong, and Macao as the core, the participation in sub-regional economic cooperation and functional regional economic cooperation organizations as the means, and positively advocating and establishing new regional economic cooperation organizations as the orientation.⁸³

⁸¹Xue (2002).

⁸²Wang (2006, p. 8).

⁸³Yu and Wang (2006, pp. 304–321).

Zhao Jinping pointed out that implementing the state FTA strategy was the inevitable requirement of the long-term development of Chinese economy. China should take gradually establishing an open market system in which commodity and factor flew freely and domestic and foreign economies integrated with each other as the fundamental goal in foreign economic system reform. People should push forward institutional cooperation with neighboring countries and, first of all, realize the economic integration within regional scope and the cross-border free flow of factors. Thus it would be completely possible to accumulate experience and create conditions for achieving the goal of the open economic system reform.⁸⁴

Li Xiangyang believed that positively participating in regional economic cooperation was a strategic choice of China to adapt to the development of economic globalization. It was absolutely not an expedient choice. Participating in regional economic cooperation could, to a certain extent, create a good external environment for avoiding globalization risk, improving China's influence in formulating international economic rules, and contributing to the maintenance of the security and stability of its neighborhood. As a major country, China needed to consider not only the static economic benefits related to trade but also dynamic economic benefits and noneconomic benefits when evaluating the benefits of participating in regional economic cooperation.⁸⁵

Yu Lixin, Wang Jiajia proposed that the strategic goal of China's foreign regional economic cooperation should be as follows: China should firmly base its action on the homeland and speed up the cooperation process between mainland China, Taiwan, Hong Kong and Macao. China should take root in Asia and pursue forming regional or sub-regional economic cooperation organization with its neighboring countries. China should break boundaries, go beyond continents, and construct a global cooperation network. As far as specific measures were concerned, people should pay attention to bringing into play at the microscopic level the leading role of the government in constructing the framework of regional economic cooperation organizations. They should also pay attention to bringing into play at the microscopic level the role of the enterprises as microscopic entities and relying on the transnational operation of the enterprises to promote the process of regional economic cooperation. Besides, they should also stress on the progressive nature of the development of regional economic cooperation and pay attention to getting in line with international practice, to handling relevant matters according to the rules of the market economy, and to conceding short-term interests for long-term interests.⁸⁶

⁸⁴Zhao (2003).

⁸⁵Li (2005).

⁸⁶Yu and Wang (2006, pp. 304–321).

6 New Progress in the Legal System Construction for Foreign-Related Economy

I. Abortion, Modification and Legislation of the Laws on Foreign-Related Economy

Around the accession to the WTO, experts in the circles of economics and jurisprudence all proposed that there were inherent connections in spirit between Chinese current legal system and the WTO rules. However, people need to further enrich and improve Chinese legal system on market economy so that it would become more conformant to the common principles of market economy and completely consistent with the WTO rules.

Long Yongtu pointed out that three changes would occur to China's opening up to the outside world after its accession the WTO. First, China's economic development and international cooperation would face better international economic environment. China would engage in foreign economic trade activities in accordance with internationally accepted rules. Second, China would establish a stable transparent and predictable legal system that conformed more to the needs of socialist market economy. It would also establish a fairer and more orderly market economic environment. Third, China would establish an opener policy environment.⁸⁷ Cao Jianming pointed out that China's accession the WTO would, in general, form a more favorable situation for China's economic development and processing of foreign-related economic and trade cases.⁸⁸ But further adjustment needed to be made in the aspects of market access, tariff lowering, national treatment of foreign-invested enterprises, limitations on the quality of foreign investment, and judicial protection of intellectual property right. Wang Jiafu pointed out that China's current economic laws were consistent with the WTO rules.⁸⁹ But people needed to further exhibit the philosophy of the legal system of market economy in legislation and thoroughly implement the principles of national treatment and unification of legal system. They needed to realize the spirit of fair competition and strengthen the transparency of the law. For such purpose, China needed to formulate its civil code, complete foreign investment law, improve foreign trade law, and strengthen the promotion of the legislation on the development of knowledge economy. Li Xiaoxi pointed out that there were the three prominent defects of inconsistency incoordination and non-transparency in China's current laws and regulations with the WTO rules when they were compared with the WTO's requirements.⁹⁰ People needed to establish as quickly as possible special notification and consultation institutions and build a transparent, unified and fair legal system that could be supervised easily. Wang Liming proposed that China should take the opportunity of its accession to the WTO to get in line with international

⁸⁷Long (2002, p. 5).

⁸⁸Cao (2001).

⁸⁹Wang (2001).

⁹⁰Li (2009a).

practice.⁹¹ In order to push forward building and improving China's legal system for socialist market economy, people needed to, first of all, to formulate a full set of laws on finance, insurance, telecommunications, commerce, foreign trade, and aviation and gradually link their contents with the *General Agreement on Trade in Services*. People needed to formulate anti-dumping law as quickly as possible. People needed to coordinate, modify and unify the provisions related to super-national treatment and non-national treatment in the "three major laws on foreign investment" in accordance with the requirements on the accession to the WTO. People also needed to improve and complete building the prevention mechanism and internal control system for legal risks in state-owned commercial banks.

From the end of 1999 to 2002, China sorted out over 2300 laws, regulations and departmental regulations of various kinds in accordance with to the WTO rules. China also adopted the measures of abortion, modification and legislation on the systems of laws and regulations on goods import and export. It promulgated successively the *Regulations on the Management of Goods Import and Export* and ten supporting department regulations, which covered various aspects in China's import and export management system. On the basis of the spirit of the notice of the central government published in September 2001, local governments at various levels comprehensively sorted out over 190,000 local rules, regulations and policy measures according to the principles of unification of legal system, nondiscrimination, and openness and transparency. In July 2004, China promulgated the revised Foreign Trade Law and changed the examination and approval system of foreign trade, which had been implemented for 50 years, into registration system. A three-level legal framework system on foreign trade management was formed initially. China improved and revised the laws and regulations on an intellectual property right protection and strengthened the protection of intellectual property right. It further improved a unified, fair and transparent foreign-related economic legal system that was adapted to the needs of socialist market economy which better adjusted various economic relations between Chinese and foreign economic and entities.

From the beginning of the 21st century, China participated more positively in the revision of old international economic and trade conventions and also in the formulation of new ones and practically performed the WTO accession commitments of a responsible major country. From 2003 to 2008, the Standing Committee of the Tenth National People's Congress ratified together 74 treaties protocols and agreements that China concluded with foreign countries. In 2009 seven more were ratified.

⁹¹Wang (2000).

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Chapter 26

Reviews and Prospects on the Theoretical Study on Transition Economy



Tianqi Mao

Transitional economics became a hotspot research topic that emerged in the research area of the theoretical economics in the 1980s in response to the needs in the practice of marketization reform. The study of transitional economics took the practice of the transformation from planned economy to market economy in China as the basis and referred to the experiences and lessons of transition countries in the international community. It made comparisons on the historical process of the vertical institutional change of the same country and the experiences and lessons of the horizontal institutional change of different countries. Through the comparison, people clearly identified specific characteristics of the planned economic systems and found out where the start point of transition study was. People clearly found out what kind of transition strategies and paths different countries had adopted and what kind of path transition study should take. People also clearly found out what kind of market economy different countries could establish eventually and studied what the target model of transition in different countries was. The study of this emerging discipline covered a series of most fundamental theoretical and practical issues on transition and development, such as where a transition country should start with, where it should go, and what the path was.

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1 The Objects and Methods of the Study in Transition Economics

I. The Start Point of Economic Transition: Transition Causes and Reflection on Traditional Economic Theory

Generally speaking, poor economic benefits or low efficiency was the deep-level cause that made China and former socialist countries abandon centralized planned economic system and turn to practice market economic system.

From 1949 to 1979, China practiced centralized planned economy for 30 years. Although it had achieved some successes, there had also been major economy fluctuations nationwide. Statistical data showed that China's economic growth during the thirty years was fast in fact. But China's economic structure was disproportionate and more weight was given too heavy industry and less to light industry. Its statistical system only calculated newly-added product, which resulted in repeated calculation. As a result, what people actually felt was completely different from what was in governmental publicity. What the common citizens felt in person was that they were still very poor in daily economic life after they worked hard on socialism for 30 years. Deng Xiaoping said frankly, "We are too poor and too backward. To be honest, it's not fair for people."¹ "During the whole period of 20 years from 1958 to 1978, peasants and workers had very little income increase and very low living standard. Productivity did not have much development."² He also said, "China's national income ranked around twenty something counting backwards, as one of the poor countries, among over one hundred countries in the whole world. One of the manifestations of the superiority of socialism was developing social productivity at a high speed. If the speed of its social productivity development was slower than that of capitalism, it has no superiority."³ These judgments of Deng Xiaoping truthfully expressed the actual feelings of common citizens in China.

Radically speaking, the low efficiency of centralized planned economy came from the misunderstandings on several important issues in economic theory. The starting and process of transition always concerned the true clear understanding of these issues.

(I) What Kind of Social Development Stage China Was in?

Clearly understanding the social development stage that China was in was the basis for formulating economic, social and political policies. In 1940, Mao Zedong proposed the program of New Democracy. But he proposed a different set of theory on social development stages after 1953, in which he wanted to accelerate the socialist transformation in handicraft industry and individual commerce.⁴ Soon after it was

¹*Deng Xiaoping Chronicles*, pp. 89–90.

²*Selected Works of Deng Xiaoping*, Vol.3, p. 115.

³*Deng Xiaoping Chronicles*, p. 83.

⁴How should people evaluate the socialist transformation of the ownership system of the means of production in middle of the 1950s? It was pointed out in the document of *Resolution on Several*

declared that the fundamental system of socialism was basically established in China. Although it was still specifically proposed at the Eighth CPC National Congress that the primary task was developing social productivity, Mao Zedong believed that the rightist force, including the intelligentsia, attempted to overthrow the communist party. As a result, anti-rightist struggle was deployed nationwide from May 1957, which called for carrying out revolution constantly on the ideological frontiers. From then on, Mao Zedong kept launching political movements to transform productive relations, calling his initiative “speeding up the transition toward communism”. However, China was dragged into an unprecedented great famine, starting from the second half of 1959, in which thousands of people died of hunger.⁵In August 1962, Mao Zedong proposed at the Tenth Plenary Session of the Eighth CPC Central Committee that there were the class struggle between the proletariat and the bourgeoisie and the struggle between the two roads of socialism and capitalism during the entire historical periods of proletariat revolution and dictatorship which might last several decades or even longer. This was in fact the theory of “continuing to carrying

Historical Issues of the Party since the Founding of the People's Republic of China in June 1981 that “After the summer of 1955, the cooperative transformation of agriculture and the transformation of handicraft industry and individual commerce showed too rash requirements, too rough work, too fast change and too simplistic and monotonous form so that some problems were left unsolved over a long period of time. After the transformation of capitalist industry and commerce was basically completed in 1956, the use and handling of some of the former industrial and commercial workers was rather improper.” However in the circle of and theoretical study, there were always different views on the judgement of the nature of the issues that occurred in this period. Bo Yibo reviewed this period of history in 1991. He said that the socialist transformation of agriculture violated the principle of voluntariness and it was completed with the dual means of political movement and economic measures. If people did not hurriedly and immediately carry out the transition towards socialism or shake private ownership but continued to implement the policies of new democratism after the land reform, it might be more favorable to the development of productivity. He also said that it was inevitable that polarization occurred in the countryside after land reform and it was the inevitable product of the development of commodity economy. He affirmed in particular the view that Liu Shaoqi supported at the time. He also particularly proposed very different views on the socialist transformation of handicraft industry. He believed that individual handicraft industry was different from individual agriculture. People in the industry did not have much means of production. They were small commodity producers and their production and sale activities depended on the market. The industry was characterized by numerous trades and flexible operation. Many technologies with specific ethnic features were passed on in the way that a master taught his apprentices. Therefore, it was a social transformation that “takes shape under the guidance of incorrect theory” those cooperatives were formed blindly in individual handicraft industry and, later, they were changed into cooperative factories operated by cooperative associations or directly into local state-owned factories.

⁵In the second volume of *A Review on Several Important Decisions and Events*, Bo Yibo recorded a sentence from a folk song that “On the Mount Lu, a person was wrongly criticized/ And thousands were starved to death nationwide”. He also said that people nationwide suffered from malnutrition because of food scarcity during the Three Years of Difficult Time. Edema disease became epidemic and mortality rate increased because of famine in many villages in the countryside. According to statistics, total national population decreased by over 10 million in 1960. Chinese communists felt greatly sorry for the citizens when such terrible thing occurred during the period of peaceful construction. According to the record on page 91 in *China Statistical Yearbook* in 1986, China's total national population did not increased from 1958 to 1961 and decreased by 13.46 million from

out revolution under proletariat dictatorship”. After 1976, the whole CPC cleared out the left-deviated wrong tendency and reflected on Mao Zedong’s social development theory. Right before the convening of the Thirteenth CPC National Congress, Deng Xiaoping pointed out that “Socialism itself is the primary stage of communism. And China is in the primary stage of socialism, namely an underdeveloped stage. Everything needs to start with this reality and planning needs to be made on the basis of this reality”.⁶ The Thirteenth CPC National Congress systematically expounded the primary stage of socialism. The Fifteenth CPC National Congress further specified the main economic tasks that China needed to complete in the primary stage of socialism and clearly and specifically proposed that the primary stage of socialism ‘needs to last at least one hundred years’. Because of this, whether it was favorable to the development of productivity became the start point for considering all the issues and the radical standard for testing all work in this historical period. Today, people also incorporated guaranteeing and realizing social fairness and justice into the intrinsic tasks of the primary stage of socialism so that economic development had new scientific outlook as its guarantee.⁷

The theory of the primary stage of socialism corrected deviations in Mao Zedong’s left-deviated social development theory. It accurately identified that China was still in the primary stage of socialism and specifically defined the main tasks in this stage. Thus, it thoroughly corrected Mao Zedong’s social development thought in which people took class struggle as the guiding principle and engaged in transition in poverty.

(II) What Kind of Socialism Did China Need?

China built socialist economy on the ruins of a semi-feudal and semi-colonial society. The country had weak economic foundation, large population, scarce farmland, and very imbalance economic development standard. When building socialism in a nation with relatively backward economy and culture like China, people first had to concentrate their energy on developing social productivity in order to realize the tasks of industrialization and the socialization, marketization and modernization of the economy that many other countries had realized under the condition of capitalism.

Marx and Engels lived in the early period of capitalism after its birth in which cruel primitive capital accumulation resulted in very sharp social conflicts. On the basis of exposing the fundamental contradiction in capitalist society, Marx foresaw in *On Capital* that the society that would replace capitalism was a society without classes in which all the means of production were owned by the whole society. He called such

1959 to 1961. In a paper written in 1999, Lin Yifu analyzed the reason that caused the famine in China from 1959 to 1961 with the methods in econometrics through the study on food supplies and entitlements. The main reason was the deprivation of food entitlements. The additional mortality caused by the crisis totaled about 30 million and urban, rural and regional mortalities varied. The disaster should be mainly attributed the systems and policies in planned economy. See Lin Yifu, *Another Discussion on System, Technology and China’s Agricultural Development*, Peking University Press, 2000.

⁶ *Selected Works of Deng Xiaoping*, Vol.3, p. 252.

⁷ See Wen (2007).

a society the communist society. It needed to be pointed out that the conclusion that Marx drew in *On Capital* was only limited to the countries in Western Europe.⁸ And Marx and Engels did not have any practice on the conclusion. From implementing wartime communism to implementing new economic policies, Lenin held an attitude of exploration on the issue of what socialism was. However, after Stalin published *Issues on the Socialist Economy in the Soviet Union*, the socialism with centralized planned economy as its main characteristic became a fixed model that spread on the globe. China copied the soviet model over a long period of time. In 1985, Deng Xiaoping said, “What on earth is socialism like? The Soviet Union worked on that for many years, but they did not figure it out clearly and completely. ... Later, the Soviet model became rigid.”⁹ On the basis of acquiring academic materials, people earnestly studied the ideological legacies over generations. There were in fact no fixed models for socialism. How could different countries build socialism with the clear country-specific regional and ethnic features? At the Twelfth CPC National Congress, Deng Xiaoping specifically proposed the new proposition of “building socialism with Chinese characteristics” and distinguished it from the rigid model of socialism of the former Soviet Union. He also explained in particular that, “Although we are building socialism now, we’re not qualified for it in fact. Only when it comes to the middle of the next century and China reaches the level of a moderately developed country can we say that we truly build socialism and can we say with good confidence that socialism is superior to capitalism.”¹⁰

The proposal of the theory of socialism with Chinese characteristics thoroughly negated Stalin’s model of socialism in the Soviet Union and made clear the wrong understandings of the Chinese people on theory of socialism.

(III) Whether the Market Economy Was an “Alien” Demon?

The natures of market economy and planned economy perplexed the circle of theoretical study for a long time. When viewed from the classical literature available, Marx never used the concept of planned economy. When talking about the future society, he generally used the concepts of “planned”, “conscious”, “spontaneous”, and so on. Engels once treated “planned organization” as the opposite of capitalism. He said that, once the society possessed the means of production, the anarchy inside

⁸ *Complete Works of Marx and Engels*, Vol.19, pp. 268–269. In 1880s, the Marxist group in Russia, namely the labor liberation society, had an argument in their study of *On Capital* when associating to rural communes, which were generally present in Russia at the time, and also on the Russian revolutionary process generated on the basis of such situation. A member of the group wrote directly to Marx on February 16, 1881 to ask about the question. He mentioned in particular in his letter, whether the historical necessity that you mentioned in *On Capital* was applicable to all countries in the world? After he received the letter, Marx made in-depth research on the social and economic conditions in Russia and wrote four manuscript replies successively. In the reply dated March 8, 1881, he said that the deprivation of peasants and “the ‘historical necessity’ of this movement” that the deprivation of the depriver would definitely occur were specifically limited to the countries in Western Europe and not applicable to the backward countries in the east.

⁹ *Selected Works of Deng Xiaoping*, Vol. 3, p. 139.

¹⁰ *Ibid*, p. 225.

social production would be replaced by planned and conscious organization.¹¹ But he also did not use the concept of planned economy. At the end of the 19th century, Engels changed his views in the past as monopoly emerged in some major industrial departments. He said that, if we examined the joint-stock companies and also the trusts that controlled and monopolized the entire industrial sector, we would find that private production stopped in there and that planning was also absent.¹² Lenin was the first person who put planned economy and market economy in opposition and treated them as social systems the earliest. But he did not become rigid because of this.¹³ Stalin always tied planned economy and socialism tightly together and believed that market economy was solely reserved for capitalism. China's theoretical economics was limited by the models in the Stalin's *Issues on the Socialist Economy in the Soviet Union* for a long time. These models controlled the Chinese circle of economic thought for nearly 30 years. Anyone who dared to talk about market economy and the views related to it in the academic circle might be subject to extreme political punishment. On November 26, 1979, Deng Xiaoping said, "It is definitely incorrect to say that market economy only exists in capitalist society and there is only capitalist market economy. Why cannot people do market economy in socialism ... Market economy has burgeoned early in the period of feudal society. People can do market economy in socialism."¹⁴

It was the challenge and rectification to the traditional theory of Marxism that people could also do market economy in socialism. It became the general guiding thought for China's economic transformation and social development.

II. Basic Theory on Economic Transition: The Establishment of the Theory of Market Economy in China

The existence of market economy was in fact already a history of several hundred years. The effectiveness of market economy always depended on how to rationalize the relationship between market and government in different countries in different historical development stages in these several hundred years.

In the middle of the 18th century, abolishing feudal barriers and increasing national wealth became the main task of industrial capitalists. In the book *The Wealth of Nations* that Adam Smith wrote in 1770s, he discussed for the first time the operation rules of completely free market economy and furnished the necessary ideological materials for free market economy. However, in the 1920s, the British economy,

¹¹ *Selections of Karl Marx and Friedrich Engels* Vol.3, People's Publishing House, 1972, p. 323.

¹² *Complete Works of Marx and Engels*, Vol.22, p. 270.

¹³ In 1906, Lenin said that, as long as monetary power and capital were preserved, any law in the world was unable to eliminate inequality and exploitation. Exploitation could be eliminated only when people implemented huge socialized planned economic system and, at the same time, gave the ownership of all lands, factories and tools to the working class. But after more than 10 years passed, Lenin spoke highly of Engels' view that capitalism was also a kind of planned economy on the basis of the new situations that emerged in the development of capitalism at the Seventh Congress of Social Democratic Party of Russia in 1917. He recognized frankly that capitalism was transforming towards its higher planned form.

¹⁴ *Selected Works of Deng Xiaoping*, Vol.2, p. 236.

which experienced completely free market development, encountered serious crisis and depression. The unemployment of a large number of workers resulted in a series of social and economic issues. In 1930s, John Maynard Keynes published *General Theory of Employment, Interest and Money*, in which he systematically criticized laissez-faire economic thought and proposed the idea of the government's intervention in economy. Around the time of the World War II, major capitalist countries, such as the UK and the USA, all adopted Keynes's policy suggestions and the Roosevelt New Deal achieved good effect in the USA. Adam Smith and John Maynard Keynes created two types of different frameworks for market economy theories in different historical periods. And various schools in economics after them all were basically generated from these two types of different theoretical frameworks and exerted their influence on the social and economic development of various countries. For example, the neoclassical synthesis school in the middle of the 20th century, represented by Paul A. Samuelson and Alvin Harvey Hansen in the USA, and the neo-Cambridge school, represented by Joan Robinson in the UK, developed Keynes economic thought in the aspect of attaching more importance to the role of the government. For another example, the neoclassical school, represented by Alfred Marshall in the UK in the end of the 20th century, and monetarism, represented by Milton Friedman in the 1970s, developed the completely free market economic thought of Adam Smith in the new period. In particular, monetarism had extensive influence in the current world and even infiltrated in the decision-making thought of transition countries. In addition, the Freiburg school in Germany and the neo-institutional economic school, represented by John Kenneth Galbraith in the USA, both started with the fundamental issue of how to rationalize the relationship between government and market and formed different schools in modern economics. And different models of modern market economy emerged under different cultural backgrounds in different countries.

From 1949 to 1979, the Chinese academic circle made arduous exploration on the relationship between planning and market under very austere political environment. In the middle of the 1950s, Sun Yefang examined the disadvantages of planned economy and believed that the law of value was the law of the existence and movement of value. It was a natural law that could not be abolished in any socialized mass production. As socialized production, socialist economy also contained the mechanisms for the law of value to play its role. Under the general theme of the theory of the internal cause of the law of value and the theory of the external cause of commodity production, he emphasized in particular the decisive role of value because the law of value could promote the improvement of social labor productivity. He also emphasized in particular the role of exchange at equal values because the law of value could urge the enterprises to do well their economic accounting. As long as people carried out exchange at production prices, calculate the consumption of living labor and materialized labor, namely the effect of funds occupation, on the basis of the profit rate of funds, they could realize the roles of the law of value and exchange at equal values. Sun Yefang made sharp criticism on the centralized planned economic system on the basis of the theory of the internal cause of the law

of value and theory of the external cause of commodity production.¹⁵ In the same period, Gu Zhun proposed market regulation theory. He believed that the law of value played an important restrictive role on planned economy. The law of value regulated the production and circulation of not only the means of consumption but also the means of production. The regulatory role of the law of value to social production was realized through economic calculation. One important method for this was to create close connections between the material remuneration of workers and the profit and loss of the enterprises and to make price an important instrument to regulate production.¹⁶ The theory of the internal cause of the law of value of Sun Yefang and the market regulation theory of Gu Zhun touched the soft spot of centralized planned economy. The scholars were given very unfair treatment because of them: imprisonment. At the end of the 1950s, Chinese academic circle did discuss the topic that “the law of value is a great school”. But that was just using the law of value during the time of economic difficulty because, deep in the heart of the power holders, the law of value was just like a maid in the court, who was on call at any moment. The criticism on market economy reached its peak from 1966 to 1976. It was said that the law of value was an alien force and commodity exchange was the hotbed, soil and so on for the generation of capitalism and bourgeoisie so that they had to be limited by means of proletariat dictatorship.

Confronted with the impending crisis of the collapse of national economy, many Chinese economists reflected on the issues related to commodity, money and market from the second half of 1978 and proposed that people should bring into play the role of the law of value. Sun Yefang proposed once again that, of all kinds of economic laws and principles, the law of value was the primary one. Competent departments in charge of comprehensive national economic work also organized the re-study of Sun Yefang’s views that had been criticized in the past, such as basing planning on the law of value. Xue Muqiao proposed that people should use the market to invigorate circulation and establish proper reputation for long-distance goods transportation for sale. Li Xiannian openly proposed the slogan of “combining planned economy and market economy”. In this period, Deng Xiaoping said that people could do market economy in socialism. However, these views did not have much influence on the circle of economic theories and decision-making departments because the idea acceptable to the people in- and outside the CPC at the time was to adopt some measures of market regulation under the premise of implementing planned economy so as to increase the flexibility of socialist economy and to satisfy various needs of the people in life. In September 1980, the Economic System Reform Office of the State Council proposed relevant opinions on the economic system reform, in which it was said that the direction of economic system reform should be that people consciously utilized the law of value and changed from implementing monotonous planned regulation to fully bringing into play the role of market regulation under the guidance of planning under the condition of adhering to the dominance of the public ownership system of the means of production and on the basis of the requirements

¹⁵Sun (1956, 1959).

¹⁶Gu (1957).

in developing commodity production and socialized mass production. Xue Muqiao gave such an explanation on the idea: Proposing that China's socialist economy at present stage was the commodity economy in which the public ownership system of the means of production dominated and multiple economic sectors coexisted jointly represented a challenge against the dogmatism that enjoyed a dominant status for thirty years. Hence, the proposal resolved the question in what form people should build socialist economy on the land of China. The solution to such a question was an important development in Marxist doctrine of socialism. In this period, Zhao Ziyang implemented the pilot project on "expanding enterprise autonomy" in Sichuan and Wang Li implemented the pilot project on "fixing farming output quotas by household" in Anhui. These two types of reform opened the gate for fully bringing into play the role of market forces and also raised the curtain on China's transformation from planned economy into market economy.

However, in the process of drafting the political report of the Twelfth CPC National Congress, Hu Qiaomu organized the discussion on and transmitted with his notes a letter sent to him from five comrades including Wang Rengzhi and Yuan Mu. This letter sharply criticized the view of the circle of economics about bringing into play the role of the law of value. Because of misguidance of this letter, some major newspapers and magazines published many articles that criticized the view that stressed on the role of the law of value and market regulation from 1982 to 1983. Xue Muqiao had to make open self-criticism at a meeting because he said that "Most of the planned regulation has to be realized through market regulation". In September 1984, Zhao Ziyang wrote a letter to other members of the Standing Committee of the Political Bureau of the CPC Central Committee and said that the representation that planning came first and the law of value second was inaccurate and people should better not to continue to use it any more. He also said that socialist economy was planned commodity economy with public ownership system as the basis. People should realize planning through the law of value and utilize the law of value to serve planning. This opinion won the support of Deng Xiaoping, Chen Yun and others.¹⁷ It was said in the resolution at the Third Plenary Session of the Twelfth CPC National Congress held in October 1984 that people had to take the law of value as basis consciously and apply it in socialist planned economy, which was planned commodity economy based on public ownership system. Fully developing commodity economy was a stage in social and economic development that could not be omitted and also a necessary condition for realizing China's economic modernization. Only when people fully developed commodity economy could they truly invigorate economy and urge various enterprises to improve efficiency, operate flexibly and sensitively adapt themselves to complicated and ever-changing social demand. And this was something that people could not achieve relying on administrative means and mandatory plans. Deng Xiaoping praised the resolution that "the document on economic system reform this time is good. It explains what socialism is. Some words are what our ancestors have never said before. These are new things. I feel that we get it clarified." He also

¹⁷Zhang et al. (1998).

said that the document was “the political economics that combines the fundamental principles of Marxism and the practice of socialism in China”.¹⁸

The circle of economic theories also broke through the concept of market only understood in the sense of the market of consumer goods and emphasized that people should develop capital market, labor market, and technology market. Hence the term market was transformed from a concept about the buy and sell of consumer goods to a scientific category about the fact that market could allocate resources. On February 6, 1987, right before the convening of the Thirteenth CPC National Congress, Deng Xiaoping and several central leaders purposefully talked about the issue of planning and market and pointed out that planning and market were both means. In the past, China learned from the Soviet Union and engaged in planned economy. Later people said that China took planned economy as the main means. Now people should not talk about this anymore. The political report of the Thirteenth CPC National Congress comprehensively summarized the practical experience since the reform and opening up. It did not mention the term “planned economy” any more but proposed the assertion that both planning and market covered the entire society in socialist economic system. On the basis of this thought, it was proposed specifically that the system for socialist planned commodity economy should be a system with the intrinsic unification of planning and market. “The new economic operation mechanism should be in general a mechanism in which the state regulates the market and the market guides the enterprises.”

After the Thirteen CPC National Congress, the circle of economic theories became unprecedentedly active. Ma Hong wrote in his article that China’s economic system reform was to replace traditional mode of resource allocation in which administrative orders dominated with the mode of resource allocation based on market mechanisms. In other words, the socialist planned commodity economy that China wanted to establish through reform was a kind of economy in which the market under macroscopic management was utilized to allocate resources. In this sense, it could also be called socialist market economy. People needed to further liberate thought and establish a proper reputation for market economy. This was very important for establishing the new economic operation mechanism in which the state regulated the market and the market guided the enterprises.¹⁹ Yu Guangyuan wrote in his article that the plans in market economy should have larger flexibility and better features to adapt to market situations. People should discard the planning models that took fixed goals that allowed no flexibility as their goals.²⁰ Xue Muqiao wrote in his article that he advocated that people did not talk about the theory of the three pieces of mandatory plans, guidance plans and market regulation. Were market regulation and market economy of two kinds of substances that allowed no confusion? People needed to have good discussion about it. China always used to the term market economy and not market economy while the Soviet Union only used the term market economy and

¹⁸*Selected Works of Deng Xiaoping*, Vol. 3, p. 83, p. 91.

¹⁹Editorial Group of the Guangdong Provincial Market Economics Society ed., *Market Economy in the Primary Stage of Socialism*, Dongbei University of Finance and Economics Press, 1988, p. 3.

²⁰Yu (1988).

not commodity economy. China used to the term planned commodity economy while the Soviet Union the term regulated market economy. Xue believed that these were of the same substance. None should be equalized to capitalism as long as people retained the dominance of the public ownership system of the means of production.²¹ Wu Jinglian wrote in his article that neoclassical economics analyzed the operational mechanism of commodity economy and explained how it effectively allocated resources through the operation of market mechanism. Market was identified as the operation hub of commodity economy. Therefore, commodity economy was generally known as market economy. The so-called market economy was the kind of economy in which the allocation of resources was guided by the market. So the term market economy was established on the basis of the operation mode of economy, namely the mode of resource allocation from the very beginning.²² In this period, Chinese economists adhered to thinking independently and provided very sufficient theoretical basis for China's marketization reform.

At the end of 1980s, a political turmoil occurred in China. Some politicians and theorists took advantage of the temporary difficulty present in organization reform and launched an attack on the reform line proposed at the Thirteenth CPC National Congress and also the discussion about market economy in the circle of economic theories. These people said that the reform and opening up introduced capitalism and the main danger of the peaceful evolution from socialism back to capitalism came from economic area. At the time, there was an overwhelming wave of articles that criticized marketization reform which caused new ideological chaos. The retrogression in ideology resulted in a standstill of marketization reform. Under such a circumstance, Deng Xiaoping traveled to South China to directly face the mass and delivered an inspiring and refreshing talk on the relationship between planning and market. Deng Xiaoping's South Tour Talk was of very important meaning to the establishment of the theory of socialist market economy. He pointed out poignantly, "Some people dare not to make big steps and advance boldly in the reform and opening up. In the end, it is because they fear that there are too many capitalist things and China takes the road of capitalism. The key here is the issue of whether being capitalist or socialist in nature. The criteria of judgment should mainly be whether it is favorable to developing the productivity of socialist society, to enhancing the comprehensive national strength of the socialist country, and to improving the living standard of the people." "Whether there is more planning or market is not the substantial difference between socialism and capitalism. Planned economy is not equal to socialism. There is planning in capitalism. Market economy is not equal to capitalism. There is market in socialism. Planning and market are both economic means."²³ Deng Xiaoping's talk won warm welcome from the extensive community of the people. In March 1992, specific provisions were formulated on the issue of the relationship between planning and market at the meeting of the Political Bureau of the CPC Central Committee. It was pointed out that planning and market were both economic means. People should

²¹ *Special Zone Times*, January 4, 1991.

²² See *Social Sciences in China*, Issue 6, 1991; Wu (1991).

²³ *Selected Works of Deng Xiaoping*, Vol. 3, pp. 372–373.

be good at applying this means to speed up developing socialist commodity economy. Under such circumstances, numerous comrades in the circle of economics in China published a series of opinions on the basis of the development of Marxist theory and China's actual process of reform and, in particular, on the basis of Deng Xiaoping's in-depth thinking on China's economic construction and system reform. They suggested that the discussions and statements on the issue of planning and market from the Third Plenary Session of the Eleventh CPC Central Committee be raised to a new height. It should be specifically stipulated that the goal of China's socialist economic reform be the establishment of market mechanism, namely replacing the mode of resource allocation based on administrative orders with that based on market mechanisms. Only in this way could people more accurately and clearly express the substance of China's economic system reform and lay the theoretical foundation for formulating China's trans-century economic development program. In October 1992, the Fourteenth CPC National Congress announced that the goal of China's economic system reform was building socialist market economic system. In the *Decision of the CPC Central Committee on Several Issues on Building Socialist Market Economic System* made at the Third Plenary Session of Fourteenth CPC Central Committee in November 1993, a brilliant blueprint was drawn for building socialist market economic system at the end of the present century.

The establishment of market economy theory in the Chinese circle of economics experienced a long historical process and many economists paid the cost of blood for it. When looking back at present at the road that the circle of economic theories had taken, people all felt deep regret: In certain period, there was just too narrow and too cruel social environment for the independent thinking of economists. Without Deng Xiaoping's epoch-making theoretical judgment that "people can do market economy in socialism", the circle of economics might still be groping in the cold in the contention on this theoretical issue.

III. The Goal of Economic Transition: The Basic Framework of Socialist Market Economic System

With the clarification and return to the truth in economic theory, China started the transition from centralized planned economic system to market economy at the end of 1970s. And the basic framework of the new system of socialist market economy was formed in the practice of transition.

In the first stage of transition, the priorities were in the countryside. In the Third Plenary Session of the Eleventh CPC Central Committee held in December 1978, people initially summarized the tortuous road that China's rural areas went through in their development and supported the experiences that came from practice so that the improved rural household contracted responsibility system achieved general development. During the same period, the state largely raised the purchase price of agricultural and sideline products and the peasants received rich benefits from such price rise. With these reform measures, China's agriculture achieved rapid development in the beginning of 1980s. The supply of main agricultural products changed from long-time shortage to basic self-sufficiency. The subsistence issue of the Chinese people was initially resolved. The thriving and development of township and town

enterprises was another new development in the rural economic system reform in this stage. It not only opened new sources for state fiscal revenue but also offered jobs to large amounts of surplus labor in the countryside. The three reform measures in the countryside at the time braved out a new path for China's agricultural modernization and rural urbanization.

After the Third Plenary Session of the Twelfth CPC Central Committee in October 1984, the priorities of the transition were transferred into the city, which mainly involved state-owned enterprises. On the one hand, state-owned enterprises held in the deposition and operated large amounts of state-owned assets and, on the other hand, they provided the fiscal revenue that the state needed. However, centralized planned economic system could not coordinate these two aspects so that investment could not yield matching output. Therefore, it was specifically pointed out in the decision on economic system reform in 1984 that strengthening the dynamism of state-owned enterprises was the central link in the entire economic system reform with the city as the priority. However, the reform of state-owned enterprises at the time had a prominent characteristic, namely highlighting contracting. In the area of the relationship between the state and the enterprises, people took adjusting profit distribution as the main line and successively implemented production operation responsibility system, replacing profit submission with tax payment, and contracting system. In support to enterprise reform, "serving meals to different diners from different pots", namely the system of dividing revenue and expenditure between the central and local governments and holding each responsible for balancing their budgets, was practiced in the area of the fiscal relation between central and local authorities. In comparison, price system reform was changed from mainly adjusting to mainly opening up. The prices of consumer goods for daily life were gradually opened up. But within certain period, double-track prices were practiced in the pricing of the means of production. This could naturally play a stimulating role to production, but it also provided the conditions for the corruption of some law breakers.²⁴

The Fourteenth CPC National Congress held in 1992 summarized the experiences in the reform and made a general description on what socialist market economic system was. It was required that people should endeavor to guide the sale, supply and production of the enterprises through price signals, realize the selection of the superior and the elimination of the inferior in open and fair market competition, and allocate scarce economic and natural resources to the industries that the society needed the most. It was also required that the state should regulate the market and correct the defects of the market through economic policies, laws and regulations and various economic parameters. The Third Plenary Session of the Fourteenth CPC Central Committee held in November 1993 further outlined the basic framework of socialist market economic system, which included the following: People should adhere to the guideline of taking public ownership as the dominant one and achieving

²⁴In his late years, Su Xing wrote a work of economic history with distinctive features. He sorted and selected a large amount of historical data and materials to describe the process of China's transformation from planned economy to market economy. Refer to *Economic History of the People's Republic of China*, Press of the Party School of the CPC Central Committee, 1999.

the joint development of multiple ownership economies. People should further transform the operation mechanism of state-owned enterprises and establish modern enterprise system adapted to the requirements of market economy and characterized by clearly-defined ownership title, specifically-determined rights and responsibilities, separation of administration and enterprise functions, and scientific management. People should establish a nationally unified open market system, realize the close combination of urban and rural markets, set up the interconnection between domestic and international markets, and promote the optimal allocation of resources. People should establish multileveled social insurance system and provide social insurance to urban and rural residents that were adapted to China's national situation so as to promote economic development and social stability. Besides, people should establish complete macroscopic management system. In fact, just like what Deng Xiaoping said, socialist market economy was "basically similar to capitalism in methodology", as far as the general operation of economy was concerned. Therefore, it is absolutely appropriate for China to boldly absorb and borrow from the advanced operation and management experiences of various countries in the current world, including developed capitalist countries that reflected the principles of modern socialized production in the area of developing socialist market economy.

In the middle of 1990s, the practice of marketization reform resulted in radical change to the pattern that state controlled the economic operation of the entire society in a centralized manner. In the book *The Study on The Economic Relations in China during the Transition Period* published in 1997, the author made the following generalization and summarization on such a situation: First, the state did not bear unlimited liability to the operation of the enterprises anymore and the enterprises could not continue to feed on the "big rice pot" given by the state. State-owned enterprises gradually became legal person entities. Second, the distribution of the fruits of society to individuals was no longer based on abstract labor payment but had to be based on necessary social labor. The labor of an individual was measured by social standards and various production factors also participated with compensation in the creation, realization and distribution of social value. The government adjusted the gaps in income distribution with various policies and gradually created conditions for realizing common prosperity. Third, both the countryside and the city took industrialization as their goal. The countryside was no more the source of funds accumulation for the industrialization of the city. People improved agricultural productivity and the commodity rate of agricultural product and developed the commodity relationship between the city and countryside. Fourth, central and local governments were set up within unified organization of state power. Each level of government handled specific matters at their level and possessed independent authority to fiscal receipts and payments. Besides, tax distribution was implemented and legalized between the central and local governments. Radical change occurred to various economic relations under centralized planned economic system.²⁵

In comparison with mature market economy modes in the world, socialist market economy mode was still in the process of exploration. In fact, before China proposed

²⁵Mao (1997).

socialist market economy mode, there were economists who carried out studies on how to implement market economy in socialism in the international community. Early in 1930s, Oscar Lange proposed the mode of “competitive socialism” and Yugoslavia proposed the “socialism with individual autonomy” in the great debate on socialist economy. Both exerted large influence on the economic transition in eastern European countries. The social democratic parties in Western Europe also advocated the combination between market economy and socialism in order to achieve the goal of fairer wealth distribution and social equality. They paid special attention to the redistribution of wealth and income and required establishing social welfare state. These developments provided some ideological materials that China could draw from in constructing socialist market economy mode with Chinese characteristics.²⁶ In 1994, the author participated in the composition of *What Is Socialist Market Economy*, edited by Ma Hong, and carried out comparative study on the successful market economies in the world, from the World War II. Three modes were proposed in the study: The consumer-oriented market economy model of the USA paid more attention to the interests of the consumers. The state expanded market through the government procurement of commodities and labor services and influenced the operation of economy through monetary policies. The administration-oriented market economy mode of France and Japan relied on economic plans and industrial policies to coordinate market operation. The social market economy mode of Germany paid more attention to social fairness and justice while coordinating the market through economic plans. Some countries in northern Europe such as Sweden also implemented social market economy.²⁷

The establishment of the theory on the transition from planned economy to market economy was a process in which Stalin’s socialist economic theory gradually phased out from China’s guiding thought, in which the theory of socialism with Chinese characteristics gradually became mature, and in which the socialist market economic system gradually improved.

IV. The Approach in the Study of Transition: The Vertical and Horizontal Comparison of Institution Change

The study on transition economy involved the most fundamental theories in economics, such as Marx’s theory on the transformation of production relations, the institution change theory in new institutional economics and development economics, and also how to evaluate new classical economics. But what was the most directly related to it was the theory on comparative economics.

²⁶American economist Joseph E. Stiglitz said in his work *Economics* that market socialism faced two key problems. One was obtaining the information needed for determining prices. The other was the absence of incentives for managers. When an enterprise gained profits, the manufacturer could not obtain rewards. But when an enterprise suffered loss, the government had to make it up. He said such market economy lacked both the market incentive structure in capitalism and the economic control mechanism in traditional socialism. He also pointed out that China achieved success in the production responsibility system in agriculture and improved the labor productivity in agriculture. But its reforms in other areas were still controversial. See Joseph (1998).

²⁷Ma (1993).

In the traditional sense, comparative economics generally referred to the study of the economic systems currently present in the world through dividing them into capitalism, fascism, democratic socialism and communism, namely scientific socialism. Because of the fall of communism in Eastern Europe and the dissolution of the Soviet Union at the end of 1980s, the socialism in the Soviet Union and Eastern Europe ceased to exist as a social system. Comparative economics, which took the comparison of the “-isms” as the main objects of study, faced new challenges. And whether the comparative economics with the “-isms” as the basic research approach would still exist became the primary question. Second, although traditional comparative economics studied economic systems, it basically carried out static comparison on several systems horizontally and there was no dynamic comparative study carried out vertically on the evolution of one system. It could be said to be a new branch in comparative economics which took China, Russia and former socialist countries in Eastern Europe as the cases to explain various economic issues in the transition from planned economy to market economy and which carried out a comparative study on institution change in general, namely the study of transitional economics. *Transition* written by Aleksandr Buzgalin in 1995, *Whither Socialism?* by Joseph E. Stiglitz in 1998,²⁸ *Toward A Comparative Institutional Analysis* by Masahiko Aoki in 1999,²⁹ and *Transition and Economics* by Gerard Roland in 2002,³⁰ these works carried out theoretical summarization on the transition from planned economy to market economy in former socialist countries. *China's Transitional Economics*³¹ edited by Chinese scholar Sheng Hong presented the theoretical exploration on various aspects of China's economic reform. *China Miracle: Development Strategy and Economic Reform*³² written by Lin Yifu et. al. summarized China's reform achievements as miracle in the comparative study with Russia. *A Comparative Study on the Degree of Transition between Chinese and Foreign Economies* written by Zhang Rende et. al. and *Transitional Economics* edited by Jing Weimin both very skillfully applied the latest research results in comparative economics to study China's economic transition.

“Transition” and “reform” generally both meant the theory and practice of the transition from traditional centralized planned economy to modern market economy. But in the international academic circle, there were different understandings on the meaning of the two concepts. Polish economist Grzegorz W. Kolodko pointed out that “transition” referred to a process in which radical change occurred and it meant the introduction of completely new institutional arrangement while “reform” referred to some improvements made in the scope of the original socialist system but no radical change occurred to the system.

The Chinese academic circle did not make very strict distinction between transition and reform. But the term “transition” in China had different connotations with the

²⁸Joseph (1998).

²⁹Masahiko (1999).

³⁰Gerard (2002).

³¹Sheng (1994).

³²Lin et al. (1994).

term “transition” in Russia. The term transition had two different layers of meanings in Russia: One was the shifting from one-party totalitarian regime of the communist party to multi-party parliamentary system in the political structure of the state. The other was the shifting from centralized planned economic system to market economic system. This meaning layer included two stages: One was the free market economic system during Yeltsin’s administrations and the other was regulatory or social market economic system during Putin’s administrations. But the term “transition” in China referred, first, to the shifting from centralized planned economic system to modern or socialist market economic system and, second, to the transformation from a backward agricultural country to a modern industrial country. Therefore, social transition and economic development were the main meanings of “transition” in China.

2 Main Areas in the Study or Comparative Study of Economic Transition

I. The Comparative Study on the Strategies for the Transition into Market Economy, Namely the Selection of the Path of Transition

The main research method which was popular within a period was to take economic growth as the rule and compare and comment the radical model in Russia, also known as the “shock” model, and the Chinese progressive model, also known as the model of “crossing the river by feeling the stones”.

Joseph E. Stiglitz’s article “Whither Reform? Ten Years of the Transition” compared the transitions in China and Russia as respectively being “progressive” and “radical” and also their results. He focused on analyzing that the reasons of the failure of Russia’s “radical” transition were the mistakes in understanding the most fundamental concepts of market economy and, in particular, the mistakes in the decision making related to the political procedure for adopting the suggestions of economists. Although he praised the achievements of China’s progressive reform, he had his own judgment on whether the so-called model of “socialist market economy” would finally succeed.³³ His views were generally regarded as belonging to the school of post-Keynesian economics.

Xiaokai Yang took the side opposite to the view above and believed that the kernel of economic transition was the large-scale transformation of constitutional

³³Joseph E. Stiglitz made reflections on the basis of the theories of information economics, transaction cost theory and neoclassical economics. He also discussed some important issues in transition countries, for example, centralization and decentralization, property right definition, privatization, corporate governance structure, bank and legal person controlling, innovation, rent seeking behavior, distribution relation, adverse selection, moral risks, information asymmetry, capital market, financial policy, monopoly and competition, government function, market failure and government failure. He connected the economic transition of the former socialist countries with the world’s economic integration and financial internationalization and believed that there were defects in socialist market economy.

system. In the article *Economic Reforms and Constitutional Transition*,³⁴ he criticized that the economists who approved of the “progressive” model lacked constitutional thinking. They drew their conclusion too easily when they only saw the short-term economic effects of different modes of transition. People could not negate the failure of the “shock therapy” in Russia with the achievements of China’s progressive reform. When long-term factors were taken into account, the long-term constitutional transition, which was created with China’s current reform, might involve costs that existed the benefits obtained in the short term. Therefore, people needed to reevaluate the achievements of China’s current reform. Generally, his view was regarded as belonging to the school of neoliberalism.

Economists in China proposed views different from the conclusion of Xiaokai Yang. Lin Yifu believed that, now that constitutionalism was the game rules recognized and accepted by the people rather than the constitution written on paper, the recognition and acceptance of new game rules by the people was a slow process subject to the restriction of cultural factors. So transition was definitely a long-term process which would not be completed because of the promulgation of the constitution or the holding of an election. Therefore, people could not truly realize constitutional transition with radical reform. But the damage to the economy caused by such reform was direct and immediate. Hence, progress of reform was better than radical reform.

In his book *From Shock to Therapy*, Polish economist Grzegorz W. Kolodko analyzed the choice between being “radical” or “progressive” from another angle. He believed that, if political reform process was not very deep, then economic development would be limited. When viewed within a long time span, system reform was the necessary premise of economic development and it was not scientific to judge the gains and losses in the selection of transition strategy on the basis of the speed of economic growth within a period. The selection between being “radical” or “progressive” mainly occurred in three areas: (1) In the aspect of economic liberalization and the stability of microscopic economy, the selection was determined by the stability of money and finance. If there was very high degree of control in the economy before transition and financial instability occurred in the early period of the transition, implementing the “radical” mode could achieve the purpose of economic liberalization. (2) The “progressive” method had to be adopted in the area of structural reform and system transformation, including privatization and establishing corporate governance structure, because people needed to take longer time and spend high fiscal and social costs to complete such reform. (3) In the aspect of the restructuring of the microscopic structure of an industry, people needed to inject new investments and shut down old factories. They also needed to re-transfer and re-train workers, to improve the competitiveness of the industry, and to absorb floating capital. All these measures needed time, so they could not adapt to a “radical” method when addressing this issue. Thus people could not just make the simple choice for transition between being “progressive” or “radical”. Therefore, the economist specifically proposed that people should not pay too much attention to economic growth or recession within

³⁴Yang et al. (2003).

a period and commented about it in the comparative study on the “transitions” of China and Russia.³⁵ His view was regarded as belonging to the school of new political economy.

It was noteworthy that, as Russian economy restored and developed rapidly, the debate on commenting on the transitions of China and Russia with the standard of economic growth or recession almost disappeared completely since 1990s.

II. Constructing the Microscopic Foundation of the Market: Property Right Allocation and Enterprise System Construction

Breaking the monopoly of state-owned assets in national economy and carrying out the re-allocation of state-owned assets was the primary task in the transition from centralized planned economy to modern market economy.

The reform of state-owned enterprises in China was gradually pushed forward, starting from “expanding power and conceding profits” at the end of 1970s. However, the specific measures implemented at the time, for example, restoration of bonus system, proportional distribution of the part of the profits beyond the planned figure, and product production and sale outside the plans, all mainly focused on how to distribute profits. The methods of distribution mainly included profit retention, fixed profit payment quota disregard of profit and loss, replacement of tax with profits, and assumption of the sole responsibility for the profit or loss of the enterprise itself. In order to stabilize the source of fiscal revenue of the state, “replacing profit submission with tax payment” was implemented in the first half of 1983. However, because no regulation was made to the differential incomes between the enterprise obtained in the areas of price, assets occupation and resource use, “replacing profit submission with tax payment”, in its actual effect, not only caused more burdens to the enterprises but also aggravated the imbalance between the enterprise in operation conditions so that it ended completely one year after its implementation. The “contracted managerial responsibility system” was a measure gradually improved in the process of expanding the operation autonomy of the enterprises in the middle of 1980s and promoted nationwide in the beginning of 1987. The basic principles of the measure included completely fixed contracting base to ensure payments to superior authorities, retention of the part beyond the fixed base, and making up by the enterprise itself of the shortage part below the fixed base. The rights, responsibilities and interests of the state and the enterprises were divided in the form of contract to ensure that state fiscal base did not decrease and to mobilize the enterprises to increase income. However, the measure was implemented only for one year and its defect was gradually exposed. Some enterprises pursued income maximization so that their short-term conduct drastically inflated. In the enterprises that fulfilled their contracting base, bonuses were paid through misappropriating profits. And the enterprises that suffered loss continued to bargain with competent departments in the government and requested to adjust contracting base. Thus damage was done to state fiscal revenue. In sum, the general thought of the reform of state-owned enterprises

³⁵Grzegorz (2000).

in China was basically limited to how to adjust the distribution of profits between the state and the enterprises in the 1980s.

With economic development and marketization reform, the enterprise had more and more urgent demand for funds. Gathering social idle funds through fund raising and allowing their own employees to become shareholders was the most convenient and easy-to-do method to get fund for a developing enterprise. An ancient property organization form, namely shareholding system, burgeoned slowly in marketization reform. Of course, there were two other direct economic reasons for the emergence of shareholding system. One was that the amount of self-owned funds of the enterprises gradually grew with the improvement of contracting system, which provided stable sources of funds for the enterprises' self-accumulation, self-transformation, assumption of the sole responsibility for the profit or loss of the enterprise itself, and even formation of legal person entity. The other was that the enterprises took each other's products as guiding factor to break through the boundaries of different ownership systems and carried out mutual share participation and financing. In addition, their technologies, materials and human resources permeated with each other so that different enterprises gradually evolved into shareholders. Such mixed property organization form, namely joint-stock company, achieved great development as a new-type enterprise system after the Fourteenth CPC National Congress. Forming various types of joint-stock companies was established as the main form for carrying out the reform of state-owned enterprises. As a result, qualitative change occurred to the general thought of state-owned enterprise reform from the beginning of 1990s. It turned from how to achieve the reasonable distribution of profits in the past to how to achieve the effective operation of capital. As far as deep-level theory was concerned, there were mainly two points in the economic theory that affected the changes in practice. One was the theories that ownership right could be separated properly from operation rights, such as "replacing profit submission with tax payment", "contracting system", and "leasing system". In a particular period, the "separation of the two rights of ownership right and management right" became an ideological weapon to take back some operational autonomy of the enterprises from centralized management system. It was favorable to bringing into play the initiative and spontaneity of the enterprises in production and operation and to strengthening the dynamism of the enterprises. The other was the theory about the separation of the ownership right of the investor and the property right of enterprise legal person. The theory was favorable to separating government functions from enterprise management and transforming operation mechanisms so that the enterprises could get out of their dependency to administrative organs and the state could be freed from the unlimited liability that it bore to the enterprises. A large number of companies with diversified shareholders played a very large primitive role to establishing new mechanisms.

The separation of the ownership right of investor and the property right of enterprise legal person was the important theory to achieve the effective operation of capital. However, because of historical reasons, these two rights were basically in an incomplete status. As far as the ownership right of investor was concerned, the assets of the state-owned enterprises were owned by the state and the State Council represented the state to exercise the functions of the owner. But it was very unclear

what organ should specifically exercise the ownership functions of investor. Any government department could manage an enterprise, but none of them was responsible for the consequence of enterprise operation. This was the system factor that caused the drain of state owned assets. As far as the property right of enterprise legal person was concerned, the enterprises had to rely on bank loans for all the funds that they needed for development after the measure of “changing fund allocation into loans” was adopted in state fiscal budget. As a result, state fiscal budget owed allocations, subsidies and refunds to state-owned enterprises. A considerable number of large- and medium-sized state-owned enterprises operated according to the principles of market economy, on the one hand, and undertook the policy businesses of the state, on the other hand. This was the system reason that caused too heavy debt burden to state-owned enterprises. Establishing modern enterprise system meant in substance to fix and repair these two incomplete rights. For example, in the enterprises in ownership system transformation, people needed first to define property right and specifically identify investment entities. They should establish scientific corporate governance structure and let owner representatives into the enterprises. A mechanism should be formed to achieve the mutual coordination and balancing between owner, operator and worker, through the organs of power, decision-making, supervision and execution inside the enterprise. An investor should enjoy investment rights and benefits and the value increase of state-owned assets should also be guaranteed. The work of “increasing investments and reducing debts” was carried out in all enterprises in China’s ownership system transformation, which included the following: A certain proportion of the income tax and urban construction tax that enterprises actually paid to superior authorities were refunded to the enterprises as state capital. Energy construction fund and budget adjustment fund that local fiscal departments had borrowed or failed to pay, depreciation cost in concentration, and local fund involved in “changing fund allocation into loans” were all turned into state capital. People also increased the depreciation rate of the enterprises and left part of post-tax profits to the enterprises so as to increase state capital. Scientific corporate governance structure restrained the intervention of the original administrative subordination relations to the operation activities of the enterprises.

In addition to adopting the method of ownership system transformation to push forward the separation of the ownership right of investor and the property right of enterprise legal person, another method to ensure the effectiveness of capital operation was the flowing and restructuring of property right. In market economic mechanism, the flowing and restructuring of property right in stock was the condition for improving the effective operation of capital. But in practice, the merger and acquisition of enterprises faced many difficulties. For example, it was very difficult to implement merger and acquisition because of the absence of transaction entities as the ownership right of investor or the property right legal person was not in place. And it was also difficult to determine the discount of state-owned assets and to relocate surplus personnel. Besides, the intervention of rigid ideology also caused great difficulty to the merger and acquisition process.

In the comparison between the documents on carrying out the reform of state-owned enterprises in China and other transition countries, for example, Russia, the

specific measure for state-owned enterprises reform was generally the same: Either it was to implement shareholding system transformation and transfer the ownership right of state owned property or it was to implement the leasing system and transfer the operation right to property right of property. But the performance of such implementation was rather different. The key to the situation was mainly related to the determination of the goal of the re-allocation of state-owned property rights. The goal of the re-allocation of state-owned property right in Russia was to cultivate new property owners while that in China was to adjust the distribution of state-owned assets, to break the monopoly of state-owned economy in national economy, to transform the management system of state-owned assets, and to establish modern enterprise system. When viewed from the result of such implementation, both China and Russia had re-allocated the microscopic foundation of market economy. It should be said that they proceeded on the different paths that led to the same destination as far as transition was concerned.

The situation was not that the designers of the Russian reform plan did not understand the commonsense related to privatization such as opening up prices, clearing balance sheet, creating capital market, establishing legal framework, and ensuring contract and competition. The primary question, about which they were concerned, was that establishment of relevant legal system would delay the practical progress of privatization and resulted in retrogression or even the restoration of centralized economic system and totalitarian political system. Therefore, in their eyes, the speed of realizing privatization was more important than how to realize privatization. And they advocated that people had to implement privatization quickly, or as quickly as possible. Who was the first owner in privatization was not important? The market would soon reallocate capital into new owners who could effectively use the capital. Thus a new powerful political force would form and it would become the social base for implementing free market economy. They would further push forward a more extensive and thorough transition plan with more positive attitude.

The privatization of the state-owned enterprises in Russia posed many thought-provoking questions to researchers, which mainly concentrated on two areas:

One was how to establish strict corporate governance structure.

According to statistics, the employees in the companies in Russia owned more shares of their companies than those in any other countries in the world. But they had very little power. The actual control power of the company was completely in the hands of the president and the managers. The president and the managers continued to follow the way of thinking under the centralized planned economy. When their enterprises did not have enough funds, they would try to continue to survive through reducing production, firing workers, relying on government subsidies and loans, or delaying paying their debts. Such companies only transformed on the surface and nothing was changed much in substance. Such a situation indicated that it was very important to establish a scientific corporate governance structure and determine a diversified equity structure that conformed to national situation.

The other was how to realize the “orderly exit” of part of the state-owned assets.

In the reallocation of the property rights of state-owned assets in Russia, the “disorderly exit” of some state-owned assets caused economic chaos and, at the same time,

triggered sharp conflicts of interests between various social questions. China drew from this lesson. It proposed basic thought of “both entry and exit” and made relatively meticulous arrangements on “orderly exit”. First, it stipulated the areas where state-owned economy would “exit”. Second, people had to listen to the opinions of their employees, operate according to relevant standards, and pay more attention to the practical effect when implementing the “exit”. Third, people needed to speed up building social security system and expanded the coverage of pension, unemployment and medical care social insurances in accordance with the law. And fourth, people emphasized particularly the important role of stable macroeconomic environment and government in adjusting the distribution of state-owned economy. But it was also undoubted that the vicious cases of stealing state-owned assets occurred frequently in specific implementation process.

These two lessons were very important to the success of China’s state-owned enterprise reform. And there was still a long way to go in the reform of state-owned economy. If China’s state-owned enterprises did not work on reform further or even degraded into state- or government-run monopolistic economy, they would cause new troubles to socialist market economy.

Developing state-owned economy to create the external competitive environment for breaking the monopoly of state-owned economy, this was the China’s experience in cultivating the microscopic foundation for market economy, which was more successful than Russia. The development of non-state-owned economy experienced twists and turns or even risks in the thirty years of reform and opening up in China, but, in general, it gradually won policy support and system guarantee. According to the latest statistics, total urban employed population reached 302.1 million at the end of 2008. Among them, state-owned units employed 64.47 million, which accounted for 21.34% of urban employed population and private enterprises and individual businesses employed 87.33 million, which accounted for 28.9% of urban employed population. Individual and private economy provided a large number of jobs to the city. At the end of 2008, the total of enterprises above designated size reached 426,113 nationwide and their total industrial product and total assets amounted to 50,744.8 billion RMB and 43,130.6 billion RMB respectively. Among them, 9,682 were state-owned enterprises and their total industrial product and total assets amounted to 4,685.7 billion RMB and 6,710.2 billion RMB respectively. And the percentages of these three figures to the totals were respectively 2.27%, 9.23% and 15.56%. And 245,850 were private enterprises and their total industrial product and total assets amounted to 13,634 billion RMB and 7,588 billion RMB respectively. And the percentages of these three figures to the totals were respectively 57.7%, 26.87% and 17.6%. The production capacity contribution of private economy in industry started to exceed that of state-owned economy.³⁶ This indicated that non-public economy made increasingly larger contribution to the development of social economy.

³⁶See *China Statistical Yearbook 2009*.

III. The Construction of the Macroscopic Regulation Mechanism of the Market: Transforming Government Functions

China and Russia took completely different roads in this area. The foothold of the Russian reform of government functions was based on the thought of disintegrating and rebuilding the original form of government and form of state of the country.

Some Russian thinkers believed that the Russian culture did not possess the potential to create economic growth and ensure the original welfare standard. So people needed to break the original social structure and system and remove Russian culture and traditions with ferocious measures and at all costs. Yuri Afanassiev, former president of the Moscow State Institute for History and Archives, said that such system should not be mended. It had three pillars: The original Soviet Union as a centralized state, state socialism as non-market economy, and monopoly of the party. These three pillars should be removed gradually without bloodshed.³⁷ Therefore, the transition of Russia had very specific positioning at the very beginning. The original state apartments had to be dismantled. People thoroughly destroyed the original form of government and form of state of the country and established a new state system and government organization.

Russian thinkers also believed that large government meant insufficiency and small government meant high efficiency. So people had to build a small government after the transition. American economist Jeffrey Sachs pointed out in 1993 that market would thrive immediately once the central planning bureaucratic body resigned from its position. He believed that the most convenient approach to turn around economic contraction and realize economic restoration and growth after the transition took place was to adopt various measures to reduce the intervention of the government in economic matters and hence build a small government. The situation that Yeltsin's government attempted and accomplished nothing in the operation of market economy came from such an idea.

The case in China was completely different. The government functions experienced a huge transformation from management to service in the transition.

The goal in transforming government functions was administration in accordance with the law. Transforming government functions was both the key to economic transition and the start point in pushing forward the transition of political system. The basic mode for the government to perform its functions under traditional management model was the administrative examination and approval system. Examination and approval had the weaknesses of extensive scope, multiple links and low efficiency. As it was subject to almost no restriction of the law, examination and approval involved very large discretionary power. The prior examination and approval for market access created various obstructions for the entry and flow of human resources and greatly reduced the efficiency of the market in allocating resources. Irresponsible administrative examination and approval of projects caused serious waste to the society. And because of examination and approval, the government undertook unlimited liability to the society and paid expensive price for such liability. Examination and approval

³⁷See *Social Science Weekly*, April 19, 2007.

also provided the hotbed for government officials to commit corruptions, such as rent seeking and abuse of power for personal gain. Therefore, reforming administrative examination and approval system, pushing forward administrative system reform, and rebuilding an administrative examination and approval system adapted to socialist market economy was the key in transforming government functions. Only when people had transformed government functions and built a new system consistent with the operation of modern market economy could they talk about how to carry out regulation on the operation of market economy through employing fiscal policies, monetary policies, industry policies and income policies. The government whose functions were connected with the period of revolution instinctively intended to exercise the centralized management of economy, but the government whose functions were connected with the period of construction naturally should exercise the function of public service.

Building a public service-oriented government was a new issue in transforming government functions. Government existed for the purpose of correcting the malfunction of the market and for providing the society with public products and services that the market could not effectively supply. Besides, it formulated fair rules, strengthened supervision, and guaranteed the effectiveness of market competition and the fundamental role of the market in allocating resources. The government minimized the costs and risks in economic development in economic activities through microscopic regulation, fair law enforcement and the service of providing public goods. It also maintained social justice, public security and the legal rights of citizens and legal persons. In the operation of market economy, the government was not to rule the society but to serve the society and people needed to build a complete public service-oriented government. Therefore, people should adhere to the principle of people-orientedness and pay attention to and build the interest expression mechanisms for different interest entities. They should define the powers of fiscal matters and office between the central and local governments, speed up the legislation on public service, build information disclosure system, and construct new type government functions with the philosophy of Market economy.

IV. Building a Safety Net for the Market: Social Security System

Whenever transition was implemented, people had to carry out distribution adjustment and structure reform to the original monopoly of state-owned economy. They had to make adjustments to the original equalitarian income distribution system and gradually adapt the macroscopic regulation in industry, finance and fiscal matters to the needs of the operation of modern market economy. And all these would cause new contradictions in social and economic interests and thus triggered some social issues or social turbulences. Many issues in the society in the city and the countryside would pose threats, such as inflation or deflection pressure, unemployment and re-employment, urban retirement and pension, rural pension and other insurances, culture, education and medical care, and underground economy. How to realize the healthy transition of the society? This not only required the establishment of the complete operation mechanism of market economy but also required the establishment of a complete social security system and the construction of a new social safety

net. Formal and informal departments and organizations that possessed the functions of social security, social service and social aid should form a social umbrella together to maintain the social justice that matched the standard of economic development.

Because of the difference in national situation and the selection of transition strategy, the social issues caused by such difference and the social unrest caused by these issues also showed conspicuous difference. Generally speaking, enterprise shutdown and even bankruptcy both became normal economic phenomena during transition as economic structure adjustment deepened and management bodies were streamlined. Such a situation caused social security, which was based on enterprises or institutions in the past, to lose its foundation. In addition, pension was generally paid in public finance in former socialist countries. But as time passed, most of these countries entered the stage of aged society and average life span extended in these countries. This caused growing pressure to public finance and the deficit in social security became the deficit in central fiscal budget. If there was not the support of economic growth and the taxation system was incomplete in the process of transition, the conditions of central fiscal budget would become more deteriorated and normal social security items would lose their source so that the original social security system suffered damages, which was of lower social insurance standard but was still very stable before. The serious economic recession and drastic social unrest in Russia completely destroyed the original social security system and the country paid a huge price for it. Therefore, people should reform and improve the social system and make it the safety net for avoiding market transition risks and the guarantee for pushing forward orderly transition.³⁸

People should find new thoughts mainly in the aspects of fund raising mode, financial management, and operation supervision system of social security when improving and reforming social security system during transition so as to transform enterprise guarantee under centralized planned economy into social security under modern market economy. There were many lessons to learn in Russia in this area. In China's economic transition process, its social security system contained more complicated difficulties and the entire social security system faced more cumbersome

³⁸In the former Soviet Union, each citizen enjoyed rather complete social welfare. People could ride a bus and get medical care for free. The government made up for the loss of the railway and medical care systems from its fiscal budget. After the dissolution of the Soviet Union, welfare and preferential policies were inherited although privatization was implemented. During Yeltsin's administration, the government increased social welfare without any principle in order to win over the voters. As a result, 103 million people among the 144 million Russian population, distributed in different industries and social classes, continued to enjoy the various preferential policies such as free medical care, education and property management. The great variety of preferential policies and the tremendous amount of welfare subsidies became a heavy burden of the Russian government. On August 5, 2004, the state дума passed the act of "replacing preferences with allowances". According to this act, the welfare treatment for 32 million aged and disadvantaged population, including using city public transit for free, free drugs and rehabilitation, using municipal services such as water, electricity and gas at low prices, would all be canceled from January 1, 2005 and it would be replaced by the subsidies paid by the government in ruble cash. But in the process of its implementation, veterans, retirees and the disabled suffered the most serious impact because of unequal distribution in the reform and the social welfare preferences given to public servants at various levels were not changed. This caused new social contradictions.

financial crisis. China's social security standard was originally lower than Russia. During the transition, the proportion of its central fiscal revenue to gross domestic product decreased year by year until 1994 and sharp contradiction was formed in fiscal budget between the spending on social security and those in other areas, such as infrastructure, culture and education. It was noteworthy that there was the difference between over-protection to urban employees and inadequate protection to rural population during the time of centralized planned economy in China. In the past, the workers enjoyed all-round life assurance and welfare benefits "from cradle to tomb" in enterprise guarantee. Sudden unemployment not only caused them to lose the main source of income so that the conditions of their family life quickly worsened but also took away all social security that they had in the past. Therefore, the social contradiction caused by social security crisis was far sharper in the city than in the countryside. Unemployed population confronted the government directly. It was very hard to avoid the concentrated social conflicts or unrests caused by large-scale unemployment in the city. But the kernel issue that troubled China's social security system was serious fund insufficiency. The situation was compounded with the population ageing issue that China was facing so that China's social security work contained very complicated and burdensome tasks. During transition, China gradually implemented the system of combining personal account with social collection. According to relevant provisions, individuals paid contribution at a proportion of 8% of their wages with personal accounts established while enterprises or employers paid contribution at a proportion of 20% of the wages of their employees with social collection accounts established. However, many of the people who were retired now in fact never paid pension contribution in the past. At the time, their enterprises paid the contributions of pension. Now these people received the pension, but they did not have personal accounts or their personal accounts only had very little pension fund and the social connection accounts for them also did not have sufficient fund. So there was the issue that the state took the funds in personal accounts to pay the pension of retired people and thus empty accounts appeared in personal pension insurance. How to resolve the issue of the empty accounts in personal pension insurance? It was a new issue worth thinking about. But people should recognize that the pension that the workers in state-owned enterprises and institutions had accumulated with the low wages in centralized planned economy was used by the government as investment to constantly expand production. It was materialized in the state-owned assets at present. Those retired workers who did not have pension accumulation in personal accounts under the old system had the right to claim pension and retiring benefits from the government. Such rights and benefits were in substance the implicit pension insurance debt that the government bore. To liquidate part of state-owned assets into the funds for social security was in fact to return to the employees in state-owned enterprises part of their labor accumulation in state-owned assets. But now people still had not found the effective approach and mechanism for such returning. In general, the social security system was rather incomplete in a country that implemented transition in a later period. From 1978 to 2008, China's state fiscal revenue increased from RMB 113.2 billion yuan to 6,133 billion yuan. But the construction of social welfare system lagged behind largely and people felt great pressure from the

four major areas of medical care, education, pension and housing. Although Chinese economy achieved high-speed growth, poor people seldom got to share the fruits of high-speed economic development.

As economic transition was implemented, social issues became increasingly complicated at the same pace. The start point of China's economic transition was to focus on economic development. People overlooked the seriousness of the institutional legislation related to the market. This offered chances for officials to commit embezzlement and corruption and take bribes. The powers of the officials were transformed into capital. China's economic transition also focused more on economic growth speed and overlooked the effectiveness of social policy. Because of the enlargement of the gap between the rich and the poor, China already became one of the countries with very high-income inequality in the current world. On January 12, 1983, Deng Xiaoping advocated that people should allow part of the people to get rich through working. But at the time, he did not seem to foresee that, once the surplus fund was converted into capital after people become wealthy through the working, the speed of getting wealth with capital and the income gap caused by such phenomenon would both grew larger quickly. On September 16, 1993, Deng Xiaoping reflected with gravity and sincerity that we said in the past that China should become more developed first. Now it seemed that there were no less issues after China became more developed than when it was undeveloped. How should people distribute wealth after the country became wealthy? Resolving this issue was more difficult than resolving the issue of letting China become developed. People should use various means, methods and plans to resolve the issues related to this.³⁹ The issue that Deng Xiaoping thought about in his late years was very practical and it was also the issue about which various social classes were deeply concerned. The accumulation of many social issues threatened the effectiveness of social safety net. In correspondence with the situation, the study on China's social transition and social structure evolution attracted the attention from both within and without the academic circle. Chinese sociologist Sun Liping proposed such concepts and views as power imbalance, gaming of interests, and the tendencies of oligarchy at the upper levels and of populism at the lower levels in the society, which reflected his profound thinking on social issues.⁴⁰

3 The Study of Transition Economics Needed Further Development and Deepening

Whether transition economics was an independent discipline in economics was a question that people were exploring through hard work. Up to the present, no systems

³⁹See *Deng Xiaoping Chronicles (1975–1997)* Vol.2, Central Party Literature Press, 2004, pp. 1356–1364.

⁴⁰Sun (2002).

or categories were formed initially in this area. The study in transition economics needed further development and depending.

I. The Study in Transition Economics Needed the Strengthening of the Study of System Construction

From the beginning of the 21st century, paying attention to the system construction in the countries that implemented transition in a later period became a new angle in the study of transition economics. This situation was particularly obvious in Russian academic circle during the transformation from Yeltsin's free market economy to Putin's regulatory market economy.

Russian scholar Leonid Polishchuk gave specific explanation on system construction, taking into account the practice of economic transition in Russia, in the article "The Evolution of Institutional Demand in Transition Economy".⁴¹ In the early stage of the transition, financial and industrial oligarchs, who obtained economic controlling powers, did not support or even oppose the system construction for property right protection. But as the transition deepened and, in particular, after financial crisis occurred in 1998, economic entities had increasing interests in transparent, stable and effective legal system. They became more willing to transfer their businesses from underground economy into formal sectors and to pay taxes in full amount in exchange for the public protection of property right and law and order. However, the construction of the rule of law was a gaming process, which involved the relations between political culture, constitutional restrictions, fiscal and supervisory instruments available to the government, and the ability of the society to make political organization. Simeon Djankov, Rafael la Porta et. al. said in the article "New Comparative Economics"⁴² that the excessive stress on the speed of transition was eventually proved as being meaningless. There were huge differences in the achievements of various countries in economic transition and such achievements depended, to a large extent, on the effectiveness of the new systems that these countries established. And when building these new systems, people needed to weigh and select between controlling the harms of disorder or despotism. The function of a new system was to control the dangers of disorder and despotism. Serious disorder would bring huge loss to the society, but controlling disorder with larger power would generate stronger despotism or even abuse of power. Such an angle of thinking was greatly illuminating in meaning to building new systems in the countries that implemented transition in a later period.

Wu Jinglian constantly paid attention to system construction in market operation and he believed that market economy was the economy with the rule of law. The government had to provide a system platform for market mechanism. Without such a system platform, it would be very hard for people to get rid of the situations such as distortion of rules, chaotic order, and the intervention of power in market transaction.⁴³ The author also pointed out in his article "Different System Arrangements and

⁴¹Leonid.

⁴²Simeon et al.

⁴³Wu (2003).

Value Orientations in Transition Countries’,⁴⁴ that the history in the recent century and the practices and lessons of transition countries indicated that market economy was indeed a mechanism to improve efficiency for a country but, if things were not done correctly, it could also be a mechanism that destroyed the society. There were two kinds of market economies worldwide, one benign and the other vicious. People needed to study what on earth benign market economy was, what vicious market economy was, what kind of form of market economy tended to develop into benign market economy, and what kind of form of market economy tended to develop into vicious market economy. And what kind of factors would influence the evolution process of market economy? Were there any other factors in addition to those like corporate structure, property right structure, market structure, distribution system, and political system? Improving China’s current market economic system meant to develop the current market economic system into benign market economy. But if no adequate consideration was given to many other factors, system construction left behind, and the mechanisms for supervision, check and balance, and accountability were insufficient in the use of administrative power, people could not rule out the possibility that it would evolve into vicious market economy.

⁴⁴Mao (2007).

II. The Study on Transition Economy Needed to Strengthen the Study on the Economic Relationship between Power, Labor and Capital and to Construct New Economic Thinking on the Harmony between Capital and Labor in Democratic Politics

From 1949 to 2009, capital experienced a process of full of twists and turns in which it was either “eradicated or developed”. To both develop and restrain capital in the practice of exploring socialism with Chinese characteristics was a novel theoretical issue.

Early in 1953, China implemented the general line for the transitional period and carried out the large-scale socialist transformation of capitalist industry and commerce. At the time, Mao Zedong believed that the substance of the CPC’s general line for the transitional period was to make the socialist ownership system of the means of production the only economic foundation for China’s state and society.⁴⁵ In the process of the transformation, Mao Zedong proposed that people should “eradicate both capitalism and small production”.⁴⁶ Under such guiding thought, private capitalist economy was basically eradicated on mainland China as an economic form from that time until early 1980s. People had very painful memory about it. Growing vegetables and raise chickens and selling things on vendor’s stands were all regarded as the tail of capitalism and eradicated. These activities were afflicted with criticism and denouncement.

In reform and opening up, China implemented the policies completely in opposition to those in the period of Mao Zedong. Both domestic private capital and overseas and foreign capital achieved great development on mainland China because of the guidance and policy support of the government. The proportion of private economy exceeded 50% in some of the traditional industry industries nationwide. Private economy accounted for over 70% in the industries like light industry and textile, machinery, construction, transportation and commercial and trade service. The practice in the reform and opening approved that the rapid development of Chinese and foreign capital in the area of non-public ownership system accelerated the development of a group of emerging industries and supported the high-speed growth of national economy. Besides, it widened employment channels and increased national fiscal income. Thus it played an important role in enhancing the dynamism of the entire national economy and fully mobilizing the initiative of various circles in the society. Chinese and foreign capital already became the foundation of national economy, an important component of socialist market economy, and an important force in promoting the development of social productivity.

However, people should be aware clearly that capital was capital in the end. The pursuit to surplus profit was the natural attribute of capital. And in economic transition, such natural attribute might be indulged because of the special national situation in China if things were not done correctly. First, China implemented socialist market economy and such market economy was operated under the guidance of

⁴⁵*Collected Works of Mao Zedong*, Vol.6, People’s Publishing House, 1999, p. 316.

⁴⁶*Selected Important Literature from the Founding of the People’s Republic of China*, Book 7, Central Party Literature Press, 1993, p. 310.

the power of the government. The thresholds of the capital's access to the market were completely controlled by the power of the government. Once economic growth became the theme of the government's decision making, capital would naturally become the preferred area of the government. It would be very hard to avoid a series of social issues caused by the collusion of power and capital, such as taking and offering bribes, embezzlement and corruption. Second, employment would be an important economic and social issue in China within a very long period of time. The presence of surplus labor would put labor in very unfavorable position against capital because capital would never worry about finding new labor. Thus, it would become very hard to avoid the issue of profit eating into wages. Capital would persist in lowering wages or become unwilling to raise wages so that income gap would be enlarged gradually.

People should adjust the relationship between power and capital and labor. They should change the role of the government in leading economic development as quickly as possible and build a public-service-oriented government. They should enhance the functions of the social security system through tax system reform. From 1978 to 2008, China's state fiscal income rose from 113.2 billion RMB to 6,133 billion RMB.⁴⁷ People should propose more policy and system innovations so that the poor people could share the fruits of rapid economy development through new ways as the economy grew in high speed. People needed to build a complete social security system and form a social safety net with the departments and organizations that possessed the functions of social security, social service and social aid so as to maintain the social fairness that matched the standard of economic development.

People should build new economic relationship between labor and capital. Friedrich Engels once believed that, although Karl Marx profoundly analyzed the economic relationship between labor and capital in his value theory of labor, his analysis represented an abstraction of market competition and price, which was very hard to be found in actual economic life. Engels believed that value was the relationship between production expenses and utility if people started with the actual operation of market economy in the analysis and took into account the factors like market competition and price change. The theory was criticized in the Chinese circle of theoretical study within certain period. Chinese economists Sun Yefang was also treated unfairly because he criticized the low efficiency of centralized planned economy on the basis of Engels' value theory. However, in the early 1920s, Eduard Bernstein gave a new explanation on Engels' value theory on the basis of the new situation in the development of capitalism. He believed that production expenses undoubtedly played an important role in the formation of the magnitude of value but the question that needed to be resolved was about the analysis on utility. The realization of the utility of goods was related to the purchasing power of various classes on the market. In other words, utility was realized through the effective purchasing power on the market. After expenses were invested and products were produced, surplus value still could not be realized when the products could not be sold on the market because of insufficient purchasing power. Therefore, people needed to raise the wages of

⁴⁷See *China Statistical Yearbook 2009*, China Statistics Press, 2009.

the workers, enhance social purchasing power, and improve social welfare. Later, this point became the economic theoretical basis of the social democratic parties in Europe in paying more attention to social welfare.

At present, China was experiencing a major change of transforming from planned economy to market economy, which was also an irreversible major trend. The presence and development of capital already became an objective economic fact. However, either profit eating into wages or wages eating into profit would distort the existence and development of enterprises. Under the general background that labor was in surplus and jobs in shortage in China at present, people should pay more attention and maintain the interest of workers. They should implement strict and scientific labor-capital negotiation mechanisms, strengthen the independence of trade unions, contain the greed of capital, and protect the interests of workers. The capital should understand that, only through improving the social purchasing power of workers, could people realize the surplus value formed in the domain of production. It was also the substance in the theory of Engels that value was the comparison between expenses and utility.

Constructing the harmonious relationship between power, labor and capital was a brand new theoretical issue in the practice of socialism with Chinese characteristics.

III. The Study of Transition Economics Needed the Deeper Mergence of Various Schools in Economics and the Further Coordination of Multiple Disciplines in Social Sciences to Tackle and Crack Key Issues through Cooperation

Beneficial exploration was made in the study of transition economics with respect to the combination of the theory of productive relationship reform in Marxism and the institutional change theory in neo-institutional economics. Scientific absorption of some opinions in neo-institutional economics could enrich the institutional change theory in Marxism. Of course, people should clearly realize that the theory of productive relationship reform in Marxism studied the supersession of different economic systems while neo-institutional economics studied how to make a system more efficient under a given economic system.

Comparative economics was applied extensively in the study of transition economics. In 2002, Wu Jinglian presided over and established the magazine *Comparative Studies* and advocated “Spreading philosophy, thought and knowledge through comparison”. The magazine selectively introduced the theory and practice and the experiences and lessons of transition countries on the basis of the important issues that people encountered in economic transition in China. Up to the present, over 40 issues of the magazine were edited and published, which promoted the study in traditional economics to deepen constantly. In his book *Comparative Economics and China’s Economic Reform*, Zhang Yugui made a systematic introduction on the extensive spreading of comparative economics in the practice of China’s economic transition.⁴⁸

Applying evolutionary economics to study the evolution of social and economic systems played a promotive role in deepening the study in transitional economics.

⁴⁸Zhang (2006).

German scholar Carsten Herrmann-Pillath studied the transition of major countries with the research framework of evolutionary economics. He believed that huge spatial or regional differences existed in China and Russia. Nationally uniform economic transition policy would cause different political and economic responses in various regions and such feedback difference would in turn cause various regions to gradually form different transition routes so that local interests would gradually take form and become increasingly stronger. Only when people faced such evolutionary process squarely could they create an operable policy framework for government competition. Karl Marx pointed out that Darwin's theory of evolution constituted the natural and historical foundation of his theory. Technological progress was similar to the co-evolution of species and their mutual transformation in the ecological system. This was a kind of economics based on the theory of evolution. In his book *Evolutionary Economics: The Hotbed of Economic Revolution*⁴⁹, Jia Genliang made detailed demonstration about this point.

Frankly speaking, the majority of the research results in the area of transition economics at present stayed at the level of explaining economic development policies and seldom gave clear explanation on the questions at deeper levels. So studying transition from the angle of economics or comparing the process of transition countries might be a dead end in research because such study also involved theoretical questions in all other areas such as politics, culture, ethnic groups, history and religion and needed multidisciplinary collaborative study and democratic discussion.

The study of transition economics needed further coordination in multiple disciplines and cooperation in tackling and cracking key issues in the disciplines of political study, sociology, history, and ethnography.

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Part V
Important Progress of Chinese Economics

Chapter 27

The Main Line of the Theoretical Study on China's Economic Growth: The Transformation of the Model of Economy Catch-up and the Paradigm of Growth Theory



Hongmiao Wang and Ping Zhang

China started its development as a backward country plagued by poverty and blankness and scarred and battered by war from the founding of the People's Republic of China in 1949. After over 60 years of non-conventional and accelerated growth, China got out of poverty trap and approached modernization in general. In 2010, it rose to become the second largest economy in the world, its per capital income exceeding USD 4,000, and started to advance towards the rank of upper middle-income countries. Such economic takeoff and catch-up process could be said to be miraculous and it was full of twists and turns and hardships. What accompanied such process was the painstaking thinking on the road of China's prosperity and strength of several generations of Chinese economists and their arduous exploration on the theory of China's economic growth. In this chapter, the author will take into account the process of the formation and transformation of China's economic catch-up model from the founding of the People's Republic of China and review and sort out the progress in the research area of China's economic growth during over 60 years. The discussion would be carried out in the following three areas: The first area was the theoretical discussion on the catch-up and growth of heavy industrialization from the founding of the People's Republic of China and relevant issues. The second was the adjustment of catch-up model, the transformation of the paradigm of growth theory, and growth miracle from the reform and opening up. And the third was the discussion on the transformation of China's economic growth model and its growth prospects in the future in recent years.

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1 The Catch-up Growth of Heavy Industrialization, Population Expansion After the Founding of the People's Republic of China and Its Theoretical Discussion

From early modern times, saving the nation from subjugation, ensuring its survival and realizing its development was always the dream of every person of patriotism and noble aspiration in China and the inevitable economic process to achieve such a goal was industrialization. After the founding of the People's Republic of China in 1949, to concentrate resources to quickly realize industrialization became a necessary choice in state policy as China was confronted with a situation that it was suppressed with political and military pressures and many things needed to be done in economic and social restoration.¹ Because China implemented “one-sided” foreign policy at the time, the domestic circle of economics was basically isolated from western academic world in a very long period of time so that they knew very little about the modern economic growth theory, which achieved breakthrough progress in the international world. On the other side, inspired by the strong political influence of the Soviet Union and its catch-up achievements in industrialization, the Chinese circles of economics and economic work completely accepted the industrialization outlook that the Soviet Union had established in 1920–30s. Its basic symbolic feature was that the gross industrial product dominated in the gross product of industry and agriculture and the gross product of heavy industry dominated in gross industry product. As national economy was gradually restored and the First Five Year Plan was implemented, China very naturally started the construction process which prioritized the development of heavy industry to realize industrialization and took the 156 major construction projects implemented with the aid of the Soviet Union as the starting point and the basis.

I. The Catch-up Model that Prioritized the Growth of Heavy Industry and Its Economic Mobilization

The characteristics of heavy industry included capital and technology intensiveness, large amount of initial investment, continual input of large amounts of raw materials, and longer construction cycle. In the early period after the founding of the People's Republic of China, economic development began at a very low start point. The scarcity in resource, capital and technology formed the “three major gaps”. If the absence of security caused by war threats was added to them, there were “four

¹Early at the Seventh CPC National Congress in 1945, Mao Zedong proposed the economical goal in the future: “After obtaining the political conditions of New Democratism, the Chinese people and their government must adopt practical measures to gradually establish heavy and light industries within several years so that China can change from an agricultural country to an industrial country.” (Mao 1991, p. 1081). The *Common Program* of the Chinese People's Political Consultation Conference, which played the role of provisional constitution after the founding of the People's Republic of China in 1949, and the *Constitution* in 1954 both took gradually realizing the socialist industrialization of the country and “turning an agricultural country into an industrial country” as the state goal.

major gaps". Under such condition, the Chinese government adopted responsive and supportive measures to carry out economic mobilization nationwide in order to implement the catch-up strategy that prioritized the growth of heavy industry.

- (1) China advocated "More people make greater force" and encouraged population growth so as to increase the quantity of labor input and, of course, to meet the needs in war preparedness to a certain extent.
- (2) China took the development road of high accumulation, low consumption and high concentration of the resources of the entire society, commonly known as "pooling resources to achieve major goals". From the middle of the 1950s, the Chinese government adopted a series of economic measures and political movements, such as "Movements against the 'Three Evils' and the 'Five Evils'", "Three Great Remolds", "People's Commune", and "Collective Canteens", to unify ownership system, highly mobilize and concentrate social resources, and effectively control the consumption demand of the entire society at the level of maintaining subsistence so as to quickly accumulate economic surplus, promote the capital formation in heavy industry, and realize catch-up growth.² For such purpose, people even extremely promoted the "great campaign of smelting steel".
- (3) In the beginning, China completely relied on the Soviet Union in technology introduction. The reversion of Sino-Soviet relations in late the 1950s made it impossible for China to introduce technology from any developed country. Hence, China had to develop through self-reliance various industries and technologies that concerned the lifeline of the country. Such a situation further forced China to truly implement the planned economy of high accumulation and low consumption.
- (4) In macroeconomic policy, the macroscopic policy that matched the strategic goal of prioritizing the growth of heavy industry completely repelled the action of market mechanism and intentionally distorted the relative prices of productive factors and products. Because heavy industry was highly capital-intensive industry, interest rate would definitely grow very high under the condition of capital scarcity so that the strategy of prioritizing the development of heavy industry could not be implemented, if interest rates were decided by the supply and demand on the capital market. Therefore, in order to implement such a strategy, people had to control the prices of capital, foreign exchange, energy, raw materials, labor, and life necessities so as to lower the cost of the capital

²Such a development model definitely required the leadership of a powerful government. It could not be realized without the push of a powerful and omnipotent government. The road of the Soviet Union was one that highly depended on a few technical experts to implement the central orders of planned economy. During the time of Mao Zedong, the power of developing economy was delegated to the leaders and cadres of the CPC and government at various levels through local decentralization of power. It was required that the cadres of the entire CPC should all engage in economy and construction, that common citizens should all engage in industrialization construction, and that CPC and government leaders and cadres in various counties, prefectures and provinces should all work on economy and industry. It was also proposed that "Non-experts direct experts" and "Politics leads economy".

formation of heavy industry. Such measure further strengthened the formation of the systems such as “centralized procurement and distribution” and “cooperative transformation of agriculture”.

- (5) Under such environment of unbalanced structure and distorted macroscopic policy, the development of light industry and service industry lagged behind, trade and private commercial conduct was strictly restricted or even cancelled or banned, and scarcity became a normal phenomenon in economy. If market and free trade were allowed to freely guide the direction of resource use, it would be very hard to maintain price control policy and to ensure that resources were channeled into strategic sectors prioritized in development. In order to allocate scarce resources into the industries that the government prioritized in development, people needed to establish a set of planned resource allocation systems. Therefore, the government redefined the entitlement sets and economic incentives of individuals and enterprises through the reforms in the systems of ownership,³ residence registration, employment and migration. For example, the right to free transaction was deemed as “black market transaction” subject to certain punishment. Thus, all labor surplus that could be mobilized were transferred onto the goal of industrialization. When the government’s strategy of prioritizing the development of heavy industry conflicted with resource endowment in reality, people had to adopt mandatory measures to control resources so that the “transaction” between the government and individual, enterprise and society could be realized.⁴

II. Theoretical Origin of the Catch-up Growth Model of Heavy Industrialization

Under the economic and social conditions and in the environment of “letting politics take command” during the period of planned economy, the study of economic theories in China, like that in all other socialist countries, had very little freedom so that it was very hard for people to find larger space of innovation. Such study was mainly divided into two categories. One was to popularize and study the works of classical writers of Marxism. The other was to find the theoretical basis in the works of classical writers to support the current lines, policies and guidelines and interpret them to enhance their legitimacy in theory. The economic strategy and policy of the

³For example, light industry possessed comparative advantage and higher profit level in the early period after the founding of the People’s Republic of China but these enterprises were often owned and operated privately. The reasonable choice of private enterprises, which take getting profits as operation motivation, was to invest resources into the sectors that could generate the largest returns. And these sectors were often irrelevant to the development goal of the state. In order to obtain the right of disposal of surpluses and control the direction of accumulation, people had to transform private enterprises into state-owned enterprises so that a microscopic operation system, which lacked autonomy, was formed.

⁴Some literature contained special study on the planned economy under socialist system, such as Kornai (1992), Zhang An trans., *The Socialist System: The Political Economy of Communism*, Central Compilation and Translation Press, 2007, Lin et al. (1994), and so on.

state was determined all by political leaders. And only these people were qualified to propose theoretical innovations different from those of classical writers.⁵

The Chinese edition of Stalin's book *Issues on the Socialist Economy in the Soviet Union* was published in November 1952, which triggered a trend of study in various circles in China. From the middle of the 1950s to the middle of 1960s, the circle of economic theories focused on discussing the issue of prioritizing the development of heavy industry, taking the study and dissemination of the discussion on Marxist theory of reproduction in the book as an opportunity and centering round the actual needs in economic construction. They demonstrated that the guideline of prioritizing the development of heavy industry was consistent with the principles of the relationship between the two major departments in extended reproduction, proposed by Marx, and of prioritizing the growth of the means of production, proposed by Lenin. And starting from the reality in China's economic development, they further discussed the issue how to retain certain development proportions between industry and agriculture, heavy and light industries, and infrastructure construction and people's life under the premise of prioritizing the development of heavy industry and proposed the empirical standards and quantitative limits for retaining coordinated economic development.⁶ Rarely-seen counterpoints related to the issue of economic growth also emerged in the intelligentsia in the 1950s. For example, Liang Shuming proposed the issue of the gap between the city and countryside and Ma Yinchu proposed the "new population theory" and the "theoretical issue of comprehensive balance". But all these views sustained harsh political criticism.

The theory of prioritizing the growth of the means of production was in fact the theory of capital accumulation and growth in the paradigm of Marxism. The discussion on prioritizing the growth of the means of production was carried out with different understandings and argumentations on Marx's reproduction theory. This was an issue with the most discussion and largest controversy in reproduction theory. Marx once pointed out in *On Capital* that, under the condition of extended reproduction, there had to be a balance of all the products in the first department in addition to those provided to the first and second departments to replace consumed means of production. In other words, the sum of the variable capital and surplus value in the first department had to be larger than the constant capital in the second department, namely $I(V + m) > IIC$. When analyzing the extended reproduction under the condition of technical progress on the basis of the fundamental principles of Marxism, Lenin incorporated the factor that the organic composition of capital increased constantly in the reproduction formula and elucidated the trend of the prioritized growth of the production of the means of production. In Lenin's eyes, the substance of modernization was that backward countries caught up with advanced countries to get in pace with the time. Namely, people adopted catch-up methods to transform economic foundation from small-scale peasant economy to large-scale industry. Only when the country realized electrification and laid the technological

⁵Lin and Hu (2001).

⁶*On Ten Major Relations*, published by Mao Zedong in 1956, contained concentrated discussion on these issues.

foundation of modern large-scale industry for industry, agriculture and transportation could socialism win the final victory. Under such special historical condition, development strategy played a decisive role to economic system. In 1927, the Soviet Union already established the five year plan system. It concentrated on developing heavy industry and collective agriculture and started to study the plans for accelerated growth and development. At the time, the Soviet Union, in fact, already abandoned the economic development strategy of the “coordinated development school” of Bukharin and adopted the model of “ultra-industrialization school” represented by Preobrazhensky.⁷ This model seemed to resolve the issue how industrial growth could obtain original capital and market in a country with a very large proportion of small scale peasant economy. In order to support the implementation of the five year plans, Grigory A. Feldman, who worked in Gosplan at the time, constructed the first socialist economic growth model on the basis of the thought of prioritizing the means of production and the development requirements of ultra-industrialization.⁸ The kernel idea of the model was to form a closed supply and demand cycle inside modern industrial sectors with the associated demands inside modern industry driven by heavy industry, in which agriculture only passively provide capital accumulation and labor in the whole process of modernization.⁹ Later, Stalin focused on formulating socialist economic laws and value laws and other issues in his book *Issues on the Socialist Economy in the Soviet Union* published in the 1950s and established that “the growth of the means of production has a prioritized status under extended reproduction” as one of the principles of Marx’s reproduction theory.¹⁰

III. Two Major Waves of Study in the 1950s–60s and 1980s

In the 1950s–60s, the Chinese academic circle discussed the issues such as the conditions of prioritizing growth, the restrictive role of the means of consumption, the scope of prioritizing growth, namely whether the means of production in agriculture should be included, and the generality of the law of prioritizing growth.¹¹ Such discussion was disrupted and rose again in the 1980s. Most people were of the opinion that the principle of prioritizing the growth of the means of production was generated from the requirements for technological progress and the improvement of labor

⁷The ultra-industrialization model referred to the mandatory realization of industrial accumulation through imposing taxes on non-socialist economic components, mainly those in agriculture, and allowing inflation, namely imposing taxes on all the citizens, through the monopolistic status of the state.

⁸The report of Feldman was summarized in the famous paper *On the Theory of the Rates of Growth of the National Income*, published in the magazine *Planned Economy* edited by the Gosplan in November 1928.

⁹Domar (1957), Jones (1976).

¹⁰See “About the Mistake of Comrade Yaroshenko”, in Stalin (1958), p. 17, pp. 44–63.

¹¹Song Chengxian made a special exploration on this issue early in the 1950s. See Song Chengxian, “The Initial Study on Marx’s Formula on Extended Reproduction and the Principle of Prioritizing the Growth of the Means of Production”, *Fudan Journal (Social Science Edition)*, Issue 2, 1956. A special discussion in the 1960s included the following: Jiang (1962), Qi and Zhuo (1962), Dong (1963).

productivity and thus it was inappropriate to take $I(V + m) > IIC$ as a condition for prioritizing growth. Although there were some scholars who continued to insist that prioritizing growth was an objective law in extended reproduction, many people now took a negative attitude. Those people who negated prioritizing growth held their opinions from different angles and on different bases. Some people believed that the original conclusion was built on the calculation of a series of data with such hypotheses that the accumulation rates of the two major departments were different and that added variable capital would be consumed within one year and hence it was not scientific. For example, one kind of opinion believed that the growth speed of the two major departments was not completely restricted by the organic composition of capital and the improvement of such organic composition was not a continuous process. Another kind of opinion believed that modern technological progress saved both living labor and materialized labor. There were also scholars who started their study from the internal structure of the production of the means of production and its trend of change and believed that faster growth of the means of consumption would emerge and the area of the fastest growth was not necessarily the production of the means of production for manufacturing the means of production but that for manufacturing the means of consumption. These opinions showed bold challenge to classical writers and precious spirit of exploration and reflected the progress of the Chinese circle of economics from certain angle (Table 1).

In this period, research methods also experienced expansion and development. In addition to common theoretical analysis, people also adopted the methods of empirical demonstration and mathematical demonstration. The articles of empirical demonstration mostly used large amounts of historical materials from the UK, the USA, France, Japan and Federal Germany. The treatise of Wang (1983) concentrated on discussing the principle that the production of the means of production grew faster

Table 1 Conditions for extended reproduction: argumentation on basic formula

Representative papers ^a	Marx's basic formula on extended reproduction	Extensions by Chinese scholars	
	Reflecting the requirement for adding the means of production and the decisive role of the first department (formula 1)	Reflecting the requirement for adding the necessary means of production and the restrictive role of the second department (formula 2)	conditions of the balance for extended reproduction (formula 3)
Shi (1961)	$I(V + m) > IIC$	$II(C + m) > I(V + m/x)$	
Song (1961)	$I(V + m) > IIC$	$II(C + m - m/x) > I(V + m/x)$	
Liu (1962)	$I(V + m) > IIC$	Unnecessary, all included in basic formula	

^aShi (1961), Song (1961, 1962), Liu (1962), Ouyang (1979), Lin (1979), Zhang (1979), Xu et al. (1980)

than the production of the means of consumption and its role. He focused on analyzing the whole process of economic development and suggested that the principle be represented as “the principle that the production of the means of production grows faster than the means of consumption” on the basis of the concept that Lenin had used, or as “the principle that the production of the means of production grows faster” for short.¹² The paper of Zhou and Xiong (1981) focused more on piecewise analysis.¹³ Mathematical demonstration was a direction of the development of Marxist growth theory. Before 1966, Ding Xiaokui (1956) applied this method in earlier time and caused relevant debate and calculation.¹⁴ Around 1980s, many papers continued the study and discussion in this respect, for example, the articles of He Juhuang,¹⁵ Xu Xingya¹⁶ and Li Zhou and Yang Xiong as mentioned in the above. One common characteristic of these articles was that they pointed out through quantitative analysis which one of the two major departments grew faster under what kind of specific conditions, depending on what kind of factors, and how they were combined. For example, Juhuang (1979) believed through calculation that prioritizing the growth of the means of production was only a long-term trend rather than something inevitable in the short term under the condition that the organic composition of capital constantly improved. It was an incorrect view that “the growth of the means of production will definitely be prioritized as long as the organic composition of capital increases”, regardless of the span of time.

IV. Discussions on the Growth of Population and Labor in Quantity and on Efficiency

The quantity and quality of population and, in particular, labor was one of the main factors that determined economic growth. In the beginning of the founding of the People’s Republic of China in 1949, the country’s total population was 550 million. After that, the population grew rapidly and it already reached 600 million at the time of the first population census in 1953. The annual increase was about 12–13 million at an annual growth rate of about 2%. After the population census, Ma Yinchu, a famous Chinese economist and the then president of the Peking University, carried out investigation and research for three years and found that the China’s annual population growth rate was over 2.2% and even 3% in some places. After thinking and study, Ma Yinchu published his view on population control successively at the Zhejiang Section of the National People’s Congress in July 1955 and the Eleventh Enlarged Meeting of the Supreme State Conference in February 1957. This was the famous “new population theory”.¹⁷ The reason that it was called “new” was because

¹²Wang (1983), p. 71.

¹³Li and Yang (1981).

¹⁴Zhang (1957).

¹⁵He (1979, 1980).

¹⁶Xu (1980).

¹⁷Of course, people should not think that such population thought was completely invented by Ma Yinchu because the academic and policy positions on population control already had a history of over one hundred years in China. Chinese thinkers such as Hong Liangji, who was reputed as “China’s

Ma Yinchu believed that he was different from Malthus in position, start point and view on population prospect. The “new population theory” believed that “the contradictions in China in the past were class contradictions but now they are mainly production contradictions.” In order to improve people’s life, they had to expand production and reproduction. In order to expand production and reproduction, they had to increase accumulation. And in order to increase accumulation, they had to increase national income. But “if China’s population develops in such a pattern, it will reach 810 million ten years later. What will it be 50 years later? It will be a terrifying figure of 2,619 million.”¹⁸ Population grew too fast and fund accumulation was too slow, so it became necessary to control population so as to lower the proportion of consumption and speed up the accumulation for industrialization. It was also necessary to control population for reasons like food, industrial raw materials and promoting scientific research. Hence, Ma Yinchu proposed the method to resolve population issue: (1) developing production, (2) controlling the quantity of population, (3) improving the quality of population. But he opposed induced abortion and believed that “it is the best that a couple only have two children. The parents who only have two children should be awarded and taxes should be imposed on those who have more than two children”. The view above was relatively, sensitive under special political atmosphere. Out of considerations in politics, Ma Yinchu’s “New Population Theory” was published on *People’s Daily* on July 5, 1957 during the time of “Letting one hundred schools of thought contend”. But this article unexpectedly “forms a trend” with the views of Fei Xiaotong and Wu Jingchao and other scholars, who were about to be condemned as rightists at the time.¹⁹ In 1959, Ma Yinchu’s “new population theory” was criticized. But Ma Yinchu fought back alone tenaciously on the basis of his own position until 1976.

Malthus by American scholar Ho Ping-ti, Yan Fu, Liang Qichao, Sun Yat-sen and Chen Da all had similar views”. The distinctiveness of Ma Yinchu perhaps laid in the fact that he participated in political affairs as an intellectual or a famous economist and asserted that “Production contradictions rather than class contradictions is the main contradiction in the new society” and “There is population issue in socialist society”. And it also laid in his anticipation and vision and the independent spirit of a scholar.

¹⁸Ma (1999).

¹⁹MacFarquhar and Fairbanks (1990).

Very unfortunately, China really fell into the “Malthusian trap”²⁰ in its development later and Ma Yinchu’s concerns became reality. In 1949, China’s national total population was 540 million, which included 480 million rural population. In 1978, its national total population reached 960 million, which included 790 million rural population. During the same period, China’s national farmland area decreased at the rate of 7% or about 7–10 million *mu* (*mu* is a traditional Chinese measurement of area approximate to 667 m².) each year. In the middle of the 1950s, each agricultural worker farmed about 8.8 *mu* land and, in 1978, he only farmed 4.6 *mu*. A great famine occurred from 1959 to 1961 and caused huge social turbulence. It had direct relation with the three years of natural disasters and the mandatory implementation of the people’s commune. But in fact, it was also a reflection in reality of the situation that the weak “tight balance” in the relationship between man and land in China was broken and a Malthusian crisis broke out as the whole society was under population pressure.

After the large-scale movement of the cooperative transformation of agriculture in 1956, serious blind population movement occurred nationwide. In 1957, the government proposed the slogan of “go and work in the countryside and mountainous areas” and called for educated urban youths going to the countryside. According to some estimations, 20 million urban population was transferred to the countryside after 1960. Immediately after that, nearly 18 million educated urban youths were transferred to the countryside.²¹ The government adopted the measure of the large-scale transfer of urban population into the countryside and took the countryside as a pooling space to contain surplus labor. In 1952, urban employment pending rate was 13.2%. In 1957, it was lowered to 5.9% and, in 1978, to 5.3%.²² And because “collective ownership system” and “distribution according to performance” was practiced in the countryside, rural surplus labor was hidden in agriculture. This not only “eliminated” unemployment but also allowed the reception of educated youths, who were actually urban unemployed population, in the movement of “going and

²⁰In 1798, Malthus published *Principle of Population*, in which he pointed out that population grew in the pattern of geometric progression of 1, 2, 4, 8, 16, 32, 64, 128 and 256 each 25 years while food production grew in the pattern of an arithmetic progression of 1, 2, 3, 4, 5, 6, 7, 8 and 9. 200 years later, the proportion between population and food should be 256:9. Hence, the slow growth of food would definitely force the growth of population to drop correspondingly because the iron law that food was the necessity of mankind’s survival would restrict the too fast growth of population at any time. (See the first and second chapters in the Chinese translation published by the Commercial Press in 1992.) Such restriction was also called the “Malthusian trap” or “low-level equilibrium trap”. On September 16, 1949, Mao Zedong published his famous article “The Bankruptcy of Idealistic Historical Outlook”, in which he criticized the explanation on the occurrence of revolution in China proposed by US Secretary of State Dean Gooderham Acheson and negated Malthusianism. He pointed out that “It is a great thing that China has a huge population. We can totally find a solution no matter how many times our population increases and the solution is production.” During a very long period of time after that, the Chinese academic circle basically held a criticizing attitude toward Malthusianism.

²¹For the treatises published recently in the study in this area, see Jin and Jin (2009). Bonnin and Annie (2010). Michel Bonnin is now the professor of the École des Hautes Études en Sciences Sociales.

²²Wu (2003).

working in the countryside and mountainous areas". When viewed from the angle of economics, such social movement was in fact a distorted system design in which the government carried out mandatory population transfer under specific social and political conditions to ease the employment pressure in the city and thus resolve social contradictions.

On the one hand, the general supply of low-quality labor greatly exceeded demand and showed serious excess. On the other hand, high-quality labor with technical expertise was in great scarcity. Besides, the allocation of labor resources was also rather backward. The majority of the resources concentrated in the backward countryside. In response to such a situation, the "new population theory" held, in addition to proposing the view of controlling population, that the fastest way to accumulate funds was to raise labor productivity. Not only the labor productivity of workers but also that of peasants should be improved. Similar views were also reflected in the treatises of other scholars during the same period. For example, Liu (1961)²³ proposed that, after the social labor resources were fully utilized, people could not mainly rely on the increase of the amount of labor but on the improvement of labor productivity to create the source of growth in socialist extended reproduction. Liu Guoguang believed that the speed of economic growth was determined by the speed of the growth of the amount of labor and the speed of the improvement of labor productivity under the condition of the complete match between labor and the means of production, when examined from the consumption of living labor. And when examined from materialized labor, it was directly determined by the growth speed of production fund and the speed of the improvement of the effect of using production fund. On such basis, Liu Guoguang proposed the economic growth model: $t = t_n \times t_h = t_k \times t_i$, in which t stood for the speed of the development of social production, t_n for the speed of the increase of the amount of labor, t_h for the speed of the improvement of labor productivity, t_k for the speed of the increase of production fund, and t_i for the speed of the increase of the effect of using production fund. The economic meaning of such formula was as follows: In order to guarantee that the human resources and material resources in the entire society could both be fully utilized, balance had to be achieved in the distribution of productive accumulation fund among the production units at different technology levels and in different production scales. Only under the condition that the speed of the increase of production fund was equal to the speed of labor increase could social resources be fully utilized and economic growth reach the optimal speed. This conclusion was almost the same as the result obtained from the neo-classical growth theory of Robert M. Solow although they were drawn with different approaches. Solow's conclusion was that, only when the proportion between capital and labor reached the desirable ratio could economy reach the status of stable growth.²⁴

²³Liu (1961).

²⁴See Li Jianwei's comments in "Economic Growth Theory of Prof. Liu Guoguang—Theoretical System and Empirical Study before the Reform and Opening Up", *Economic Perspectives*, Issue 11, 2003.

2 Adjustment of Catch-up Model, Transformation of the Paradigm of Growth Theory and “Growth Miracle” from the Reform and Opening up

The Third Plenary Session of the Eleventh CPC Central Committee held in December 1978 opened up a new road for China’s economic development and brought about the gradual improvement of the environment of academic study. From the time around the launch of the reform and opening up to the end of 1980s, the theoretical study of the academic circle on economic growth mainly followed three lines: The first one was the re-discussion of the Marxist growth model of pure theoretical nature as mentioned above. The second one faced the situation of economic disorder directly and reflected on the economic growth and construction practice from the founding of the People’s Republic of China. Discussion mainly concentrated in the areas of whether people should develop light industry and increase consumption or not and how they should retain moderate growth rate. And the third one included the introduction, study and application of modern economic growth theory.

I. The Defects of the Catch-up Model 30 Years Ago, Its Adjustment and Theoretical Consensus

In the heavy industry catch-up growth model in nearly 30 years after the founding of the People’s Republic of China, people started with breaking the restraints of resource scarcity to economic growth and implemented strict administrative control, price control, and planned rationing system on products and factors so as to ensure the prioritized flow of resources into heavy industry sectors at lower economic costs and to overcome the “short side effect” of weak heavy industry in industrial structure caused to national security and economic development so that the growth of national economy could speed up within the shortest time to achieve the goal of realizing industrialization, catching up with developed economy, making China a powerful country. Such a model possessed the characteristics of low base and high growth, low consumption and high accumulation, low light industry and high heavy industry, low urbanization and high industrialization, lower urban-rural integration and high dual division, low free job choice and high recessive unemployment, low labor incentive and high equalitarianism, low market competition and high quality control, low open exchange and high close cycle, and low stability and high fluctuation. The practice of carrying out heavy industrialization on a land of poverty and blankness through concentrating resources with highly political command economy achieved quantity-driven supra-conventional growth similar to the “Soviet model” within twenty or thirty years after the founding of the People’s Republic of China. But the deviations of such growth model definitely caused huge economic price and negative consequence. There were many studies and reflections in this respect. Observable stylized facts included that the self-driving of heavy industry caused huge periodical fluctuation, which the living standard of the residents could not be improved, and that economic structure became seriously deformed. Economic growth showed rapid development in the 1950s–60s and, after that, Chinese economy fell into serious stagnation and

even approached the brink of collapse from the middle of 1960s to the end of 1970s. The traditional model of allocating resources through command economy seriously restricted the improvement of productivity and social development standard.

China's economic growth rate before the reform and opening up was, in fact, very high. But when examined from "per capital income", a typical index that represented the standard of economic development, the gap between China and the international community in terms of income in this period did not narrow at all but showed a constantly enlarging trend. Calculated on the basis of the materials in the database of the World Bank, the per capita income of "upper middle-income countries" as defined by the World Bank was 3.82 times of that of China in 1965. And in 1982, the figure reached its historical high of 9.43 times. The income gap enlarged by six times in about 20 years. In 1967, the per capita income of "non-OECD high income countries" was 5.24 times of that of China. This figure reached its historical high of 32.13 times in 1981. The income gap between China and these countries increased by 27 times in 15 years. Contradictions between national interests and people's livelihood, accumulation and consumption, and the city and the countryside became increasingly prominent in China in the 1970s.

Subsistence issue forced China to turn around from its catch-up structure and new economic growth model was launched in the reform. In the 1980s, the academic circle already recognized in general consensus that (1) Prioritizing the growth of the means of production and, in particular, heavy industry, for example, the guideline of "taking steel as the key link", was partial. The serious disproportions in national economy that existed for a long period of time from the founding of the People's Republic of China already became the obstruction to the further development of national economy. In order to radically change such irrational economic structure, people had to follow the requirements of basic economic principles in socialism and take satisfying the needs of the people's livelihood as the start point and foothold in the formulation of national economic plans. They should first arrange well the development of agriculture and light industry and then arrange the development of heavy industry centering round the needs of the development of the production in agriculture and light industry. (Feng et al. 1980; Ji 1981, etc.)²⁵ Otherwise, because the development of light industry lagged behind, supply would fall short of demand. This would affect the situation of stability and unity as the extensive community of the mass could not timely get the consumer goods that they needed, which would damage the initiative of the mass to work hard for the "Four Modernizations" of agriculture, industry, national defense, and science and technology. And accelerating the development of light industry could create the important condition of the situation of stability and unity for the construction of the Four Modernizations. (Lü 1980)²⁶ (2) In the transition of economic catch-up model brought about by the reform and opening up, people need to handle well the relationship between the strength of reform, the speed and quality of economic growth and economic stability. For

²⁵Feng et al. (1980), Ji (1981).

²⁶Lü (1980).

example, Wang and Dong (1981)²⁷ pointed out that what the new economic construction road required was to retain the speed of economic development and to achieve sustained, stable and substantial growth. Therefore, it was completely necessary to retain proper accumulation rate. On the one hand, people should avoid the practice of high accumulation rate and low consumption standard in the past and, on the other hand, they should not take the road of low accumulation rate and high consumption standard. At the same time, they should avoid the sharp rises and falls of the accumulation rate, pay more attention to economic effect, and endeavor to realize the unity of the speed, proportion and effect of economic development. In this way, they could avoid various large mistakes and problems that emerged in economic construction in the past so that national economy could retain sustained, stable and high-speed development. Liu and Wei (1985)²⁸ further analyzed the importance of correctly handling the relationship between quality and quantity and between benefit and speed. Hu Ji (1986) proposed that people should correctly handle the relationship between economic system reform and economic development in response to the phenomenon of inflation at the time: On the one hand, they should adhere to reform, advance steadily, and promote economic stability and, on the other hand, they should retain moderate growth, regulate economic environment, and create conditions for further reforms. (3) Studies were made on the regulatory means of the government to promote growth and guarantee stability. For example, a group of middle-aged and young economists proposed the “double-track system” and that people should retain moderate economic growth on the basis of the requirements in the three areas of empirical data, namely, “fiscal boxes”, accumulation-consumption proportion, people-centered comprehensive social development objectives.²⁹ (Dai 1989).

II. The Transformation of Paradigm of the Economic Growth Theory Under the Condition of the Reform and Opening up

As the reform and opening up was pushed forward, the trend of the study on economic growth started to turn from the paradigm of Marxist growth theory to the paradigm of modern economic growth theory. In fact, when the neo-classical economic growth theory underwent the faster formation period early in the 1950s–60s, Chen Biaoru and other Chinese scholars took the magazine *Digest of Modern Foreign Philosophy and Social Sciences* as their learning platform and made several brief introductions on the treatises on economic growth written by western economists, such as Domar, Aitken, Khan, Mead and Joan Robinson. From 1960 to 1964, pitifully such a learning process was disrupted. Right before the launch of the reform and opening up in 1978, Hang Qin published an article entitled “The Role of Science and Technology Revolution to the Economic Growth of Capitalism” after the World War II in the first issue of the magazine *Journal of International Trade* in 1978. Perhaps it was the first paper that directly discussed “economic growth” after the end of 1976 and it signified that the issue of modern economic growth started to officially enter the view of Chinese

²⁷Wang and Dong (1981).

²⁸Liu and Wei (1985).

²⁹Dai (1989).

scholars. After that, several other papers were published in China that examined and studied the issues related to economic growth in the capitalist countries such as the USA, Japan, the UK and France. And Li (1980), Shen (1981) and Liang and Sheng (1982)³⁰ analyzed the relationship of China's economic growth respectively with education, accumulation rate and infrastructure investment, taking into account China's reality. But at the time, the work of the economists in China still mainly focused on introducing and studying the socialist economic growth model proposed by Michal Kalecki³¹ and on exploring the balanced growth of the two major departments and establishing the comprehensive analysis theory that incorporated finance, credit and materials. In August 1985 Tan Chongtai published an article entitled "People Should Study the Thoughts on Economic Growth and Economic Development in the History on the Theories of Economics" in the mainstream academic periodical in China *Economic Research Journal*. This meant that a group of Chinese scholars already started to pay full attention to and study the economic growth theories in the West. After that, theories on economic growth were introduced into China successively and applied in the empirical study on Chinese economy.

In 1984, the Chinese edition of *Agriculture and Industrialization*,³² a treatise written by Mr. Pei-kang Zhang in his early years, was published in China. In 1994, Lin Yifu, Cai Fang and Li Zhou summarized the facts before and after the start of China's economic reform with the standard methods in modern economics and published the book *China's Miracle*. During these 10 years, such theories as "capital formation", "technology innovation", "learning by doing", "structural model", and "comparative advantage" became familiar to the Chinese people as they made reference to international literature in their study. The research paradigm of modern economic growth became main theoretical instruments. People gradually turned in their study from static structural analysis to dynamic path analysis in terms of the method of analysis. Treatises that studied the economic growth were gradually published and a research trend was formed after the start of the new century. It was discovered³³ through the further analysis on the basis of a piece of early statistical work of the author that there were altogether 309 papers that related to "economic growth" in their abstract and 164 that had the term "economic growth" in their title among all the papers published in *Economic Research Journal*, one of China's mainstream economic periodicals, during the 26 years from 1985 to 2010, one every two months on average. And these articles were published in a concentrative manner after 1999—a key period of China's reform when it's economic growth faced important challenges. From 2007, the number of the articles published in *Economic Research Journal* that had the term "economic growth" in their title amounted to 15 each year on average or 1.3 per issue on average, excluding those articles that related to growth. (See Fig. 1) This indicated that people gave more and more weight to growth issue as the reform kept being pushed forward. People not only studied economic growth theories and cared

³⁰Li (1980), Shen (1981), Liang and Sheng (1982).

³¹For example, Yu (1982).

³²Chang (1984).

³³Zhang and Wang (2009).

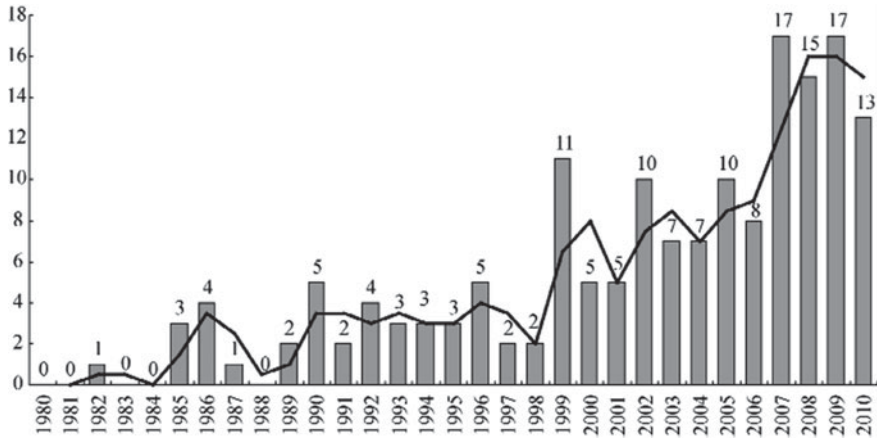


Fig. 1 Economic growth issue attracted increasing attention as the reform kept deepening. *Note* The numbers in the figure are the numbers of the articles that had the term “economic growth” in their title, published in the magazine *Economic Research Journal* in each year during nearly 30 years. The black line is a trend line

about economic indexes related to growth such as GDP but also started to employ new research paradigms and results to serve China’s economic growth and structural adjustment in reality.

The transformation of the paradigm of economic growth theories resulted from the situation that academic atmosphere grew increasingly tolerant under the condition of reform and opening up so that people could better absorb international knowledge dissemination and boldly face Chinese problems in reality. And such transformation in turn provided new theoretical instruments and decision-making supports to the practice in economy. The knowledge innovation effect generated from “learning by doing” and reform innovation effect promoted each other to form a virtuous cycle.

III. Debates and Facts on the “Growth Miracle” of Chinese Economy During the Time of Reform

The progress in economic growth theory was always closely related to reality. The high-speed growth and quick rise of Chinese economy in the second half of the 20th century was an important event in the world’s development history in the century that attracted extensive attention among all the people in the world. In the study on this growth process and its mechanisms, relevant data, theories and empirical literature constantly emerged in China and abroad and relevant stylized facts were constantly summarized. However, just like what was said in a Chinese poem, “It is a ridge when seen horizontally and a peak when seen vertically; it just varies when seen at different distances and heights”, different people had different views and understandings on China’s economic growth when starting their study from different perspectives.

Yifu et al. (1994) proposed the proposition of China’s “growth miracle” early in the 1990s. As time passed, more and more Chinese and foreign scholars recognized

the formulation of China's "growth miracle" when they examined once again the enormous achievement that Chinese economy obtained at the 30th anniversary of the reform and opening up. They would agree more to this view especially after they studied through international comparison. But, of course, there were different voices. Also in 1994, American economist Krugman proposed his challenge on "East Asian Miracle"³⁴ and, after that, he also always disapproved of the formulation of "China Miracle". He believed that the high growth of Chinese economy was to a very large extent caused by the low base after 1976 and China's economic statistical data contained much exaggeration. He also strongly criticized that China produced pollution, wantonly practiced production subsidization and protectionism, and implemented predatory exchange rate policies to accumulate huge trade surplus. He even vehemently called China a "rogue country" in his blog and column. Other scholars believed that it would certainly be easy to see miracle if a country only compare vertically with itself. In fact, China's growth was not miraculous at all. It was only because it had the good luck of meeting the trend of globalization. China's economic achievement at least included two main reasons: Matured industrial technology and a world order favorable to free trade. Such a development condition or opportunity came from the world or, specifically speaking, from the west and not from China. If people made horizontal comparison between China's development in 30 and 150 years in the past in the general framework of the whole world, they could find that the development in the 30 years in the past should be said to be a miracle brought about by the world rather than China's own miracle. The contribution of the reform and opening up laid in that it pushed China to join a world trend that originated from outside China and let China take advantage of the chance of globalization. The reason that there was "advantage" for a latecomer also laid in the fact that such a chance already existed. If China could rely on imitation to make a miracle, it exactly implied the importance of the development of science and technology in the West in 500 years in the past and also of the world order that it established.³⁵ (Chen 2008) Qin Hui believed in a number of articles that it was not overstatement at all to call the enormous achievement of China's reform in 30 years. There was progress when compared vertically and gap when compared horizontally. There was still a long way to go and important tasks to fulfill in China's reform.³⁶

How on earth should people understand the views above? They needed to find an answer from many angles on the basis of the facts about China's growth.

First, when viewed from both horizontal and vertical comparisons in terms of growth speed, economic scale and growth stability, the growth miracle of Chinese economy truly existed. China's GDP annual growth rate approached 10% in the reform and opening up during over 30 years. By the end of 2010, China's GDP aggregate rose to the second place in the world. Its foreign exchange reserve, amounting to over USD 3 trillion, and import and export trade both ranked the top place in the world. The foreign investment that it attracted continued to rank the top place among

³⁴Krugman (1994), pp. 62–68.

³⁵Chen (2008).

³⁶See Qin (2008) and other articles.

developing countries. Its contribution to global GDP already exceeded the USA so that China became an important engine that drove the growth of the world's economy. Calculated With purchasing power parity, the contribution of China's economic growth to the world's GDP growth increased from 2.5% in 1981 to 23% in 2008 and the share of Chinese output in global output rose from 1.8% in 1978 to 9.5% in 2010. When viewed from the stability of growth, prices retained basic stability in China for a long time. The coefficient of variation of economic growth was only 0.29 in 32 years, which reflected the typical characteristic of high steady growth. This was truly rare among high growth countries. It was not exaggeration at all to call such a series of achievements as China's growth miracle.

Second, when viewed from per capita income, China already resolved the issue of food, clothing, housing and transportation of one fifth of the population on the globe. It got out of the poverty trap and entered the upper middle-income development stage. Its income gap with developed countries exhibited a converging tendency and its economic growth brought benefits to the people's livelihood. Its per capita GDP increased from USD 313 in 1980 to nearly USD 4,500 in 2010 and its growth rate ranked in the front among the countries in the world. During 30 years of reform and opening up, China's absolute poverty population reduced by 235 million from 250 million to 15 million. According to the United Nations Millennium Development Goals Report 2008, China already achieved, ahead of schedule, the goal of halving poverty and hunger populations. The data published by the World Bank indicated that 67% of the achievements in poverty alleviation undertakings on the globe came from China in the past 25 years.³⁷ When viewed from the per capita income groups of the world bank, the per capita national incomes of high income OECD countries, high income non-OECD countries, upper middle income countries and middle income countries were respectively 37.5, 20.6, 7.5 and 2.8 times of that of China when the reform was launched in 1978. 32 years later, namely in 2010, these figures were respectively 9.4, 5.7, 1.9 and 0.6 times of that of China. The effect of catch-up of China's per capita income was truly exceptionally noticeable and the gap of wealth between China and developed countries increasingly narrowed.³⁸ It was estimated that the gap of per capita income between China and high income OECD countries would narrow to 3.4 times (See Fig. 2) in 2020. When viewed from such a point, "China Miracle" did have the substance that matched its name.

Third, when viewed from the nature of growth, China was in the development stage of economic catch-up during 30 years of reform. It was still a kind of economic growth with structural disequilibrium. The driving power of this growth mainly came from the following:

³⁷"30 Years of Reform and Opening Up: Absolute Poverty Population Reduced by 235 Million", *People's Daily (Overseas Edition)*, November 5, 2008; also see http://news.xinhuanet.com/politics/2008-11/05/content_10307774.htm.

³⁸One of the most direct testing hypothesis in neo-classical growth theory was about the estimation and prediction of convergence of the economic growth by country or region, which included σ convergence, β convergence, club convergence and γ convergence. In particular, there was already a large amount of literature on the calculation of convergence in the area of the comparison between different regions in China.

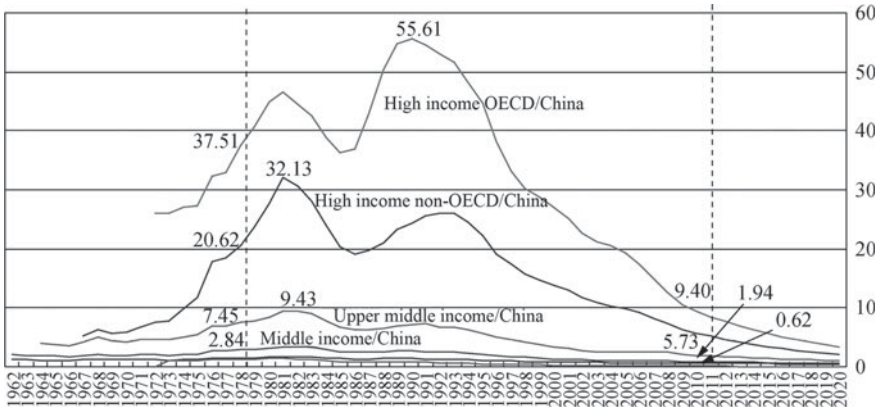


Fig. 2 China and the international community in over 30 years of reform: the catch-up and converging of per capita income. *Source* Calculated and fabricated on the basis of the data of the World Bank. The figures after 2011 were the predictions of the author

1. Factor Investment

The high growth process of Chinese economy from the beginning of the reform and opening up showed great relevance to high investment rate and also high savings rate. This point was supported by almost all related research. From 1979 to 2010, average annual investment rate reached 38.3% and average annual GDP growth rate reached 9.9%. In recent years, investment rate and growth rate also rose very quickly because of the high speed expansion in urbanization. From 2003 to 2010, average annual investment rate reached 43.7% and GDP growth rate reached 10.9% on average.³⁹ In addition to high investment rate, the capital supply that came from the high savings brought about by population dividend and the continuous supply of labor also directly increased the speed of economic growth.

2. System Reform

Reform liberated productivity, promoted personal freedom and economic freedom, pushed forward the optimization of factor allocation, and stimulated the high-speed growth of Chinese economy. The radical driving power for China to realize industrialization and modernization and turn dual economic structure into modern economic structure came from the economic system reform that matched development model. To bring into play the fundamental role of the market in resource allocation was the

³⁹The speed of China's large scale investment and construction was amazing internationally. In the five developed countries in the West after the World War II, namely the USA, Japan, Germany, the UK and France, the investment rate hardly exceeded 30% even when investment was made out of the reasons such as post-war reconstruction. The investment rate in Japan was higher and reached 35% on average from 1960 to 1970. Most of the time, such investment rate in these countries was around 25%. It was still lower in recent years or even below 20%.

key to economic efficiency improvement and continuous economic growth.⁴⁰ (Zhang 2005) But, as reform factors gradually became regularized, such as the establishment of modern enterprise system, the incremental contribution of system reform to technological progress was decreasing.

3. Structural Transformation

The typical characteristics of China's transition economy were continuous high savings rate and high investment rate. The continuous transfer of surplus labor from agriculture to industry, namely industrialization, from the countryside to the city, namely urbanization, and from state-owned entities to non-state-owned entities, namely marketization, was the key that Chinese economy could achieve high-speed growth in a long period.⁴¹ (Yang and Jianfeng 2005) And the transformation from close economy into open economy, namely internationalization, also greatly promoted expansion of economic scale, market expansion, optimization of resource allocation, and technological progress.⁴²

4. Technological Progress

In the early period, scholars in development economics believed that the driving power of economic takeoff laid in capital accumulation but modern economic growth theory believed that technological progress was the determining factor of economic growth and the source of technological progress came from human resource investment and knowledge innovation. Theoretical study had already proven that large amounts of technological introduction, learning by doing, and competitive low-cost imitation-arbitrage mechanism under the condition of opening up accelerated China's technological progress but its effect would decrease as the country's standard of technological progress approached international technological frontiers.⁴³ (Research Group of Chinese Economic Growth Frontiers 2006) However, there was great controversy in empirical study. For example, the research conclusion of a large group of growth calculation literature was that China's TFP growth rate was not high and showed large fluctuation from the beginning of the reform and opening up. It even showed continual decrease in some years, for example, in middle and late 1990s, and it had certain recovery only after the start of the new century. Generally, Chinese economy mainly relied on factor accumulation and, in particular, high investment to drive growth. Low technological progress and high investment and high growth formed huge contrast.⁴⁴ (Zhang and Shi 2003; Pengfei and Bing 2004; Jinghai and An'gang 2005; Qingwang and Junxue 2005; We and Hui 2008, etc.) Some

⁴⁰Zhang (2005).

⁴¹Li and Yin (2005).

⁴²Jiang et al. (2007).

⁴³Research Group of Chinese Economic Growth Frontiers of the Institute of Economics of the Chinese Academy of Social Sciences, "Learning by Doing, Low-Cost Competition and the Transformation of the Path of Growth", *Economic Research Journal*, Issue 6, 2006.

⁴⁴Zhang and Shi (2003), Yan and Wang (2004), Zheng and Hu (2005), Sun and Ren (2005), Guo and Jia (2005), Liu and Zhang (2008).

other research and calculations discovered that the growth of productivity came from embodied and non-embodied technological progress. China's technological progress might be more of embodied or materialized technological progress.⁴⁵ (Zheng 1999; Gang et al. 2003; Yifu and Ren 2007; Yuan and Guowei 2007; Zhao et al. 2007; Wang et al. 2009) In addition, Bai et al. (2006)⁴⁶ and the "Chinese Economy Observation Research Group" (2006) of the China Center for Economic Research (CCER) in the Peking University⁴⁷ discovered that the average return on capital in China was noticeably higher than that of most of developed economies and also higher than that of many other economies in different development stages. This implied larger efficiency improvement because, without it, it was impossible that the phenomena of high return continually emerged and foreign investment flew into China.

5. China's Growth Rate Also Benefited from the Absence of Environmental Restraints

When viewed from the average conditions of the sampling period of 10 years, the growth rate of carbon emission was 4.7% in the 1980s, 3.4% from 1990 to 1999, and 9.2% from 2000 to 2006. The estimation of Yuan (2010)⁴⁸ indicated that China's potential economic growth rate was 9.5% on average from the beginning of the reform and opening up to the present. About 1.3% in this figure was achieved at the cost of environment. After the start of the new century, environment consumption drove about 2% of economic growth on average.

The picture of China's economic growth from the reform and opening up could be seen more clearly when examined by stage⁴⁹: (1) In the 1980s, economic growth was driven by the implementation of all-round responsibility system, the rise of township and town industry, and the "separation of administration and enterprise management"⁵⁰ in state-owned industry. In the first half of the ten years, the one-time improvement of economic efficiency in agriculture, stimulated by rural system innovation, played a more noticeable role to growth. And in the second half, capital accumulation, stimulated by agricultural surplus capitalization and financial diversification, started to lead economic processes as total factor productivity started to drop.

⁴⁵Zheng (1999), Yi et al. (2003), Lin and Ren (2007), Shu and Cai (2007), Zhao et al. (2007), Wang et al. (2009).

⁴⁶Bai et al. (2006).

⁴⁷Chinese Economy Observation Research Group, "China's Return on Capital: Facts, Reasons and Policy Implications", *Report of the China Center for Economic Research (CCER) of the Peking University*, 2006.

⁴⁸Yuan (2010).

⁴⁹Research Group of China's Economic Growth and Macroscopic Stability, "Capitalization Expansion and the Technological Progress of Catch-Up Economy", *Economic Research Journal*, Issue 5, 2010.

⁵⁰The so-called "separation of administration and enterprise management" in the 1980s was that urban industry introduced "market regulation" under state ownership system. It included "replacing profit submission with tax payment" in fiscal distribution, "changing fund allocation into loans" in investment, implementing double-track system in circulation, and implementing "contracting system" in operation, and also the "price reform breakthrough" that occurred in 1988.

(2) The marketization of product prices was basically achieved through the unification of the double-track price system in the 1990s. A large group of enterprises completed “reducing staff and improving efficiency”, “ownership system transformation”, and “restructuring” by means of contracting system. In this period, property right reform, supported by the initiative of “attracting businesses and investments” and financial operation division reform, caused capital formation to manifest more as the situation that scale expansion, driven by the revaluation of physical assets, escalated year by year and the role of TFP diminished year by year correspondingly. (3) After the start of the new century, China’s economic growth entered a development stage led by both internationalization expansion and urbanization acceleration. In particular after 2005, it was manifested more and more as the quick capital formation driven by the appreciation of physical assets and even virtual assets with the participation of international capital. And economic innovation was restrained and total factor productivity retained low growth.⁵¹

Finally, when viewed from the cost of China’s economic growth, China’s growth miracle was achieved through playing a very large price—This was exactly the important reason why some scholars and international organizations believed that China’s growth was no miracle and held a pessimistic view to China’s future. For example, people distorted factor prices or mainly retained low factor prices, overlooked low resource utilization efficiency and environment pollution, and caused high accumulation and low welfare and increasingly enlarging income and regional gaps. These economic distortions and structural imbalances was the price paid for creating growth miracle. And such a kind of catch-up growth model was not sustainable.

3 The Transformation of China’s Economic Growth Model and Its Prospects in the Future

According to China’s economic development compendium, China would achieve the goal of comprehensively building a well-off society by 2020 and it would become one of the moderately developed countries and realize the great rejuvenation of the Chinese nation from 2020 to the middle of the current century. So the ten to twenty years in the future would be a key period of China’s economic growth. Many problems were accumulated in the economic catch-up over a long period of time and Chinese economy was now confronted with many challenges in its development process, such as imbalance between domestic and foreign economies, over-investment, environment and resources restraints, imbalance between the city and the countryside, regional gaps, and too large resident income gaps. The vulnerability of the growth model of Chinese economy, which highly relied on foreign demand, high investment, high resource consumption, and high mission, was fully exposed under the impact

⁵¹Research Group of China’s Economic Growth and Macroscopic Stability, “Capitalization Expansion and the Technological Progress of Catch-Up Economy”, *Economic Research Journal*, Issue 5, 2010.

of global financial crisis from 2008. It already became consensus that economic growth mode had to be transformed, but there were still many difficulties and much controversy on how and where to transform.

I. Explorations on Transforming the Growth Model of Chinese Economy

From the start of the reform and opening up, the discussion on growth model always continued. The traditional formulation about it was the transformation from extension to intension. In the Ninth Five Year Plan, it was officially proposed to transform from extensive to intensive growth model. The Eleventh Five Year Plan had more systematic content. For example, it proposed a series of specific requirements, such as energy conservation and emission reduction, independent innovation, and circular economy. When viewed from the path of growth, China's per capita GDP output path conformed to the incremental catch-up curve, so its growth model belonged to traditional industrialization road. The summarization of Lin Yifu et al. of "catch-up strategy", the proposition of Zhang Jun of "excessive industrialization",⁵² the "low price competition model" of Liu Shijin, the examination of Yuan Zhigang on Chinese economy from the three angles of system, structure and welfare,⁵³ the "exponential growth in the S-shaped growth curve" and the structural transformation between "low-price industrialization and high-price urbanization"⁵⁴ proposed by the research group of China's economic growth and stability of the Chinese Academy of Social Sciences, and the "Chinese-styled growth" summarized by Song Zheng and his two European coauthors⁵⁵ revealed the characteristics of China's growth model from different angles.

Although the Chinese government emphasized the transformation of the mode of economic growth from 1995 and proposed the "scientific outlook of development" from the beginning of the new century, the situation of the dominance of extensive growth did not see substantial change over a long period of time. The reasons for this were as follows: (1) From 1990s, it had always been the top priority among important tasks to push forward economic system reform, centering round enterprise reform, and to endeavor to initially establish socialist market economy by the end of the 20th century. As a result, people, subjectively, did not give sufficient weight in the true sense to the transformation of the mode of economic growth. And objectively, there was still certain room for extensive economic growth because China's socialist market economic system was still incomplete and its original economic growth showed very high degree of extensiveness.⁵⁶ (Zhang 2006) (2) Resource pricing under state control, industrial monopoly, fiscal and taxation system, government

⁵²Zhang (2002).

⁵³Yuan (2006).

⁵⁴The report series of the research group from 2004 to 2010 contained systematic studies on capital formation, technological progress, fiscal policy, financial development, growth imbalance and government responsibilities, and sustained development mechanisms. Its main research results could be found in three treatises. See Zhang and Liu (2007), Liu et al. (2007), Zhang et al. (2011).

⁵⁵Song et al. (2010).

⁵⁶Zhang (2006).

positioning, and cadre political performance evaluation, promotion and appointment system encouraged extensive growth and restricted transformation.⁵⁷ (Liu 2006) (3) The structural imbalance of catch-up could result in very strong path dependence in growth and interest distribution. The stimulation mechanism of government intervention could hardly be changed in the short term. This often resulted in the fixation of intervention paths so that it was difficult to make adjustments to structures and mechanisms. Under the condition of the presence of the progressive increase of the structural returns to scale, there was inherent economic logic and driving power for the government to implement intervention on resource allocation. Government intervention was effective to economic development within certain period. Only when returns to scale showed progressive decrease or could hardly offset the cost of government intervention would transition become necessary.⁵⁸ (Zhang and Wang 2010).

A key issue in China's economic growth model was government intervention. The role of the government in China's economic growth from the reform and opening up was mainly manifested in the following: (1) The CPC managed personal affairs and provided system guarantee for mobilizing, controlling and concentrating and using economics resources nationwide. (2) There was stimulating and discriminatory system supply, such as fixed exchange rate policy and foreign exchange settlement and sales system that matched export-oriented policy. In 1994, exchange rate depreciation stimulated the global competitive advantage of Chinese enterprises. From 1994, China's foreign trade continuously showed surplus and its foreign exchange accumulation increased constantly. In the area of taxation, the policy of "two years of exemption and three years of reduction by half" in enterprise income tax collection and other measures stimulated the inflow of foreign investment and tax refunding encouraged the exporting of the enterprises. The positive fiscal policies in the several years after 1997 directly improved China's infrastructure and laid a solid foundation for China's industrialization and urbanization. Large-scale government investment and industry revitalization plans were implemented after the international financial crisis in 2008. In the area of money creation, a high ratio of M2/GDP over 1.6 was retained for many years continually to provide easy monetary conditions for economic growth. In addition, residence registration management system, policy of prioritizing the development of coastal open-up regions, difference in policy support between state-owned and non-state-owned entities, large enterprise monopoly, unidirectional FDI inflow facilitation under capital control, and equal weight attached to import and export with more stress on export facilitation under the background of gradually easing trade control, and so on, all these were specific manifestations of discriminatory economic management policy under the background of non-balanced catch-up. (3) There was macroscopic counter-cyclic regulation with quantitative instruments as the main means. From the beginning of the reform and opening up, China experienced eight times of macroscopic regulation, in which quantitative instruments was taken as the main means, such as adjusting bank reserves, implementing credit

⁵⁷Liu (2006).

⁵⁸Zhang and Wang (2010).

rationing, controlling the quotas on capital market, and imposing limitations on house purchasing, with administrative means and price means as auxiliary means. Under the situation that price mechanism was not sensitive in the early period of marketization, such intervention mode often showed specific goals and quicker effects. But there were also many problems arising correspondingly.

The government intervention characteristics in China's growth model in the above caused several kinds of contradictory views. One kind of view believed that it was the manifestation of the superiority of China's socialist system with which people could pool resources to achieve major goals. For example, Deng Xiaoping held, when talking about China's reform experience in middle and late 1980s, that "There was the biggest superiority in a socialist country. Namely, when people wanted to something, they could implement immediately without hindrance once they had the determination and made the resolution."⁵⁹ China showed very strong government mobilization ability and concentrated forces in the important events from the beginning of the reform and opening up, such as the continuous large-scale infrastructure construction, a series of macroscopic regulations, and the fight against the impacts of the two international financial crisis in 1997 and 2008. This was summarized by some people as system advantage and even elevated as the "China Model" in recent years. And it attracted a large number of scholars to participate in the discussion about the issue. He Daxing and Yao Yang took "neutral government" as the main characteristics of the "China Model" in their article and believed that it was an important factor for China to succeed in creating economic growth. They believed that the representative government in other countries either represented the rich to implement "rightist" policies or represented the poor to engage in "populism". Only the Chinese government depended on neither the poor nor the rich and thus it did not fear to offend either the poor or the rich.⁶⁰ One example to this was that China laid off over 40 million workers in state-owned enterprise reform, which was something that no other government dared to try. But Qin Xiao et al. believed that strong government intervention should not be regarded as a kind of advantage⁶¹; nor as the specificity of the China model. It might be more of a kind of system defect. Qin Hui seemed to find it difficult to draw a simple conclusion and did not easily recognize the two views above. On the one hand, he found that the so-called "local state corporatism", in which China's local governments got into a race to enter the market to gain profits, broke the lifeless situation under the central control before the reform. It was indeed one of the reasons why Chinese economy was "full of vigor". On the other hand, the situation that the government took advantage of its power to "gain profits freely" was

⁵⁹See a speech of Deng Xiaoping when meeting Stefan Korosec, member of the Presidium of the Central Committee of the League of Communists of Yugoslavia, on June 12, 1987, in "The Pace of the Reform Should Be Stepped Up", *Selected Works of Deng Xiaoping*, Vol. 3, People's Publishing House, 1993, p. 240.

⁶⁰He and Yao (2009), He and Yao (2011).

⁶¹Qin (2010a), pp. 10–11; Qin (2010b).

something completely opposite to non-governmental economic freedom. Therefore, the Chinese economy could rise with it but the China Model should not be popular.⁶²

How on earth should the economic growth model be transformed? Wu (2005)⁶³ proposed the direction of new-type industrialization—technological innovation and the development of service industry. Liu (2006)⁶⁴ made an analysis from the angle of economic development stages. He believed that the Chinese economy was currently in the period of accelerated industrialization and this period was one in which the economy continuously grew at a high speed, the structure of national economy changed drastically, and the cost of social development rose quickly. These phenomena caused the imbalance between the aggregate and structure of macroscopic economy and also resulted in massive unemployment, which aggravated the contradictions between micro- and macroscopic economies. At the same time, he also believed that China's reform entered the stage of historic change. The kernel of the reform changed from enterprise reform to government reform, from the construction of socialist market economy to its improvement, from product marketization to factor marketization, and from the sole criterion in reform performance evaluation to comprehensive criteria. Therefore, he proposed that the radical measure to resolve contradictions in the background of the period of accelerated industrialization and to deepen the current reform laid in transforming the mode of economic growth from one that relied on the amount of factor input to one that relied on the improvement of efficiency. Besides, Gu and Shen (2006)⁶⁵ carried out more detailed classification and quantitative analysis on the transformation of the mode of economic growth and classified it into four types. In addition to the extensive and intensive type (A Type), which were generally familiar to people, there were also three other types of investment- and consumption-driven type (B Type), government- and market-led type (C Type), and developed and underdeveloped type (D Type). They also made quantitative analysis on the transformation of these types of growth modes respectively. They believed that the difficulty of the transformation of A type would become increasingly larger and that the key to the transformation of B type laid in improving the structure and quality of fixed assets investment. Great progress has already been achieved in the transformation of C type but the excessive regulation and control of the factors such as manpower, fund and resources already caused such transformation of the mode of growth to show the lack of vigor. The transformation of D type involved the issues of social justice and the establishment of a harmonious society. Greater efforts needed to be made in improving the harmony in group interests, promoting government integrity, and strengthening environment protection.

The research group of China's economic growth and macroscopic stability of the Institute of Economics of the Chinese Academy of Social Sciences started from 2003 the exploration on the principles related to the dynamic structural transformation

⁶²Qin (2010c); also see *The Economic Observer*, April 2, 2010 at the website: <http://www.eeo.com.cn/2010/0402/166726.shtml>.; Qin (2010d).

⁶³Wu (2005).

⁶⁴Liu (2006).

⁶⁵Gu and Shen (2006).

caused by the situation that urbanization drove the economy, the features of relevant benefits and returns, government intervention, and technological progress and systematically described the stage feature of “incremental returns to scale” in China’s catch-up. The research group also explored the issues that the cost of policy stimulation increased and its returns decreased progressively, that the effect of learning by doing decreased progressively in technological progress, and that the provision of low-cost factors was not sustainable. It also proposed a series of policy suggestions in response to the situation that the original positive factors in catch-up started to exhibit on their negative effect and directly challenged the sustained development of economy. It was believed that people should take space re-allocation as the kernel and gradually turn to the “growth with structural equilibrium” in response to the new development cycle.⁶⁶

II. Predictions and Estimations on Development Prospects of Chinese Economy in the Future

Historical experience indicated that an economy would generally slow down its growth after a period of high growth. Both developed countries in the West and the “Four Tigers” in East Asia all showed similar characteristics of growth slowdown in their development history in the past. Some countries in Latin America and Southeast Asia even fell into the middle income trap because of such slowdown (Table 2).

A large amount of domestic and foreign predictions on China’s economic prospects at present believed that China had retained high growth for over thirty years and that it was very hard for it to become an exception to the historical principle of decreasing growth rate in 10–20 years in the future although China might not fall into “middle income trap”. In earlier time, Wang and Fan (2000) estimated that the growth rate from 2001 to 2010 was 6.58%, which was obviously proven as having a larger deviation from the reality, and the growth rate from 2011 to 2020 was 6.21%. Lin et al. (2003) estimated that the growth rate from 2004 to 2014 was 8.56% and the growth rate from 2014 to 2024 was 7.08%. Qiu et al. (2006)⁶⁷ made calculation and analysis on the prospects of economic growth of China in 16 years in the future. They believed that China could support faster GDP growth at 7% to 9% when examined from the demand space while it could support an annual GDP growth of 7–8% when examined from supply space. But China would have greater difficulty in retaining the growth rate of 9% under its current growth model because of the factors of the economic structure distortions and resource supply bottlenecks caused by too large capital demand. Wang et al. (2009) predicted that China’s potential growth rate was 6.7% in Scenario I and 9.3% in Scenario II from 2008 to 2020. The estimations of Zhang Yanqun, Lou Feng (2009) were 8.3% from 2011 to 2015 and 6.7% from 2016 to 2020. The calculations of the authors were that the potential growth rates of Chinese economy were 9.5% from 2010 to 2015, 7.3% from 2016 to 2020, and 5.8% from 2020 to 2030.

⁶⁶Loc. cit.: Zhang and Liu (2007), Liu et al. (2008), Zhang et al. (2011).

⁶⁷Qiu et al. (2006).

Table 2 Some predictions on the potential growth rate of Chinese economy in the future

Paper ^a	Predicted period (Year)	GDP growth rate (%)
Wang and Fan (2000)	2001 Xiao	6.58
	2011–2020	6.21
Li et al. (2003)	2006hanto	7.8
	2011–2015	7.1
	2016–2020	6.2
	2001–2015	7.7
	2001–2020	7.2
Lin et al. (2003)	2004 Yifu	8.56
	2014–2024	7.08
Wang et al. (2009)	2008 Xiaol(I)	6.70
	2008–2020 (II)	9.34
Zhang and Lou (2009)	2008 u Fen	8.2
	2011–2015	8.3
	2016–2020	6.7
Zhang and Wang (2010)	2010 g Pin	9.5
	2016–2020	7.3
	2020–2030	5.8

Note (1) Some papers had multiple scenario predictions. The table only listed the prediction result of its benchmark model. (2) The table only listed part of domestic literature and did not include the calculations of foreign scholars

^aWang and Fan (2000), Li et al. (2003), Lin et al. (2003), Zhang and Lou (2009), Wang et al. (2009), Zhang and Wang (2010), loc. cit

It could be known from the above that almost all the protections about China’s economic growth in the future in recent years came to the conclusion that its economic growth rate would decrease. From 2010 to 2020, China’s potential economic growth rate would slow down its increase and roughly stayed in the range between 6.7 and 9.6%. After 2020, it would decrease into the range between 5 and 7%. It needs to be emphasized here that China’s economic growth still belonged to the relatively high speed stage when compared internationally although there would not be any two-digit high growth rate in the future like in the 30 years in the past. If Chinese economy could successfully pass the key ten years in the future from 2011 to 2020 at this growth rate, its per capita GDP would approach USD 10,000 in 2020, the lower income limit of high income economy, and China’s GDP, measured according to the purchasing power parity method with the value effect brought about by exchange rate appreciation, could catch up with the USA’s around 2025.

Chinese scholars not only studied in the area of predicting growth speed but also paid more attention to the mechanism of growth in the future. In particular, they took breaking the middle income trap as the basis and proposed more extensive propositions on the driving power, mechanism and path of growth in the future.

The concept “middle income trap” came from the World Bank’s summarization of the experiences of various countries in the world in development. It did not have specific academic logic but contained “experiential revelations”.⁶⁸ “The strategies that various economies relied on to grow from low income economies into middle income economies could not be repeated in their rise to high income economies. Further economic growth will be locked up by original growth mechanism and per capita gross national income cannot break the ceiling of USD 10,000. A country can easily enter a stagnation period in this economic growth stage.”⁶⁹ (Translated from a Chinese edition) With the further discussion of the World Bank and the enrichment of other scholars, the experiential characteristics of the middle income trap could be further summarized as followed: (1) People could not repeat the strategy used in the catch-up stage. Innovation and specialization was the key in the development after a country entered the middle income stage. (2) The government intervention model had to be revised so that the government could optimize resources allocation in a better way to lower the risks in development. (3) As the process of internationalization accelerated, the country needed to increase management experience to avoid the economic recession caused by external impact. (4) The middle-income stage was also a period in which income gap could enlarge easily and quickly, which could in turn cause social conflicts and resulted in stagnation.

The experiential facts in the above about “middle income trap” also seemed to be the main issues that China faced currently in its development. Cai (2008) explored how Chinese economy should get across “middle- and low-income traps”.⁷⁰ Ma Yan (2009) made a systematic international comparison about middle income trap. The Research Group of China’s Economic Growth and Macroscopic Stability (2008) took into consideration on the middle income trap and focused on discussing “sustained growth mechanism”.⁷¹ After 2010, more scholars participated in this theoretical discussion, relating to the formulation of the Twelfth Five Year Plan, and published a large number of papers in the magazines in the China. The core idea of all these papers was how China should successfully carry out structural and mechanism transformation, avoid traps and retain sustained development.

The driving power of the middle and long-term development in the future was also a topic that scholars cared about. (1) Population dividend was a topic in question. For example, Cai (2010) studied the impact of population change to economic growth on the basis of the “Lewis turning point”.⁷² He discussed on the basis of relevant experiences the issue of economic development after the population dividend ended in China in 2015 and estimated the fallback of natural economic growth rate. (2) It was already consensus that urbanization should be taken as the most important

⁶⁸Gill et al. (2007).

⁶⁹Quoted from Ma (2009).

⁷⁰Cai (2008).

⁷¹Research Group of China’s Economic Growth and Macroscopic Stability, “The Mechanism of China’s Sustained Growth: Evidence, Theory and Policy”, *Economic Research Journal*, Issue 10, 2008.

⁷²Cai (2010).

contributor of economic growth and the kernel driving power of the economy. Many topics in this area were discussed, such as the layout, principles, efficiency, financing and sustainability of urbanization. There are so many treatises about it and the representative discussions included Wang Xiaolu's analysis on the size of the cities⁷³ and the study of the Research Group of China's Economic Growth and Macroscopic Stability on the propositions on urbanization like the one that it changed the objectives of government spending.⁷⁴ (3) There were also a great multitude of documents and articles about technological progress, industrial structure and the transformation of the mode of economic development. However, the effect of the transformation was still unsatisfactory and the key was system and mechanism reform.

III. The Still Proceeding Reform in China and the Theoretical Exploration on China's Economic Growth

The nature and origin of national wealth was that kernel content in economics, about which the scholars needed to find an answer. Economic growth theory tried to give an answer about the mystery of the growth of national wealth. The reproduction theory in Marxist economics generated the economic catch-up model of prioritizing the growth of heavy industry under the system of the Soviet Union and such model became the fundamental basis to guide China's economic construction after the founding of the People's Republic of China. Under the special political environment and planned economic system during nearly 30 years, such catch-up model promoted the development of heavy industrialization in China and realized higher growth speed. But it also caused serious consequences such as structural imbalance, distressful people's livelihood, and large economic fluctuations. After the reform and opening up, the introduction of new theoretical paradigms, such as neo-classical growth theory and endogenous growth theory, provided basic thoughts and methods for adjusting the catch-up model of Chinese economy and searching for the road of sustained growth. People achieved a large amount of consensus but there were also many controversies. However, key issues such as system characteristics and structural transformation were still not answered and they were the most critical part in the economic growth of a large group of developing countries, including China.

Another important direction was the theoretical exploration on the growth path and mechanism in post-crisis time. Typical post-crisis characteristics already gradually became noticeable: (1) Traditional global economic division-of-work system disintegrated and the new characteristic of the division of work was that developed countries became consumers and currency suppliers while resources countries and emerging manufacturing countries became production suppliers and world economic growth engines in the outer layer. Thus the re-balancing between various countries was inevitable. (2) The reserve currency statuses and output abilities of developed countries showed constantly enlarging gaps. This resulted in greater global currency-real economy frictions. The economic growth of various countries faced constantly

⁷³Wang (2010).

⁷⁴Research Group of China's Economic Growth and Macroscopic Stability, "Urbanization, Industrial Efficiency and Economic Growth", *Economic Research Journal*, Issue 10, 2009.

rising risks of external impacts. (3) Global financial crisis resulted in the lowering standard of resource mobilization of the governments of developed and developing countries. Debt crisis occurred in succession in European and American countries, the governments' abilities to stabilize economic cycles diminished, and economic fluctuation worsened. On the basis of the characteristics in the above, finding new balanced growth structure and mechanisms for sustained development to effectively defend internal and external risks became the frontier topics in the study of economic growth.

Chinese economy still faced many challenges in reality, China's reform was still far from its destination, and the exploration on the mystery of china's economic growth, would continue. It can be said that the Chinese people faced an unprecedented and very complicated economic development stage in human history in which a major country transformed from catch-up growth to balanced development. The abstraction and resolving of the mystery of Chinese economy and the judgement and prediction on the trends in China became the most intriguing research topics in modern economics. Looking into the future, people have good reasons to believe that Chinese growth miracle would continue. And as the study in growth theory constantly deepens, people will have more profound understandings on the wonderful stories about the process of the growth of national wealth that occur on China's vast land.

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Chapter 28

The Study and Discussion on the Issues of China's Economic Transition and the Transformation of the Mode of Development



Zhouyuan Zhang

On September 15, 2008, the Lehman Brothers, one of the five major investment banks in the USA, declared bankruptcy, which signified the outbreak of the most serious financial crisis and economic crisis on the globe since 1929. According to the materials of the International Monetary Fund, the crisis caused the world's economic growth rate in 2008 to drop to 2.8% from 5.2% and 5.3% in 2006 and 2007. Negative growth rate of -0.6% appeared in 2009. And among developed economies, the growth rate of the USA was -2.6%, that of the Euro zone -4.1%, and that of Japan -5.2%. The International Financial Crisis also exerted larger impact on China. How to respond to the influence of the International Financial Crisis and how to retain the trend of sustained rapid development of Chinese economy, became the hotspot and key area in the discussion and study of Chinese economists in the recent several years.

1 International Financial Crisis Made the Transformation of the Mode of Economic Development in China a Very Urgent Task

At the end of 2009, the central economic work meeting proposed when arranging for the tasks in the economic work in 2010 that "This International Financial Crisis makes the issue of transforming the mode of China's economic development more prominent. With both the international and domestic situation taken into account, there is no time to delay in transforming the mode of economic development. People need to take speeding up the transformation of the mode of economic development

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as the important objective and strategic measure and profoundly implementing and carrying out the scientific outlook of development.”

Immediately after this meeting, main provincial and ministerial leaders and cadres nationwide convened in the Central Party School to make special study and discussion of the issues on profoundly implementing and carrying out the scientific outlook of development and speeding up the transformation of the mode of economic development during February 3–7, 2010. General Secretary Hu Jintao and other comrades in the central leadership made reports. The size of the meeting and the importance attached to it were comparable to the study of the scientific outlook of development several years before.

General Secretary Hu Jintao emphasized in his report on February 3, 2010 that International Financial Crisis made the issue of transforming the mode of economic development in China more prominent and that the impact of International Financial Crisis to the Chinese economy was the impact to the speed of economic growth on the surface but, in essence, it was the impact to the mode of economic development. Speeding up the transformation of the mode of economic development represented to the necessary requirements in adapting to the importance changes in global demand structure and strengthening the ability of Chinese economy in resisting the risks in the international market and improving China's ability of sustained development, in seizing vantage points and winning innovation advantages in international competition in the period after the International Financial Crisis, in realizing the rationalization of the distribution of national income and promoting social harmony and instability, and in adapting to the new requirements in realizing the goal of struggle of comprehensively building a well-off society and satisfying the new expectations of the people and the mass in living a better life. Hu Jintao pointed out that the key to transforming the mode of economic development laid in making efforts in “speeding up” and achieving true effects. And he proposed eight opinions on work priorities. First, people should speed up pushing forward the adjustment of economic structure. Second, people should speed up pushing forward the adjustment of industrial structure. Third, people should speed up pushing forward independent innovation. Fourth, people should speed up pushing forward transforming the mode of the development of agriculture. Fifth, people should speed up pushing forward the construction of ecological civilization. Sixth, people should speed up pushing forward coordinated economic and social development. Seventh, people should speed up developing cultural industries. And eighth, people should speed up pushing forward the transformation of foreign-related development.

Why did the transformation of the mode of economic development become more prominent in China under the attack of the International Financial Crisis? Economists pointed out that some of imbalanced, coordinated and unsustainable problems were accumulated, which seriously restricted the stable, highly efficient and sustainable growth of Chinese economy, as the two-digit or over two-digit growth rates from 2003 to 2007 were basically realized along the path of extensive expansion. The outbreak of the International Financial Crisis in 2008 and its impact made the issues of imbalances and extensive expansion in China more prominent. Decreasing export

required the solution in expanding domestic demand. The improvement of competitiveness in the international market could not continue to be retained with low-price factor costs and free-of-charge environment pollution. Resident consumption accounted for a seriously low proportion to its GDP. Too large gap resident income caused discontent among the public and sharp social contradictions. So there were greater urgency and no time to delay in transforming the mode of economic development. Transforming the mode of economic development meant economic transition, namely the transformation from pursuing quantitative expansion to paying attention to the quality and benefits of growth, so that the economy could truly get on the track of stable, coordinated, highly efficient and sustainable development, or the track of scientific development. In March 2011, it was specifically determined in the compendium of the 12th Five Year Plan adopted at the Fourth Plenary Meeting of the 11th CPC National Congress that people should take development as the theme and accelerating the transformation of the mode of economic development as the main line. Thus transforming the mode of economic development already became the key area and hotspot in the attention and study in various circles.

2 People Had to Take the Strategic Adjustment of Economic Structure as the Main Direction of Their Efforts in Transforming the Mode of Economic Development

If people wanted to accelerate economic transition and the transformation of the mode of development, they had to take the strategic adjustment of economic structure as the main direction of their efforts. This was the consensus of various circles.

In the adjustment of economic structure, people mainly needed to resolve the issue of the imbalance that confronted Chinese economy and to readjust and coordinate the main proportional relations in national economy. Some articles proposed that the current economic imbalance in China was mainly shown in the five following aspects.

I. The Imbalance between Savings and Consumption Which Showed Too High Savings Rate and Too Low Consumption Rate

In 1978, China's savings rate was 37.9%, 12.8% higher than the 25.1% world's average savings rate. In 2008, China's savings rate was 51.4%, 27.5% higher than the 23.9% world's average savings rate. This was because savings rate rose by 13.5% from 1978 to 2008 after the reform and opening up started in China, showing an average annual increase of 0.45%. And in this period, the savings abruptly rose from 40.4 to 51.4% from 2002 to 2008, showing an average annual increase of 1.83%. At the same time, consumption rate dropped largely. In 1978, China's consumption rate was 62.1%. In 2008, it dropped by 13.5% to 48.6%. And in this period, the consumption rate dropped continuously from 2002 to 2008 with an annual average

drop of 1.6%. The decrease of consumption rate was mainly caused by the decrease of resident consumption rate. Resident consumption rate already dropped from 48.8% in 1978 to 35.3% in 2008 or by 13.5% totally. People often talked about the problem of the imbalance between domestic and foreign demands and too high export dependency, which was 18% in 1998 and rose to 36% in 2007. Inadequate domestic demand was in substance seriously inadequate resident consumption demand. Inadequate resident consumption caused China to more and more fall into the vicious circle of production for the production's sake and seriously depart from the purpose of socialist production and the philosophy of "people orientedness". Some experts proposed that consumption rate should be raised to over 55% to the GDP during the 12th Five Year Plan so as to resolve such imbalance issue and the proportion of resident consumption to the GDP should be raised by at least 1% each year. This was very reasonable.

II. The Development of the Tertiary Industry Lagged Behind and Economic Growth Depended on the Secondary Industry Too Much

China's per capita GDP exceeded USD 1,000 from 2002 and reached USD 3,600 in 2009. But the proportion of the added value of China's tertiary industry to the GDP did not rise with the doubled or manifold growth of its per capita GDP but lingered around 40% all the time. It was 41.5% in 2002, 41.8% in 2008, and 42.9% in 2009. At present, the proportion of the added value of China's tertiary industry to GDP was already more than 10% lower than that of other countries at the same development level. The development of the tertiary industry lagged behind and the development of modern service industry also lagged behind. This seriously restricted the improvement of the quality and benefits of China's economic growth, the transformation of the mode of China's economic development, and the improvement of the living standard of Chinese residents. At the same time, China's economic growth depended too much on the development of the secondary industry and, in particular, the development of the industries of "two highs and one resource", namely those of high energy consumption, high pollution and resource product manufacturing, and the real estate industry among the secondary industry. Reportedly, real estate investment generally accounted for 4–6% of GDP on the globe. But the figure exceeded 10% in China in the recent several years so that some people said that the real estate industry abducted the Chinese economy. People needed to speed up the development of the tertiary industry in the future. The growth of the added value of the tertiary industry should be faster than GDP growth so that the proportion of the tertiary industry could be raised step by step. This was also helpful for expanding employment, which included creating a large number of jobs for college graduates, so that human resources could be fully utilized.

III. Input Structure Was Irrational, Too Much Material Resources Was Consumed, and the Contribution Rate of Technological Progress Was Low

Up to now, Chinese economy mainly relied on extensive expansion, which needed large material consumption and showed low efficiency. In 2009, China's GDP accounted for 8% of the global aggregate but it consumed 18% of the world's

energy consumption, 44% of iron and steel, and 53% of cement. And such huge resource consumption was unsustainable. Tremendous resource consumption and low resource possession, and in particular per capita resource possession, caused China's foreign dependency of some main mineral products, such as crude oil and iron ore, to rise from 5% in 1990 to over 50% in the recent several years. Scientific and technological progress did not show fast development. The spending on the funds for research and experimental development accounted for a low proportion to GDP. It was 0.9% in 2000, 1.47% in 2008, and 1.62% in 2009, which was lower than the standard of an innovative country of at least 2%. Accordingly, China showed very high foreign dependency in technology, which exceeded 50%. China was the top automobile manufacturer in the world but almost all of the core technologies and brands of its products were foreign. China was reputed as the "world factory" but it did not own one single world brand. In the recent several years, 90% of its exported commodities were OEM products. In the future, China had to focus on gradually transforming from extensive growth, characterized by "high consumption, high emission and low efficiency", to resource-saving growth mode, characterized by "low consumption, low emission and high efficiency". This was where the kernel of transforming the mode of economic development laid.

IV. The Relationship between Man and Nature Was Not Harmonious and Coordinated

One price of the hyper-speed economic development from 2003 was that ecology and environment deteriorated and the relationship between man and nature became more inharmonious. It was also confirmed in the report of the 17th CPC National Congress in 2007 that economic growth paid large resources and environment prices. The reason for the deterioration of environment and ecology was that China blindly developed a group of industries of high energy consumption, high pollution and high emission. In the 11th Five Year Plan, energy conservation and emission reduction was listed as an obligatory target. But China did not fully achieve the goal of reducing unit GDP energy consumption by 20% as required in the 11th Five Year Plan. Now, resources, environment and ecology already became the largest bottleneck and true hard constraint from the sustained development of Chinese economy. China could not continue to go along the old path of local improvement and general deterioration. Rather, people should resolutely carry on along the road of green development with both local and general improvement and should not take away the interests of later generations anymore.

V. Resident Income Gap Became Too Large

The Gini coefficient, which reflected resident income gap, stayed over the 0.4 warning line in China after the beginning of the new century and it showed a rising trend. The data of the World Bank indicated that the figure reached 0.48 in 2007. Some research report pointed out that the income gap between the 10% of the population with the highest income and that with the lowest income rose from 7.3 times to 23 times from 1988 to 2007, which showed that polarization between the rich and the

poor was worsening. In 2009, the per capita consumption spending of urban resident household was RMB 12,264.55 yuan while that of rural resident household RMB 3,993.45 yuan, the latter being less than one third of the former. This indicated that the consumption gap between urban and rural residents was very large. And if urban and rural inequalities in public services, such as medical care, education and social insurance, were included, the consumption gap between urban and rural residents would be further expanded to the level of 5 to 1. The gap in per capita local gross product was also very large. In 2007, that of Shanghai was RMB 78,225 yuan and that of Guizhou RMB 10,258 yuan, the former being over seven times of the latter. Recently, Wang Xiaolu published an article in the third issue of *Comparative Studies* of the year 2010. He calculated that there was RMB 9.3 trillion yuan invisible income, including RMB 5.4 trillion yuan grey income, which was not included in the statistics of China's total national income. And these two figures nearly doubled than those in 2005. He proposed that, if invisible income was included in the calculation, China's per capita income gap, measured with 10% of the resident households of the highest and lowest incomes respectively throughout the country, should be adjusted to 65 times from 23 times as indicated in statistical data. And correspondingly, the Gini coefficient would be higher than the level of 0.47–0.5. The main reasons for too large resident income gap in China included unfair distribution, power-for-money deal, chaotic distribution order, and inadequate government regulation. Paying attention to fair distribution, speeding up raising the income and consumption standard of high and low-income groups, letting all the people share the fruits of reform and development already became the key to ease social contradiction and maintain social stability. Recently, central leaders proposed the realization of “inclusive growth” and it included to the content of letting the public share the fruits of growth.

At present, developed countries and regions in the world already realized the transformation of the mode of economic development and some principals that appeared in their mode of transformation were worth paying attention to and borrowing from.

Some data indicated that there were three major principles and signs in the transformation of the mode of economic development worldwide (See Table 1).

3 The Relationship Between Transforming Mode, Adjusting Structure and Guaranteeing Growth

Some economists pointed out that people needed to properly slow down economic growth and give up the idea of taking growth speed and GDP as top priorities. They pointed out that the radical cause of China's economic structure imbalance was that people pursued continual hyper-speed economic growth for years. In order to pursue short-term hyper-speed growth, they kept adding investment and implementing industrial and heavy chemical industrial projects in large scale, both of which squeezed consumption. Very high investment increase speed and extensive expansion would typically cause the payment of too large prices in resources and

Table 1 Three major principles and signs in the transformation of the mode of economic development worldwide

Principle	Sign	The time of realization in developed countries and regions
I. Service industry became the main driving power	The proportion of the tertiary industry in GDP exceeded the sum of those of the primary and secondary industries	The proportion of the tertiary industry in GDP in the USA exceeded 50% in the 1940s and later it rose steadily. Now it reached around 80%. The proportion of the tertiary industry in GDP in Japan exceeded 50% in the 1970s and later it rose steadily. Now it reached over 70%
II. Consumption became the main driving power	The relationship between consumption rate and the economic growth formed a U-shaped curve. And after passing the bottom of the U-shape, a steadily rising trend was formed	The rising turning point of the consumption rate of Japan appeared in around 1970. The rising turning point of consumption rate of South Korea appeared in around 1990. At that time, their Engel's coefficient both lowered to below 30%, their proportions of the primary industry lowered to below 10%, and their levels of urbanization rose to over 70%
III. Total factor productivity became the main contribution rate	The part of economic growth explained with the factors of capital and labor input gradually decreased while the part of economic growth explained with total factor productivity gradually increased	The proportion of the economic growth obtained through improving total factor productivity in Singapore was around 10.1% in the 1960s. It rose to 35.5% in the 1970s. And it further rose to 64.1% in the 1980s. The improvement of total factor productivity became the main contribution of economic growth. Such a situation occurred in the USA roughly in the 1950s, in Germany in the 1960s, in the UK, France and Japan in the 1970s, in Singapore and the regions of Hong Kong and Macao in China in the 1980s, and in South Korea in the 1990s

Source *Information for Leaders' Decision Making*, Issue 31, August 2010, p. 5

environment. In order to guarantee increasingly higher economic growth speed, fiscal expenditure was mostly put in infrastructure construction so that there were inadequate fiscal resources to use to support underdeveloped regions and increase the income of low-income groups and the development of social and public undertakings lagged behind. Because of such pursuit of the short-term hyper-speed economic growth, the imbalance of economic structure became more and more serious and prominent.

Therefore, China needed to properly slow down economic growth at present so as to ease the issue of the imbalance of economic structure. It needed to turn gradually from pursuing two-digit growth rates in the past to pursuing a growth rate around 8%. From 2010, the government strengthened the phasing out of backward production capacities, cancelled the export tax refund of part of the products in the industries of “two highs and one resource”, and strengthened the work in energy conservation and consumption reduction. Various local authorities all raised minimum wage standard, controlled the scale and growth speed of lending in the banking industry, rectified local financing platforms, implemented regulation and control on real estate industries, and so on. All these measures contributed to bring down economic growth rate and hence they were helpful to the adjustment of economic structure.

However, some of the economists worried that the government measures in the above might cause “double dip” to occur to Chinese economy, which was unfavorable to the steady faster development of the economy. But in fact, such concern was unnecessary. Chinese economy fell back to a certain extent in the second half of 2010. This met the requirements of the government’s macroscopic regulation and thus it was favorable to mode transformation and structural adjustment. And it was not a “double dip” at all. The economic growth rates of the third and fourth quarters of 2010 still approached two digits and reached 9.6 and 9.8%. And the economic growth rate in the whole year still reached 10.3%. If people could not tolerate the fallback of growth rate to a certain extent and always kept it at two digits, the so-called structural adjustment would end up in nothing. Such a practice would even make structural imbalance more serious so that Chinese economy would eventually come to “hard landing”. This indicated that people needed to change the philosophy of growth and development in the process of China’s economic transition. They needed to turn from pursuing two-digit growth to pursuing normal medium high-speed growth, namely the growth rate of 8–9%. Only in this way could they create relatively good environment and conditions for speeding up the adjustment of economic structure.

Some economists pointed out that people did not need to worry about economic dip at all under China’s current system and policy situation. At present, various circles and, in particular, local governments still took GDP as their top priority. They sought quick success and instant benefits and they would do everything to increase economic growth speed whenever there was a bit possibility. Namely there was strong driving power in pursuing higher and even higher economic growth speed and people hoped that expansionary macroscopic economic policies would always be implemented. The most difficult task in China at present was to control the issues brought about by too fast economic growth, such as resource strain, environmental deterioration, inflation, extreme disparity between the rich and the poor, and the failure to make

the people better off while the country became powerful. The gradual return to normal growth was possible only under two circumstances. One was that domestic and foreign environments forced China to slow down economic growth. Otherwise, the social turbulence would occur and social stability would be endangered. This was passive adjustment. The other was to achieve such a goal through deepening reform, which was mainly to push forward government transition. The government did not take pursuing GDP growth as its top priority but changed into a public service government. This was spontaneous adjustment. People should endeavor to realize spontaneous adjustment.¹

4 How to Speed up the Transformation of the Mode of Economic Development

There were many approaches to speed up the transformation of the mode of economic development, including vigorously improving the ability of independent innovation, developing strategic emerging industries, improving laws, regulations and rules, adjusting policies, and so on. In addition, many economists emphasized more on deepening the reform in various areas to provide systems support to the transformation of the mode of economic development.

Some economists believed that the four major strategies needed to be implemented in speeding up the transformation of the mode of economic development. The first strategy was the strategy of improving people's livelihood and expanding domestic demand, which took improving social security and expanding basic public service as its priority. The second was the strategy of urbanization, which took turning peasant workers into urban residents as its priority. The third was the strategy of industrial transformation and upgrading, which took enhancing the competitiveness of middle- and high-end industries as its priority. And the fourth was the strategy of green development, which took promoting energy conservation, emission reduction and efficiency improvement and ecological environment protection and lowering unit GDP carbon intensity as its priority. Some believed that people should speed up forming the systems and mechanisms favorable to the transformation of the mode of economic development. First, they should speed up the economic system reform which took the transformation of the mode of economic development as its main line. Second, they should speed up the administrative management system reform which took government transition as its main line. Third, they should speed up the social system reform which took adapting to the transformation of society and public undertakings as its main line. And fourth, they should speed up the all-round reform which took adapting to the development of low-carbon economy as its goal.²

Some economists emphasized that people had to unswervingly push forward reform and opening up and establish a standardized and legalized market system

¹See Zhang (2010), Chang (2010).

²See Wei and Zhang (2011).

so that market could fully play its fundamental role in resource allocation. Some believed that people should take government transition and fiscal work transition as priorities when deepening reform. In order to support the work of taking the transformation of the mode of economic growth as the key link in implementing the 11th Five Year Plan, in 2005 it was specifically proposed in the suggestion of the CPC Central Committee on the 11th Five Year Plan that speeding up the administrative management system reform was the key to comprehensively deepening reform and improving the standard of opening up to the outside world. There were inherent connections in this point. At the time, it was generally recognized that people had to depend on government transition to push forward and guarantee if they wanted to practically transform the mode of economic growth. Government transition was the main content in administrative management system reform in the current stage. But pitifully this important assertion on the important meaning of speeding up administrative management system reform was later weakened and not put into practice so that the construction of service-oriented government lagged behind. Therefore, people should highlight government transition in economic transition in the future. They should implement the transformation from economic construction oriented government to service-oriented government and handle well the relationship between government and market and enterprise. The government should not take pursuing high-speed GDP growth as its main goal but should take doing well public service as its top priority.

Fiscal work transition was very important in the process of government transition. Fiscal work needed to be transformed from economic construction oriented type to public service oriented type. The fiscal expenditure in both central and local authorities should mainly be used in public service rather than economic construction. In addition to necessary infrastructure, fiscal expenditure in economic construction was mainly used in the area of the “Three issues of agriculture, the countryside and farmers” issue of agriculture, the countryside and farmers, such as implementing water resource projects, improving crop strains, promoting and spreading advanced agricultural technologies, and providing direct subsidies to peasants for growing grains and other items. People needed to vigorously adjust the structure of fiscal expenditure and largely raise the spending on public service, which included education, medical care and health, employment training and service, social security, and public culture construction. These items could effectively raise the standard of income and consumption of the public and in particular low-incomers and increase the proportion of resident consumption to GDP. This was exactly what was required in transforming the mode of economic development.³

³See Wu Jinglian, “There Is Absolutely No Way Out if People Turn Back in Economic Transition”, Chi Fulin, “The Reform during the 12th Five Year Plan That Takes Transforming the Mode of Development as the Main Line”, in China Institute for Reform and Development ed., *30 Renowned Economists Diagnosing China’s Economic Development Mode*, China Friendship Publishing Company, 2010.

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Chapter 29

The Rewriting of the Textbook of Sinicized Marxist Political Economics After the Beginning of the New Century



Jiayong Hu

The textbooks of Marxist political economics played a very important role in making Marxism applicable and acceptable to China, to the time and to the public. From the founding of the People's Republic of China and, in particular, from the reform and opening up, the textbooks of Marxist political economics experienced constant change and development with the developments in practice. From the beginning of the new century, the textbooks of Marxist political economics constantly absorbed the latest results of theoretical study of sinicized Marxism. These books paid more attention to the general principles of market economy, to the issues of resource allocation and economic development, to the evolution of international interest structure under economic globalization and its influence to China, and to the new changes in contemporary capitalism. New editions of these textbooks appeared constantly.

1 The Compilation of the Textbooks of Marxist Political Economics in China in the Beginning

Marxist political economics was one of the three major components of Marxism and the “most profound, comprehensive and detailed demonstration and application” of the theory of Marxism.¹ It was a fundamental discipline of economics which provided basic theoretical support to major policies and guidelines of the CPC and the Chinese government. The CPC and the Chinese government always attached great importance to the work of teaching and studying Marxist political economics. In 1954, the Institute of Economics of the Soviet Academy of Sciences compiled and

¹Marx (2009), p. 17.

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published *The Textbook of Political Economics* and its Chinese edition was published by the People's Publishing House the next year. In 1959, Mao Zedong required that leaders and cadres at various levels should read this textbook. He published a series of important talks² on reading *The Textbook of Political Economics* of the Soviet Union and proposed several important thoughts on the basic theoretical issues in political economics, such as the object of research in political economics and the productivity, productive relations and ownership systems in socialism. All these exerted profound influence.

There were mainly three theoretical origins of the textbooks of Marxist political economics in China.

First, the chief source of the part on capitalism in political economics was *On Capital* by Marx and *On Imperialism* by Lenin. Its basic concepts, theoretical framework and basic political connections all came from these two classical works. Because *On Capital* and *On Imperialism* possessed theoretical completeness and logical rigor, both the basic categories and framework structure of the part on capitalism in political economics, which was based on them, retained stability and remained basically intact until today.

Second, the part on socialism in political economics mainly came from the conceptions of Marx and Engels on future society and the thoughts of socialist economy proposed by Lenin, Stalin and Mao Zedong when they led the practice of socialist revolution and construction. Marx and Engels did not give a detailed blueprint on future society. They conceived and discovered the new world when criticizing the old world. Their conceptions about the future society mainly included the public ownership of the means of production, planned social production, distribution of the means of consumption according to performance, and the gradual perishing of the state. These thoughts were mainly seen in their classical works, such as *The Communist Manifesto*, *Critique of the Gotha Program*, *Socialism: Utopian and Scientific*, and *On Capital*. These theoretical views exerted profound and significant influence on socialist political economics. In the practice of leading the proletariat to seize power and implement the transition into a socialist society, Lenin formed the theory on socialist transition and construction. Lenin believed that the economic foundation of socialism had to be formed through vigorously developing productivity and constantly improving labor productivity. In the socialist transition in a country with relatively low development standard of capitalism or a colonial or semi-colonial country and, in particular, those in the East, people needed to retain commodity-money relationship and formed, developed and strengthened with that the economic foundation of socialism. Particularly, when new economic policies were implemented at the end of 1920 and in the beginning of 1921, Lenin proposed the thoughts of paying attention to the principle of material interests, developing the economy with multiple ownership systems, and developing market economy. In the book *Issues on the Socialist Economy in the Soviet Union*, Stalin made initial exploration on the theory of socialist economy and proposed many important thoughts. He believed that, because there were two forms of public ownership systems, namely whole

²See Mao (1999), pp. 103–140.

people ownership system and collective ownership system, under the condition of socialism, there would definitely be commodity exchange between them and that the law of value still played its role but its action was mainly limited to the area of circulation. He also believes that socialist economic principles had objectivity and formulated some important principles in socialist economy. When the first generation of the CPC central leadership, centered round Comrade Mao Zedong, led China's revolution and construction processes, the Mao Zedong thought, which contained the innovations in Marxist political economics, was formed. Thoughts that had far-reaching influence were proposed in the areas of the basic and main contradictions of socialism, the fundamental task of socialism, the important proportional relations of national economy, and commodity and money in socialist society.

Third, the system structure of China's political economics mainly came from *The Textbook of Political Economics* of the Soviet Union. The system structure of this textbook was one that included an "introduction" and "three parts".³ Namely a "dichotomous method" was adopted in general to divide political economics into the "part on capitalism" and the "part on socialism". It was worth pointing out that the part on socialism in *The Textbook of Political Economics* of the Soviet Union was compiled according to the logic of planned economy. For example, it was pointed out in the analysis on the nature of labor under socialist system that "labor possesses direct sociality under socialist system and it is the labor organized in a planned manner."⁴ And it was pointed out in the analysis on commodity production and the law of value under the condition of socialism that "the necessity of commodity production under socialist system is determined by the two basic forms of socialist production, state form and collective farm form", that "commodity production and circulation is limited to personal consumer goods in its scope", and that "the law of value cannot play the role of the production regulator under socialist system".⁵

The textbooks of Marxist political economics published in China before the reform and opening up in which the part on capitalism were influential mainly included *Political Economics* edited by Yu Guangyuan and Su Xing and *Political Economics* edited by Xu He. The system structure and basic concepts in these books followed *On Capital*, which were relatively mature, and they basically remained intact in use until the present. Those textbooks of political economics in which the part on socialism was influential mainly included *Political Economics* edited by the Department of Economics of the Peking University, *Political Economics* edited by the Department of Economics of the Renmin University, *Political Economics* edited by the Department of Political Economics and the Institute of Economics of the Nankai University, *The Talks on Political Economics* edited by the Department of Politics and Economics of the Liaoning University, and *The Lectures on Political Economics* edited by the Department of Political Economics of the Wuhan University. When

³See the Institute of Economics of the Soviet Academy of Sciences ed., *The Textbook of Political Economics*, Vol. 1 & 2, People's Publishing House, 1956.

⁴The Institute of Economics of the Soviet Academy of Sciences ed., *The Textbook of Political Economics*, Vol. 2, People's Publishing House, 1956, p. 477.

⁵Ibid, pp. 495–500.

viewed from system structure and basic content, the part on socialism in political economics in this period followed the logic of planned economy and developed with socialist public ownership system, basic economic principles of socialism, and principle of developing in a planned and proportionate manner as its main contents. Take the part on socialism in the textbook *Political Economics* edited by the Department of Political Economics and the Institute of Economics of the Nankai University as an example. Its revised edition was printed in 1976. It was divided into six parts in structure. “Part One General Introduction” discussed the nature of socialist society. “Part Two Production Process of Socialism” discussed the characteristics of socialist public ownership system and socialist production. “Part Three Circulation Process of Socialism” discussed product exchange, money circulation and the law of value under the condition of socialism. “Part Four Distribution Process of Socialism” discussed the distribution according to performance of personal consumer goods. “Part Five General Process of Socialist Production” discussed the principle of developing in a planned and proportionate manner. And “Part Six Socialism and Communism” discussed the transition from socialism to communism. This textbook had theoretically inspiring points. For example, it was believed that the production process in socialism was the unification of direct social production and commodity production. And it was pointed out that socialist production possessed the side of commodity production. But its base tone was of planned economy.

It was worth pointing out that the Chinese circle of economics already started to break through the restraints of the thought of planned economy and explore the theory of socialist market economy before the reform and opening up. These explorations exerted important influence to the compilation of the textbooks of Marxist political economics in China after the reform and opening up. For example, Sun Yefang published in 1956 the article *Putting Planning and Statistical Work on the Basis of the Law of Value* and pointed out that, “only when putting planning on the basis of the law of value can people make planning the planning in reality and bring into full play the effectiveness of planning”. In 1960, Sun Yefang organized the researchers in the Institute of Economics of the Chinese Academy of Sciences and wrote the book *On Socialist Economy* according to the process method for the first time ever, which contained the parts of “production process”, “circulation process” and “general process of social reproduction”. After Sun Yefang passed away in 1983, his assistants and students sorted out, selected and published *The Outline of On Socialist Economy*.⁶ For another example, Gu Zhun published in 1957 “A Tentative Discussion on Commodity Production and the Law of Value under Socialist System”, which could be said to be a pioneering work of the theory of socialist market economy. In this famous paper, Gu Zhun went beyond the particular assertion of classical writers that “commodity exchange and money will be abolished in socialism”. He believed that economic accounting was the fundamental reason why there were the categories of money and value in socialism. Socialist economy was the unification of economic planning and economic accounting. The law of value was the basic

⁶Sun (1956, 1998).

economic principle of socialism. People could apply the law of value in different degrees in socialist economy, even to the extent of “letting price float freely to regulate production and distribution”.⁷

2 The Compilation of the Textbooks of Marxist Political Economics in China from 1978 to the End of the 20th Century

In 1978, China entered the new historical period of the reform and opening up. Important changes started to occur to China's economic system and the interest relations between people showed constant adjustments. Changes occurred to the reality from which Marxist political economics originated. The CPC constantly deepened the understandings on the substance of socialism, the socialist economic system and regime, and the development principles of socialist economy and achieved new important theoretical innovations. The circle of political economics carried out heated discussion on the basic theoretical and practical issues with respect to socialist commodity production and the law of value, distribution according to performance, rural reform and state-owned economy and enterprise reform and achieved important theoretical progress. And changes occurred constantly with such discussion to the content of the textbooks in political economics and, in particular, to the content in the part on socialism.

In the 1980s, the textbooks of political economics published in China that had important influence were *Political Economics*, edited by 13 colleges and universities in North China, or the “North China edition” for short, and *Political Economics*, edited by 16 colleges and universities in South China, or the “South China edition” for short. Compared with the textbooks in the past, these textbooks already incorporated the contents related to commodity economy and economic system reform into the original system framework. Take the part on socialism in the “North China edition” of *Political Economics* as example.⁸ The first edition of the book already included the contents related to commodity economy, such as the principle of material interests, commodity production, the law of value, distribution according to performance, enterprise independence, cost and profit, as important contents. When analyzing commodity production and commodity circulation, the textbook believed that “commodity production and commodity circulation must be retained between state-operated enterprises and collective enterprises and between collective economies. Besides, commodity production and commodity exchange must also be implemented between various state-operated enterprises inside the whole people ownership system.” The existence of commodity production and commodity circulation was “determined by the material interest relations between the producers which

⁷Gu (1957).

⁸See Editorial Group of 13 Colleges and Universities in North China, *Political Economics (The Part on Socialism)*, Shaanxi People's Publishing House, 1980.

were restricted by the nature of socialist labor”.⁹ The textbook further recognized the regulatory role of the law of value to production. When compared with *The Textbook of Political Economics* of the Soviet Union, these representations showed noticeable progress. The third edition of the textbook was published in 1985 and it absorbed the spirit of the “Decision of the CPC Central Committee on Economic System Reform” adopted at the Third Plenary Session of the 11th CPC Central Committee in 1984. Large modifications were made to the structure of parts and chapters and to the contents. Chapters and sections were added to the book, which were about the contents related to the economic system and model of socialism, planned socialist commodity production, market and market mechanism in socialism, and foreign related economic relations of socialist countries.

In the 1980s, another textbook that showed interesting exploration was the *General Theory of Socialist Economics* edited by Gu Shutang and published by Shanghai People’s Publishing House in 1989. The textbook took contemporary socialist economy as its object of study and made bold and novel attempts on the system structure of the part on socialism in political economics. The whole book consisted of four parts, namely “Part One Intrinsic Characteristics of Socialist Economy”, “Part Two Microscopic Economic Operation”, “Part Three Macroscopic Economic Operation” and “Part Four Economic Development”. Such a system structure was rather original even when examined from the economic research perspective of the present time.

The textbooks published in the 1980s that had important influence also included the following, as listed in the order of the year of publishing: *A Textbook of Political Economics* (First Edition) edited by Jiang Xuemo and published by Shanghai People’s Publishing House in 1980, *A Course of Political Economics* (First Edition) edited by Song Tao and published by China Renmin University Press in 1981, *Political Economics (The Part on Socialism)* edited by Zhang Youren, Liu Fangyu, Li Kegang, Chen Dehua et al. and published by Peking University Press in 1984, *Political Economics (The Part on Socialism)* edited by Zhang Zhuoyuan and Yu Zuyao and published by China Outlook Press in 1985, and *The Principles of Political Economics* (First Edition) edited by Wei Xinghua and Gu Xuerong and published by Economic Science Press in 1989.

In the 1990s, the undertakings of socialism with Chinese characteristics and of the reform and opening up achieved further advancement and the CPC made a series of important theoretical innovation. The theoretical innovations that exerted important influence to the compilation of textbooks of political economics mainly included the following: The first one was the South Tour Speech of Deng Xiaoping in 1992. This was a concentrated manifestation of the important developments of the sinicization of Marxism. It was proposed that the substance of socialism was to liberate and develop productivity, to eliminate exploitation and polarization between the rich and the poor, and to finally reach common prosperity. Planned economy was not equal to socialism while market economy was not equal to capitalism. Planning and market

⁹Editorial Group of 13 Colleges and Universities in North China, *Political Economics (The Part on Socialism)*, Shaanxi People’s Publishing House, 1980, p. 102.

were both means. Whether there was more planning or market was not the substantial distinction between socialism and capitalism. Development was the top priority, and so on. The second one was that the 14th CPC National Congress held in October 1992 determined that the goal of China's economic system reform was to establish socialist market economic system and pointed out the basic direction of China's reform and opening up. The third one was that the Third Plenary Session of the 14th CPC Central Committee held in November 1993 adopted the "Decision of the CPC Central Committee on Several Issues on Building Socialist Market Economic System" and gave a specific definition of the basic framework of socialist market economic system. And the fourth one was that the 15th CPC National Congress in 1997 proposed that the form of realization of public ownership system could and should be diversified and nonpublic ownership economy was an important component of China's socialist market economy. People should allow and encourage capital, technology and other production factors to participate in income distribution. The discussion on socialist market economy in the Chinese circle of political economics also deepened gradually. A group of important theoretical works emerged, discussing important theoretical issues such as the target model and path of economic system reform, price reform, ownership system reform, strategic restructuring of state-owned economy, and distribution of courting to production factors.

In the 1990s, the system structure and content of the textbooks of political economics in China experienced further change on the basis of the important theoretical innovations of the CPC and the progress in the study of political economics. Take the textbook *Political Economics* edited by the Department of Social Sciences of the State Education Commission as an example. Although the overall structure of the textbook did not change, which still consisted of the part on capitalism and the part on socialism, important innovation was made in the system structure of the part on socialism, which proposed the structure of the "four parts" respectively of basic economic system of socialism, socialist market economic system, microscopic economic operation of socialism, and macroscopic economic cooperation and regulation of socialism. It was convenient to make a theoretical discussion and deduction on the system characteristics and operation mechanisms of socialist market economy with such a system structure. It had higher conformity to the reality and won higher recognition among the students and teachers in colleges and universities.

3 The Compilation of the Textbooks of Marxist Political Economics in the New Century

From the beginning of the new century, China initially established socialist market economic system and faced the task of improving socialist market economics system. Economic development entered a new stage of speeding up the transformation of the mode of economic development, pursuing the quality and benefit of economic development, and constructing harmonious society. Economic globalization showed rapid

development. In 2001, China became a WTO member. International division of work and interest structure underwent profound changes. The CPC achieved new breakthrough in theoretical innovation. It proposed the outlook of scientific development and formed a theoretical system of socialism with Chinese characteristics, which included the important strategic thoughts of the Deng Xiaoping theory, the important thought of the “Three Represents”, and the outlook of scientific development. Change occurred to the focal point of the theoretical discussion and the circle of political economics. Basic theoretical issues in political economics attracted attention once again. New progress was achieved in the study of wealth theory, labor theory, value theory, distribution theory, ownership system theory, fairness and efficiency, planning and market, and opening up theory. In the study of economic system transition, more attention was paid to discussing the reform of the supportive systems, key areas and important links of modern market economy. Economic development theory received more and more attention. A series of research results were obtained on the issues of economic development, such as the source and driving power of economic development, economic development and structural evolution, the new roads of industrialization and urbanization, and the construction of resource-saving and environment-friendly society (Table 1).

Under the background of new practice and theory, important changes occurred to both system structure and content of the textbooks of Marxist political economics.

First, people attempted to break the “dichotomous method” with which traditional textbooks structurally divided political economics into the part on capitalism and the part on socialism. Basically, there were two ways to achieve such breakthrough.

One way was to add a new piece in traditional textbook in addition to the part on capitalism and the part on socialism and formulate the general theory of market economy. The basic theoretical basis was that both socialist and capitalist market economies were modern market economy and thus possessed the general characteristics of modern market economy. To abstract the generalities of market economy was an important task of the textbooks of political economics, which could help the students clearly understand the general principles of the operation of modern market economy. Of course, the circle of political economics had controversies on what categories could be included in the generalities of market economy. And the largest controversy was whether the two categories of “capital” and “residual value” could be included in the generalities of market economy. The representative textbook in this aspect was *Political Economics* edited by Pang Jinju, Hong Yinxing, Lin Gang and Liu Wei with Wu Shuqing as advisor. The first edition of the textbook was published by Higher Education Press in 2002 and the second edition in 2008. The textbook consisted of “introduction” and “three parts” as its system structure. The “three parts” were respectively “Part One General Theory of Political Economics”, “Part Two Capitalist Economy” and “Part Three Socialist Economy”. The first part discussed the general theory of market economy. It covered a very extensive area and included commodity, value, money, capital, credit, competition, monopoly, reproduction, income distribution, fairness and efficiency all as the general categories of market economy. And the most distinctive and controversial category included in the generality of market economy was capital.

Table 1 Important theoretical and practical innovations that exerted important influence to the compilation of the textbooks of marxist political economics in China

December 1978	The Third Plenary Session of the 11th CPC Central Committee was convened. It was resolved that the focus of the work of the whole party be transferred to the construction of socialist modernization. Major policies and guidelines were determined about the reform and opening up. China entered the new period of the reform and opening up and the construction of socialist modernization
September 1982	The 12th CPC National Congress was convened. The construction of socialism with Chinese characteristics and the principle of “taking planned economy as the main part and market regulation as the auxiliary means” were proposed
October 1984	The Third Plenary Session of the 12th CPC Central Committee adopted the “Decision of the CPC Central Committee on Economic System Reform” and proposed that socialist economy was planned commodity economy based on public ownership system. Deng Xiaoping commented that the decision “writes an initial draft of political economics. It is the political economics that combines the basic principles of Marxism with China’s practice in socialism.” ^a
October 1987	The 13th CPC National Congress expounded the theory of the primary stage of socialism and pointed out that the planned socialist commodity economic system was a system of the inherent unification of planning and market. In general, the new economic operation mechanism was one in which “the state regulates the market and the market guides the enterprises”
January and February 1992	The South Tour Speech of Deng Xiaoping was a concentrated manifestation of the important developments in the sinicization of Marxism
October 1992	The 14th CPC National Congress determined that the goal of China’s economic system reform was to build socialist market economic system
November 1993	The Third Plenary Session of the 14th CPC Central Committee adopted the “Decision of the CPC Central Committee on Several Issues on Building Socialist Market Economic System” and proposed the basic framework of socialist market economic system
September 1995	The Fifth Plenary Session of the 14th CPC Central Committee adopted the “Suggestions of the CPC Central Committee on Formulating the Ninth Five Year Plan on National Economic and Social Development and the 2010 Prospective Goal” and proposed the implementation of two fundamental transformations significant to the general situation: one was the transformation of economic system from traditional planned economic system to socialist market economic system and the other was the transformation of the mode of economic growth from the extensive type to the intensive type
September 1997	The 15th CPC National Congress proposed that the form of realization of public ownership system could and should be diversified and nonpublic ownership economy was an important component of China’s socialist market economy. People should allow and encourage capital, technology and other production factors to participate in distribution

(continued)

Table 1 (continued)

October 2000	The Fifth Plenary Session of the 15th CPC Central Committee adopted the “Suggestions of the CPC Central Committee on Formulating the Tenth Five Year Plan on National Economic and Social Development” and pointed out that people had to take development as the theme, structural adjustment as the mainline, the reform and opening up and scientific and technological progress as the driving power, and improving the living standard of the people as the fundamental start point
November 2001	China officially became a WTO member, which signified that China’s opening up to the outside world entered a new stage
November 2002	The report of the 16th CPC National Congress proposed the goal of struggle of comprehensively building of a well-off society. People should take the road of new-type industrialization, speed up urbanization process, and promote coordinated regional development. They had to unswervingly consolidate and develop public ownership economy, unswervingly encourage, support and guide the development of nonpublic ownership economy, strengthen and improve macroscopic regulation, deepen distribution system reform, and complete social security system
October 2003	The Third Plenary Session of the 16th CPC Central Committee adopted the “Decision of the CPC Central Committee on Several Issues on Improving Socialist Market Economic System” and proposed the outlook of scientific development, which defined people-oriented, comprehensively coordinated and sustainable scientific development
January 2004	The central authorities decided to implement the project of the study and construction of the theories of Marxism and organized the compilation of the textbooks in the disciplines of philosophy and political economics that comprehensively reflected Deng Xiaoping theory and important thought of the “Three Represents”
March 2004	Hu Jintao formulated the connotation of the outlook of scientific development from four aspects in the “Speech at the Colloquium of the Work of the Central Authorities on Population, Resources and Environment”
October 2005	The Fifth Plenary Session of the 16th CPC Central Committee adopted the “Suggestions of the CPC Central Committee on Formulating the Eleventh Five Year Plan on National Economic and Social Development” and proposed building the new socialist countryside, pushing forward the optimization and upgrading of industrial structure, promoting coordinated regional development, building resource-saving and environment-friendly society, deepening system reform and improving the standard of opening up to the outside world, implementing the strategies of rejuvenating China through science and technology and of reinvigorating China through human resource development, and pushing forward the construction of socialist harmonious society
October 2006	The Sixth Plenary Session of the 16th CPC Central Committee adopted the “Decision of the CPC Central Committee on Several Important Issues on Constructing Socialist Harmonious Society”

(continued)

Table 1 (continued)

October 2007	The 17th CPC National Congress proposed the theoretical system of socialism with Chinese characteristics which included the important strategic thoughts of the Deng Xiaoping theory, the important thought of the “Three Represents”, and the outlook of scientific development
December 2008	Hu Jintao published the “Speech at the Conference in Commemoration of the 13th Anniversary of the Convening of the Third Plenary Session of the 11th CPC Central Committee” and summarized from 10 aspects the precious experiences accumulated in the tremendous achievement obtained in in China’s reform and opening up
October 2010	The Fifth Plenary Session of the 17th CPC Central Committee adopted the “Suggestions of the CPC Central Committee on Formulating the Twelfth Five Year Plan on National Economy and Social Development” and proposed that people should take scientific development as the theme and speeding up the transformation of the mode of economic development as the main line, deepen the reform and opening up, guarantee and improve the people’s livelihood, promote the long-term, steady and faster economic development and social harmony and stability, and lay the foundation of decisive meaning for comprehensively complete building a well-off society

^aDeng Xiaoping, “The Speech at the Third Plenary Session of the Central Advisory Commission”, *Selected Works of Deng Xiaoping*, Vol. 3, People’s Publishing House, 1993, p. 83

The other way was to join the part on socialism and the part on capitalism together and apply a uniform analytical framework in the entire textbook. Such compilation method stressed on theoretical unity and logical consistency. Of course, the method was controversial. One valuable opposite view was that different ages should have their own political economics. Take *Modern Political Economics* compiled with Cheng Enfu as chief editor and He Changyu, Zhang Yinjie and Ma Yan as vice chief editors and published by Shanghai University of Finance and Economics Publishing House in 2000 as example. The book consisted of “introduction” and “five parts” as its system structure. The “five parts” were respectively “Part One Direct Production Process”, “Part Two Circulation Process”, “Part Three General Process of Production”, “Part Four National Economic Process”, and “Part Five International Economic Process”. To analyze capitalist economy and socialist economy with a uniform analytical framework was a highlight of the textbook. But the analysis on socialist economic system and economic operation appeared weaker in the content presented in the textbook. This might be because there was indeed difficulty in compilation when capitalist economy and socialist economy were included in a uniform analytical framework.

Second, the textbooks of political economics had great enrichment in content from the beginning of the new century. The contents closely related to China’s economic system reform and economic development, such as general categories of market economy, economic operation and economic development, took up noticeably increasing proportion in the books so that the textbooks showed obviously stronger features of reality and clear targets. Take *Political Economics* compiled with Zhang Weida as chief editor and Song Donglin and Xie Di as vice chief editor as an example.

The textbook was published by Higher Education Press in 2000. It did not follow the “dichotomous method” used in the past but consisted of “introduction” and the “four parts” of “Part One Commodity Economy”, “Part Two Economic System”, “Part Three Economic Cooperation” and “Part Four Economic Development”. “Economic operation” and “economic development” were included in the textbook respectively as one part to emphasize the importance of these two issues and thus the book closely related to the reality that China faced the dual tasks of “transition” and “development”. *Advanced Political Economics: The Ontology of Socialism* edited by Jiang Xuemo and published by Fudan University Press in 2001 was a textbook for postgraduate students. It consisted of “The Part on Socialist Production Process”, “The Part on Socialist Circulation Process”, and “The Part of the General Process of Socialist Production”. Its system structure showed originality and it had very rich contents.

It can be seen that China’s textbooks of Marxist political economics had always advanced with the time both in system structure and in specific contents from the beginning of the reform and opening up. But it also should be recognized that these textbooks had the problem of lagging behind in development when compared with the great practice of socialism with Chinese characteristics, with the historical process of China’s reform and opening up, with a series of important theoretical innovations of the CPC, and with the knowledge demand of the college students.

In 2004, the central authorities decided to implement the project of the study and construction of the theories of Marxism and organized the compilation of a batch of textbooks of philosophy and social sciences that comprehensively reflected Deng Xiaoping theory and the important thought of the “Three Represents”. *Marxist Political Economics* was determined as one of the first group of key textbooks. The textbook research and compilation group was formed, which was led by the Chinese Academy of Social Sciences and based in the Institute of Economics of the Chinese Academy of Social Sciences and in which experts and scholars from various organizations, such as China Renmin University, Peking University, Nankai University, Nanjing University, Party School of the CPC Central Committee, Policy Research Office of the CPC Central Committee, and National Development and Reform Commission, took part. After over seven years of hard work, *An Introduction to Marxist Political Economics* would be published by People’s Publishing House as one of the important results of the project of the central authorities of the study and construction of the theories of Marxism. This textbook of Marxist political economics was the result of the full cooperation and joint efforts of various areas under the guidance of the system of the theories of socialism with Chinese characteristics. It epitomized to the maximum the consensus of experts and scholars in the circle of political economics and the departments of practical work in China. It also fully manifested the important theoretical progress achieved in the study of Marxist political economics in China during over 60 years after the founding of the People’s Republic of China and, in particular, during over 30 years after the beginning of the reform and opening up. It represented the innovation and development in the compilation of the textbooks of Marxist political economics in China. Its prominent characteristics were mainly manifested in the following several aspects.

First, it possessed stronger sense of contemporariness. “Three Fully Reflects” were achieved in it through hard work: It fully reflected the latest result of theoretical innovation in the sinicization of Marxism and highlighted the enrichment and development of Marxist political economics in the system of the theory of socialism with Chinese characteristics. It fully reflected the lively practice and basic experience of the CPC in leading the people in all China to carry out socialist modernization construction and reform and opening up. And it fully reflected the latest research result in the disciplinary construction of political economics under the guidance of Marxism. With these “Three Fully Reflects”, it could guide the students to apply the positions, views and methods of Marxism to scientifically understand the economic phenomena and principles of the present world on the basis of carefully studying and mastering the basic principles of Marxist political economics. And thus they could better understand and master the economic theory and practice of socialism with Chinese characteristics.

Second, it realized innovation in framework structure. A structure of “four parts” was adopted as framework structure. Namely the book developed into four parts after the “Introduction”: “Part One Commodity and Money”, “Part Two Capitalist Economy”, “Part Three Socialist Economy”, and “Part Four Economic Globalization and Opening Up to the Outside World”. Such framework structure absorbed the latest practice in textbook compilation and exhibited further innovation. It was helpful to comprehensively mastering the general characteristics of market economy and its different characteristics under the different social systems of capitalism and socialism and to comprehensively mastering the two general situations of domestic and international situations.

Third, it highlighted the analysis of the new changes in contemporary capitalism in the part on capitalist economy on the basis of formulating the basic principles of political economics in *On Capital* by Marx and *On Imperialism* by Lenin. New contents were added to it, such as “State Monopoly Capitalism and Its New Developments”, “New Changes in Contemporary Capitalist Production”, “New Changes in Contemporary Capitalist Distribution Relations”, and “Financial and Economic Crises in Contemporary Capitalism”.

Fourth, it comprehensively and systematically formulated the basic content of the economic theory of socialism with Chinese characteristics in the part on socialist economy. Such content mainly included the establishment of socialist economic system and its fundamental task of liberating and developing productivity, the primary stage of socialism, economic system reform and socialist market economic system, the basic economic system of the primary stage of socialism characterized by taking public ownership as the dominant one and achieving the joint development of multiple ownership economies, the distribution system of the primary stage of socialism, the economic development in socialism with Chinese characteristics, and the economic function of the government in socialist market economy. Such a logical arrangement of the parts and chapters manifested, on the one hand, the basic economic principles that productivity determined productive relations and protective relations had reaction on productivity and that economic foundation determined superstructure and superstructure had reaction on economic foundation. On the other hand, it was

helpful to including into the textbook system a full set of lines, policies and guidelines and the latest experiences that the CPC had formed when it successfully opened up the road of socialism with Chinese characteristics. And thus the textbook possessed stronger features of contemporariness, clear target and relation to policy.

And fifth, a separate part “Economic Globalization and Opening Up to the Outside World” was written to analyze international economic relations. This was an important innovation in the system structure of the textbook of political economics. Most of the textbooks available at present only analyzed China’s foreign economic relations in one chapter in the part on socialism. Although economic globalization was covered in it, the weight given to it was far from being adequate. A separate part is written to analyze the basic theoretical and practical issues that economic globalization and China’s opening up to the outside world that involved showed adaptation to the new situations in international and domestic economic development.¹⁰

In addition to the five prominent characteristics in the above, the textbook also showed important innovations in the formulation of important theoretical issues, the expression of important logical connections and the arrangement of specific contents. The innovations in the formulation of important theoretical issues could be seen in many places. The analysis and formulation on the “object of study of Marxist political economics” in the “introduction” was a good example. The circle of academic study had controversy of the objects of study of political economics. One type of view believed that the object of study of Marxist political economics should be defined as production mode. Thus people could have good grounds to include productivity, resource allocation and economic cooperation into the scope of study of political economics. However, most scholars still insisted that the object of study of political economics was “productive relation”. But if the object of study of political economics was defined as “productive relation”, how could such important contents as productivity, resource allocation, economic cooperation and economic development be inherently included in the study of political economics? This was a theoretical difficulty that people often encountered in the argument about the object of study of political economics. The textbook resolved this theoretical difficulty in a good way for returning to the classics. It believed that “the object of study of Marxist political economics is productive relation and such study needs to relate to productivity and superstructure”. And productive relation was manifested in the four links of social reproduction of production, distribution, exchange and consumption. Then the textbook carried out scientific demonstration on the categories of production, distribution, exchange and consumption and their mutual relations according to the theoretical logic in the “Introduction to *Critique of Political Economy*” written by Marx. Thus, it inherently included productivity, resource allocation, economic operation and economic development into the scope of study of political economics. Take the category of distribution as an example. The textbook pointed out according to the

¹⁰In writing five points above, the author made reference to the summarization made by Liu Shucheng, research fellow and president and chief expert of the textbook research and compilation group of *Marxist Political Economics* in the project of the central authorities of the study and construction of the theory of Marxism.

statements of classical writers that distribution referred to not only the distribution of products or the means of consumption but also the distribution of productive factors. And the distribution of productive factors already included in the process of direct production before the distribution of products. It included the distribution of the instruments of production and the distribution of social members between various kinds of production. Thus, the textbook inherently included resource allocation and economic operation into the horizon of political economics through the scientific understanding of the category of distribution.

The textbook also had distinctive arrangement of important logical connections. Take “Part Three Socialist Economy” as an example. Most of the textbooks available at present took the basic economic system of socialism or the ownership system of the means of production as the logical start point of the part on socialism and presented the analysis of other important theoretical issues on such basis. This textbook presented the contents of the part on socialism according to the theoretical logic of socialist market economy. It took the fundamental task of socialism and socialist market economic system as the logical start point to present the basic contents of the basic economic system of the primary stage of socialism, the distribution system of the primary stage of socialism, the economic development in socialism with Chinese characteristics, and the economic functions of government in socialist market economy. Such logical arrangement conformed more to the inherent connections of socialist market economy and to the basic principle of Marxism that productivity determined productive relations.

The textbook also had innovations in the arrangement of specific contents. “Chapter 15 The Economic Functions of the Government in Socialist Market Economy” made more comprehensive and scientific summary of the economic functions of the government. The summarization of the economic functions of the government in the textbooks available at present mainly focused on the macroscopic economic functions of the government so that it caused the partial and not scientific understanding that the economic function of the government was macroscopic regulation. In fact, the government needed to carry out both macroscopic and microscopic regulation in modern market economy so as to maintain market order and create an environment of fair competition. This was the case both in China and abroad. When discussing the economic functions of the government, the textbook not only analyzed the function of microscopic regulation of the government but also discussed the function of market supervision of the government. Thus it established the theoretical framework to understand the economic functions of the government from a more comprehensive and scientific angle. In “Part Four Economic Globalization and Opening Up to the Outside World”, the textbook omitted the contents at the technical level in international trade and international finance and concentrated on discussing basic theoretical issues such as international division of work, international economic order, economic globalization, China’s strategy of opening up to the outside world, and national economic security. This was helpful for the students to grasp some intrinsic connections in the process of economic globalization. Such approach fully embodied the disciplinary positioning of political economics in the study of the substance of economic phenomena.

4 Conclusions

The following four important issues had to be resolved well in the compilation of a new textbook of Marxist political economics that conformed to the development of the time and met the requirements of the students.

First, the textbook needed to fully embody a series of important theoretical innovation resolves of the CPC. During over 60 years after the founding of the People's Republic of China and, in particular, during over 30 years after the beginning of the reform and opening up, the CPC and Chinese circle of economics achieved a series of important theoretical innovations. These were the latest results of the sinicization of Marxism. A considerable part in them were important theoretical innovations in Marxist political economics, which mainly included the four major theoretical innovations of the theory of the primary stage of socialism, the theory of the reform and opening up of socialism, the theory of the socialist market economy, and the theory of scientific development. To write these important theoretical innovations into the textbook of Marxist political economics was the inherent requirement of the sinicization, modernization and popularization of Marxist political economics.

Second, the textbook needed to systematically summarize the experience of the development of socialism with Chinese characteristics and elevate it to the level of fundamental theory. China opened up a road of socialism with Chinese characteristics and made achievements that attracted the attention of the whole world. In this process, socialist economic system and the principles of the development of socialist economy gradually unfolded. At present, "China Model" and "China Road" became hotspots in the discussion of the international academic circle. The great practice of socialism with Chinese characteristics provided rich soil in reality for the development of Marxist political economics. The textbooks of Marxist political economics should apply scientific concepts and frameworks to establish a relatively complete theoretical representation of the economic systems and the principles of economic development of socialism with Chinese characteristics.

Third, the textbook needed to fully reflect the development of economic globalization. When designing the "Structural Plan of Five Parts" and the "Structural Plan of Six Books" of political economics, Marx listed the international relation of production and world market as an important component of political economics. At the present time, the flow of commodity and productive factors was already globalized and the width and depth of international division of work was unprecedented. To analyze in depth the international division of work and interest structure under constant adjustment in the age of globalization appeared to be even more urgent than any time in the past. Marxist political economics should make its own contribution in this task.

And fourth, the textbook needed to analyze in depth the new changes and new characteristics of modern capitalism on the basis of strictly following the logical structure and basic outlook of capitalism. From the time when Marx established Marxist political economics to today, capitalism developed for another century and more. Although the historical trend of capitalism did not change, capitalist productive

relations underwent new important adjustments, which eased the basic contradictions of capitalism to certain extent and created new development space for productivity. Marxist political economics had to analyze the new phenomena in the process of development and change of the basic contradictions of capitalism and to exhibit its theoretical quality of advancing with the time.

The undertakings of socialism with Chinese characteristics kept developing. Socialist market economic system kept improving. The process of China's economic development kept unfolding. The system of the theory of socialism with Chinese characteristics kept enriching. As a scientific and open theoretical system, Marxist political economics would keep enriching and developing with these situations.

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Chapter 30

The Development of Economic History in the People's Republic of China



Li Wu

The founding of the People's Republic of China in 1949 signified the ending of semi-colonial and semi-feudal society and the beginning of the new era of socialism.¹ It was also the beginning of the transformation from century-long wartime to peaceful construction in China. Such change provided huge social demand and material conditions for the prosperity and development of social sciences in China. And such prosperity and development was achieved under the guidance of Marxism. Its object of service was very specific. Namely, it needed to serve the development of various political economic and social undertakings in The People's Republic of China under the leadership of the Communist Party of China. In the time of "taking class struggle as the guiding principle" before 1978, the study of Chinese economic history became an important component in social sciences. In drastic social changes and frequent economic movement, history became a prestigious discipline and the materialistic historical outlook of Marxism determined that economic history enjoyed an important status in the entire historical study. Thus the study of Chinese economic history became a hotspot in the study of history in which very rich research results were achieved. Among the five major theoretical explorations in the study of history from 1949 to 1978, four were directly related to economic history. As the work priority of the entire nation was shifted to economic construction after the beginning of the

¹ As the chapter involves a tremendous amount of the contents, which was very hard for the author to cover, it is necessary to make explanation to two points: a. The chapter does not cover the situations and results of research on the Chinese economic history in Hong Kong, Macau and Taiwan and in foreign countries and of the world economic history inside China. And b. Because of the limitations in study and time, the author could not sort out and study all the aspects involved by himself. So this chapter absorbed the research results of the scholars such as Li Genpan, Li Bozhong, Lin Ganquan, Yang Guozhen, Zhang Haiying, Yu Heping, Xu Jiansheng, Peng Nansheng and Zhao Xuejun. Their works were listed in the References at the end of the chapter for the readers to refer to.

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reform and opening up in 1978, economics became a prestigious discipline. And as economic system reform deepened and western economics became widely known, the study of the Chinese economic history gradually attracted the attention of the circle of economics. In the study of history, which was greatly prosperous in the past, many people turned to study social history at the microscopic level so as to rectify the defect of “grandiose narrative” in the past. This promoted the study of economic history in the area of the study of history. Therefore, when examined from its study during over 60 years after the founding of the People’s Republic of China, Chinese economic history has extensive development space, rich research results and bright prospects as an inter-discipline between history and economics that shoulders the dual missions of innovating in the study of economics and history in China.

1 Two Major Stages in the Study of Economic History in the People’s Republic of China

Modern economic history emerged in China after western modern social sciences was introduced into China in the beginning of the 20th century. It should be said to be the product of the academic transition in China in early modern times. In 1903, Liang Qichao published the famous paper *New History*, advocating the “revolution of the circle of history” and calling for the establishment of the “new history”. People in later generations had much controversy on the idea “what new history is” and argued for different views. But Liang Qichao himself already made it clear: The main characteristic of such new history was that it had to “have the general principles and rules of various kinds of learning”. Namely, people should take advantage of the theoretical method of social sciences to study history. In the conception of Liang Qichao about “new history”, economic history possessed the most important position. In 1904, Liang Qichao wrote the book *The History of National Debts in China* and the works in the study of Chinese economic history published later were all influenced directly or indirectly by this book. Because of this, the Chinese circle of economic history generally took the publishing of Liang Qichao’s *The History of National Debts in China* as the symbol of the emergence of economic history in China.² After that, economic history underwent this stage of formation during the periods of Republic of China and exhibited short prosperity in 1930s centering round the nature of Chinese society and China’s social history. When viewed from the perspective of theory and methodology, the study of economic history in this period could be divided into the school characterized by western evolution theory and empirical study and the school guided by Marxist materialistic outlook and class struggle theory.

The study of economic history during over 60 years after the founding of the People’s Republic of China could roughly be divided into the two periods of before

²See Zhao Dexin, “Review and Regulation of the Development of Economic History in China in the First Half of the 20th Century”, originally published in *South Central China Economic Forum* and quoted from http://jyw.znufe.edu.cn/znijslt/xyd/sxglyjjsxs/t20051223_1384.Htm.

and after the defining event of the Third Plenary Session of the 11th CPC Central Committee in 1978, the mark of the beginning of the reform and opening up.³

I. The Course of the Study of Chinese Economic History from 1949 to 1978

In the first period, people took re-understanding and explaining history as the duty and applied materialistic historical outlook and class struggle theory to carry out the study of Chinese economic history according to the principle of “making the past serve the present” and under the general background of the democratic revolution and socialist revolution led by the Communist Party of China and the continued revolution under the proletariat dictatorship. They established the predominant status of the materialistic historical outlook and, at the same time, formed theoretical systems and conclusions that could systematically explain Chinese economic development history and achieved a large group of research results that were influential until today. The prominent characteristic of the study of economic history in this period was rather similar to the characteristic of the study of history. Namely, the people stressed on grand historical narrative and theoretical issues or on using basic Marxist theory to construct historical theoretical system that could explain the reality of Chinese history. The objects of the study of economic history in this period mainly concentrated in China’s ancient and early modern times, namely pre-capitalist period and the period of semi-colonial and semi-feudal society. And the main task of the study of economics in The People’s Republic of China at the time was to resolve the issues in socialist economic construction. Hence the study of economic history did not make much contribution in it.

As a discipline in a sense of modern science, the study of Chinese economic history emerged at the end of the Qing Dynasty and took form in the period of the Republic of China. Driven by the development of the two emerging disciplines in the above, it mainly developed centering round resolving the issues that China faced in responding to national crisis. It thrived with the debate on China’s social history in 1930s but declined due to the influence of war.

After the founding of the People’s Republic of China in 1949, drastic transition started in the study of social sciences. Namely, it quickly and thoroughly transformed from the status in which the several schools of thought of traditional feudal culture, capitalist culture and Marxism contended into the situation in which people took the theory of Marxism as the sole guiding thought. As far as the angle, content and purpose of the study of Chinese economic history in this period was concerned, it could be said that the study of Chinese economic history was more of an important component of the study of history. This discipline also quickly completed the theoretical integration under the guidance of Marxist materialistic historical outlook in this period.

³Li Bozhong divided the course of Chinese economic history in the 20th century into the four stages of burgeoning (1904–1931), formation (1932–1949), transition (1949–1978) and prosperity (1978–2007). See Li (2008). The author approves of and adopts such division in this chapter.

The study of economic history and, in particular, the economic history as a component of the study of history became particularly prominent in the process of transition because of the needs in the political and cultural construction of the newly-established state regime.

The scholar who relatively systematically formulated Marxist historical outlook was Li Dazhao. From 1919 to 1924, he successively published the articles of “My Marxist Outlook”, “The Value of Materialistic Historical Outlook in the Modern Study of History”, “Material Change and Moral Change”, and “Explaining the Reasons of the Changes of Thought in China in Early Modern Times from the Perspective of the Economy” and introduced the basic contents in Marxism related to materialistic historical outlook, residual value and class struggle theory. In 1924, Li Dazhao wrote *The Essentials of the Study of History* and scientifically and systematically formulated some important theoretical issues in a study of history such as what history was, what the study of history was, the issue of historical outlook, the issue of the system of the study of history, the issue of the relationship between history and philosophy, and the influence of history to the establishment of the positive and aggressive outlook of life of the people. In the book, Li Dazhao gave great prominence to the application of Marx’s historical outlook to study history. He pointed out that “The historians in the past intended explain the transformation of society, or history, from the upper level of the society regardless of the foundation of the society. Such a method cannot lead to the true understanding of history. The upper level of the society changes with the foundation of economy. Therefore, history has to be explained from economic relations. This is the general content of Marx’s historical outlook. The reason that Marx advocated that people should take economy as the center in the examination of the change of the society was because they could make discoveries that conformed to the law of causation just like in natural sciences. Hence the study of history is elevated to the status of science.” *The Essentials of the Study of History* was a work of historical theory in the area of the study of history published the earliest in China in the 20th century. In the development of Marxism in China, this was the first work that opened up a road in theory and became the cornerstone in theory of the Marxist study of history in China. In addition, Li Dazhao also wrote other papers such as “The Materialistic Reflection of the Primitive Society in Writings and Texts” and “Explaining the Change of Thoughts in China in Early Modern Time from the Perspective of the Economy” to explore the road of studying Chinese history with the guidance of materialistic historical outlook.

On the one hand, people needed to re-understand and explain Chinese history with materialistic historical outlook after the founding of the People’s Republic of China. On the other hand, they needed to study the former regime, or the history from the beginning of early modern time, to demonstrate the historical inevitability and progressiveness of the New Democratic Revolution, the founding of the People’s Republic of China and the Socialist Revolution. And the historical outlook in Marxism about the evolution of five social and economic forms exactly met these two needs. *A Concise Course of the History of the Soviet Union Communist Party (Bolshevik)*, an important piece of literature for intellectuals to study Marxism around the founding of the People’s Republic of China, made the following summarization

on materialistic historical outlook and how people should engage in the study of the history: "Social development history is, first of all, the development history of production and thus the development history of the modes of production, which successively replaced each other over many centuries, and of productivity and the protective relations between the people." If people wanted to make the historical science into a science in the true sense, "they should first study the history of the producers of physical materials, of the working mass and of the people in various countries." "The primary task of the historical science was to study and reveal the principles of production, of the development of productivity and productive relations, and of social and economic development." The book also pointed out that "productivity is not only the most active and revolutionary factor in production but also the determinant factor of production development. How productivity looks like determines what productive relations are." "As social productivity changes and develops in history, the productive and economic relations between the people also change and develop accordingly." As a result, "there are five kinds of basic types of productive relations in history: those of primitive commune system, slave owning system, feudal system, capitalism and socialism". The book made relatively detailed introduction to five kinds of social productive relations.

The study of economic history in The People's Republic of China was carried out under the guidance of the above thought. Thus, the issues on the division of the periods in ancient society, the landlords system economy, the burgeoning of capitalism, peasant wars and their role, and the failure of the development of capitalism in early modern times became the key issues and hotspots in the historical study, and also in the study of economic history, during the 17 years of the founding of the People's Republic of China.

The main objects of study in the period from 1949 to 1978 were ancient and early modern economic histories. In the study of Chinese economic history of this period, people mainly adopted the paradigms in traditional historical study. There were two main reasons for this: one was that there were certain difficulty in describing and explaining China's pre-capitalist society with Marxist materialistic historical outlook and political economics as guiding thought and the sole theory. The other was that the behavior of the people in the past time did not have one single economic outlook as the premise and there were another set of theories, methods and rules for their words and conducts so that it was very difficult to explain the people and events in the past with the outlooks in economics which appeared later.

From the founding of the People's Republic of China in 1949 to early the 1950s, the Chinese circle of social sciences carried out an ideological remoulding movement of intellectuals and formed a great wave of studying Marxism. The victory of the democratic revolution led by the Communist Party of China and the founding of the People's Republic of China indicated that people succeeded in applying the basic principles in Marxism to understand and resolve the social issues in China from the beginning of early modern times. The scientific nature of the works, written by Marxist economists and historians through applying materialistic historical outlook before the founding of the People's Republic of China in 1949, was proved. This greatly encouraged and inspired the workers in a study of history in The People's

Republic of China. Through study, the majority of the researchers in history and economics possessed certain basic knowledge of Marxism and made fruitful explorations on how to use Marxism to guide academic research. And for the study of economic history, the application of materialistic historical outlook was not only necessary but also effective. This was because the classical writers of Marxism already provided a brand new historical perspective, a complete theoretical system and analytical framework. Hence, people naturally preferred applying Marxist materialistic historical outlook to interpret China's ancient and early modern histories in economic history before 1966, a new disciplinary system with materialistic historical outlook as guidance and the study of social economic forms as the main part was formed in the research area of economic history in China.

There were certain issues in the research work during this period. Those were mainly seen in the labelling-like dogmatic trend in the process of applying Marxism to study history which often made complicated history simplified or stereotyped. The left-deviation mistake in politics aggravated such trend so that it evolved into innuendo historical study and the situation of total silence during the period of 1966–1976. However, people still needed to see that achievements dominated in the study of economic history during the 17 years before 1966. In this period, people established the guiding status of Marxism which provided powerful world outlook and methodology to the study of economic history so that it became the mainstream in the study of history. Besides, people cultivated a group of talents and published a batch of research results through study. And all of these laid the foundation for the surge of the large amounts of research results and economic history after the beginning of the reform and opening up in 1978.

II. The Course of the Study of Chinese Economic History from 1978 to 2010

The 32 years from the beginning of the reform and opening up in 1978 was the period in which the study of Chinese economic history quickly developed and prospered. The needs of economic development in reform, the accumulation in the study of history in 30 previous years and the influence of opening up to the outside world became the three basic factors that brought about growing research teams, extensive research area, diverse research methodology and rich research results in the study of economic history in this period.

First, the research team in the study of Chinese economic history quickly grew, its research area became more extensive and a great abundance of research results were achieved. After the beginning of the reform and opening up in 1978, the study of economic history was regarded as a breakthrough point in the study of history in the new age. The research topics related to economic history were all placed on an important position in national plans on philosophy and social sciences formulated during the “Sixth and Seventh Five Year Plans” of the state. The initiative of the people in the study of economic history was mobilized and many scholars who originally engaged in the study in other areas, for example, in the study of peasant war, turned to the area of economic history. Research institutions and teams in the study of Chinese economic history, which was damaged from 1966 to 1976, were

quickly restored and developed. In the research team of economic history which was expanded unprecedentedly, there were senior and middle aged scholars who started to engage in research work in the 1930s–the 1940s and the 1950s–1960s. They had their academic youth rejuvenated in the new period and achieved rich results in scientific research and talent cultivation. A group of doctors and masters were cultivated after the post-graduate cultivation system was restored in the new period. In the late 1980s, these people quickly grew into backbone research forces that possessed great vigor, pioneering spirit and new knowledge structure. Now, they became the pillar that supported the discipline of Chinese economic history. As research work unfolded, research personnel had urgent requirement to strengthen communication and collaboration. Academic organizations in the study of economic history were established in various places such as Northeast China and Guangdong. The Chinese Economic History Society, the national research institution attached to the Institute of Economics of the Chinese Academy of Social Sciences, was formed officially in 1986. *The Journal of Chinese Social and Economic History*, edited by the Department of History of the Xiamen University, and *Research in Chinese Economic History*, edited by the Institute of Economics of the Chinese Academy of Social Sciences, started publication respectively in 1982 and 1986. The website China Economic History was established in 2000 and became an important academic frontier of the study of Chinese economic history. In 2002, the Chinese Economic History Society joined the International Economic History Association after a long period of preparation and further strengthened the international communication of the research teams in the study of economic history in China. Thus, both research perspectives and areas were greatly widened than before 1978. In the past, the study of economic history focused more on the study of productive relations and economic systems, of the ancient and early modern times, and of the Han nationality and agricultural economy and on the general study of the economic activities of the state and the important economic events, characterized by “macroscopic narrative”. Now the study was expanded to productivity and economic cooperation, to contemporary Chinese economic history, to nomadic economy and marine economy, and to social economic history and regional economic history.

Second, the study of economic history had more extensive and abundant material basis. Before 1966, the work on the literature of economic history basically solely concentrated on early modern times. The sorting of the materials on early modern economic history continued to develop in the new period. The sorting, publishing, discovering and utilizing of the materials of ancient economic history showed larger progress achieved. The work of systematically sorting the materials also started in the study of contemporary economic history. A large amount of literature, archives and materials of economic history were sorted and published in this period. The Institute of Economics in Academia Sinica of Taiwan, the Institute of Economics of the Chinese Academy of Social Sciences and other organizations cooperated to input into computer the data on the grain prices in the archives in the imperial palace of the Qing Dynasty and build a database on relevant materials. The Chinese Academy of Social Sciences and other organizations also implemented the projects of sorting and publishing in a large scale the economic archives of the People’s Republic of

China. A large multitude of diverse archeological materials, including unearthed objects and textual materials, such as agricultural products, tools, town sites, objects with inscriptions on bones or tortoise shells or bronze, bamboo and wooden slips made in the Qin and Han Dynasties, and documents unearthed in Dunhuang and Turpan, were extensively used in the study of economic history. They were used to verify the records in literature, constantly updating, correcting and deepening people's understanding and adding vigor and dynamism to the study. In the present time, there were still rich and living materials among the people and in real life such as the documents used by the people, clan pedigree, tablet inscriptions, and social, custom and ethnic surveys. These materials attracted more and more attention from the researchers of economic history, who also started to utilize them more and more.

Third, academic thoughts became unprecedentedly active and theoretical methods showed a tendency of diversification. Under the guidance of the ideological lines of "seeking facts from truth and liberating the thought", the researchers in economic history got out of the confinement of dogmatism in the past, broke through various forbidden areas, and deepened the understanding on Marxism. After the beginning of reform and opening up, international academic communication became increasingly frequent and new theories and methods were introduced constantly. A new situation emerged in which the academic study on the mainland China and overseas interacted with and promoted each other. Because of these, the researchers of Chinese economic history showed unprecedentedly active thought and new ideas and insights emerged endlessly. They made solid steps in exploring the characteristics and principles of Chinese economic history. What was associated with this was that people broke through monotonous models in theoretical methodology and carried out extensive exploration. The trend of diversified development emerged and different academic styles and schools were gradually formed. Some scholars advocated that people should use the theories and methods in economics to study economic history and stressed on metrical study and economic analysis with an attempt to make Chinese economic history more precise. Some of the scholars paid more attention to applying the methods in sociology and anthropology in the study of economic history, stressed on the interactive relationship between economy and culture, and tried to realize the combination of social history and economic history. In addition, many scholars combined the study in economic history respectively with historical geography, environmental ecology, historical demography, archaeology and ethnology and formed a trend of the crossing and merging of multiple disciplines and the mutual permeation of their theoretical methodology. These disciplines developed both in separation and in combination, advanced in parallel without contradiction, and formed a lively and dynamic situation like a hundred kinds of flowers blooming. Many researchers in economic history were not content with generalized qualitative narrative. Under the situation that the conditions allowed, they would do some quantitative analysis as much as possible. And a batch of works appeared, calculating yield per unit area, labor productivity, goods turnover and price change. This was also a great step forward in the study of economic history in China in the new period.

2 The Evolution of Research Team and Method in the Study of Economic History in the People's Republic of China

The study of economic history in over 60 years after the founding of the People's Republic of China was established on the foundation of the development and prosperity of the two major disciplines of history and economics.⁴ It was a sub-discipline formed in the crossing of history and theoretical economics. When examined from the disciplinary classification and perspective of research of the researchers, the study in this area could be divided into two major types although these two types had the same object of study and might also have the same research conclusion in study. One was the study of economic history as a disciplinary component of history. The researchers of this type were basically workers in the study of history from the research and teaching institutions of the discipline of history. The other was the study of economic history as a disciplinary component of theoretical economics. The researchers of this type were basically the scholars of economics from the research and teaching institutions of the discipline of economics. As history and economics were both mature in theory and methodology, the research topic selection and research result in the study of economic history both exhibited the characteristics of the two major types above, either one of them dominating or the two showing equal weight, regardless of the occupational needs, research perspective and advantages of knowledge structure of the researchers and the orientation of social demand although people always emphasized that "there is no fixed methodology in history" in the study of economic history. The reasons of making such a division in this chapter were to understand and grasp the inherent structure and factors of the academic development and evolution of the study of economic history in The People's Republic of China, on the one hand, and to summarize historical experience so as to promote the merge and integration of the theories and methods in a study of Chinese economic history, on the other hand.

As far as economics was concerned, there were two lines in the development of the economic discipline in China from the introduction of western economics into China at the end of the Qing Dynasty, to the burgeoning of the discipline in the earlier time of the Republic of China, and to the time before the founding of the People's Republic of China in 1949. Many Chinese scholars studied in Europe and the USA and received systematic training in western economics. After they returned to China, they positively spread western economic theories learned from Europe and the USA. On the other side, the sharp class contradiction and class struggle in old China caused Marxist economic theory to spread quickly in China. However, because national contradiction and class contradiction became the two major contradictions of the Chinese society in this period was always in the status of

⁴Wu Chengming had an educational background in economics and he engaged in economic work before the liberation of China and in the earlier time after the founding of the People's Republic of China. However, he believed after he engaged in the study of economic history for a long time. "Economic history is first of all history, so there needs to be a historical outlook." See Wu (2001).

division and turbulence, economics did not become a prestigious discipline. Although its focus was to resolve the economic issues that China faced at the time, people failed to form a theoretical system of economics that could completely interpret China's economic system, economic phenomena and economic operation. And the study of history threw in this period on the basis of the original cultural tradition of the Chinese nation of highly valuing history and its profound accumulation of the Chinese national learning after absorbing various theories of western social sciences. And such thriving and prosperity was still "to administer affairs and attain practical use", namely to re-understand and interpret history for solving the issues in reality and find answers through it.

During the period from the founding of the People's Republic of China in 1949 to the beginning of the reform and opening up in 1978, the research institutions and teams of Chinese economic history could be clearly divided into two major parts. One was the workers in the study of history in the governmental research institution of history and the teaching and research institutions of history in higher education institutions. The other was that workers in economics the governmental research institution of economics and the teaching and research institutions of economics in higher education institutions. Although these two parts had the same object of study, their work still showed differences in the area, perspective and methodology of study because the institutions were of different nature and had different tasks in study and the knowledge structure of the researchers and the research atmosphere in them were also different. The former included the Institute of History and the Institute of Modern History of the Chinese Academy of Sciences and the departments of history in colleges and universities. Their research and teaching task was about the study of history and the people working in them were historians. Their knowledge structure and research methods mostly came from the historical knowledge and methodological accumulations formed in China in a very long period of time. These scholars were particularly proficient in textual research and empirical study. The latter included the Institute of Economics of the Chinese Academy of Sciences, the Institute of Economics of the Shanghai Academy of Sciences, and the department of economics of the Peking University, the Renmin University of China, the Nankai University and some colleges and universities of finance and economics. The research and teaching task was about economics and the people working in them mostly had educational background in economics. The scholars were familiar with the basic theories and methods in economics.

When viewed from the area of study, the former mainly focused on ancient economic history, an area in which they could bring into play their strength and advantage in the study of history, while the latter mainly focused on modern economic history because the majority of the scholars in them came from the research departments and special areas about the practical economic issues in old China. Because they could not adapt to the study of the practical economic issues in The People's Republic of China in politics or in knowledge, they had to turn to the study of the economy of old China which had just become history and with which they were familiar, an area in which they could play their role and bring into play their advantages in economics.

After the beginning of the reform and opening up, the study of Chinese economic history exhibited a trend that research institutions kept increasing, research teams kept growing, composition of researcher group kept changing, and knowledge and methodology kept merging and diversifying.

First, research teams grew quickly. A large group of people who engaged in practical economic work and economists carried out the research work on the economic history of the People's Republic of China. They studied Chinese economic history as a secondary research area, either starting from summarizing China's own historical experiences and lessons or studying from applying western economic theories to re-understand the purpose of China's economic development. An example of the former was that several hundred of people once engaged in or were engaging in practical economic management work were gathered together to write the histories of the special topics or departments of economy in the PRC in the various volumes on economy in the large book series "Contemporary China Series" compiled under the organization of the Chinese Academy of Social Sciences in the middle of 1980s. The latter included Liu Guoguang, Li Yining, Wu Jinglian, Wang Haibo and Lin Yifu, whose works brought many highlights into the study of Chinese economic history.

In addition, the transfer of the work priority of the CPC and all China onto economic construction, the vigorous and dynamic economic development situation and the dazzling economic system reform all attracted a large group of scholars in the area of historical study who were not specialized in economic history and other scholars of social sciences who were not specialized in economics to engage in the research work in Chinese economic history. An example of the former was that many scholars who specialized in the history of the Communist Party of China and in contemporary Chinese history turned the focus of their study onto economic history. An example of the latter was that many scholars who specialized in politics, culture, society, diplomacy and even national defense turned the focus of their study onto the research or cross-disciplinary research related to economic history.

However, the study of economic history from the beginning of the reform and opening up already showed a tendency of inclining to economics more and more in general from the beginning of the new century as the research deepened, the knowledge of economics became popularized, and relevant theories and instruments became diversified. A part of the researchers were from the specialized field of history and familiar with the methodology of historical study turned to applying the theories and methods in sociality to carry out the study of social economic history characterized by empirical and case study.

When examined from the development trend of the research, there were two kinds of tendencies that advanced in parallel without contradiction in the study of Chinese economic history after the beginning of the reform and opening up, namely the tendencies of "separation" and "combination" as summarized by Li Genpan. The so-called "separation" included two meanings: one referred to the diversification of theories and methods and the other to the further division of the discipline. The most noticeable manifestation was the rise of the study of regional, department and special topic histories. The entire China or the entire economy was not taken in general as the object of study. The so-called "combination" also had two meanings: one referred

to the mutual permeation of the theories and methods in different disciplines and schools and the other to the research perspective of comprehensive examination in all aspects and over a long-time span. People did not study economic factors separately but studied economic development in the mutual connections between economy and society, culture and nature. People did not study Chinese economic history separately but studied the development of Chinese economy in the general background of the world's economic development. People did not study a time period separately but looked into the periods before and after it and examined its development trends in the past and the future.

Early at the end of 1960s and early in the 1970s, a thought trend of new economic history emerged in the USA and gave rise to a revolution of applying the theories and methods in economics in the study of economic history. In particular, American economists Douglass C. North and Robert W. Fogel successfully applied the methods of indirect measurement and counterfactual measurement and formed a popular novel research style in the study of economic history. While the revolution of new economic history advanced with great vigor on the east side of the Pacific Ocean, the study of economic history in China entered the age of reform and opening up. In early 1980s, Wu Chengming and Kong Jingwei, two elder generation scholars, respectively published the articles "Opinions on the Study of Modern Chinese Economic History" and "Some Theoretical Issues on Chinese Economic History" in *Academic Journal of Jinyang*, Issue 1, 1982 and *Journal of Jilin University*, Issue 1, 1982 and formulated the importance of theories and methods. Later, Wu Chengming listed in relevant academic speeches and papers the methods of various foreign academic schools in the study of Chinese economic history, such as the methods in econometrics, development economics, regional economics, sociology and system theory, and analyzed their advantages and disadvantages. His work showed much originality to the readers. After that, the theories and methods in the study of economic history attracted more and more attentions of Chinese scholars. From 1990s, a great many of foreign works on theories of economics and economic history were translated and introduced into China. The most famous ones were the modernization theory of Cyril Black, Samuel Huntington and other scholars, *A Theory of Economic History* written by John R. Hicks, *Structure and Change in Economic History* written by Douglass C. North, *The Theory of Share Tenancy* written by Steven N. S. Cheung, *Transforming Traditional Agriculture* written by Theodore W. Schultz, and the proto-industrialization theory of Franklin F. Mendels. All these exerted extensive and profound influence. Besides, some foreign sinology works in the area of economic history also became widespread in the academic circle, such as *The Peasant Economy and Social Change in North China* and *The Peasant Family and Rural Development in the Yangzi Delta 1350–1988*, two companion pieces written by Philip Chung-chih Huang, *The Chinese Peasant Economy: Agricultural Development in Hopei and Shantung 1890–1949* written by Ramon H. Myers, and *The Great Divergence: Europe, China and the Making of the Modern World Economy* written by Kenneth Pomeranz. The original theories and distinctive methods in these books exerted large influence in the study of Chinese economic history.

In sum, the academic horizon of both economy and history was greatly expanded and the research methods of these disciplines were greatly enriched after the beginning of the reform and opening up in 1978 because of thought liberation and the construction of market economic system. The political pressure that confined the study of economic history in the past ceased to exist. The connection between the study of economic history and the economic issues in reality became even closer. As economy became a prestigious discipline and a large amount of economic theories and methods were introduced, the focus of the study of economic history started to turn to economics. In addition, a new vigorous force in the study of economic history emerged in the area of historical study from the beginning of the reform and opening up. Namely, a group of researchers who carried out study from the angle of social history rose and thrived. Before the reform and opening up, a group of scholars, represented by Mr. Fu Yiling, employed the theories and methods in sociology to carry out the grassroots and microscopic study of economic history and achieved distinctive results.⁵ But there were not too many research in this aspect due to the influence of the situation that the entire circle of historical study focused on important issues in that period. After the beginning of the reform and opening up, many scholars turned to the microscopic and concrete issues in the study of social economic history because of the demand in the society, the correction of the deviation of “grand historical narrative” in the past, and the influence of international social economic history study. For example, such studies in social history as regional economic history, the “Three issues of agriculture, the countryside and farmers” issue of agriculture, the countryside and farmers in the history, social security, disaster relief and aid, and disease prevention greatly enriched to the content of the study of economic history. Such study of social economic history became the turning point and hotspot in the circle of historical study after the beginning of the reform and opening up and it achieved remarkable results. This indicated that historical study still had huge space in a study of economic history. It could fully play its role and was full of vigor.

Mr. Wu Chengming once pointed out that there were three major schools in general in the study of economic history in China. One school focused on the study of economic development from history itself, which included the study of politics and ancient laws and regulations that originally belonged to the study of history. One school focused more on explaining the development of economy with economic theories. Some scholars in it also paid more attention to quantitative analysis. And one school focused on social changes and could be called the school of social economic history.⁶

⁵Fu Yiling received training in sociology in Japan in his early years. So he paid special attention in the study to studying economic history from the perspective of social history and with the methodology in sociology. For example, he stressed on detailed regional study and that economic study of rural communities. And he also stressed on paying attention to sorting and examining non-official literature which was overlooked in traditional historical study, such as contracts, documents, heritage albums, annals, collected works, account books and tablet inscriptions. He advocated field survey and proved the ancient with the present.

⁶Wu (1999).

Another important breakthrough and innovation brought about by the reform and opening up to the study of economic history was comparative study. Before 1978, the older generation scholars of economic history already emphasized that people “cannot discuss economy for economy’s sake, China for China’s sake, and a certain period for the certain period’s sake”. And in fact, the study of Chinese economic history was carried out to a certain extent as the comparative study with the European economic history on the basis of the theory of five social forms in Marxism. But the comparative study at the time mainly focused on the examination of differences and similarities at the theoretical level and seldom went deep into the study of social economic history at the microscopic and concrete level. Constantly deepening, free and extensive international communication promoted such comparative study. And a group of economists and historians who grew up after the beginning of the reform and opening up, such as Li Bozhong, Hou Jianxin, Zhu Yingui, Lin Yifu and Hu An’gang, achieved outstanding research results.

3 The Progress in the Study of Ancient Chinese Economic History

The study of Chinese economic history can be said to start with the study of ancient economic history. Before the foundation of the PRC, the Chinese circle of thought had a debate about the nature of Chinese society and such debate gave rise to another debate in the academic circle about China’s social history in 1930s. The Marxist materialistic historical outlook and social forms theory were widespread in the debates. After the foundation of the PRC, Marxist materialistic historical outlook became the basic theory of the discipline of history and also of state ideology and applying it to re-understand and interpret the Chinese historical issues became the main and urgent task of the workers in a study of history. China had a long and brilliant ancient civilization before the Opium War in 1840. Its economic foundation and superstructure built on the basis of agricultural civilization was very developed during the Ming and Qing Dynasties. There were many differences between its development course and characteristics and the mutually progressive five social forms in Marxism summarized on the basis of the European history and also the “Asian mode of production” in the East summarized in Marxism. As a result, employing materialistic historical outlook to interpret Chinese history became a very cumbersome task which involved not only the application of theories and the sinicization of Marxism but also the resorting and study of a myriad of historical literature and a great multitude of historical relics or objects. Therefore, people carried out, after the foundation of the PRC, the comprehensive study on ancient Chinese history with respect to the issues of the division of periods of ancient Chinese history, the economic forms of Chinese feudal society and landlord economy, the historical role of the mass, and the burgeoning of capitalism.

The issues of the division of periods of ancient Chinese history, the Asian mode of production, and the long continuation of feudal society in China involved not only the characteristics and principles of the development of ancient society in China but also relevant important theoretical issues such as how to employ the doctrine of the forms of social development in Marxism to study ancient Chinese history and how to combine materialistic historical outlook with the reality of Chinese history. The discussion of these issues greatly promoted the in-depth study of a series of important basic theoretical issues in history such as the standard of the division of periods of ancient Chinese history. Moreover, the situation that hundred schools of thought contended with each other that emerged in the discussion became an important phenomenon in the period of the first 17 years after the foundation of the PRC in the study of history.

The discussion on the issue of the form of feudal land ownership system in China started with the article “The Issue of the Form of Feudal Land Ownership System in China” published by Hou Wailu in the inaugural issue of *Historical Study* in 1954. The article proposed that the feudal land ownership system in China was “imperial family ownership system” or a kind of state ownership system. This point caused heated response in the circle of historical study and over 150 papers participated in the discussion. The argumentation on the issue of land ownership mainly concentrated on the issue of land ownership title. The focus of the argumentation was seen in the issue whether the dominant form of feudal land ownership in China was state ownership, landlord ownership or various coexisting ownerships. Although no consensus was achieved in the discussion on the issue of the land ownership forms in ancient China at the time, the confrontation and comparison of various insights undoubtedly greatly promoted the activation of the academic atmosphere in the circle of history in China and the improvement of the theoretical standard of historical study. It also laid a good foundation for gradually resolving this important theoretical issue.

The discussion on the issue of the burgeoning of capitalism in China mainly emerged after the foundation of the PRC. On January 9, 1955, Deng Tuo published an article “On the Social Background and Historical Meaning of *The Dream of Red Mansions*” on *People’s Daily* and proposed the issue that capitalist economic factors grew from inside the feudal economic system. His view attracted the attention of the circle of historical study and many scholars wrote articles and published their opinions. Hence, the issue of the burgeoning of capitalism started to become an important issue that attracted great attention of the academic circle. At the time, the scholars in the discussion almost unanimously recognized that capitalism burgeoned in China’s feudal society. The main controversy was when the burgeoning of capitalism in China occurred and to what extent it developed. As far as the degree of development was concerned, some scholars believed that there was a higher degree of development. The burgeoning was not limited to coastal cities geographically and class relations changed. Other scholars believed that the degree of development was lower. The society was still of the nature of feudal society in which agriculture and household handicraft industry was combined together. The semi-colonial and semi-feudal period of early modern China started from the Opium Wars. In the discussion, the scholars also made in-depth discussion on the issue of the influence

of the bourgeoning of capitalism in China to class structure. The academic circle carried out comprehensive and in-depth study on the issue of the bourgeoning of capitalism in China through discussion. They discovered a large amount of materials and employed rich historical facts to demonstrate this issue. They also made systematic sorting and discovery of historical materials on ancient Chinese economic history and, in particular, the economic development history during the Ming and Qing Dynasties. Hence, exceptionally remarkable progress was achieved in the study in this area.

After the beginning of the reform and opening up in 1978, the study of ancient Chinese economic history reached a new climax as social sciences prospered. First of all, a large batch of literature, archives and materials of economic history were sorted, edited and published. Main agricultural books in ancient China were sorted, collated and annotated, and published. The “Records of Food and Goods” in the historical books of various dynasties were all sorted, collated and annotated. The materials of economic history about various economic sectors, industries, regions and special research topics were also sorted and edited. Rich and diverse archeological materials, including unearthed objects and textual materials, were employed extensively in the study of economic history. Among them, those that played the most noticeable promotive role in study included the Yunmeng bamboo slips of the Qing Dynasty in the area of the study of the land system and the social and economic study of the Qin Dynasty, relevant unearthed cultural relics, bamboo slips and silk in the area of the study of the Chu Kingdom, including the economic history of the Chu Kingdom, and the social economic history of the Han Dynasty, and the documents unearthed in Dunhuang and Turpan in the study of the economic history of the Tang Dynasty. Besides more and more researchers in economic history valued and utilized the diverse non-official materials and those in real life in China, such as non-official documents, clan pedigree, tablet inscriptions, and social, custom and ethnic surveys. The tablet inscription materials on economic history in Shanghai, Suzhou, Foshan and Beijing and a large amount of materials about the social and historical surveys of minority nationalities were also sorted, edited and published comprehensively. These works provided important material foundation for the study on regional economic history, social economic history of minority nationalities, and pre-capitalism social economic forms.

Second, the horizon and area of the study of ancient economic history also greatly widened and deepened during over 30 years from the beginning of the reform and opening up. In addition to the issues of macroscopic nature and stronger theoretical characteristic that people studied and discussed in the past, such as the bourgeoning of capitalism and landlord system economy, the issues such as commodity economy and natural economy in traditional society and traditional market and market economy started to attract people’s attention. In the study of traditional market, people paid attention to the conditions of the growth of various kinds of markets, such as rural market, urban market, regional market, national market, living goods market, market of the means of production, labor market, fund market and land market, and their mutual relations, to the calculation of commodity turnover and the analysis of

commodity composition, and to market price system and its transformation. Many research results were already published in these areas.

In this period, the study of agriculture history, commerce history, communications history, histories of salt industry and textile industry in handicraft industry was also unfolding. The perspectives of the study covered various aspects of science and technology, productivity, productive relations, operation and management system, intervention and management of the state of various kinds of handicraft industry economies, and Chinese and foreign economic and trade communication. The history of agricultural ecology also attracted increasing attention. Remarkable achievements were made in the sorting and study of the materials in fiscal and financial history and taxes and corvee history. The studies in troop station and land reclamation, horse policy, government monopoly system, government grain procurement, water grain transportation to the capital, granary operation and famine relief policy were also successively unfolded. The study of the history of economic laws and regulations was opened up as a new area. Progress was also achieved in the study of state economic policy and economic thought. Greater progress was achieved in the study of money and finance history and population history. Some pioneering and relatively mature works emerged.

The study of regional economic history in this period mainly focused on the Ming and Qing Dynasties and the early modern times or extended into the contemporary time. The regions studied covered the entire country. The areas in which remarkable achievements were made included the study of the Southern Yangtze River and South China regions. The Hui study, centering round the social economic history of Huizhou, rose as an exceptional highlight and became a prestigious area of study. Some scholars proposed that the discipline of marine social economic history be established on the basis of the study of coastal social economic history through integrating coastal economic history, marine fishery industry, foreign trade history, overseas Chinese economic history and history of coastal areas and sea territory. In the area of the study of minority nationality and regional economy, the traditional study of the economic history of the minority nationalities in Northwest, Southwest and North China continued to develop and new progress was made in the study of the economy of minority nationalities in Central China and border foreign trade.

After the beginning of reform and opening up, the study of ancient economic history exhibited the tendency of diversification and pluralization in theory and methodology as Chinese economy developed rapidly, system reform and opening up to the outside world deepened, and academic communication became frequent. Some scholars advocated that people should use metrical methodology and economic model in economics to analyze the issues in ancient economy. Some of the scholars paid more attention to applying the methods in sociality and anthropology in the study of economic history, stressed on the interactive relationship between economy and culture, and tried to realize the combination of social history and economic history. In addition, many scholars combined the study in economic history respectively with historical geography, environmental ecology, historical demography, archaeology and ethnology and formed a trend of the crossing and merging of multiple disciplines and the mutual permeation of their theoretical methodology. Many researchers

in economic history were not content with generalized qualitative narrative. And a batch of works appeared, calculating yield per unit area, labor productivity, goods turnover and price change. This was also a great step forward in the study of economic history in China in the new period.

4 The Progress in the Study of Modern Economic History in China

The foundation of the PRC in 1949 signified the end of the semi-colonial and semi-feudal society and the beginning of the new age. As a result, the study of the social and economic development and change in over one hundred years from the Opium War in 1840–1949 and relevant issues turned from the study of the practical issues of modern or contemporary times and the applied study for countermeasures into the study of history or the study of early modern Chinese history. Because of the needs to consolidate the regime and ideology of the PRC, the Communist Party of China and the Chinese government attached high importance to the study of the history in this period. And according to the materialistic historical outlook, the early modern Chinese economic history naturally became an important component part in such study.

In 1953, the Committee of the Study of China's Historical Issue of the State Council decided that Yan Zhongping from the Economic History Research Group of the Institute of Economics of the Chinese Academy of Sciences should take in charge of the compilation and publishing of a set of the "Collection of Referential Materials of Early Modern Chinese Economic History", which would start from 1954. In 1955, Yan Zhongping et al. compiled the *Collected Statistical Materials of Early Modern Chinese Economic History*. With its publishing as a start, the collections of materials on special topics, such as industry, agriculture, handicraft industry, foreign trade, railway, foreign debts and public debts, were compiled and published in succession. From 1958, the Central Administration of Industry and Commerce cooperated with the Institute of the Chinese Academy of Sciences and organized the departments of the administration of industry and commerce in the cities of Shanghai, Qingdao and Harbin to compile the "Collection of the Historical Materials on China's Capitalist Industry and Commerce". By 1966, they published five types of historical materials. During the same period, the Institute of Economics of the Shanghai Academy of Sciences organized the compilation of the "Historical Materials of Typical Capitalist Enterprises in Shanghai" and published four types of such materials. The Ministry of Foreign Trade and the General Administration of Customs compiled and published 15 books of the materials on "Imperialism and Chinese Customs". According to the instruction of Mao Zedong that "it is very necessary to write a development history of capitalism in China", Zhou Enlai organized in 1960 Xu Dixin, Wu Chengming and other experts who worked at the Central Administration of Industry and Commerce at the time to start the compilation of the *Development History of Capitalism in China* in

multiple volumes on the basis of the compilation and publishing of the "Collection of the Historical Materials on China's Capitalist Industry and Commerce". These fruits of the solid material research work not only greatly promoted the study of relevant special topics but also contributed to the cultivation of a group of high-caliber research backbone forces. The economic invasion of imperialism to China and the development of Chinese capitalism were the main research topics in the study and discussion on early modern Chinese economic history in this period. By 1966, 38 material collections, 61 treatises and over 570 papers were published in the study of early modern economic history in the PRC during 17 years. The important works among them included *Early Modern Chinese National Economic History* written by Wu Jie, *The Issue of Primitive Accumulation of Capital* written by Fu Zhufu and Gu Shutang, *An Initial Study on the Occurrence and Evolution of Capitalist Relations in China* written by Shang Yue, *The Investments of Imperialism in Old China* written by Wu Chengming, *The History of the Economic Invasion of American Imperialism in China* written by Qin Benli, *The Development History of Chinese Banking Industry* written by Zhang Yulan, and *Inflations in Old China* written by Yang Peixin.

The situation of prosperity in the study of early modern Chinese economic history mentioned in the above was disrupted in 1966. The study of early modern Chinese economic history suffered serious damage during the ten years from 1966 to 1976. The majority of the research results before the foundation of the PRC and during the seventeen years before 1966 were negated. Originally-established scientific research plans were suspended and research work came to a standstill. Academic discussion was replaced by mass criticism and setting up forbidden zones. During the ten years of from 1966 to 1976, only one book entitled *The History of Jiangnan Shipyard* and nine articles were published under the background of extremely left-deviated lines were published and these publications were almost of no academic value.

After the beginning of the reform and opening up in 1978, the study of early modern Chinese economic history entered an unprecedentedly prosperous and thriving period. Research institutions and teams grew stronger, research horizons and areas expanded, research methods became diverse, and very rich research results were achieved.

First, a large batch of literature, archives and materials of economic history were sorted and published. Among them, *The Collection of the Archives and Materials of the Republic of China*, selected and compiled by the Second Historical Archives of China, was of enormous size. The Institute of Economics of the Chinese Academies of Social Sciences worked together with the Institute of Economics of Academia Sinica in Taiwan and other organizations and built a database on the materials of grain prices in the archives of the imperial court of the Qing Dynasty. And the Institute of Economics of the Chinese Academy of Social Sciences continued to compile and publish the second collection of *The Materials of the Shipping History of Early Modern Times in China* and the second collection of *The Materials of the Railway History of Early Modern Times in China* in the *Collections of the Referential Materials on Early Modern Chinese Economic History* and started to sort and publish the materials on the South Manchurian Railway.

In addition, the materials of the economic history of various departments, industries and regions were published successively in over 30 years, such as the materials of the department and industry histories about shipping, salt business and commerce, the historical materials of the large enterprises of the British American Tobacco Company, the South Manchurian Railway, the Anshan Steel and Iron Works, the Central Bank of the “Manchukuo” Puppet Regime, the Kincheng Banking Corporation, the Shanghai Commercial and Savings Bank, the Bank of China, the Juxingcheng Bank, the Han-Ye-Ping Company, the Yudahua Company, the Dasheng Company, the Liu Hongsheng Company, and the Wu Yunchu Company, the materials on special topics including the statistics on the customs of the old China and its taxation and tax distribution, the foreign debts of the Qing Dynasty and the Republic of China, domestic enterprises invested by overseas Chinese, industrial survey and statistics of the Jiangsu province, materials about Tianjin Chamber of Commerce, Suzhou Chamber of Commerce and the Nankai Economic Index, Zigong salt industry contracts, Zhang Jian’s archives, Sheng Xuanhuai’s archives, and archives and materials about natural disasters, and the financial and economic historical materials about the main revolutionary bases during the Chinese People’s War of Resistance against Japanese Aggression, or the War of Resistance for short. Various local governments and economic departments carried out extensive compilation and publishing work of local chronicles and specialized historical records. There were innumerable referential books about local industry and commerce history, agriculture and forestry industry, finance industry, fiscal administration history, port history, road history and postal service industry. Moreover, the materials about meteorological, hydrological and geographical changes and various archeological materials and materials collected from the public were also published continually.

Secondly, the number of the works on early modern Chinese economic history published from 1978 was far more than the sum of relevant works published in the first 80 years of the 20th century. Two works were the most noticeable among these academic research results. One was *The Development History of Capitalism in China* in three volumes edited successively by Xu Dixin and Wu Chengming. Another volume *The Socialist Transformation of China’s Capitalist Industry and Commerce* was added as one book in the *Contemporary China Series* published later and also as the fourth volume to this book. The other was *Early Modern Chinese Economic History* in three volumes successively edited by Yan Zhongping, Wang Jingyu, Wu Taichang and Liu Kexiang. The compilation of these two works started in the 1950s. A large amount of special topic research were taken as the basis in general history. They represented the frontier standard of the general study in the discipline. There were no less than 15 types of other works in general history. A large number of works were also published about some pioneering special topic research. For example, Zhang Zhongli, Kui Yingtao, Luo Shuwei and Pi Mingxiu edited the city histories of Shanghai, Chongqing, Tianjin and Wuhan. Cong Hanxiang, Yuan Shuyi, Kong Jingwei, Duan Benluo, Yuan Shuyi, Qiao Zhiqiang, Xing Long and Ma Junya compiled and edited the regional or rural economic histories of North China, Northeast China and South Yangtze River regions. Cheng Shiqi and Dai Yifeng wrote customs history. Xu Dingxin, Ma Min, Zhu Ying and Yu Heping wrote the

history of chambers of commerce of Shanghai, Suzhou and all China. Liu Foding, Wang Yuru and Chen Zhengping wrote the economic cliometrics related to economic development, price structure and international receipts and expenses. And Zhu Ying, Shi Bolin and Xu Jiansheng wrote the history of economic policies in early modern times.

5 The Progress in the Study of Contemporary Economic History in China

The study of the economic history of the PRC or the study of contemporary Chinese economic history truly started after the beginning of the 1978. There were sporadic researches in this area before this. For example, the Hebei University published *The Economic History of the People's Republic of China* in 1958. There were also some such research that particularly served the politics at the time. For example, the Institute of Economics of the Chinese Academy of Sciences and the State Administration of Industry and Commerce compiled in cooperation *The Socialist Transformation of Capitalist Industry and Commerce*. Xue Muqiao et al. edited *The Socialist Transformation of Chinese National Economy*. Zhao Yiwen wrote *The Development and Transformation of the Handicraft Industry in China*. And Shi Jingtang et al. edited *The Historical Materials of Agricultural Cooperative Transformation Movement in China*. However, no stable scientific research teams and specialized fields were formed at the time. The study of the economic history of the PRC started to be valued in the circle of economics after 1978 because of the needs of the country to summarize its own historical experience. The Institute of Economics of the Chinese Academy of Sciences, namely the predecessor of the Institute of Economics of the Chinese Academy of Sciences today, the Institute of Economics of the State Planning Commission, the Institute of Financial Sciences of the Ministry of Finance, Prof. Li Debin of the School of Economics of the Peking University, Prof. Sun Jian of the School of Economics of the Renmin University of China, and Prof. Zhao Dexin of the Economics School of the Zhongnan University of Economics and Law all carried out study on the economic history of the PRC. In 1984, the Chinese Academy of Social Sciences organized and initiated the compilation of *Contemporary China Series*, which caused various central economic departments and related local institutions to carry out the study on contemporary economic history. Besides, the Party History Research Center and the Party Literature Research Office of the CPC Central Committee and other historical research institutions also participated in the work. Hence, a stable group of research institutions and teams of considerable size was formed in the study of contemporary Chinese economic history.

When examined in the time span of over 30 years after the beginning of the reform and opening up, the key research areas and results of the study could roughly be divided into the following several aspects:

I. The Characteristics of the Study and the Division of Stages from the Beginning of the Reform and Opening Up

The study of the economic history of the PRC or the contemporary Chinese economic history truly started and thrived after the beginning of the reform and opening up in 1978. Before this time point, Xue Muqiao, Xu Dixin, Shen Zhiyuan, Wu Chengming and Zhao Dexin studied New Democratic economy, socialist transformation, and principles of economic development of the PRC. But such study was mostly carried out because of the needs in social transformation and economic work at the time. After the beginning of the reform and opening up, the CPC and the state needed to carefully summarize the experiences and lessons of the economic construction in the past. From 1978, the study of the economic development and system transformation of the revolutionary bases and in the first 30 years of the PRC gradually became the hotspots in the study of the CPC party history and economic history. The study of modern Chinese economic history in over 30 years could roughly be divided into the following three time periods:

(I) 1980s as the First Stage.

The characteristic of this stage was that equal weight was given to collecting and salvaging historical materials and summarizing experiences. Relevant institutions formed by the state and specialized institutions formed by various departments were the main entities involved. In this stage, a large group of senior comrades who engaged in economic work retired from leadership positions. They believed that they had the responsibility and obligation to summarize historical experiences from their personal experiences. And relevant institutions also believed that time was pressing and people had to seize the opportunity to carry it out. The main scientific research work and work results in this stage included the following three aspects: First, the Central Party History Material Collection Committee organized relevant work and collected, sorted and published historical literature series on economic history, for example, the historical materials about the transformation of capitalist industry and commerce in multiple volumes. Second, the Ministry of Finance organized relevant work and collected, sorted and published a large amount of financial and economic historical literature about revolutionary bases and published a group of research treatises on such basis. And third, the *Contemporary China Series* editorial committee led and organized various economic departments to compile, write and publish the volumes on economy in *Contemporary China Series* and a large amount of spinoff publications such as material selections and chronicles of events.

(II) 1990s as the Second Stage

The characteristic of this stage was that it was a stage of relative silence dominated by research. First, the task proposed in the 1980s was gradually completed after more than ten years of collection and sorting of historical materials. A large group of advisors and senior comrades who retired and worked in the study before did not have sufficient energy to carry on with their study because of their senior age. Second,

socialist market economy was determined as the goal of reform and development, which was different from the reform in the 1980s centering round how to improve public ownership system and planned economy. Therefore, many people believed that time was different and historical experience did not have much value for people to draw from or find guidance. And third, rapid economic development and urgent needs in reality caused the CPC, the state and relevant research institutions, or even individuals to turn their focus of attention from historical research to the study of issues in reality or even directly participate in practical economic work.

(III) The More than Ten Years after the Beginning of the New Century as the Third Stage

The first characteristic of this stage was that the study of contemporary Chinese economic history broke the silence in the 1990s and became once again the hotspot in economics and, in particular, the basic research in economics. After over 20 years of introduction of western academic thoughts into China, western economics were widespread and became familiar to the people. The key issue and opportunity for the circle of economics laid in how to apply the knowledge of economics to serve China's economic development and system change. So it was necessary for people to understand China's national situation. And history was the key to understand reality. Thus the scholars who studied China's economic issues both in China and abroad started to carry out study on economic history. The second one was that China resolved the issue of subsistence in all industries and areas after over 20 years of development. And in academic circle, research work became more specialized and management system tended to be more rigorous. Changing the field of research involved even higher costs and risks. The scholars who engaged in academic study were urged to innovate. And economic history became an area with very large space for innovation to the scholars in the study of economics. Third, the state raised its attention and funding given to the study of the sinicization of Marxism. The Ministry of Education listed the study of Marxism as a first-level discipline in its catalogue of specialized fields and also vigorously supported the development of the teaching and study of Marxism in higher education institutions and research institutions. And the Department of Propaganda of the CPC Central Committee established the project of Marxism. All these developments made economic history thrive as the most important area of the sinicization of Marxism. And fourth, relevant institutions published a large batch of selected works, chronicles and biographies of Chinese leaders such as Mao Zedong, Liu Shaoqi, Zhou Enlai, Deng Xiaoping and Chen Yun after 20 years of sorting and study and created conditions for the deepening of study. The study in this stage showed three characteristics. First, research teams were mainly specialized state institutions in the 1980s but they were now mainly from higher education institutions after the relative silence in the 1990s. Second, the hotspots of study almost covered every aspect and the study showed a noticeable deepening tendency. People were no longer satisfied with the conclusions in the past but expanded the study on many issues to microscopic and case empirical analyses.

Third, research theories and methods were more diverse than in the past. In the 1980s–1990s, the researchers of contemporary Chinese economic history were mostly senior comrades in the specialized field of history, including the history of the Communist Party of China, and those who retired from the departments of practical work. They mostly employed narrative or summarization methods. In this decade, more and more scholars in the specialized field of philosophy, economics and sociology entered the area of the study of economic history and brought many new theories, methods and perspectives into it.

II. **The Study on the Strategies of Industrialization and Economic Development of The People’s Republic of China**

The People’s Republic of China was founded on the basis of a thorough New Democratic revolution. The government led by the Communist Party of China always took up the dominant position in the economic development and system change in the PRC. Therefore, the economic development in the 60 years after the foundation of the PRC was typically government-led development. Industrialization was the most important and basic task that the PRC faced after its foundation. It was also the kernel line in the study of the economic development and system change in the 60 years after the foundation of the PRC. These developments made the thought and practice in industrialization of the CPC and the Chinese government and their economic development strategies the basic issues and constant hotspots in the study of contemporary Chinese economic history.

The study of the economic development strategy and industrialization history of the PRC started from the beginning of the reform and opening up. The three major issues of imbalanced economic structure, the failure to improve the living standard of the people over a long period of time, and poor economic benefits caused China to implement reform and opening up and adjust national economy, on the one hand, and urged the circle of economics to reflect on the losses and gains of industrialization and development strategies in the past, on the other hand. The study of economic development strategies in the 1980s generated two major research results. One was achieved by Chinese economists who studied domestically, represented by Dong Fureng. He summarized the historical experiences of China and the Soviet Union and analyzed the background and losses and gains of the strategy of prioritizing the development of heavy industry proposed by Stalin. He believed that, although we recognized the defects of the Soviet model and proposed the thought of the comprehensive development of agriculture and light and heavy industries of “taking agriculture as the basis and industry as the dominant area”, people did not thoroughly and properly implement the thought in practical work.⁷ The other was achieved by the first group of Chinese economists who studied overseas and returned to China, represented by Lin Yifu. He started his study from the perspective and experience of the world’s economic development and applied the theory of comparative advantage. He proposed that China’s comparative advantage was human resources and capital was the scarcest resource. So China should fully utilize such comparative advantage

⁷See Dong (1988).

rather than overstressing the development of heavy industry which entailed high organic composition of capital.⁸

During over 30 years of the reform and opening up, industrialization was still the kernel and main driving power of China's economic development. Besides, China's economic foundation was weak, per capita resources were deficient, and large amounts of rural residual labor urgently needed to be transferred in the beginning. Therefore, how to address well the relations between agriculture and light and heavy industries, the relationship between market and planning, the relationship between extension and intension development, and the relationships between the city and the countryside, between different regions and between China and foreign countries were always the issues that needed to be resolved and were never fully resolved. Therefore, the discussion and study on the history of the formation and evolution of industrialization and development strategy emerged and thrived from 1990s and generated a batch of research results.⁹ In the recent several years, the issue evolved into the discussion on the "China model".

III. The Study on the Economic Development and the Losses and Gains of Its Systems in the First 30 Years of The People's Republic of China after Its Foundation

After the reform and opening up, how to understand and evaluate the establishment of socialist economy characterized by sole public ownership system and planned economy before 1978 and its losses and gains became an important question as time passed and history precipitated because it was not only the foundation and start point of the economic development after the beginning of the reform and opening up but also the start point and object of the reform of systems and policies. Why did China sublate New Democratic economy and choose socialist economic system in the 1950s? What was the relationship between New Democratism, socialism and socialism with Chinese characteristics in terms of theory, system, inheritance and losses and gains in addition to the successive temporal sequence between them? And also the questions related to land reform, the movements against "three evils" and "five evils", the general line for the transitional period of the CPC, centralized procurement and distribution, the "Three Great Remoulds" of socialism, the "Rash Advancement" and "Anti-Rash Advancement" in 1956, the "First Five Year Plan", the Grand Leap-Forward, people's commune, the famine in the early 1960s, the adjustment of national economy, the Third Front Construction Movement, whether economy was at the brink of collapse from 1966 to 1976 and so on all became the research objects that attracted the scholar's attention once again. The most important and constant hotspot issues among them could be summarized into the following three aspects: The first aspect was how to understand China's transition from New Democratic economy to socialist economy. The second aspect was how to understand planned economy. And the third aspect was how to evaluate economic achievements and mistakes before the reform and opening up. The study in this area became an

⁸See Lin et al. (1995).

⁹See Wu (2006); Liu et al. (2006); Gao (2008); Zhu (2009).

important issue that could not be avoided in the study of economic history in early 1980s. At the time, Sun Yefang, Xue Muqiao, Ma Hong, Yu Guangyuan, Yang Jianbai and Wang Haibo in the circle of economics published treatises and opinions of larger influence in this area. In addition, Hu Qiaomu, Hu Sheng and Gong Yuzhi also published a large number of treatises in the perspective of the study of the party history of the CPC and some opinions in these works exerted even larger influence to the society and the academic circle. In summary, the following consensus was basically formed in this area in the discipline of contemporary modern economic history as the study constantly deepened over 30 years: Just like other socialist countries, the primary task that the CPC faced after the foundation of the PRC was industrialization, which should originally be completed in capitalism. And the international environment at the time did not allow a socialist country to fulfil this task slowly and step by step. In 1953, the CPC abandoned the economic and social form of New Democracy and sped up the transition into sole public ownership system and planned economy. The reason was not that the New Democratic economy, in which multiple economic sectors coexisted and developed, did not match the development standard of productivity at the time but that it did not match the economic development strategy established under the background that national security and unity was under threat. In other words, too low industrialization standard and heavy industry became the bottleneck of development. And they could not meet the needs in guaranteeing national security and unity. Thus it was necessary to prioritize the rapid development of heavy industry. And it was necessary to establish a system that could guarantee high accumulation and social stability and also the concentrated use of capital at the level of low income. This was the radical reason that China quickly completed the transformation from New Democratic economy into socialist economy during the “First Five-Year Plan” in the 1950s. As far as how to understand the losses and gains in the economic construction in the first 30 years of the PRC, it should be said that achievements represented the mainstream of development when viewed in the long run although China experienced large detours and had painful lessons and the living standard of the people only had slow improvement over a long period of time. Under the condition of deficient per capita resources and low per capita income, China broke the Malthusian trap and the poverty trap as defined in development economics, relying on its own forces. It established independent and relatively complete industrial system, laid the material foundation for transforming traditional agriculture, and improved the standard of human capital. Thus it laid the foundation for the rapid economic development after 1978.

IV. How to Understand the Relations between Industry and Agriculture and between the City and the Countryside in the First 30 Years of The People’s Republic of China after Its Foundation

The economic development and system transformation in the 60 years after the foundation of the PRC was in substance the history of the transformation of China from a backward country in which traditional agriculture and rural economy dominated to a country in which modern industry and urban economy dominated. Because China

had large population and weak economic foundation, it had to rely on agriculture and peasants to provide necessary accumulation for the country's industrialization in the pre-stage of such industrialization. Besides, economic system reform achieved breakthrough and then important success first in the countryside. Then there were the cancellation of people's commune, the quick rise of town and township enterprises, and the cancellation of the centralized procurement and sale of agricultural and sideline products. And later, there were the issues of migrant workers, urbanization, land requisition in the development of the city and real estate industry, overburden of peasants, too slow income growth of peasants, "rewarding agriculture" in the latest several years, the construction of socialist new countryside, and so on. These developments and issues made the relations between industry and agriculture and between the city and the countryside a constant research hotspot in over 30 years of the reform and opening up. Some people even said that the day when the "Three issues of agriculture, the countryside and farmers" issue was resolved was the moment when China realized modernization. Therefore, the relations between industry and agriculture and the city and the countryside were always the important issues and research hotspots in the study of contemporary Chinese economic history. They were the best areas to embody the principles of "making the past serve the present" and "administering affairs and attaining practical use" in the study of economic history and they did play an important role. The research teams and results in this area should be said to be the most outstanding and powerful in the discipline of contemporary Chinese economic history.

V. The Study about Economic Development and System Change from the Beginning of the Reform and Opening Up

The reform and opening up, marked by the Third Plenary Session of the Eleventh CPC Central Committee in 1978, has passed a development course of 32 years until now. During this period, China achieved marvelous achievements in economic development that made the world amazed. And its economic system underwent drastic and profound change. As far as such development was concerned, some people claimed that anyone who interpreted Chinese economy very well could win the Nobel Prize for economics. During over 30 years, the study on economic system reform and development in the 1980s could be said to belong to the study on the issues in reality and their countermeasures. Then from the beginning of the 21st century, the economic development and system change from the beginning of the reform and opening up became more and more the object of study in economic history and more and more scholars started to review and study this historical period. In particular, a large group of treatises were written and published about the study of the economic development and system change in China from the beginning of the reform and opening up in the two years of 2008 and 2009 in commemoration of the 30 years of reform and opening up and the 60 years of the PRC after its foundation.

Because this historical period was closely related to the study of the issues in reality, it was very hard to strictly distinguish which works belonged to the treatises of economic history and which works to the study of the issues in reality and their countermeasures. So the author generally adopted two kinds of division standards:

One was that the object of study in a treatise belonged to economic events or issues 10 years ago. The other was that it belonged to the issues that occurred consecutively for no less than 10 years in temporal sequence. Those works, which involved the review and evaluation of historical issues in the study but did not take them as the main purpose, did not belong to the treatises on economic history. In summary, the great multitude of treatises on the economic history of the latest over 30 years could be divided roughly into two types: One was the comprehensive study on the course, stages, characteristics, driving power, gains and losses of the reform and opening up and economic development and also on economic transition, development mode transition, urban-rural relationship, industrialization, marketization and urbanization standards and degree of opening up to the outside work, which included the thoughts, policies, mechanisms, effects and international comparisons of economic development and system change. The other included special topic research in various areas in the economic realm in over 30 years, which included macroscopic economic management, state-owned enterprise reform, rise of town and township enterprise, development of private economy, introduction of foreign and overseas investments, industry, agriculture, commerce, price, fiscal affairs, finance, foreign trade, human resources and employment, consumption, social security, and also income distribution, education, medical care and housing reform, which included the people's livelihood.

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Chapter 31

Western Economics in China Over 60 Years After the Founding of the People's Republic of China



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It can be seen that western economics met very rough treatment in China during over 60 years of the PRC after its foundation. Its status and role changed in different historical stages. Roughly speaking, the period could be divided into two stages, namely the nearly 30 years before the reform and opening up and the over 30 years after it. In the first stage, it could be said that western economics was totally negated and criticized. In the second stage of over 30 years, it gradually won fair evaluation and attention and played an important referential role. The focus of this chapter was to formulate the influence and referential role of western economics to the development of economic theories in China in over 30 years after the beginning of the reform and opening up.

The term “western economics” that the author used here was a general term that referred to macro- and microeconomics and other related economics, such as monetary finance, cameralistics, international economics, development economics and econometrics, which were popular in western countries. In the author’s opinion, it was not appropriate and scientific to define an area of economics with regional concept. In fact, macro- and microeconomics, as the main part of western economics, both belonged to the theoretical system of market economy because macro- and microscopic economics both belonged to market economy.¹ And market economy was, in the end, the product of socialized mass production after it developed into certain stage. The combination of socialized mass production and private ownership created capitalist market economy while the combination of socialized mass production and public ownership would hopefully create socialist market economy. It can be said that capitalist market economy existed and developed for several centuries in

¹Huang (1998), Sects. 3–4, Chap. 1.

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history and so did the economic theories that reflected such market economy. China was building market economy on the basis of public ownership system, which was unprecedented in history. It was still in the process of construction or in incubation. The Chinese people were “crossing the river by feeling the stones” and there was still a long way to go for them. Although there was a vague outline in their mind, nobody could explain it in detail at present. And the economics or the theoretical system that studied and reflected socialist market economy was far from being established. So in the current historical period, only the capitalist market economy in western countries was the mature market economy in the world. And the economic theories in relation to it formed a relatively complete system. Some people called the latter modern economics, which was in fact a proper term. But people needed to be aware that modern economics, which studied market economic system, should include two major parts. Namely it should also include the theoretical system that studied socialist market economic system in addition to that studied capitalist market economic system. And the former still needed to be established by the Chinese people in the practice of economic reform and development in the future. The discussion in the chapter was only limited to the influence of the first part in modern economics to the development of economic theory in China in nearly 50 years or to the role that it played in such development. Considering that modern economics was also generally known as western economics, which became a term established by usage in higher education institutions at present, the author also uses such a term in this chapter.

1 The First 30 Years Before the Reform and Opening up

In the first nearly 30 years of the PRC after its foundation, western economics was always in a situation of being criticized and stifled in China. Newspapers and magazines were only allowed to criticize western economics and not to introduce it objectively or evaluate fairly. The course of western economics was cancelled in higher education institutions. Relevant courses in various departments of finance and economics only included Marxist political economics, which included the part on capitalism and the part on socialism, and *On Capital*. The textbooks used were those on political economics compiled by Soviet experts and those for various other courses in finance and economics. Historical differentiation was made among western economics and economists completely according to the standards given by Karl Marx in the books of *On Capital* and *The History of the Doctrine of Residual Value*. The economists in the classical economic school, such as William Petty, Adam Smith, David Ricardo, and Francois Quesnay, were basically recognized. The economic theories established by Jean Baptiste Say and Thomas Robert Malthus and those later than them were classified as the “vulgar” economic school of capitalist economics, which was regarded as being defensive, pseudo-scientific or anti-scientific or even reactionary. The more these theories were closer to the contemporary times, the more “vulgar” or “reactionary” they became. The radical reason for this was that they defended for capitalism market economic and profit motives. So they needed

to be negated completely and criticized thoroughly. Such “left-deviated” guiding thought of historical nihilism reached its apex in development from 1966 to 1976.

It was absolutely not incidental that China adopted an attitude of complete negation on western economics during the 30 years before the reform and opening up. There were certain economic and political origins and needs in it.

I. The Need in Implementing Planned Economy

After the foundation of the PRC, the state immediately started implementing centralized planned economic system. Thus, the state immediately monopolized foreign trade and finance and limited and cancelled commodity circulation and free market. Comprehensive socialist transformation was implemented on private industry and commerce and individual handicraft industry. National economy was shifted onto the economic foundation of public ownership system, which was dominated by state ownership and state operation. Thus it became possible to implement centralized planned economic system nationwide. Such a system required that people depended on administrative power to implement the planned operation of national economy. The government determined what to produce, how many or how much to produce, and for whom to produce. Planning replaced market mechanism as the basic means to distribute social resources. State-owned enterprises were included in governmental fiscal system under unified state control over income and expenditure. Banks became the “cashiers” of state fiscal organs. “Material transfer and allocation” replaced commodity circulation between enterprises, departments and regions. Fiscal allocations replaced enterprise investment. People never considered costs in production and expenses in fund using. Repeated constructions occurred endlessly and “investment hunger” became more and more serious. Like what Sun Yefang described, the entire national economy became a modern “natural economy”.² As a kind of modern “natural economy”, planned economic system was naturally incompatible with market economy. All economic categories and theories that reflected and studied market economy were completely opposite to it so that they were regarded as being “alien” or destructive because “natural economy” was actually disintegrated by commodity-money relationship. Therefore, planned economic system resolutely stifled market economy and abandoned western economics so as to maintain its own survival.

II. The Need in Theory or Ideology

In the teachings of Marx, Engels, Lenin and Stalin, socialism could only be established on the basis of planned economy. Besides, the Soviet Union relied on planned economic system to mobilize huge material resources and forces after the October Revolution and thus it realized industrialization within a short period of over 20 years and defeated German fascism. As a result, it was regarded as an unalterable principle that planned economy could only be inherent to socialism while market economy should be inherent to capitalism. Later, this doctrine was taken as the standard by traditional Marxists in the whole world led by the Soviet Union. Moreover, this

²See Sun (1979). Huang (1983).

doctrine exaggerated the incompatibility between market economy and planned economy as the incompatibility between market economy and socialist system. It put planned economy under the protection of the halo of socialism and regarded various mechanism and categories, such as market economy, market mechanism, profit motive and free competition, as dreadful things harmful to socialist system, which should be completely exterminated in practice and thoroughly criticized in theory. This doctrine dominated China's economic construction for nearly 30 years and it was broken by Deng Xiaoping after the Third Plenary Session of the Eleventh CPC Central Committee. This determined that western economics could not avoid suffering from the fate of being criticized and suppressed in early 30 years after the foundation of the PRC.

III. The Need in the Implementation of the Political Line of “Taking Class Struggle as the Guiding Principle”

After the foundation of the PRC, the country adhered to implementing the measures such as suppressing and eliminating counterrevolutionaries, bandits and local depots and punishing embezzlement. These measures were necessary for the young republic to maintain its political and social stability as it was confronted with the blockade and embargo of western countries and also forced to resist the USA's aggression and aid Korea. In 1956, the Three Great Remoulds concluded, namely the socialist transformation of agriculture, handicraft industry and capitalist industry and commerce. It was pointed out in the resolution of the Eighth National Congress of the CPC that the age of fierce class struggle ended and the main domestic contradiction in the future was the contradiction between backward productivity and advanced productive relations. The priority of the work should be transferred to economic construction. However, such line was quickly drowned by the left-deviated line and thought trend which “takes class struggle as the guiding principle”. The target of “class struggle” quickly shifted from outside to inside the people, then to inside the CPC, and eventually to its kernel leadership from 1966 to 1976, the start of which was symbolized by the big-character poster “Bombard the Command”. It needed to be mentioned that the so-called “capitalist rightists” were the first group of people who suffered the impact when the target of “taking class struggle as the guiding principle” turned to inside the people in the middle the 1950s. These people were mainly non-CPC personages and scholars. And naturally, the economists who studied abroad and the western economics that they studied could not evade such disaster.

The three reasons above determined the historical fate of western economics that it was always criticized and abandoned in the 30 years after the foundation of the PRC. In early the 1950s, the criticism mainly targeted various western economic theories, such as Keynesianism and Malthusianism. And the scholars in China who were accomplished in the study of western economics only proposed “learning afresh”, namely “self-criticism”. However, after the start of the Anti-Rightist Movement, people implemented the idea of “taking class struggle as the guiding principle” and targeted the criticism on the people. A group of economists who studied overseas in their early years and had great academic accomplishment were labelled rightists in the

movement. Many people were forced to accept criticism under high political pressure and suffered unfair treatment or even personal attacks. A very representative case was the criticism on “Some Opinions on the Work of Economic Science at Present” (or the “Opinion Letter” for short) written by the six professors of Chen Zhenhan, Xu Yu’nan, Luo Zhiru, Gu Chunfan, Wu Baosan and Ning Jiafeng.

These six scholars were all renowned economists who studied in the USA and the UK in their early years and returned to and worked in China for many years. Among them, Gu Chunfan and Ning Jiafeng served in government organs, Wu Baosan worked at the then Institute of Economics of the Chinese Academy of Sciences, and the rest three were deeply-respected and famous scholars of the Peking University. Although they were not communists, their words and deeds in their whole life showed that they loved the motherland and supported the CPC. They actively studied Marxism and Leninism, worked enthusiastically at their positions, and wanted to contribute their learning to the economic construction undertakings in the motherland. They felt greatly encouraged by the new line centering round economic construction formulated at the Eighth CPC National Congress. They spoke frankly and sincerely when invited to help the CPC to rectify its working style. And the most important one among these opinions was that people should not overlook the positive role of the theories of western economics to economic construction work. They bravely wrote this “Opinion Letter”³ about economics and called for changing the negative attitude toward western economics.

The basic view in the “Opinion Letter” was that people needed to resolve issues in two aspects in order to bring into play the “guiding role” of the economic science in Marxism and Leninism in socialist economic construction. On the one hand, workers in economic areas and state economic organs should pay more attention to the role of economic science and overcome the attitude of despising economic science. They should respect objective economic laws in their work and avoid subjectivism and blind action. On the other hand, they should develop the economic science in Marxism and Leninism in the practice of socialist economic construction. They should seriously establish the understanding that China’s economic science still “stay in a very infantile stage” and that it was still very “weak”. Frankly speaking, the issues in the second aspect were more important and arduous. Those involved not only the issue of how to correctly treat classical works in Marxism and Leninism and the experiences and textbooks in the Soviet Union but also the issue of how to correct treat western economics.

The Opinion Letter opposed treating the classical works of Marxism and Leninism with an attitude of dogmatism. It emphasized that the purpose of study laid in “understanding the thoughts, outlooks and methods of classical writers rather than their words”. It showed much disapproval to the phenomenon that the circle of economics depended on using a great amount of quotes from classical works, 50% of them bearing quotations marks and 40% not bearing, to write their articles. It emphasized that people should closely relate to the practice of China’s construction and should not “become accustomed to putting the label of revisionism on any words different

³Chen et al. (1958).

from the texts in classical works". Besides, the Opinion Letter also opposed the practice of copying and replicating everything in the Soviet experiences in economic construction and the Soviet textbooks on economics, which was rather popular at the time.

The Opinion Letter also focused on discussing the issue of how to treat western economics. It used traditional term and called western economics "capitalist economics". But it disapproved of the attitude of constantly criticizing and completely negating toward it and proposed the issue of "critical reception of capitalist economics". Under the circumstance that the circle of theoretical study at the time adopted the attitude of constantly criticizing toward western philosophy and social sciences, including economics, it was truly rare and commendable that the Opinion Letter proposed the issue of "absorption or reception" in addition to criticism. The Opinion Letter also gave examples on the issue of criticizing and absorbing western economics to make further analysis. It said, "For instance, the multiplier theory of Keynes is only a kind of mathematical concept. Can it be used to analysis the effects of our investment? For another instance, the concept of margin is often used in vulgar economics. Does it have some value in practical use as an analytical instrument? In particular, the science of statistics possesses the same important meaning to the scientific study of social phenomena whether it is in capitalist or socialist society. There are many methods and concepts in capitalist statistics, such as sampling theory, normal curve, time series, correlation coefficient, and so on. The authors feel that people can also apply them to analyze our social economic phenomena. But all these are excluded from the area of statistical work so that the statistics taught and learned in China becomes nothing but the four rules of arithmetic and simple average."

It was a scientific attitude to both criticize and absorb western economics, which was exactly the attitude that Chinese people adopted today. As a discipline that reflected and studied capitalist market economy, western economics contained both many things that were not applicable to China's socialist economic construction or its construction of socialist market economy and many things that people could borrow from and absorb. This was because contemporary capitalist and socialist economies both relied on socialized mass production and practiced market economy. There were naturally many related categories and principles between them that people could borrow from and absorb. In fact, classical writers of Marxism and Leninism advocated that people should adopt an attitude of critically inheriting when treating history and culture. They all both criticized and absorbed their theories when treating capitalist economists. Today, absorbing the useful components in western economics already became a consensus of the majority of the circle of economics in China. Moreover, many categories and methods, such as multiplier theory, marginal analysis, sampling theory, normal curve, time series and correlation coefficient, were already employed by the extensive community of the workers in the study and teaching of economics and practical economic work in their own practice. An issue, which seemed to be very easy to understand today, became one that caused great controversy 40 years ago. In addition to the situation that people still did not have adequate practice and understanding at the time, one important reason why western economics

was completely negated was that the planned economy that China practiced and maintained with its best efforts at the time was a kind of modern “natural economy” incompatible to market economy.

The Opinion Letter also mentioned some other issues. Its basic view and thought trend were positive and many opinions were pertinent. Some of them still had referential value today. People should in fact follow the double-hundred policy of letting a hundred flowers blossom and a hundred schools of thought contend when doing things in the academic area. They should allow different views, allow contention and allow correcting mistakes. But at the time, because people implemented the principle of “taking class struggle as the guiding principle”, the Anti-Rightist Movement was launched nationwide in which “rightists” were hunted down everywhere. The Opinion Letter of these six professors became the first target in the circle of economics. In the so-called “criticism”, people raised the issue to a higher plane of principle and two-line struggle and related to political programs unlimitedly. The Opinion Letter, a paper about economics written by the six economists, were said to be an “anti-socialist scientific program”, a “rampant attack” on socialism, the “summoning of the ghost of capitalist economics”, and so on. An academic issue was wrongly treated as a political issue. Before this event, the criticism on western economics was only limited to textual “criticism” on theories. Then after that, the criticism turned to further condemning people in both speech and writing. Some scholars were given various political labels and suffered political prosecution to which they should never become a victim. Such criticism in which untrue charges were made up with easy excuses caused serious mental damage to its victims. Besides, because of political pressure, it drew the extensive community of researchers and teachers and common people into the political movement in which things were related to political programs unlimitedly. In the end, all the people suffered mental damages of different degrees. Such practice that made an academic issue into a political issue caused everybody to regard the study of western economics as a dangerous thing. Thus, western economics truly become oblivious. It was not brought down by criticism but crushed with pressure. This was an example of treating academic issue with a pernicious attitude.

Although the Anti-Rightist Movement caused deep spiritual trauma to the extensive community of the intelligentsia, the intellectuals still had great patriotic enthusiasm and support to the CPC. In particular, some senior economists not only cared about the construction of the state and important issues in national economy but also employed their knowledge and learning to provide proposals and suggestions to the government although they clearly knew the political risks, just like what was described in an ancient poem that read “An aged steed lying by the manger still has the ambition to run for a thousand miles; a heroic champion in his late years will never abandon his lofty aspirations.” Ma Yinchu was a prominent representative of them.

Ma Yinchu was a famous Chinese economist who studied abroad in his early years. He was esteemed by the Chinese people because of his academic accomplishment. During the several decades of the PRC after its foundation, he always worked hard to make progress in political awareness. Because he revealed the corruption

and darkness of the rule of Kuomintang with a dauntless spirit, he was once put into concentration camp by the Kuomintang government during the Chinese People's War of Resistance against Japanese Aggression. After the war ended, he devoted himself to democratic movement under the danger of being assassinated by Kuomintang agents. He was a patriotic democratic personage deeply respected by the Chinese people. Soon after the foundation of the PRC, he was appointed president of the Peking University because of his talent, virtue and prestige. In addition to his heavy work in managing the university, he also earnestly studied important issues in national economy, such as population and comprehensive balance. Each year he would take advantage of the opportunity of the work inspection as a member of the Standing Committee of the National People's Congress to make surveys in factories and rural areas. Population issue was the center of his study and survey. In 1955, Ma Yinchu submitted a written speech entitled "Controlling Population and Its Scientific Research" at the discussion meeting of the Zhejiang Group at the National People's Congress. At the time, people did not realize the importance of this issue. In 1957, he wrote the *New Population Theory* and he made a speech on it at the Fourth Plenary Meeting of the First National People's Congress. His speech won the attention of the central authorities and *People's Daily* published it as one of written speeches of the representatives of the National People Congress on July 5 that year. Soon later, an evil left-deviated trend rose, in which his *New Population Theory* was called "new Malthusianism". And Ma Yinchu was regarded as harmful as Dean Gooderham Acheson, the US Secretary of State whom Ma Zedong had criticized. Then one after another articles of criticism and attack were written against him. An academic issue was turned into a political issue once again.

What on earth were the basic outlooks of the *New Population Theory*⁴? First, Ma Yinchu poignantly proposed in his article the issue that China's population grew too fast. On the basis of the data of the National Population Census in 1953 and the results of his personal inspections in many provinces and municipalities and rural areas from 1953 to 1955, he found that China's annual natural population growth rate was 22.29‰ during the four years from 1954 to 1957, which was much higher than in 1953. Too fast population growth and slow fund accumulation caused deep concern in the mind of Ma Yinchu. He felt that he had to raise the high attention of the people in all China. Second, Ma Yinchu was the person who proposed the issue of population quality earlier in the world. He believed that people should consider the issue of population quantity in association with population quality. He stressed on developing education and raising the standard of knowledge acquisition to improve population quality. He believed that large population was both a kind of "great resource" and a kind of "great burden". He advocated controlling population quantity and improving population quality. Only in this way could people keep its benefits and remove its disadvantages or maintain the great resource and avoid the great burden. Third, he emphasized particularly that too fast population growth would seriously affected national economy. For example, (1) it was impossible to accelerate fund accumulation. (2) It was necessary to expand the planting area of grain and reduce the planting

⁴Ma (1998a).

area of economic crops and to reduce the supply of industrial raw materials and thus postpone the advancement in industrialization. (3) it would weaken the foundation of industrialization and affect the research and development in science and technology. In summary, controlling population was absolutely not an optional policy but an indispensable one. It already became an urgent task that allowed no delay and omission. In order to effectively control population growth, Ma Yinchu proposed three major measures. First, people should strengthen relevant publicity work and break the feudal thought of "having a baby as early as possible in life". Second, people should revise marriage law and encourage late marriage. And third, people should publicize artificial contraception and oppose artificial abortion to avoid killing lives.

In order that more people could understand and accept his view, Ma Yinchu solemnly clarified in his paper that "my population theory is different from the Malthusian ones in position. His followers advocate reducing population by cruel means such as plague, disease and war. ... I do not advocate reducing population. Rather I support improving the labor productivity of the working people so as to improve the standard of their material and cultural life."

The points in the above were the basic views and suggestions that Ma Yinchu formulated in his paper. These views were correct in theory and these suggestions were practical and feasible. Over 40 years ago, he pointed out poignantly that people needed to control population growth and it was truly a visionary basic state policy. Then how could these views and suggestions be wrong? Most critical articles were simply limited to using the so-called "man's hand theory" to criticize Ma Yinchu's "population theory". It was said that "man is not only consumer but also producer" just like that man had not only "mouth" but also "hands". They blamed that Ma Yinchu only "sees mouth and does not see hands". With such simplistic exaggeration of the "man's hand theory", they could easily draw the wrong conclusion that the greater the population, the better. In fact, such criticism was untenable because man could not just rely on his hands although he was truly producer. There also needed to be land, including other natural resources, capital and equipment. Exploiting nature and making equipment both needed the increase of accumulation. Too fast population would result in growing consumption and weaken accumulation so that the production capacity of the people themselves was weakened. Ma Yinchu felt concerned about too fast population growth and called for countermeasures mainly because of such a point. His sincere heart with his love of the country and the people could be seen in his article. But truth, fact and conscience were all drowned in the left-deviation thought trend at the time. One after another articles attacking him brought one after another political labels, such as "opposing the party and socialism", "always opposing Marxism", "always serving imperialism, feudalism and capitalism", and "practically attacking the party and socialism under the pretext of academic research". All these were poured on Ma Yinchu.

However, Ma Yinchu not only found the truth but also had the tough spirit to adhere to the truth and not to yield to power. Although the criticism on his theory lasted for several years and although he knew a "theoretical authority", namely Kang Sheng, in the superior authorities conspired the attack on him, he would not step back to abandon the truth that he found. He indicated in a "statement" made in November

1959 that “I am nearly 80 years old and I know I will not win when I fight them all single-handed. But I still will stand out and fight them alone until the moment I fall. I will not surrender to those critics who only try to suppress me with power and not to convince me with reasoning.”⁵ He also expressed his pity for not accepting the advice of a good friend in his statement. His friend saved him by all means when he suffered afflictions in Chongqing before the foundation of the PRC. When the PRC was founded, he responded to the invitation of this friend and left Hong Kong to North China to participate in political affairs. But this time, the friend sincerely told him to make an apology to end the fight. But Ma Yinchu said, although he was “very grateful” and “always bear in mind” the care of his old friend for all the time, “I have not accepted his sincere advice and I feel greatly sorry because I am in the debate of an academic issue this time and I am very confident in my theory. I cannot stop adhering to it. I have to defend for the honor of academic study. So I have to refuse to apologize.” Soon after, this important article of programmatic value to state affairs was suppressed after several years of attack.

When Ma Yinchu’s correct view was under unreasonable political attack, his great virtue and prestige still won several chances to defend for himself when he worked at the important office of the president of the Peking University. This was hardly possible for those so-called “capitalist rightists” and “capitalist academic authorities”. It should be pointed out that most of these “rightists”, “reactionary authorities” and “capitalist scholars” who suffered political criticism still emphasized that people should apply some theories in western economics under the guidance of Marxist and Leninist thoughts to serve China’s economic construction. Nonetheless, they were still criticized and the majority of them were given no chance to defend themselves. All these indicated that western economics was always in the wretched situation of total negation during nearly 30 years after the foundation of the PRC.

Some changes occurred in the early 1960s. In 1961, the Propaganda Department of the CPC Central Committee and the Ministry of Education organized the compilation of the textbooks on liberal arts for the teachers and students in the specialized fields of liberal arts and law, including the specialized fields of economics and finance and economics, in various colleges and universities nationwide. Before this, Soviet textbooks or the textbooks compiled by Soviet experts sent to China were used in the teaching of all specialized fields of liberal arts and law, including those of economics and finance and economics, in China. And nobody was permitted to say anything to oppose this. Now the Propaganda Department of the CPC Central Committee and the Ministry of Education needed to organize Chinese experts and scholars to compile their own textbooks for the specialized fields of liberal arts and law. Textbooks were also required to be compiled about various contemporary schools and theories in economics and other disciplines in western countries for the purpose of broadening the view of the teachers and students in higher education institutions. At the time, specific instructions were given about how to treat western economics. They needed to criticize and introduce it and do it in an “objective” and “systematic” manner. The two authorities commanded that textbooks needed to be compiled with

⁵Ma (1998b).

a tight schedule and Zhou Yang, vice director of the Propaganda Department of the CPC Central Committee, took in charge of the compilation of all textbooks in the specialized fields of liberal arts and law.

Why such a situation occurred at the time? The author believed that the political movements of the Three Red Banners, namely the General Line for Socialist Construction, the People's Communes, which was raised by left-deviated thoughts and lines, all failed, on the one hand. Then there were three years of natural disasters. The "people's commune" movement ended up in failure for the time being and the public dining halls in the countryside were shut down. Some rural areas started to spontaneously implement the system of "fixing farming output quotas by household". Left-deviated thoughts and lines had setbacks for the moment. On the other hand, the party and state relations between China and the Soviet Union broke. The Soviet Union stopped its aid and withdrew its experts. The policy of "completely following the Soviet Union" and "taking the Soviet Union as teacher" would not work any longer. China had to find its own road in the future and it was necessary to know more about the outside world other than the Soviet Union. Under such a situation, the Propaganda Department of the CPC Central Committee and the Ministry of Education organized some Chinese scholars to work on the compilation of various textbooks in liberal arts and required them to compile textbooks on western economics. These authorities also instructed that people needed to both criticize and understand and borrow from western economics. And they emphatically required that introduction needed to be both objective and systematic so that people could learn about the true status of western economic theories. In order to ease the editors' concerns, they emphasized in the instruction that the compilers were responsible for academic quality while organizers for political quality. Compilers should take the responsibility of making the introduction objective and systematic. They did not need to worry about whether criticism was adequate and thus did not need to have concerns about it. The instructions above indicated that the authorities already started to let the extensive community of young students learn about the economic conditions and theories of the outside world and, in particular, of western countries. This was the first time that there was some easing in the attitude of total negation toward western economics which was adopted for more than ten years after the foundation of the PRC.

Two textbooks on western economics were compiled under the organization at the time. One was about the history of western economics, a textbook entitled *The History of the Theories of Economics*. The other was about contemporary western economics, entitled *Main Schools in Contemporary Capitalist Economics*. The first one explained the history of economic theories over a large time span from the ancient Greco-Roman times to the time of the Keynesian economic theory. Its diverse numerous contents included both ancient Greco-Roman economic thoughts and the economic thoughts in utopian socialism and those of Marx, Engels and Lenin. In addition to these, a considerable part of the book introduced the history of capitalist economic theories. It was edited by Lu Youzhang and Li Zongzheng, two professors of the Renmin University of China. A number of professors from the Renmin University of China, the Peking University, the Nankai University and the Jilin University participated in the compilation of the book. *The History of Political Economic History* written by

D. I. Rozenberg and other relevant Soviet textbooks were the main references for the compilation of the book. Another book *Main Schools in Contemporary Capitalist Economics* was compiled with Prof. Luo Zhiru from the Peking University as the director of the editorial group and Wu Baosan from the Institute of Economics in the Chinese Academy of Sciences and Prof. Gao Hongye from the Renmin University of China as the vice directors. A number of scholars from the Peking University, the Renmin University of China and the Institute of Economics of the Chinese Academy of Sciences participated in the compilation. The work had altogether five books: (1) Keynesianism, (2) monopoly economics, (3) welfare economics, (4) econometrics, (5) “people’s capitalism”. Most references in the compilation of this book were works of Soviet scholars such as I. G. Bliumin. These five books were successively published by The Commercial Press from 1962 to 1965. *The History of the Theories of Economics Vol. 1* was published by the People’s Publishing House in 1964. And then its publishing was disrupted. The second volume of the book was not published until 1982.

Although Zhou Yang made the instruction that people needed to make “objective and systematic” introduction to western economics, the leaders and the compilers were still influenced largely by the ideological restrictions of left deviation under the general environment that the “left-deviated” thought trend took up the dominant status. And most of the references used in the compilation of the textbooks of western economics at the time were the works popular in the Soviet Union, such as those of D. I. Rozenberg and I. G. Bliumin. As a result, the author felt deeply as one of the compilers of the textbook *Main Schools in Contemporary Capitalist Economics* that people still basically adopted an attitude of criticizing and negating toward western economics although the compilers made great efforts to implement the instruction of “making objective and systematic introduction” under the condition of ideology at the time. Nonetheless, the textbooks still made more adequate and systematic introduction on western economics than in the past. And the attitude toward western economics showed improvement to certain extent.

In addition to compiling and publishing textbooks, another important channel for introducing western economics was translating and publishing the original works of western economics. The organizations that undertook the work in this area mainly included The Commercial Press, SDX Joint Publishing Company, People’s Publishing House, and Shanghai People’s Publishing House. The Commercial Press published works on western economics in a larger number and a more systematic manner. From the 1950s, The Commercial Press organized, translated and published in a planned manner the works as the three sources of Marxism, which included the classical economics works in the UK and France that Marx praised highly, so that the readers in China could learn more about these three sources. A critical Chinese “Foreword” had to be attached when these works were published at the time so as to provide guidance to the extensive community of the readers and to prevent them from the poisoning of capitalist thought. Nonetheless, people still had the possibility to know about western economic theory. From 1966 to 1976, the work of translating western academic works was suspended and this channel to introduce western economics was blocked.

In summary, China gave the epithet of “capitalist vulgar economics” to western economics and, in particular, the western economics from the 19th century due to the dominance of left-deviated dogmatism during nearly 30 years from the foundation of the PRC to before the reform and opening up. People believed that it was anti-scientific in theory and reactionary in politics as a defensive economics and it would become increasingly reactionary. So they adopted an attitude of total negation and comprehensive criticism toward it. Moreover, they took the criticism on western economic theory as a means of political prosecution inside the people in China. In the end, rigid and uninformed ideology was formed in the circle of theoretical economic study and the area of teaching of economics. Dogmatism became increasingly serious, theoretical study increasingly detached from reality, and the teaching of economics was even worse. The part on capitalism in political economics became more and more incompetent to explain the economy development of contemporary capitalist world while the part on socialism was more and more like a collection of the financial and economic policies and decrees of the state. The study and teaching of economics in China fell into crisis.

A particular serious problem was that such left-deviated attitude of total negation that China adopted toward western economics resulted in rigid policy guiding thought so that people overlooked or even violated economic principles. This caused serious damage to China’s economic construction, which could be seen at least in the following three aspects.

First, policy guiding thoughts became rigid under the long dominance of left-deviated and dogmatic thought so that people’s thought was tightly fixed on planned economy system. Any thought trend and specific measure that bore the trace of market was harshly criticized in theory and ruthlessly stifled or cancelled in practice. The trend of “being rather leftist than rightist” became increasingly stronger and caused increasing damage to economic development. For example, profit motive, competition, cost-benefit concept, principle of economic accounting, personal economic interest and independent status of enterprise, these mechanisms and categories of market economy were criticized and abandoned as “the stuff of capitalism”. As a result, the “communism fad”, characterized by “equalitarianism and indiscriminate transfer of resources” and “making calculations on politics and not on economy”, occurred during the period of 1958-1960. And the “subjectivist mania”, characterized by “The fields would have any amount of yields as long as you are bold enough to claim it”, “catching up and surpassing the UK and the USA” and “entering communism at a running pace”, also occurred. The “equalitarian fad”, which criticized the principle of distribution according to performance, occurred from 1966 to 1976 and the movement of “cutting capitalist tails” was launched, in which the “private plots” of the members of the people’s communes in the countryside were confiscated. All these seriously damaged industrial and agricultural production, natural resources and the production initiative of the extensive community of workers. In the end, national economy reached the brink of collapse in the middle of 1970s.

In addition, the bad consequence of rigidified policy guiding thought was also manifested in the situation that a wall to “protect” socialism was built in people’s minds through criticizing western economics. It completely isolated them from seeing the mechanisms and categories inherent to market economy. In fact, this wall prevented China from realizing the transition from planned economy into market economy at an earlier moment. This meant huge economic or material loss and, most importantly, the loss of time, which was undoubtedly a kind of bigger loss.

Second, it needed to be mentioned that China totally negated and thoroughly discarded the System of National Accounts (SNA), recommended by the United Nations and generally adopted by western countries in the 30 years after the foundation of the PRC, regarding it as a component of western economics, and followed the System of Material Product Balances (MPS) adopted later by the Soviet Union at the time. One important difference between these two different accounting systems was that MPS only included the worker’s income and social net income in material production departments in national income, because of the belief that only the labor in material production department could become the source of income and the labor of non-material production departments did not create value, while SNA included the incomes of both the material and non-material production departments into national income. It should also be mentioned that Wu Baosan, a late renowned Chinese economist, was an expert in the issue of “national income” in China who employed the SNA to study the issue of national income of old China before the liberation. After the foundation of the PRC, the theory and methodology about SNA was criticized in theory and abandoned in practical work. As a result, there were no conditions for Wu Baosan to continue his study. But the party who suffered true loss was the country because the adoption of MPS and the abandonment of SNA resulted in the overlooking of the development of non-material production departments in China. The consequence was that the development of the tertiary industry and, particularly, service industry in China lagged behind not only many developed countries but also some developing countries for a long period of time. This was a very hard and painful lesson.

Third, it was also necessary to mention the very serious consequence brought about by the wrong criticism of the New Population Theory of Ma Yinchu. If his articles and suggestions were not treated brutally, China would start carefully practicing population planning in the middle of the 1950s. At present, China’s population might be controlled at the level of about 900 million. And the pressures in population, employment, resource scarcity, and environment protection in China would ease greatly. China would have more economic accumulations and faster economic growth. As some said, the wrong criticism of a person caused several hundred million births and brought hardship to more than a billion people.

2 The More Than 30 Years After the Beginning of the Reform and Opening up and China's Socialist Market Economy

During 30 years from the beginning of the reform and opening up, China implemented the outlook of scientific development under the guidance of the Deng Xiaoping theory and the thought of "Three Represents" and advanced in the historic long March of exploring and building socialist market economy. The CPC Central Committee proposed the historical task of building socialist market economic system in 1992. The period from the proposal of the reform and opening up in 1979 to 1992 belonged to the stage of exploring market orientation of the economic system reform. The period from 1992 to the present belonged to the stage of building socialist market economic system. In both the exploration and construction periods of socialist market economy, western economics exerted important influence on the workers in economic theories and practical economic work in China and played an important referential role. In order to expound the issue, it was necessary to clarify what were the characteristics of socialist market economic system. Then people could further understand why there were the necessity and possibility to draw from western economics in the process of exploring and building socialist market economic system and how such practice of drawing from was carried out.

China's socialist market economy should be an important component of the socialist road with Chinese characteristics. What were its characteristics in comparison with the capitalist market economy in the world?

I. The Most Essential Characteristic of Socialist Market Economy: The Combination between Basic Socialist System and Market Economy

"People should combine basic socialist system with the development of market economy." This was proposed by Comrade Hu Jintao when he discussed the "Ten Major Combines" about the direction and road of the reform and opening up as a new great revolution in the report of the 17th CPC National Congress. Then what was "basic socialist system" as an economic system? It did not mean the absolute dominance of public ownership system any longer but was a "basic economic system in which public ownership system is the main part and multiple ownership system economies develop jointly". The question here was what the kernel part of such basic economic system of socialism was, how it could combine with market economy, and what the difficult point of the combination was.

The kernel part of such "basic economic system in which public ownership system is the main part and multiple ownership system economies develop jointly" was that "public ownership system is the main part". Without this kernel part, the basic economic system of socialism would not belong to socialism any longer. When there was only the combination between other non-public ownership system economies and market economy, it would become capitalist market economy. It was not difficult at all to combine non-public ownership system economics with market economy in economic system because market economy was always built on the foundation of

capitalist private ownership system in history. The biggest difficulty in combining basic economic system in socialism with market economy was the combination between its kernel part, namely public ownership system economy as the main part of economy, and market economy. In order to realize such combination, it was necessary to establish the always indispensable microeconomic foundation of market economy on the basis of public ownership economy. And this would be a historic and pioneering undertaking unprecedented in the time from the remote human history.

It was said in economics that the birth, growth and development of market economy was always merged in capitalist private ownership economy. The history of the theories of economics also showed that, although western economics and traditional Marxist political economics had opposite positions and different arguments, they had one thing in common: Both negated the possibility of the combination between market economy and socialist public ownership system. And both regarded this point as a “credo”. In 1930s, a major debate on socialism occurred in the circle of western economics and lasted for several years. Ludwig von Mises and Friedrich August von Hayek, main representatives in the circle of western economics who both became laureates of the Nobel Prize in economics later, asserted that only private enterprises could form the microeconomic foundation necessary for market economy and that it was impossible for socialist public ownership system to combine with market economy. People could only implement planned economy in such ownership system, which was a “road toward slavery”. On the other side, traditional Marxist political economics also asserted that market economy was inherent to capitalist private ownership system and it was completely incompatible with socialist public ownership system. It regarded market economy as “flood” and “monster”. In China, Comrade Deng Xiaoping took a broad and long-term view and liberated his thought. He summarized the experiences and lessons in the construction of socialism in China and abroad and resolutely decided to take the policy of reform and opening up. In the early 1990s, he proposed the basic line of building socialist market economy, with which he crushed the same fetters put on ideology from the left and right sides in traditional Marxism and western economics, namely the so-called “credo” that market economy was incompatible with socialist public ownership system. The CPC central leadership with Deng Xiaoping as the center led more than one billion Chinese people to make explorations on the lands of an ancient civilization, “crossing the river by feeling the stones”. They started the historic long March of combining socialist public ownership system with market economy, which was a great system innovation unprecedented in all the ages from the ancient times.

The biggest difficulty to establish socialist market economy was to maintain the kernel part of this basic economic system, namely taking public ownership system as the main part, and, at the same time, establish a microeconomic foundation indispensable for building market economy on the basis of public ownership system. How could it be like this?

Socialist countries were different from western countries. In western countries, enterprises were in private hands. The government only possessed the function of “public service” as a political entity. In China, the government was not just a political entity. It also performed the function of an economic entity with the entrustment of

the state and possessed a large group of state-owned enterprises. The enterprises under state ownership system, namely state-owned enterprises, were in fact under government ownership system. The government had the two identities and functions of “political entity” and “economic entity”. China learned such system from the former Soviet Union in the early period of the PRC after its foundation. The government implemented government ownership system in state-owned enterprises in the name of the state and such system dominated nationwide. The government exercised control not only over non-profit and non-competitive state-owned enterprises but also over profit-making and competitive industries that originally should be controlled by economic entities and operated according to the profit-making principle. In the end, economy became subordinate to politics. The profit-making principle or the cost-benefit principle was replaced by fiscal principles of “appropriation free of charge” and “payment free of charge”. Market mechanism and economic instruments were replaced by planning and administrative instruments. Everybody tried to take from the “big rice pot” of fiscal budget. Enterprises did not have independent operation activities and economic benefits and thus lost their economic dynamism. It was impossible to form the microeconomic foundation necessary for market economy with these enterprises. Whether the basic system of socialism could be combined with market economy mainly depended on whether the “microeconomic foundation” needed by market economy could be established on the basis of public ownership system. This was the “point of combination” of the basic economic system of socialism and market economy.

Under the guidance of Deng Xiaoping theory, the Chinese people found the “point of combination” in the practice of reform, namely building state-owned enterprises into independent producers and operators through state-owned enterprise reform, so as to form the “microeconomic foundation” of market economy on the basis of public ownership system. Besides, they also found a workable approach in their exploration, namely establishing “clearly-defined property rights, clearly-determined rights and obligations, separation of government function from enterprise management, and scientific management”. Later it was further specified that “shareholding system” should be a “form of realization” of public ownership system. And modern enterprise system could be established on the foundation of public ownership system according to such an idea so that the enterprises could possess the functions and mechanisms to realize “independent operation, assumption of sole responsibility for its own profit or loss, self-development and self-discipline”. Here, “clearly-defined property rights and separation of government function from enterprise management” were of crucial meaning. It not only directly concerned whether property rights could be clearly-defined but also concerned whether state-owned enterprises could truly enjoy the status of independent and autonomous operation and also whether the government could truly and completely transform from a government of “economic construction type” to one of “public service type”. As a result, the documents of the CPC took “separating administration from enterprise management, separating administration from state-owned property management, and separating administrative units from institution units” as a priority in economic reform within a long period of time. But in reality, there were still various obstructions although China made great efforts in

this area. For example, some competent economic departments in the government were changed into large state-owned group companies or controlling companies. The course of the reform indicated that the system origin of this economic work priority still laid in the situation that the government owned dual identities and functions. As people described, the disease was in enterprises but the source was in the government.⁶ The reform of the 17th CPC National Congress placed government system reform on a prominent position and stressed “building service-typed government”. This still needed people to make arduous efforts to fulfill.

II. The Second Characteristic of Socialist Market Economy in China Was That Its Establishment and Growth Went Through the Transition Period of China in Which Three Kinds of Transitions Interwove with Each Other

The establishment and development of capitalist market economy lasted several centuries in western countries. And these countries completed industrialization and urbanization over a century ago so that their capitalist market economy became mature and developed. China started to grow as a part of the world’s emerging market economy from the beginning of the reform and opening up over 30 years ago. The CPC central leadership centering round Deng Xiaoping pushed Chinese economy into a complicated and difficult transition period with the reform and opening up over 30 years ago. The concentrated manifestation of the complexity and difficulty of this “transition period” was that it consisted of three interweaving “transitions”. The first one was the transition from planned economy to market economy in economic system. The second one was the transition from “dual economy” to modernized economy in economic structure. And the third one was the transition from extensive growth to intensive growth in the mode of growth and, in particular, to the sustained and inclusive type of growth based on the outlook of scientific development. China had to achieve what western countries had spent several centuries to fulfill in the past. It would not be hard to imagine the great complexity and difficulty of this task. Take unemployment and employment as an example. Western developed countries completed industrialization and urbanization over one century ago. Rural population only accounted for 3–5% of their national population, national unemployment rate was about 5–8%, and they had good social security facilities. China started with “dual economy”, in which rural population accounted for over 60% of national population and 100–200 million rural residual labor population was in the status of disguised unemployment. In over 20 years in the past, 150 million migrant workers went into the cities from the countryside. Although they greatly promoted urban economic development, they also caused larger employment pressure in the city. Their employment sometimes was in an unstable status. This group of nearly 200 million migrant workers, which was in a number more than the population of many countries, was the largest disadvantaged group. The population group of migrant workers emerged with the start of transition and would disappear with the completion of transition. And it would be the main part of the population on the focus of “employment policy” within the several decades of transition. This huge population group was never seen in the

⁶See Huang (2005a).

history of western countries and western economics never studied it. In addition, state-owned and collective enterprises started to lay off workers as enterprise reform was pushed forward. According to the statistics from 1990 to 2002, the employed population in these two kinds of enterprises reduced by 56.1 million. In recent years, labor shortage occurred for some time in China's coastal areas. But this mostly was caused by the problem that low wages and high housing rent forced some workers to go to inland China or fall into disguised unemployment. Moreover, six to seven million college students graduated each year in China, which caused the employment difficulty of college graduates. In the end, the unemployment or employment issue that China faced during the transition period was far more serious than the western developed countries at present. Although China's urban registered unemployment rate was not high, the situation in reality was not negligible and the problem would become more discouraging within certain period in the future. The complicated situation in which three "transitions" interwove with each other caused China to develop with both sustained high growth and frequent high unemployment or low employment. Promoting employment would be a strategic policy during the transition period in China. Because of this policy, it was specifically proposed in the compendium of the "Twelfth Five Year Plan" that people needed to implement employment priority strategy. This was a strategy policy proposed with the reality in China as the start point.

III. The Government's Leading Role in Economic Development and Reform

As an emerging market economy, China belonged to "catch-up economy" just like other developing countries in East Asia, all of which were also emerging market economies. In his book *The Role of Government in East Asian Economic Development: Comparative Institutional Analysis*, famous Japanese economist Masahiko Aoki formulated that the government played an important leading role in the economic development of the developing countries in East Asia. In its research report *The East Asian Miracle* published in 1993, the World Bank attributed the high growth of East Asian economy to the flexibility and leadership of the economic policies of the government.⁷

The history of developed countries showed that the development from commodity market, monetary market, bond market, securities market and futures market lasted for more than 200 years. Each market, mechanism and system instrument did not emerge because of some ingenious design. Rather, it came from the agreements formed spontaneously and jointly performed by millions of people in economic practice on the basis of the needs in their activities as the market economy grew. As a developing country, China needed to complete within a shortage period of several decades what developed countries had finished within more than 200 years. And the developments in economic globalization did not allow China to first establish a relatively mature and standard market economy and then integrate with the world's economy. In order to achieve "catch-up", the government played a leading role at this point and led system innovation. Before the process of economic monetization was

⁷The World Bank (1993).

fully completed, China started to introduce securities, bonds and certificates. Before the systems for securities, bonds and certificates were fully grown and even before relevant laws and regulations for their operations were complete, the market of futures and derivatives emerged. All these almost appeared simultaneously within a short period of more than a decade or several decades. So these developments created such a situation that various market organization forms, mechanisms and system instruments were “immature” or “half mature” to different extents as China pushed forward its own economic development and got in line with the world’s economy. As the Chinese people see it, China should have everything in the market forms, mechanisms and system instruments of the mature market economy of developed countries. China should first introduce them and cultivate them in the practice of operation even though conditions were not ripe for the time being. This was like that a group of hungry people raced to eat half-cooked food before the cooking was finished. In the end, they had to eat and wait for the dishes to be cooked while the cooking was in process. As a result, the problems of incoordination, friction and disjunction often occurred to various market organization forms, mechanisms and system instruments, which constituted the inherent weakness of such “catch-up” economy. Such weakness was hard to avoid or even inevitable. It determined the necessity to carrying out coordination at various levels and in various aspects to address various areas with incoordination, friction and disjunction in the processes of the transition of Chinese economy and of the cultivation and growth of socialist market. As Comrade Hu Jintao pointed out in the report of the Seventeenth CPC National Congress, “the primary essence of the outlook of scientific development is development, its kernel is people-orientedness, its basic requirement is comprehensive coordination and sustainability, and its fundamental approach is overall planning and all-round consideration”.

The main characteristics of socialist market economy in the above and, particularly, the fundamental and intrinsic characteristic that public ownership system was the main part and multiple ownership system economies developed jointly, distinguished it from modern capitalist market economy. Modern capitalist market economy was built on the foundation of capitalist private ownership system and it experienced the development stage of *laissez-faire* capitalism of more than one century. But because of the basic contradiction between socialized production and capitalist private ownership, modern capitalist market economy was forced to combine with state intervention from 1930s to form state capitalism and establish modern developed and mature market economy. Modern western economics, both macroeconomics and microeconomics, took modern capitalist market economic system as the object of study. When compared, socialist and capitalist market economic systems were different in economic structure. The former took socialist public ownership system as the main part while the latter was built on the foundation of capitalist private ownership system. But the two were related as far as market economic system was concerned. The categories, principles, mechanisms and relevant rules, laws and regulations in them were the same or related. Therefore, it was both possible and necessary for China to borrow from the experiences and lessons of developed and mature western market economy and relevant economic theories in the

process of building socialist market economy. As a matter of fact, Chinese economists did endeavor to and actually borrowed many things useful to China from western economics during over 30 years from the beginning of the reform and opening up.

3 The Dissemination and Introduction of Western Economics in China Since the Reform and Opening up

The Third Plenary Session of the Eleventh CPC Central Committee held in December 1978 implemented the guideline of “liberating the thought, seeking truth from facts, and looking ahead in unity” proposed by Deng Xiaoping and played a role of enlightening the benighted. Chinese people started to rethink the future and destiny of the motherland. And the issue of distinguishing and understanding western economics once again also started to be put into their agenda.

The Third Plenary Session of the Eleventh CPC Central Committee made the clarion call for the “reform and opening up”. If people wanted to implement the principle of “taking economic construction as the central task”, then it was necessary to study objective economic principles with China’s economic conditions in reality as the start point and to borrow from foreign practical experiences and economic theories. Thus a question was raised naturally whether there were things in western economic system and western economics for the Chinese people to borrow and utilize? And was it right that people totally negated western economics with a “political baton” under the dominance of left-deviated thought and line in the past. Should people distinguish and understand western economics once again at present? The ideological line of “liberating the thought and seeking truth from facts” at the Third Plenary Session of the Eleventh CPC Central Committee changed the situation quietly like a drizzle in spring and prepared the ideological and political conditions for re-studying western economics and treat it scientifically. Thus the “Society of the Research of Foreign Economic Theories” was founded in response to the proper time and conditions. During May 1979, 17 scholars who studied western economics and history of economic theories led by Chen Daisun, a late professor of the Peking University, gathered in Hangzhou to discuss the issues on western economics. They felt deeply that people had to discard the practice of taking a left-deviated attitude of total negation toward western economics in the past. They also believed that there were things that Chinese people could borrow and utilize in it. And whether they wanted to “take” or “drop”, they had to study and understand it comprehensively and objectively.

The first activity after the foundation of the “Society of the Research of Foreign Economic Theories” was to hold lectures on foreign economic theories. At the time, the Society organized several dozens of teachers and researchers in this area and made relatively systematic and analytical introduction on different schools and views of the economics in western countries. The purpose of the activities was to promote the liberation of thought so that people could have a relatively systematic, general

and initial understanding on foreign economics and absorb useful things from it. These lectures on “foreign economics” started from 1980 and lasted for about one year. All the lecture notes were published in four books by the Chinese Academy of Social Sciences. Although the scholars who gave these lectures still had uncertainties in different degrees in the mind, caused by the left-deviated movements in the past several decades, all of them made great efforts in the new direction and achieved positive effects. These activities played an enlightening role to certain extent in China where western economics were blocked, confined and stifled for several decades. They were helpful for making ideological and theoretical preparations for the economic system reform in the future.

In early 1980s, the Society of the Research of Foreign Economic Theories started to disseminate and introduce the doctrines and theories of foreign economics for a very short period. Soon after the work of disseminating and introducing western economics fully unfolded, encouraged and driven by the policies of “reform and opening up” and “liberating thought and seeking truth from facts”. Such work mainly started and carried out through three aspects or three channels for over 30 years.

I. Courses in Higher Education

The extensive community of workers in practical and theoretical economic work seldom touched or learned western economics before the reform and opening up. And the undertakings in the reform and opening up required that people borrow from useful foreign theories and models. So in the early period of the reform and opening up, the mission of introducing western economics were basically put on the shoulders of some scholars who engaged in the study of western economics and history of economic theories in higher education institutions and a small number of research institutions. Although these scholars was put under very large political pressure and hurt by left-deviated line, they still resolutely assumed this important responsibility. The Society of the Research of Foreign Economic Theories organized and established the lectures on western economics and published four books. In addition to these efforts, a small number of textbooks of higher standard were published at the time, such as *Macroeconomics and Microeconomics* co-authored by Zhang Peigang and Li Yining and published by the People’s Publishing House in 1980, *Contemporary Western Economic Theories* co-authored by Liu Diyuan and Tan Congtai and published by Wuhan University Press in 1983, *Main Schools of Contemporary Capitalist Economics* co-authored by Hu Daiguang and Li Yining and published by The Commercial Press in 1982, and *A Criticism on Keynes’ Principle of Effective Demand and His Theory of Employment Multiplier* authored by Fan Hong and published by Sichuan People’s Publishing House in 1982. These works also included *A Review of Western Economic Thought Trend—On the Economics of Paul A. Samuelson* published by The Commercial Press in 1984, *Contemporary Western Economics Vol. I&II* edited by Song Chengxian and published by Fudan University Press in 1988, *Modern Economics* co-authored by Gao Hongye and Wu Yifeng, *Contemporary Western Economics Vol. I&II* co-authored by Luo Zhiru, Fan Jiayang, Li Yining and Hu Daiguang and published by Peking University Press in 1989,

New Western Economics edited by Wu Kuigang et al. and published by Shanghai People's Publishing House in 1989, and so on. Many higher education institutions also published some of textbooks of this kind successively. From early 1980s, such a group of senior scholars started to introduce western economics in China through these works and lectures and, at the same time, cultivated a large number of young students and youth economic workers. Although some people among these senior scholars still had the ideological imprint or influence of left deviation in their mind in different degrees, they opened up for a large number of outstanding students a window to look into another world and their work played an enlightening role.

It was particularly worth mentioning that many higher education institutions spontaneously and independently provided general courses introducing western economics in the first half of 1980s and the Ministry of Education permitted from the second half of 1980s that higher education institutions officially provided courses on the basic theories on macroeconomics, microeconomics and other courses of this kind, which belonged to western economics. At the same time, various specialized fields on finance and economics in higher education all used textbooks on the basic theories in western countries in their respective specialized areas. Such a practice was adopted not for the purpose of meeting the curiosity of young students but because of the fact that what's formulated in western economics were after all the structures, mechanisms and operational rules of a mature and developed market economy. When the students mastered such knowledge, they could better adapt to the demand of the development of China's socialist market economy and thus had more job opportunities.

II. Efforts of the Publishing Circle

The publishing circle also did a large amount of work in introducing western economics. The Commercial Press translated and published the representative works of classical economics in the West since 17th century before 1966. After the reform and opening up, it published a large number of important works on contemporary western economics, such as *Economics* written by Paul A. Samuelson and *Towards a Dynamic Economics* written by Roy Forbes Harrod. In the 1980s—the 1990s, China Renmin University Press, Peking University Press, Economic Science Press, China Social Sciences Press and Shanghai People's Publishing House organized, translated and published many important works on western economics, such as *The New Palgrave: A Dictionary of Economics*, a masterpiece of the laureates of Nobel Prize in economics, an economic science series including *Economics* written by Joseph E. Stiglitz and so on. From the beginning of the current century, the publishing circle spared no efforts in translating and publishing a large number of important works on western economics, such as *Macroeconomics* authored by Rudiger Dornbusch and published by China Renmin University Press in 2002, *A Handbook of Economics* including the representatives works in nine branches such as monetary economics and energy economics and published by Economic Science Press in 2002, *International Economics: Theory and Policy* authored by Paul R. Krugman and published by China Renmin University Press in 2002, *World Economic Primacy: 1500–1990*

authored by Charles P. Kindleberger and published by The Commercial Press in 2003, *The World Economy: A Millennial Perspective* authored by Angus Maddison and published by Peking University Press in 2003, *Economics* authored by Joseph E. Stiglitz and published by China Renmin University Press in 2005, *Principles of Economics* authored by N. Gregory Mankiw and published by Peking University Press in 2006, *The World Is Flat: A Brief History of the Twenty-First Century* authored by Thomas L. Friedman and published by The Oriental Press in 2006, and *The Rise and Decline of Nations: Economic Growth, Stagflation and Social Rigidities* authored by Mancur Olson and published by Shanghai People's Publishing House in 2007. It should also be mentioned that the important newspapers and magazines about economics in China, such as *Economic Research Journal*, *Comparative Studies*, *Social Economic System Comparison*, *Economist*, *Economic Perspectives*, *Economics News* and its director Gao Xiaoyong, and *The Economic Observer*, not only translated and introduced the papers of many famous foreign economists but also published a large amount of research results of many Chinese economists and, in particular, many middle-aged and young scholars achieved when they studied western economics and used it to analyze important economic issues in China. These publications reflected the basic situation in the study and application of western economics in China. And they also reflected, like a mirror, the situation that China's economic science developed constantly in the process of drawing from the research results of modern economics. In addition, it should be highlighted that the privately-run *Economics News* organized overseas special interviews with 12 American laureates of the Nobel Prize in economics and solicited their opinions and suggestions on the issues such as China's population and employment, inflation, enterprise reform, wealth gap and information highway. It published a book entitled *An Account of the Special Interviews with the Laureates of the Nobel Prize in Economics—On Chinese Economy and Economic Development* with the China Planning Publishing House in 1995. The book won high attention in the circle of academic study and exerted extensive influence in China. It should also be highlighted that the World Financial Crisis, triggered by the Subprime Mortgage Crisis in the USA in 2007, deeply exposed the absence of financial supervision in developed countries and, in particular, the USA. And the Obama administration was forced to improve financial supervision system and legislation with great determination. The US government started to formulate new financial supervision act from June 2009. In July 2010, the US Senate and House of Representatives ratified and President Obama signed the *Dodd-Frank Wall Street Reform and Consumer Protection Act* in a length of over 800 pages. As soon as the act was published in the USA, the China Financial Publishing House published its Chinese edition, translated by Dong Yuping and other experts, with a foreword written by Li Yang, vice president of the Chinese Academy of Social Sciences. As Li Yang said in this foreword, the act was "worthwhile for us to earnestly draw from in the reform of the financial supervisory system of our country".

III. Sending Abroad and Inviting Into China

During the 30 years from the beginning of the reform and opening up, China sent several hundred thousand young students abroad to study in western countries. And about 100,000 of them studied economics and finance. Besides, large groups of middle-aged and young teachers in the schools and departments of finance and economics in higher education institutions, workers in the study of economic theories, and workers in economic departments went abroad to pursue further education. It should be mentioned that the Chinese Economists Society cooperated respectively with The Commercial Press and the Shanghai People's Publishing House and published successively at the end of 1980s and in the beginning of 1990s two book series that systematically introduced western economic theories: *Frontier Special Research Topics of Modern Economics*, published by The Commercial Press in 1989, and *Market Economy Popular Reader Series*, published by Shanghai People's Publishing House in 1993. The purpose of publishing these book series was not to peddle "foreign things". The Society said in the foreword to *Frontier Special Research Topics in Modern Economics* that the purpose of publishing the book as a collection of papers was to help readers in China to "first understanding modern economics, then try to apply it to analyze Chinese economic issues, and thus find its function and weakness".⁸ Not only their scientific attitude but also their patriotic hearts are precious! Because they cared about the motherland while they lived in foreign countries. After they completed their educational programs, some of these people stayed and worked abroad but many returned to China and worked in higher education institutions, enterprises and government departments. In particular, more and more of them returned to China and participated in the construction work of the country in various areas from late 1990s. Although these people studied western economics abroad and some of them taught the same discipline in higher education institutions after they returned to China, the majority of them spontaneously and positively tried to understand and study the processes and issues in the development and reform of Chinese economy. Such a trend was advisable and gratifying. In particular, some people had the experience in practical work before they went abroad. After returning to China, they were in a better position to make contribution in theoretical and practical work, starting with the reality of Chinese economy and borrowing western economic theories and experiences. From the end of 1990s, there were already personnel who studied abroad and returned to China and played an important role or even assumed leadership positions in teaching, theoretical study and the work in government economic departments at various levels. It should be highlighted that the Peking University formed the China Center for Economic Research headed by Lin Yifu, now known as National School of Development at Peking University, in the 1990s. The center gathered a group of talents who studied abroad and returned to China and established regular communication relations with National Bureau of Economic Research (NBER). The research results attracted great attention from relevant departments.

⁸See Tang Min, Mao Yushi ed., *Frontier Special Research Topics on Modern Economics*, Book 1.

From the middle of 1980s, more and more famous economists in western countries, Japan, India and other countries were engaged or invited by higher education institutions to give lectures in China as communication were made between Chinese and foreign colleges and universities. When many organizations and even some government departments held international symposiums on important social economic issues, famous foreign economists and government officials were also invited to participate. The majority of Nobel Prize laureates came to China to give lectures and some of them, such as Robert A. Mundell, Joseph E. Stiglitz and Ronald H. Coase, came to lecture in China for a number of times. What these famous economists from western countries introduced and explained to the Chinese people was naturally the new research results that they achieved in the study of modern capitalist economy. The Chinese people should not expect or require these economists to tell them how to build socialist market economy because the construction of socialist market economy required themselves to explore and innovate in the practice of reform. But the study of the economists on market economic system and its operation principles was undoubtedly helpful for the Chinese people to promote the exploration and study on socialist market economy. It was worth mentioning that some famous western economists truly made great efforts to understand the complicated economic situations and questions that China faced and gave well-intentioned and beneficial suggestions. Here is one example. The Development Research Center of the State Council held the China Development Forum in March each year from the beginning of the 21st century and invited prestigious foreign economists and relevant Chinese experts, scholars and senior officials to make dialogues and exchanges on the hotspot issues and difficulties in China's economic development and reform. For example, during March 17–19, 2007, the forum invited renowned experts, including Dwight H. Perkins from the Harvard University, James C. Scott from the Yale University, Joseph E. Stiglitz, laureate of the Nobel Prize in economics, Martin Feldstein, former chairman of the Council of Economic Advisers of the US administration, Stephen Roach, chief economist at Morgan Stanley, and David Dollar, the World Bank's Country Director for China and Mongolia, to make exchanges with Chinese senior officials and scholars on important issues like China's mode of economics growth, distribution and consumption, energy, environment, sustained development, urban and rural medical care insurance, and new countryside construction. In the beginning of 2009, the China Center for International Economic Exchanges (CCIEE) headed by Zeng Peiyan was established and it held the first exchange meeting with important foreign think tanks. Beneficial communication was made on the current international financial crisis and the issues that confronted Chinese economy.

4 The Influence of Western Economics to China's Economic Study and Its Economy in Reality

I. The Influence to the Object of Study and Methodology of Economics in China

Traditional Chinese socialist political economics was the theoretical manifestation or reflection of socialist planned economy. On the one hand, as China advanced in the transition from planned economy to socialist market economy, it was increasingly required in practice that people change the theoretical economic theory in the Soviet model and discard traditional textbooks based on Soviet textbooks of political economics. It was also required that new systems of economic theories be created. On the other hand, Chinese economists increasingly realized in the practice of reform that, although western economics was a theory that served capitalist market economy, the Chinese people still could draw from the research results in it about various aspects such as the principles, mechanisms and operation of market economy. Thus, people closely related to the reality of economic reform and development under the guidance of the Deng Xiaoping theory in the study of economic theories in China and absorbed certain beneficial reference from western economics with proper analysis so as to constantly push forward theoretical study into deeper levels. At the same time, profound change started to occur and would continue to occur in the study of economic science in China, which mainly manifested itself in the following several aspects:

- (I). The Reflection on the Object of Study of Economics Widened the Scope and Content of Study of Economics and Ushered in the Transformation of the Methodology of the Study of Economics in China.

Traditional socialist political economics took traditional planned economy as its object of study. Such planned economy was in fact modern natural economy tied up with a planning network. The state provided the enterprises with investments free of charge. Their products were allocated and transferred by the state in a centralized manner. All the profits of these enterprises were turned into superior authorities. Everything in production, exchange and consumption was arranged according to national plans. The investment of the enterprises and their other main activities were all decided by competent government departments at various levels. In such case, the entire society was one big “enterprise” and the enterprises were nothing but “workshops”. There was no difference between macro-and microscopic economies. The entire social economy was nothing but a whole piece of mass. As a result, socialist political economics, which studied and reflected such socioeconomic form, became increasingly simplified and, in the end, it became a collection of several socialist economic principles and relevant policies, laws and decrees. Macro- and microscopic economics were absolutely not different as big or small ones or as the whole and the part. Both were categories of market economy and did not exist in planned economy. Thus it could not become a category in traditional socialist political economics.⁹

The undertaking of reform and opening up triggered the economic transition from socialist planned economy to socialist market economy. It required that economics adapt to the requirements in the transition and take socialist market economy as the object of study. Although the systems and mechanism of the market economy in China

⁹See Huang (1998a, b), Sect. 3, Chap. 1.

were still very immature and unstandardized and socialist market economy was very different from the market economy in western countries at present, there were still many things that China could borrow in western economics, which studied market economy. It was very natural that the differentiation between macro- and microscopic economics and relevant economic categories were introduced and borrowed by the circle of economics in China and used to promote the study of transition economy in China. All these caused great change to the picture of the study of economics in China and such development would advance toward greater breadth and depth in the future.

Moreover, the kernel of the discussion of all economic issues was “cost-benefit” analysis under market economic system. Profit motive and competition were the driving power of economic progress. It was the case in capitalist market economy and so was it in socialist market economy. All these should also be the categories in the economic study in China. But traditional political economics focused on productive relations in the study. Productive relations were originally closely related to economic interests. But traditional political economics only highlighted class antagonism when studying capitalist productive relations. And it discarded the issue of economic benefits when analyzing socialist productive relations and emphasized “letting politics take command” and “the consistency of the interests of the whole society”. Thus economic relations were turned into political relations and political analysis took the place of economic analysis. Now in order to adapt to the needs of the transition into socialist market economy, the economic study in China was committed to analyzing economic relations and the behavior and activity of the entities in market economy.

In addition, western economics started with market economy in the study and employed the method of cost-benefit analysis in the analysis on all economic issues. As a result, many branches of economics were formed, such as cameralistics, finance and trade and also consumption economics, population economics, environment economics, health economics, regional economics, public economics, service economics, and so on. The circle of economics in China drew from the development of multiple disciplines in western economics and broadened their view and research areas. They started with the situation in China and devoted themselves to establishing and developing various economic disciplines with Chinese characteristics. Thus the situation in the past was ended that traditional political economics not only commanded all economic disciplines but also dominated the discussions in economics. An active situation started to emerge in which a great many scholars worked with great vigor.

(II). The Policy of Reform and Opening Up Triggered the Transformation in the Research Methodology of Economics while Broadening the Research Horizon of Economics.

The methodology in economics could basically be divided into three levels. The first level was the most fundamental and abstract. It was the philosophical foundation, such as materialism or idealism or dialectics or metaphysics. The second level was the thinking method for theoretical study or construction of systems, such as logical

method or historical method or normative analysis or empirical analysis. And the third level was the technical methods in specific application, such as mathematical method, equilibrium analysis and case study. However, traditional socialist political economics was restricted too much to the method of normative analysis. It overlooked the method of empirical study and ignored the requirement of the development of socialized production for market economy in real life. It only observed the outside world, starting from its own "value judgment", rather than adapting its thought to the objective world. Rather, it required the outside world to adapt to its own value judgment. It was not accustomed to answering the question "what the world is" but focused on elaborating "what the world should be". It often overlooked the objectivity of the operation of economy in reality but emphasized how it should operate so that the conclusion of relevant research could not pass the test of experience. It should be said that such research method that overstressed normative analysis, which was persistently implemented in traditional socialist political economics, in fact betrayed the methodology in dialectic and historical materialisms. It was right because of such problem that Deng Xiaoping cried out that "practice is the sole criterion for testing truth" in the very beginning of the reform and opening up. The purpose of his call was to reunite the thought of the whole CPC onto the track of dialectic and historical materialisms and to prepare the ideological foundation for the great historic pioneering undertaking of the reform and opening up. The economists in China benefited from this great educational movement and rectified their thinking methodology. They endeavored to correctly combine the methods of normative and empirical analysis and historical and logical methods under the guidance of dialectic and historical materialisms. In this sense, the study of economics in China at present got rid of the dogmatic methodology in traditional political economics under the guidance of the Deng Xiaoping theory and thus realized the transformation in methodology.

Moreover, it also should be seen that some methodological issues, such as those related to empirical method and quantitative analysis method, in western economics also exerted beneficial influence on the study of economics in China. Here the neo-institutional school should be mentioned in particular. Why did the neo-institutional school of western economics attract the interest of the circle of economics and, in particular, middle-aged and young economists extensively? One of the main reasons for this was that the neo-institutional school was methodologically more accessible to Chinese scholars. For example, (1) The method of institutional analysis in either traditional institutional school or neo-institutional economic school emphasized the promotive role of system factors in social development. They opposed that the analysis of system be limited to abstract economic factors and stressed that non-economic factors, such as those of politics and society, also be included in the analysis. Non-economic systems consisted of formal restrictions, such as constitution, laws and regulations, and informal restrictions, such as ethics, customs and traditions. Neo-institutional school did not make the distinction between superstructure and economic foundation in the general body of the whole social system and also did not clearly identify the decisive role of economic foundation. But they did shift the driving power of social development from the subjective areas of the mankind to objective social existence. It had certain commonality with historical materialism in this point,

which made neo-institutional analytical method more acceptable to some Chinese economics. (2) Institutional analysis mostly studied systems and institutions from the angle of economic operation. The basic concepts, methods and instruments that it used was directly related to the operation of market economy. It incorporated systems and institutions into a neo-classical theoretical model. Namely, systems and institutions and, in particular, non-economic factors were regarded as the endogenous variables of the model for examining its influence to the economic behavior of the mankind. The theories and methods of the neo-institutional school, represented by Ronald H. Coase, Douglass C. North, Harold Demsetz, Armen Albert Alchian and Oliver E. Williamson, and, in particular, the neo-institutional property right theory, once became the focus of the introduction and study of western economics in China. For example, Zhang Jun's book *Modern Property Right Economics*, published by Shanghai People's Publishing House in 1994, was a treatise that contained relatively systematic study on property right theory. The institutional analysis on the operation of market economy in neo-institutional school was more sensible in comparison with traditional political economics and it was rather attractive to many Chinese economists and, in particular, middle-aged and young economists. For example, a considerable number of economists in China started to adopt the neo-institutional methods in western economics from the end of 1980s. They employed the method of combining transaction cost analysis, system endogenous analysis and neo-classical equilibrium analysis, to make in-depth study on the economics issues, such as the cost-benefit analysis of reform and the institutional arrangement of enterprise property right, in the transition process of China from planned economy to market economy. The research results in this area were of a huge number.

II. Chinese Scholars Selectively Absorbed and Borrowed the Theories in Western Economics and Studied In-Depth the Issues in China's Economic Reform and Development

The Third Plenary Session of the Eleventh CPC Central Committee made the clarion call of "reform and opening up". In order to implement the principle of "taking economic construction as the central task", the workers in economic theoretical study and practical economic work needed to start with the real situation of Chinese economy, adhere to socialist road and direction and, at the same time, break the fetters of planned economic system and relevant outlooks. They should explore the approaches to advance toward market economy and draw from foreign practical experiences and economic theories. The development of economic theories was closely associated and mutually promotive with economic development and the advancement of economic reform. It can be said that the Chinese economic theories developed during over 30 years of reform and opening up through both taking the situation in the country as the basis and selectively absorbing and borrowing foreign economic experiences and theories in the process of building socialist market economy.

In early 1980s when western economics was still mainly in the stage of being introduced in China, a small number of people already advocated drawing from particular principles in western economics to improve China's economic analysis and

economic systems at the time. As the introduction of western economics became more and more extensive and in-depth, more and more people drew from western economic theories to analyze the issues in China's economic reform and development. In 1992, China specifically declared that building socialist market economy be taken as the goal of economic development. From then on, the workers in the study of economic theories and those in practical economic work started with the actual situation in China in their work under a more clearly-defined goal. They carried out study and discussion more closely centering round the issues in economic development and reform. And as a result, they also drew from and referred to some mechanisms or system products in western economic theories and western market economy. The chapter intends to make a brief introduction on the two periods before and after 1992. Due to the limit of its length, only the important things during these periods were taken respectively as examples.

(I) From the Reform and Opening Up to 1992

This period was one of exploring the direction of reform. The Chinese people were exploring carefully whether they should “combine planning with market regulation” or further advance towards “market economy”. Many economists drew from some theories in western economics in the exploration about “market exploration”.

1. The Theory of “Buyer’s Market”

Buyer’s market and seller’s market were two conceptual counterparts. The former was associated with competition, consumer sovereignty and market mechanism while the latter with monopoly. According to the views in western economics, “consumer sovereignty” and “buyer’s market” was a status worth trying to realize while “monopoly” should be prevented or opposed. Planned economy was even regarded as the total monopoly implemented by the state. Hungarian economist Janos Kornai said that it generated “shortage economy”. In the very beginning of the reform and opening up, most economists in China advocated expanding commodity economy. In February 1979, Huang Fanzhang published an article in *Business Management Journal* and advocated establishing competition mechanism so as to realize consumer sovereignty, which was called “consumer power” at the time, in socialist economy.¹⁰ In October the next year, Liu Guoguang published an article and proposed the issue of building the “buyer’s market” of socialist economy.¹¹ In September 1983, he published an article in *Finance and Trade Economics* and proposed “discussing buyer’s market once again” from the angle of the purpose of social production.¹² He

¹⁰See Huang (1979).

¹¹See Liu (1980). In economics, “buyer’s market” was associated with competition and market mechanism. It indicated that market mechanism could allocate social resources according to the needs of the consumer. This was in fact a status worth trying to realize. In the middle of 1990s, Chinese economy once took a downturn and goods sold slowly on the market. Some people called such a situation “buyer’s market”. A few of them even published special discussions on major national newspapers and magazines. They seemed to turn the term into the synonym of “economic recession”. This was the misuse of the term “buyer’s market”.

¹²See Liu (1983).

said that the proposal of “buyer’s market” was both the discussion on the purpose of production and the continuation of the discussion of consumer rights. How could the market in China be turned into the market that truly served the consumer, listened to the consumer’s opinion, and gave the power of decision to the consumer? The article also specifically proposed a question from the angle of economic system reform and pointed out that the word “buyer” in the concept “buyer’s market” not just referred to individual consumers but also included the “consumer of production”. “It is a very important aspect in exercising enterprise autonomy that a producer makes selections in the investments of raw materials and other things.” Such “buyer’s market” could only be established through competition and could only be the product of market economy. In early 1980s, it was still impossible for people to have the idea of socialist market economy in their mind. So the opinion of building “buyer’s market” in socialist economy was in fact the expectation in the earlier time for the market economy under socialist system.

2. The Theories of Market Mechanism and Corporate Governance Structure

There were many works that drew from western economics to formulate the role of market mechanism. The representative ones among them were *On Competitive Market Mechanism* and *The Reform of Large- and Medium-Sized Enterprises: Establishing Modern Enterprise System*, both authored by Wu Jinglian and published by Tianjin People’s Publishing House respectively in 1991 and 1993.

In the book *On Competitive Market Mechanism*, Wu Jinglian analyzed and commented different models and theories proposed by Oscar Lange, Włodzimierz Brus and Ota Sik and specifically determined through such analysis and review that the kernel issue of economic system reform was the transformation of the basic means for distributing social resources, namely replacing planned management with market mechanism. He believed that market mechanism was irreplaceable and that people would not succeed even in simulating market mechanism with advanced computing technology like what Oscar Lange advocated because the main issue in resource allocation was not about calculation or information but about people’s economic interests. “Even though computer simulation could resolve the issue of information communication, it still could not regulate interest relations.”¹³ This showed that even the computer simulation of market mechanism would not work and the only choice was the market mechanism in reality. So the target model of China’s reform should be socialist commodity economy, namely socialist market economy. Hence, his theory played a promotive role for building socialist market economic system under the guidance of the Deng Xiaoping theory.

As to how to build socialist market economy, Wu Jinglian borrowed in the book the theory about administrative and economic decentralization, or market decentralization, proposed by American comparative economist Morris Bornstein, and advocated realizing the separation of administration from enterprise management in state-owned enterprises through economic decentralization. And in order to create the microscopic foundation for socialist market economy, he advocated introducing

¹³See Wu et al. (1991).

“company system” and “corporate governance structure” to help state-owned enterprises build modern enterprise system. He also drew from the theories on modern company system established by western scholars, such as Adolf A. Berle, Gardiner C. Means, Alfred D. Chandler, Jr. and Michael E. Porter, and, in particular, the theory on principal-agency relationship and promoted a series of suggestions on fulfilling the modernization reform of the management system of state-owned enterprises in China. These suggestions played a positive role. Moreover, he also proposed his objection on the “contracting system” that was popular in state-owned enterprises at the time and believed that “such contracting system in state-owned industrial enterprises might be the highest form of ‘insider-control’ in the process of the economic system transition in China”. Such contracting system was only a “transitional method” to give some autonomy to the enterprises under the condition that the separation of administration from enterprise management was yet to implement and competitive market was not formed. The radical solution still laid in establishing modern enterprise system.¹⁴ In the 1990s, Wu Jinglian called for many times for building “good” market economy and avoiding “bad” market economy. And he warned that people needed to guard against the emergence of “insider control” and “crony capitalism” and advocated “market economy under the rule of law”.¹⁵

Wu Jinglian was nicknamed “Market Wu” among the scholars. The nickname came from the colloquium on economic issues presided over by the comrades in central leadership and held at Zhongnanhai on July 5, 1990, in which Wu Jinglian participated. At the meeting, he spared no effort to advocate that market economy should be taken as the orientation of the reform. He negated the planning orientation and opposed the slogan of “combining planned economy with market regulation”. He believed that the issue at present was that “market-oriented reform was not resolute and thorough enough” and “commodity economy was market economy”. Because of this, Wu Jinglian was called “Market Wu”. At the time, “market orientation” was under question, the nickname was derogatory. But two years later, the central authorities adopted the resolution on building socialist market economic system and it became complimentary. The change from the meaning of the nickname from a derogatory one to a complimentary one reflected the difficult journey of China in the exploration for the direction of reform.

3. Property Right Theory

Chinese scholars wrote many works and papers to introduce and study western property right theory and there were many other works and papers that explored and applied such theory in association with the practice of economic reform in China. And “Modern Western Property Right Theory and Enterprise Behavior Analysis”, written by Liu Wei and Ping Xinqiao and published in the 1st issue of *Economic Research Journal* in 1989, was an excellent paper among them.

¹⁴Wu (1993).

¹⁵Wu (2007).

The paper emphatically introduced the property right theory of Ronald H. Coase and pointed out that this property right theory was built on the basis of the transaction cost theory proposed by the economist. Later, Coase took externalities into account and proposed the category of “social cost”. The set of views on property right proposed by Coase was summarized as the “Coase Theorem” by George Joseph Stigler. Although Coase himself did not make such summarization on the views in his theory, the theorem summarized by Stigler was widely accepted by the circle of academic study in the West. Liu Wei et al. related to the practice of China’s economic reform in the paper and formulated the important meanings of the property right theory to Chinese economic reform, which mainly included the following: First, “the property right theory emphasizes the position of enterprise property right in the entire process of economic operation. Such a view is helpful for us to understand the position of enterprise ownership system reform in the entire system reform.” Reasonable equilibrium price mechanism could only be the endpoint and result of clearly defining enterprise property right. Otherwise, it was impossible for an enterprise to have property and budget constraints. The result of opening up prices could only be divergent or non-convergent and prices could not rise in endless turns. Second, “property right theory emphasizes the importance of enterprise property right structure to the taking of risk responsibility. This is enlightening for us to understand the symmetry between right and responsibility in property relationship in the reform.” In modern company system, the board of directors had corporate ownership right, which was the equivalent to enterprise property right, shareholders possessed equity, which was ownership right, and managers had operation right. Under the condition of the separation of these three rights, “it is the most prominent defect of the separation of the two rights” to simply emphasize the separation of the two rights of ownership right and operation right and tend to weaken the restriction of ownership right on operation activities and not to restrict operation right with new property right. Third, “property right theory emphasizes the economic meaning of transaction cost. Such thought is helpful for us to understand the mutual relationships between the size of an enterprise and the efficiency of employing market mechanism.” It was not the case that the larger the size of a transaction participant was or the fewer the number of transaction participants were, the higher the efficiency became. Rather, people should find an equilibrium relationship between the two. Fourth, “property right theory emphasizes the necessity of the free transfer of property right. This is enlightening for us to understand the importance of socialist property right market.” In other words, people should permit the free transfer of property right and cultivate property right market so as to improve the effectiveness of resource allocation in the entire society.¹⁶

4. Disequilibrium Analysis

The so-called disequilibrium analysis was a kind of economic theory that developed after the publishing of *The General Theory of Employment, Interest and Money* written by John Maynard Keynes. It broke through the traditional Walrasian general

¹⁶See Liu and Ping (1989).

equilibrium theory and believed that Walrasian equilibrium took complete market and sensitive price mechanism as its conditions, which was just subjective conception. What existed in reality was often the situation that the market was not complete enough and price mechanism was not sensitive enough. A kind of equilibrium could still be achieved under such conditions of disequilibrium. The only problem was that the equilibrium achieved under such disequilibrium was often accompanied by unemployment and inflation. Disequilibrium analysis regarded Walrasian equilibrium as an exception. *Chinese Economy in Disequilibrium*, authored by Li Yining and published by The Economic Daily Press in China in the early 1990s, employed disequilibrium theory to analyze Chinese economy, which was in the process of transition towards socialist market economy at present.

Li Yining's analysis in the book on Chinese economy in disequilibrium at present mainly concentrated on the following several points: First, he divided disequilibrium into two types: The first type was associated with incomplete market. This concerned the problem that limited resources could not be distributed reasonably between various departments, industries and regions. The second type was associated with the lack of budget restriction in the enterprises so that resources could not be utilized effectively. People should endeavor to make economy to transform from the second type of disequilibrium to the first type and then to further narrow the degree of disequilibrium. Second, stagflation might occur under the condition of disequilibrium during the period of economic transition. Inflation might include the two types of explicit inflation and implicit inflation, in which price did not rise on the surface but there were goods to sell under such price. Stagnation might include the two types of explicit and implicit stagnation, in which actual effective supply did not increase or even decreased although certain growth rate was retained. So there were four types of combinations in stagflation. People needed to adopt relevant measures to prevent and regulate after distinguishing corresponding situations. Third, people needed to pay more attention to the role of structural imbalance in economic imbalance. The difficulty in this aspect was how to ensure the coordinated advancement of economic reform, economic growth and industrial structure adjustment. Fourth, there were various rigidities in disequilibrium economy, including enterprise rigidity as well as wage rigidity, employment rigidity and welfare rigidity. If people could not resolve the problem that state-owned enterprises did not have budget restriction or eliminate enterprise rigidity, Chinese economy could not get out of the second type of disequilibrium status. Various problems in the above all required that people pushed China toward socialist market economy through economic reform. And disequilibrium economy often caused economic reform and policy measures to become misshaped easily and made system innovation deformed. This problem was mainly related to incomplete market and unstandardized system innovation. All these required people to speed up pushing forward market-oriented economic reform.¹⁷ This book, in fact, also played a promotive role for building socialist market economic system.

5. Macroeconomic Theory

¹⁷See Li (1990), Foreword and the 10th chapter.

Many scholars in the circle of economics in China borrowed from western macroeconomic theories to analyze China's economic issues. The several mentioned in the above and their works almost all drew from macroeconomic theories in different degrees. However, there were only a few theoretical works (not textbooks on macroeconomics) that drew from macroeconomic theories and focused on the study of macroeconomic issues in China. *An Outline of the Theory of Macroscopic Economy under Public Ownership System*, authored by Fan Gang and Zhang Shuguang and published by SDX Joint Publishing Company in 1990, was one example of these several.

In this treatise, Fan Gang et al. made theoretical study on public ownership economy. The public ownership economy that it studied was a kind of theoretical abstraction rather than the economy of a certain country or a specific economic organization. And such theoretical model was based on practice. Namely, it was obtained mainly after proper summarization and abstraction were made on certain economic relations in reality in the socialist economy in China. It was generated also under the more extensive background of the economies of all socialist countries. The targets of such theory were some economic issues commonly confronted by these socialist countries. Such empirical study was not intended to tell people "what public ownership economy should be like" or "how people should act". Rather, "it truthfully explains what economic relations themselves are like in reality and how people act in reality". It started with the analysis on the "basic contradiction of public ownership system" and explained the way of act of various behavioral entities in macroscopic economy and the interest contradictions between them. It also analyzed theoretically the reasons why various kinds of macroeconomic phenomena and issues, such as inflation, excessive growth, shortage and economic fluctuation, occurred. In addition, it also proposed a series of new concepts, views and analytical methods. In summary, the work endeavored to employ the theories and methods in western macroeconomics under the guidance of Marxism and made exploratory theoretical study on macroscopic economy under socialist public ownership system. Such exploration was undoubtedly a kind of conducive attempt.

(II) From 1992 to the Present

The central authorities made the decision of "building socialist market economic system" according to the spirit of Deng Xiaoping's South Tour Speech in 1992 and pointed out that "building socialist market economic system was an unprecedented pioneering undertaking in which many very complicated issues needed to be resolved". The extensive community of the workers in theoretical study of economics and practical economic work in China made research and exploration in this pioneering undertaking and borrowed many useful things from western economics in this process. Here the author would like to mention a few of the important ones as examples.

1. The Adoption of the "System of National Accounting"

With the transition from planned economy to market economy and with the transformation from the direction control by means of administrative instructions to the macroscopic regulation in reliance to economic means, the technical methods in China's national economy management also experienced great change. Namely, the System of National Accounting, based on modern western economic theories and generally recommended by the UN to various countries in the world, was adopted to replace the System of Material Product Balances, based on traditional political economics and created by the former Soviet Union and adopted in China in the past. The difference between these two very different national economy accounting systems began with a key category, "national income". In the System of Material Product Balances, which was based on traditional socialist political economic theory, national income was only the income created by the workers in material production departments. In the System of National Accounts, which was based on modern economic theories, national income included the income created by not only material but also non-material production departments, such as service departments. It was exactly starting from the different definitions of the key category of national income that people designed two different sets of statistical index systems respectively and formed the MPS and SNA statistical systems used to manage national economy.

In 1992, the Chinese statistical departments promulgated the *Plan for Trial Implementation of the National Economy Accounting System in China*. From 1993, China officially abolished the MPS and adopted the basic accounting framework, principles and methods of the SNA so as to get in line with international practice. In order to adapt to the situation and development of the reform and opening up and the needs in macroscopic economic management, relevant departments established the accounting system of national economy in China on the basis of the SNA published by the UN in 1993 and with the national situation of China taken into consideration. They also designed and prepared table of gross domestic product and its use, input-output table, flow of fund table, balance sheet and balance of international payments and a set of revolving accounts of national economy.

It was worth mentioning that there were not many works publishing in China that studied the System of National Accounting and the issues related to China's GNP. The one with larger influence among them was *The Distribution and Use of China's GDP* authored by Guo Shuqing and Han Wenxiu and published by China Renmin University Press in 1991. The book adopted the national economy accounting method recommended by the United Nations and made field surveys about China's gross national product statistics from 1979 and its distribution and use structures. It analyzed relevant system reasons and policy background and proposed several suggestions on improving GNP distribution and use structures. It played a positive role in promoting the SNA in the practical work in China.

As foreign countries carried out the study on green GDP, Chinese scholars also carried out the study on building China's green national economy accounting system with the outlook of scientific development as guidance. *The Proceedings of the International Symposium on Building China's Green National Economy Accounting System*, edited by Pan Yue and Li Deshui and published by China Environmental Science Press in 2004, could be seen as a good beginning in the study in this area.

2. About the Labor Theory of Value and the Theory of Equilibrium Price

China built a reasonable distribution system under socialist market economic system and also established the system with distribution according to performance as the main part and the participation of various production factors such as labor, capital, technology and management in distribution according to their contribution. The system for China's national economy management changed from the System of Material Product Balances to the System of National Accounts. All these changes urgently required that people make new in-depth thinking about their theoretical cornerstone—the value theory. Obviously, the labor theory of value, which was taken as the standard in traditional socialist political economics, could no longer provide theoretical foundation for these changes. People needed to “liberate the thought” and “advance with the time” in their mind and understanding and the value theory needed to be developed. *The Social Labor Theory of Value*, authored by Qian Bohai, a late elder-generation Chinese economist, and published by China Economic Publishing House in 1997, “Solving the Puzzle of Total Value”, written by Gu Shutang and published on *China Business Times* on November 5, 2001, and *A New Theory of Wealth*, authored by Liu Shibai and published by SDX Joint Publishing Company in 2005, all believed that the traditional “labor theory of value” could no longer provide theoretical foundation for system innovation and that the theory of value needed to advance with the time in its development. These works drew from western economics in different degrees. But these scholars mostly stopped at the point of recognizing that the labor in service industry also belonged to “productive labor”. They did not recognize that the production factors other than labor were also the source of value. So their views could not provide a complete theoretical foundation for the reasonable distribution system under socialist market system.

It was worth mentioning that Yan Zhijie made further exploration and attempt in his works of “Price Determination and the Labor Theory of Value”, published in *Academic Monthly*, No.9, 1995, and *A New Exploration on the Labor Theory of Value*, published by Peking University Press in 2001. He proposed that labor was an important factor but not the only factor in the area of price determination and change. In addition to it, there was the action of various productive factors. So he proposed that the source of price was not one but many. In addition to labor, various other productive factors, such as capital, land, science and technology, and management, should all be the source of value. Besides, he believed that the situation proposed in the labor theory of value that commodity value was determined by the socially necessary labor time of commodity production applied in explaining simple commodity production or even the exchange relations under the condition of exchange in kind in earlier times. But with economic progress and the conversion of value into production price, the determination of production price also depended on whether the labor materialized in commodity met the demand of the society. So he drew from Marshall's equilibrium price theory and analyzed the question of price determination in modern economy from the two sides of supply and demand and made further explanation on relevant arguments of Karl Marx.

Of course, some people adhered to the labor theory of value and voiced disagreement on Yan Zhijie's new views. This indicated that workers in theoretical and practical economic work needed to make in-depth study on the value theory so as to adapt it to the needs in the development of socialist market economy.

3. About Shareholding System and Corporate Governance Structure

Early in the spring of 1980, Li Yining proposed the adoption of shareholding system to reform state-owned enterprises at a national labor and wage meeting. In 1989, Huang Fanzhang published the article *Shareholding System—A Good Form of Socialist Whole People Ownership System* and advocated adopting shareholding system to reform state-owned enterprises. First, people should use the separation of the two rights of ownership right and operation right in shareholding system to facilitate the separation of administration with enterprise management. Second, people could use the governance mechanism of shareholding system to build the macroscopic foundation required for building market economy on the basis of public ownership system. And third, people could ensure the foundation of public ownership system of state-owned enterprises through state controlling and, at the same time, absorb the funds in the society to strengthen state-owned enterprises. The conclusion was that shareholding system was a good form for maintaining and realizing socialist public ownership system. It can be said that people all explored and discussed how to reform state-owned enterprises so as to both maintain public ownership system and combine it with market economy in the 1980s. The discussion mainly concentrated on whether to adopt “contracting system” or “shareholding system”. But soon after, a political turbulence occurred and shareholding system met much challenge for some time.

In 1992, Deng Xiaoping proposed the historic mission of building socialist market economy. Soon after, the contracting system was abolished in the reform process. Many state-owned enterprises carried out the experiment and practice of shareholding system. Some influential scholars, such as Wu Jinglian, Gao Shangquan, Wang Jue and Qian Yingyi, some influential research institutions, such as the Development Research Center of the State Council, the China Institute for Reform and Development in Hainan, and the China Development Institute in Shenzhen, and some influential periodicals, such as *Comparative Economic and Social Systems*, *Economic Research Journal*, *China Industrial Economics* and *China Opening Journal*, made a large amount of research and published many research results on the shareholding system reform and corporate governance structure of the state-owned enterprises. It was exactly on the basis of the experiment and study of the shareholding system reform of the state-owned enterprises that the CPC Central Committee made in 2003 *The Decision on Several Issues on Improving Socialist Market Economic System* and specifically affirmed that people should “make shareholding system the main form of realization of public ownership system”. Where an enterprise needed to be controlled by state-owned capital, people might implement absolute or relative controlling by shareholding.

Shareholding system was originally born in capitalist market. It was an organization form of enterprise that emerged in adaptation to the development of socialized

production. Under shareholding system, general equity was only general property right. Only controlling stake represented enterprise property right. Private capital could exercise controlling by shareholding and so could state-owned capital. Therefore, shareholding system could be used by both capitalism and socialism. In the 1990s, people's understanding mainly focused on not regarding shareholding system as an equivalent to capitalism. But after the central authorities confirmed that people should "make shareholding system the main form of realization of public ownership system", some comrades went to the other extreme and saw shareholding system as an equivalent of public ownership system. They even believed that the shareholding enterprises in western countries were also publicly-owned enterprises. For example, Yi Lining held such a view in his article "On New Public Ownership Enterprises"¹⁸ and so did He Wei in his article "Shareholding System Was Social Ownership System".¹⁹ They quoted the position of late scholar Dong Fureng and advocated "calling public shareholding enterprises public ownership enterprises". Li Yining proposed the four forms of new public ownership system: first, new state ownership system after system transformation, second, publicly shareholding enterprises, third, publicly shareholding enterprises without state investment, and fourth, enterprises run by public interests funds. Among them, the term of so-called "publicly shareholding enterprise" only had ambiguous meaning because the companies listed on the stock market in China and abroad had millions of shareholders from the "public". He Wei specifically claimed that the shareholding systems under capitalist system could all be called "public ownership system". Wei Xinghua and Sun Yongmei published an article in *Beijing Daily* on April 14, 2005 to criticize the opinions above and pointed out that these scholars confused the forms of existence and realization of public ownership system. The author also disagreed with such a view and published three articles about it successively.²⁰ The author discussed with Prof. He Wei and pointed out that ownership system, either public or private ownership system, needed certain form of realization. People should not confuse ownership system itself with its form of realization. The centralization of capital and the dispersion of equity were the two sides of the same economic process. People should distinguish general equity from controlling stake. Only controlling shareholders were the main party in the centralization of capital and the actual disposer and controller of enterprise property right. Other shareholders were the object of the centralization of capital. The equity that they held was only general property right. Public or private ownership should be distinguished according to the holding of controlling stake. If controlling stake was confused with general equity, wrong arguments would definitely emerge from both the left- and right-deviated sides. On the one side, some people in the USA in the 1950s–1960s claimed that "everyone is a capitalist" on the pretext that many families owned stock securities. On the other side, people used the ambiguous

¹⁸Li (2004).

¹⁹He (2005).

²⁰The three articles on shareholding system written by Huang Fanzhang were published on *China Economic Times* on November 22, 2004, August 8, 2005 and January 9, 2006.

term of the so-called “public shareholding” and called all shareholding enterprises, including capitalist shareholding enterprises, as public ownership enterprises.

It should be pointed out that Karl Marx studied shareholding system in *On Capital* and pointed out that shareholding system was the “sublation of private property capital within the scope of capitalist mode”, which meant that the shareholding system concentrated medium- and small-sized capital for large capitalist to use but the enterprise was still within the range of capitalist mode of production. Western economists, such as Berle and Means, made profound study on shareholding enterprises and pointed out the separation of ownership right and operation right but they still regarded shareholding system and capitalist economy as one thing. The CPC drew from the experience of the shareholding system in the West but it used the system as the main form of realization of socialist public ownership system under the guidance of the Deng Xiaoping Theory and the important thought of the “Three Represents”. This was a unique innovation both in theory and in system.

4. About “Public Service-Oriented Government”

“Public service-oriented government” was originally a category of the market economy of western countries and western economics, which was used to define the status and role of the government in market economy. In capitalist market economy, private enterprise dominated absolutely. But there were indeed some non-excludable services and products that concerned public interests which no individual, enterprise or organization could or would supply. This required that a public service-oriented government provide such public products or services. In addition to macroscopic regulation and maintenance of market order, there were such public products and services as public health, education, infrastructure, public works, environment protection and social security that had to be provided or supported by the government. In order to build socialist market economy, China naturally and urgently needed to build a public service-oriented government. Undoubtedly, it was worthwhile for China to borrow from the West in this area.

From the late 1990s, the academic circle in China made increasingly louder calls for “public service-oriented government” and required that the government should adapt itself to the needs in the development of socialist market economy and the government should transform from traditional “economic development-oriented type” to “public service-oriented type”. Particularly, after the attack of the SARS epidemic in the beginning of the 21st century, the CPC and the government also paid more attention to the issue of the reform and transition of government system. Many scholars wrote articles to call for such transformation and many government departments and organizations also organize the study about this issue and held seminars about it. It was worth highlighting that China Institute for Reform and Development organized the study in this aspect vigorously and at an earlier time. The institute held a great event called “Building Public Service-Oriented Government—International Symposium on Government Reform in China during the Transition Period” in cooperation with the company of German Technical Cooperation in November

2003. It also had an important work *Building up a Public Service Oriented Government* published by the China Economic Publishing House in 2004, which included the article “Some Suggestions on Speeding up Building Public Service Oriented Government” that had 24 suggestions in it.

It was worth mentioning that the government did not pay adequate attention to perform its functions and duties in providing public products and services. In particular, the extensive community of rural residents enjoyed public products and services of poorer quality. In addition to this problem, there were also issues in compulsory education and basic medical care, which were originally public products and services that should be provided by the government. In certain period in the past, some people turned some hospitals and schools into profit-seeking organizations. They required or encouraged teachers and doctors to make profits for individual and organization. Thus, there was deviation in the direction of development. Liu Guoguang wrote many articles to call for not making everything marketized. People should not implement marketized operation with respect to public products and services that should be provided by the government, such as education and medical care.²¹ The CPC and the state attached great importance to this issue and made great efforts to correct deviation. The Seventeenth CPC National Congress already listed building “service-oriented government” as a key area of the reform in the future.

There were a great many articles and treatises about transforming economic construction-oriented government into public service-oriented government. But there was not much discussion about one issue, namely what the difficulty in the transition from economic construction-oriented government to public service-oriented government and its system origin were. The author proposed for many times in his writings that the radical cause laid in that the Chinese government possessed the dual identities and functions of a “political entity” and an “economic entity”.²² The government should perform the functions of “public service” as a “political entity”. In addition to this, it was also an economic entity that possessed a large group of state-owned enterprises. These state-owned enterprises were in fact those under the system of the ownership of the governments at various levels. This government system with dual identities and functions were learnt from the former Soviet Union in the early period of the PRC after its foundation. Such system was favorable to implementing planned economy. But when building socialist market economy, China was required to resolutely push forward the separation of administration from enterprise management. And the key was to separate the dual identities and functions of the government. In order to thoroughly achieve the separation of administration from enterprise management, the government should depart from its economic construction orientation and completely perform its public service-oriented functions and duties. China’s state-owned enterprises operated not only in profit-seeking and competitive industries but also in those important industries that concerned national interest and people’s livelihood, such as finance, civil aviation and communications. The government rather than state-owned enterprises should exit such industries and the state-owned

²¹See Liu (2009).

²²See Huang (2005b).

enterprises in them, as the media of the entities of state ownership economy, should be put under the jurisdiction of specific government organs at various levels, such as State-Owned Assets Supervision and Administration Commission. Until now, many scholars called for the transformation of the government into a public service-oriented one but they never mentioned how to determine the relationship of administrative subordination of state-owned enterprises. Although they proposed in a loud voice, their ideas were hard to put into practice. It should be said that the central authorities always regarded the “separation of administration from enterprise management” and the “separation of administration from economy” as the priorities in the reform and made great efforts in practice. But the separation only appeared to be achieved and there were many less noticeable connections left. Not long before, the Shanghai pension scandal and the chaotic situation in real estate market fully exposed the system origin of the problems of the “separation of administration from enterprise management” and the “separation of administration from economy”.²³ If people did not resolve the issue of the dual identities and functions of the government, it was impossible for the government to transform from an economic-oriented type into a public service-oriented type. Such issue needed to be resolved gradually through system innovation²⁴ in the government system reform.

5. About the Issue of Efficiency and Fairness

The issue of efficiency and fairness was an eternal theme in market economy and modern economics. Late American economist Arthur M. Okun published the book *Equality and Efficiency: The Big Tradeoff* in 1975, in which he highlighted this issue. Fairness included opportunity fairness, such as job opportunities, and result fairness, such as income fairness. But Okun emphasized opportunity fairness in his book. Most economists believed that efficiency was the business of enterprises while fairness meant that the government carried out distribution regulation through redistribution. As China transformed from planned economy to socialist market economy, it naturally faced the issue of efficiency and fairness. In particular, it was very necessary in the early period of the reform to place efficiency on a highlighted and prioritized position so that people could become clearly aware of market economy as the direction of reform in the mind and break through the force of habit of planned economy and the ideological resistance of equalitarianism.

“Prioritizing efficiency with due consideration to fairness” was proposed the earliest by Chinese economists Zhou Weimin and Lu Zhongyuan in a research report on social security system reform.²⁵ Because China built socialist market economy from a low start point and there were large gaps between the rich and the poor, between the city and the countryside, and between different regions, the sentence

²³See Huang (2007); “The System Origin of the Chaotic Situation in Real Estate Market and the Solution of Its Regulation and Control”, *China Opening Journal*, Issue 3, 2007.

²⁴See Huang (2006a).

²⁵Zhou and Lu (1986).

that “people should manifest the principle of prioritizing efficiency with due consideration to fairness” was written into the resolution about building socialist market economy at the Third Plenary Session of the 14th CPC Central Committee in 1993.

As China’s income and distribution gaps expanded in the 1990s, the central authorities proposed “prioritizing efficiency and paying due attention to fairness” and then further proposed “prioritizing efficiency and paying more attention to fairness” in its documents. Within the following period of time, the central authorities did not reaffirm this principle in its important documents. Some people misunderstood the situation and believed that the central authorities abandoned the principle. Some people even proposed “prioritizing fairness” or “taking fairness as the utmost goal”. But the author believed that “prioritizing efficiency is the lifeline of market economy” and successively published the articles of “defending for prioritizing efficiency” and “prioritizing efficiency and promoting fairness”.²⁶ Then Lou Jiwei published an article and proposed “prioritizing efficiency and attaching importance to fairness”.²⁷ Lou Jiwei and the author both believed that “prioritizing efficiency” was the basic requirement in market economy and paid great attention to the issue of “fairness” in China. But the author believed that people had to make the cake bigger through “prioritizing efficiency” so as to “promote fairness”. “Promoting fairness” should be the destination and goal of “prioritizing efficiency”.

The 17th CPC National Congress comprehensively examined the issue of efficiency and fairness in China and proposed “people should address well the issue of efficiency and fairness in both primary distribution and redistribution and pay more attention to fairness in redistribution”. It was also emphasized that “people should create conditions for more people among the mass to possess income from property”. This was a strategic measure for addressing well the issue of efficiency and fairness in primary distribution in practical work. Recently, the author published an article entitled “Make Income from Property Reach More People” and proposed that people should utilize shareholding and capital markets so that the extensive community of the mass could have income from property.²⁸ The reform of income distribution system in China both drew from the experiences and theories in western countries and highlighted more the Chinese characteristics in socialist market economy.

6. About the Outlook of Scientific Development

The kernel thought in the outlook of scientific development was proposed the earliest by Comrade Hu Jintao on July 28, 2003. The report of the 17th CPC National Congress in 2007 made complete formulation about the outlook of scientific development and proposed that its primary meaning was development, its kernel was people orientation, its basic requirement was comprehensive coordination and sustainability,

²⁶Huang (2006b); “People Should Scientifically and Historically Understand the Relationship between Efficiency and Fairness and Advocate ‘Prioritizing Efficiency and Improving Fairness’”, *China Reform Daily*, June 15, 2006; “The Issue of Efficiency and Fairness during the Transition Period in China”, *China Business and Market*, Issue 11, 2006.

²⁷See *Study Times*, June 19, 2006 for Lou Jiwei’s article.

²⁸Huang (2008).

and its fundamental method was overall planning and all-round consideration. The outlook of scientific development already became the fundamental guiding thought to guide China's economic and social development. The outlook of scientific development was the product of the combination of Marxism and China's practice in reform and opening up. It embodied and absorbed the advanced cultural fruits of the contemporary world. In particular, its important contents about coordinating man and nature, building ecological civilization, realizing economic sustainability and inclusive growth absorbed relevant research results in western economics.

Early in the 1950s–1960s, western scholars started to pay attention to the issues that concerned the sustained development of the mankind, such as natural resources and environment. In 1972, two American scholars published *Only One Earth* and led the study on the close relationship between the survival of the mankind and environment onto the direction of sustained development. In the same year, the Club of Rome published *Limits to Growth*, a research report written by Donella H. Meadows and Jorgen Randers, and specifically proposed the concepts of “sustained growth” and “reasonable, lasting and balanced development”. In 1987, the UN World Commission on Environment and Development published *Our Common Future* and officially proposed the concept of sustainable development. Later, western scholars expanded sustainable development into the coordinated unity between sustainable economy, sustainable ecology and sustainable society. The idea of “sustainable growth” was generally accepted by Chinese workers in theoretical and practical economic work very quickly. In fact, they increasingly felt that the issues in population, resources and environment caused huge pressure to the sustainability of economic growth in the high-speed growth of Chinese economy in several decades. Their research showed much consistence with the concerns of western scholars. For example, Fang Weizhong, a famous economist who had practical economic work experience for a long term, published in 2007 an important article entitled “2007 Was the Key to the Success of Five-Year Emission Reduction” in the influential magazine *China Policy Review*. He fully expounded the close relations between economic growth, energy conservation and environment protection on the basis of the reality in China and strongly indicated the urgency of energy conservation and emission reduction in China. He believed that it was unsustainable to pursue high-speed economic growth and advocated speeding up the transformation of the mode of growth and “putting the target on energy conservation and emission reduction in the first place and the target on GDP growth in the second place”. He believed that people needed to not only make laws on energy conservation and emission reduction but also enforce them strictly and never make concessions in this respect. There were already many treatises on saving resources and protecting environment. This indicated that the theory about the sustainability of economic growth already became won great public support.

The outlook of scientific development, which took “people orientation” as its kernel concept, not only emphasized coordinating the relationship between man and nature but also paid more attention to the relations among the people. It emphasized narrowing the gaps between the rich and the poor, between different regions, and between various groups of people. It intended to build “a harmonious society” through “letting a part of the people become rich first” and then “achieving common

prosperity” so that the people nationwide could fairly enjoy the fruits of economic development and reform. This was the “inclusive growth” proposed by the Asian Development Bank.

The concept of “inclusive growth” was proposed the earliest in 2007 by the Asian Development Bank. This concept was proposed mainly because of the fact that Chinese economy grew rapidly in years after its accession to the WTO, the gap between the poor and the rich enlarged, and the issues about resources and environment aggravated increasingly. The Asian Development Bank (ADB) organized and implemented in 2005 the study on the research topic of promoting social harmony with inclusive development. At the time, altogether eight scholars, including Tang Min, deputy representative of the ADB Representative Office in China, and Chinese scholars Lin Yifu and Fan Gang, participated in the study and published the book *Promoting Social Harmony with Inclusive Growth* in 2007. In the Chinese language, inclusive growth was also translated into a term literally meaning “shared growth”. Zhuang Jian, chief economist of the ADB Representative Office in China, indicated that the concept of “inclusive growth” was in fact consistent in meaning with the ideas of the “outlook of scientific development” and “harmonious society” proposed in China. It could also be regarded as a manifestation of these ideas. In his speech at the opening ceremony of the APEC Ministerial Meeting on Human Resources Development, which he attended on September 16, 2010, President Hu Jintao advocated that “inclusive economic growth brings the fruits of economic development to all the communities”. At the Fifth Plenary Session of the 17th CPC Central Committee held on October 16, 2010, General Secretary Hu Jintao advocated that “inclusive growth” would be included in the Twelfth Five Year Plan. It can be said that, although the ADB proposed the earliest the concept of “inclusive growth”, it bore the imprint of “Made in China” and was in fact the product of the communication, influence and borrowing between Chinese and western economic theories.

7. About Transforming the Mode of Economic Development

It was pointed out specifically in the suggestions on the Twelfth Five Year Plan adopted at the Fifth Plenary Session of the 17th CPC Central Committee that “taking speeding up the transformation of the mode of economic development is the only road to promote the outlook of scientific development. It conforms to new characteristics of China’s basic national situation and development stages”. In order to achieve such purpose, the document proposed five basic requirements: In speeding up the transformation of the mode of economic development, people should adhere to taking the strategic adjustment of economic structure as the main work direction. They should adhere to taking scientific and technological progress and innovation as the important support. They should adhere to taking guaranteeing and improving the people’s livelihood as the radical start point and endpoint. They should adhere to building resource-saving and environment-friendly society as the important force of strength. And they should adhere to taking the reform and opening up as the strong driving power. These requirements clearly pointed out the direction and approach of China’s economic work in the future.

History tells us that the transformation of the mode of economic development was the scientific reflection of the principle of economic development. No matter what the basic socioeconomic system was, the people under such a system all experienced or faced the issue of transforming the mode of economic development in the long process of economic development. In the process of economic development, people also underwent a process of understanding the issue of transforming the mode of economic development. Namely, there was a long process of changing from naturally following to consciously following the principle of economic development. The industrialization process lasted for several centuries in western countries. In the early stage, technological standard determined that people should start with labor and resource intensive industries and mainly relied on the investment of labor and natural resources to expand scale and increase production. After industrialization advanced to certain stage, the expansion of economic scale and economic aggregate would meet the bottleneck of resource supply. A more serious consequence was that it would cause excessive resource exploitation, environment damage, pollution and even climate warming. In the 1960s, the Club of Rome organized a group of scholars to make warning and reflection about the mode of economic development that western countries had followed and implemented in the past two centuries. From then on, environment and pollution issues became the ones to which the international community paid great attention. People summarized the road of economic development of western countries in the past two centuries as “polluting first and controlling and curing later”. But in fact, people had no understanding on the issues of pollution and climate warming over one century ago. The so-called road of “polluting first and controlling and curing later” was in fact the explanation given when people reflected on economic development after they made the painful and regrettable mistakes. This indicated that there was a processing of understanding in which people change from spontaneously forming development mode to consciously forming it. The problem was that the process lasted for two or three centuries and people had too many regrets about it.

China was a developing country and its industrialization fell behind western countries for one or two centuries. But China fully utilized its “latecomer advantage” and fully absorbed the experiences and lessons of advanced countries. Within a short period of several decades of its economic development, China fully understood the necessity and urgency of transforming the mode of economic development. But it could not follow the road of western countries in which people completely relied on market mechanism and enterprises spontaneously explored the transformation of the mode of economic development in the development process of one or two centuries. Rather, the China set transforming the mode of economic development as an established national policy under the guidance of scientific development. It fully utilized the leadership role of the government so as to bring into play the fundamental role of market mechanism in allocating social resources. In this way, it consciously pushed forward the transformation of the mode of economic growth. The extensive community of the workers in theoretical and practical economic work in China called for transforming the mode of economic development before the 17th CPC National Congress and wrote a great many of treatises in this area after the congress.

The one worth highlighting was *The Choices of China's Growth Model* authored by Wu Jinglian and published by Shanghai Far East Publishers in 2005. This was a masterpiece that examined the transformation of the mode of economic development in China from an international and historical perspective. He analyzed the successes and failures of the mode of economic development of developed western countries and the Soviet Union and their experiences and lessons and spared no effort to advocate that China speed up the transformation from extensive or extension growth to intensive or intension growth and change from simply relying on the investment of factors, such as labor, capital and natural resources, to relying on constantly improving the productivity of factors. The authors also quoted the views of Joseph E. Stiglitz, Amartya Sen and other scholars and distinguished economic development from economic growth. He believed that the view on economic growth that only stressed on GDP was "a kind of narrow-minded development outlook". Talent was the center of development. The radical purpose of development was to create more welfare for the people. As Amartya Sen said in his book *Development as Freedom*, its Chinese edition published by the China Renmin University Press in 2000, development could be seen as the process of expanding the true freedom that people enjoyed. These basic views were consistent with the basic view of "people orientation" in the outlook of scientific development that China proposed. The work of Wu Jinglian explored the choices of growth model for China under the guidance of such basic view. Although his view in which he opposed that there was a stage of heavy industrialization in the process of industrialization caused controversy in China, his discussion in which he spared no effort to advocate the necessity and urgency of speeding up the mode of development in the process of a new-type industrialization was very convincing. In particular, he believed that speeding up and improving the construction of socialist economic system was the inevitable requirement for truly transforming the mode of economic development. And the key point of all the key points depended on whether government reform would be successful.

Recently, Wei Xinghua published an article entitled "Several True or False Questions on Economic Development and the Transformation of Development Mode" in *Economic Weekly* on April 1, 2011. He formulated the relationship between the mode of economic growth and the mode of economic development and believed that the transformation of the mode of economic development had to take the transformation of the mode of economic growth as the premise. And the transformation of economic development included more contents. On the basis of the discussions on the development process of economic growth made by Karl Marx and western economist Michael E. Porter, he believed that "the transformation from extensive growth to intensive growth was the different stages of economic development that any country would undergo. This was not related to social and economic system or to planned economy or market economy."

It also should be mentioned that the China Institute for Reform and Development published the book *30 Renowned Economists Diagnosing China's Economic Development Mode* in 2010. In the book, the scholars expounded from different aspects that the traditional development mode in China in the past was "giving more weight to international market and less to domestic market, more to low cost advantage and

less to independent innovation, more to material investment and less to resources and environment, and more to wealth growth and less to improvement of social welfare standard". Such development mode was unsustainable and people had to speed up its transformation. They emphasized that "the forcing mechanism formed because of the international financial crisis provided a rare chance objectively for China to speed up the transformation of the mode of development". They spared no effort to advocate that people should seize the opportunity, take advantage of the trend, and push forward relevant work.

8. About Income from Property

The report of the 17th CPC National Congress proposed for the first time the concept of "income from property" and proposed that people should "create conditions for more people to have income from property".

The so-called income from property referred to the income obtained by urban and rural residents from owning movable properties, such as bank deposits and marketable securities, and immovable properties, such as house, vehicle, land and collectibles, in addition to the income of wages and salaries obtained through labor. Generally speaking, it included the income obtained through transferring property use rights, such as interests, rent and income from patent, and the income obtained through operating properties, such as dividends and property appreciation income. And "creating conditions for more people to have income from property" meant to create more ways for the extensive community of the working people to increase their wealth so that they could have multiple channels to obtain income through operating the properties that they owned in addition to the income of wages and salaries obtained through labor.

In the early 1960s, some American enterprises implemented Employee Stock Ownership Plan (ESOP) and issued minority stakes so that many American families owned a small amount of stock shares. Thus, the trend of "people's capitalism" rose in the USA, in which there was loud voice calling "everyone is a capitalist". At the time, the author wrote an article in the magazine *The Red Flag* (Issue 13) in 1962 and made criticism. The basic view was that capital centralization and equity dispersion were the two sides of the same economic process. The extensive community of shareholders was only the objects of capital centralization. Only controlling shareholders were the dominant party in capital centralization. Only controlling shareholders were the owners of the enterprises who had the rights of disposal and control of these enterprises. Ordinary shareholders were absolutely not capitalists. The author still advocated such basic view. But at the time, he wrongly held a negative attitude towards the ESOP under the influence of left-deviated thought trend. In the 1980s, the author studied, worked and made field research in the USA for four years and had the poisoning thought of left deviation cleaned up in his mind. After he returned to China in 1988, the first paper that he wrote was *Shareholding System Was a Good Form for Socialist Whole People Ownership System*. In the article, the author advocated reforming state-owned enterprises with shareholding system and also reflected and criticized his own attitude towards the ESOP. He now believed that it was a

supplementation to the income and benefits of enterprise employees. After the 17th CPC National Congress proposed that people should “let more groups in the people to own income from property”, the author immediately published the article “Make Income from Property Reach More People” in *China Reform Daily* on February 13, 2008. He proposed that people should mainly develop various factor markets and, in particular, capital market so as to create conditions for more groups of people to own income from property. People should not only encourage the enterprises to push forward ESOPs but also encourage various companies listed on the stock market to issue minority stakes. They should also bring into play the intermediary role of social security funds and, in particular, pension funds as institution investors. They should make personal accounts into actually effective ones and divided investment profits into these accounts so that the extensive community of enterprise employees could share the fruits of economic development.

It should be mentioned that Prof. Wang Jue edited in the middle of 1990s the book *He Who Works Has His Share*, published by the Guangxi Publishing House in 1993, and advocated that state-owned enterprises implemented ESOPs so that their employees could enjoy a share of capital gains in addition to wage and salary income. Xiao Jincheng and Wang Yanghong edited the book *A New Theory of Land Management* published by China Planning Publishing House in 2007. In the book, they proposed that the urban construction companies that implemented centralized requisition of the lands of the peasants in the suburbs in the process of urbanization should attract the peasants to participate in the companies’ projects through evaluating their land use rights in terms of money and converting them into the companies’ shares so that land-lost peasants could enjoy the income from land operation. In the article “Make Income from Property Reach More People” mentioned in the above, the author highlighted and recommended the views and positions of Wang Jue, Xiao Jincheng and Wang Yanghong.

In 2011, the author published the article “Pushing Forward the Reaching of Income from Property to the Public and Deepening the Reform of Income Distribution System” in the second issue of *Comparative Economic and Social Systems*. In the article, he further proposed that, when people promoted the industrialized operation of agriculture and urbanization construction, the companies that implemented the centralized requisition and operation of lands should better not adopt the measure of buying out land use right to acquire the lands of the extensive urban and rural disadvantaged groups, such as peasants, migrant workers and households relocated due to building demolition in urban development projects. Rather, they should adopt the method of the participation in the companies’ projects through evaluating their land use rights in terms of money and converting them into the companies’ shares so that the peasants, migrant workers and households relocated due to building demolition in urban development projects would not have the sense of loss caused by losing lands in their mind and, at the same time, enjoy the benefits brought about by land operation.

9. About Lewis Turning Point and Middle Income Trap

The Lewis turning point was proposed in 1968 by famous British economist Arthur Lewis. It was said in this theory that, when a developing country reached a certain stage in pushing forward the processes of industrialization and urbanization, the supply of rural surplus labor would turn from abundance to exhaustion, wages would rise increasingly, and population dividend tended to fade out. Such a turn was called the Lewis turning point. If the country did not transform the mode of economic development in this period, economy would go down or fall into long stagnation. According to the study of western scholars, when the per capita GDP of a country reached USD 4,000, it entered such critical period. If the country failed to respond properly, it would definitely fall into a so-called middle-income trap. It was reported that only Japan and the Four East Asian Tigers successfully got over such trap and rose to high income countries and many countries such as Latin American countries still stayed in the trap until now. China already developed into the second largest economy in the world and its per capita GDP reached USD 4,000 in 2010. *Business Week* in the USA published an article on June 10, 2010 saying that China's manufacturing industry reached the Lewis turning point. The article claimed on the basis of the situation that labor shortage emerged in some places in China that China's low wage advantage had disappeared and it was now moving toward the so-called "Lewis turning point". In fact, the issue already caused the attention of Chinese economists. Although Chinese scholars had slightly different understandings and estimations about this issue, they all believed that middle income trap was a serious challenge that China faced within 5–10 years in the future.

Ba Shusong published an article in *Economic Plaza* on May 6, 2001 and believed that China "already silently got over the Lewis turning point". But the situation "raised urgent demand on the transformation of the mode of economic development from a factor-driven one to a productivity-driven one". Li Jian'ge quoted his own survey on over 3,000 villages nationwide in the study on the issue of "labor recruitment difficulty" in coastal regions published at the website NETEASE.COM on July 31, 2010 and pointed out that "the population dividend in China's manufacturing industry is gradually disappearing. The Lewis turning point already arrives at an early time point." Cai Fang believed in his article published at Goodness' website on July 2, 2010 that "Chinese economy is arriving at the Lewis turning point. If people cannot find the method to respond to it, it will definitely face the middle-income trap." Many other scholars also emphasized the risk of middle-income trap. Hu An'gang published an article "Speeding up the Transformation of Development Mode and Getting over Middle Income Trap" in *Economic Information Daily* on July 1, 2011 and quoted Li Keqiang's speech published in *People's Daily* on November 15, 2010 entitled "Deeply Understanding the Theme and Main Line of the *Suggestions* and Promoting Comprehensive, Coordinated and Sustained Economic and Social Development": This period was "both an important stage in which China develops on a winding course from a middle income country to a moderately developed country and a critical stage in which it confronts increasing contradictions and advances along a bumpy road". Hu An'gang also made further analysis from the four angles of economy, society, politics and international affairs: In the area of economy, the stage was a period of the throes of economic transition in which the costs of various

factors was on the rise and potential growth rate dropped largely or even continued to be depressive. In the area of society, the gap between the rich and the poor expanded and social contradictions became prominent. In the area of politics, the period was a period of high probability of political risks. Many countries suffered frequent political turbulences in this period. In the international affairs, this period was one of the test of international pressure in which a country was confronted with strong external pressure or even intervention.

In an interview, Lin Yifu, chief economist of the World Bank, emphasized that China needed to address well the challenges in three aspects so as to avoid middle income trap. First, China needed to continue to promote technical innovation and industry upgrading and continue to retain its competitiveness in the process. Second, it needed to address well the issue of income distribution. Otherwise, it could easily cause social contradiction. Without a stable social and economic environment, it was impossible for China to achieve economic development. Third, China needed address well the relationship between economic growth and environment. He emphasized that, as long as China proceeded on the road that it took from the reform and opening up and addressed well the challenges in the above three aspects, “China can avoid middle income trap”. He also predicted that Chinese economy would retain quick and steady growth within about 20 years in the future.

It was worth highlighting that Song Li proposed from the domestic and international perspectives the two major challenges that China faced and also his strategic thoughts on them in his article “Getting over the Two Major Traps of ‘Surpassing the Second Place and Catching Up with the First Place in Economic Aggregate’ and ‘Upper Middle Income’” published on February 23–24, 2011. He suggested that, while China faced the middle-income trap, Chinese economy was developing into the second largest economy in the world and thus it encountered the trap period of “surpassing the second place and catching up with the first place in economic aggregate” at a very inconvenient moment. He indicated that history told us that both the Soviet Union and Japan failed to challenge the first place of the USA in terms of economic aggregate. And he believed that, as China faced the task of getting over the two traps of middle income and “surpassing the second place and catching up with the first place in economic aggregate” at the same time, it needed to pay more attention to various challenges that it faced when “surpassing the second place and catching up with the first place in economic aggregate” while it promoted industrial optimization and upgrading through technological innovation and implemented the economic transition from an economy driven by external demand to one driven by internal demand. He also believed that avoiding the catch-up trap that Japan experienced was the necessary prerequisite for getting over middle income trap. He made strategic proposals on getting over catch-up trap: First, people should not exaggerate and overestimate the standard of China’s economic aggregate. They needed to be clearly aware of the huge gap of China with other developed countries in terms of per capita standards. Second, they should pay great attention to improving international public relations and state image and promote winning the general support of the idea of harmonious world. And third, they should treat the USA and the western world with an attitude of cooperation rather than competition and of reconciliation

rather than liquidation. In addition, they should gradually reform the distortion to systems and policies caused by disequilibrium model over long time at the level of domestic system and strategy and make great efforts to build the driving power mechanism for long-term sustained development and its system guarantee.

It should also be highlighted that Liu Shijin published an article “Trap or High Wall” in the third issue of *Comparative Studies* in 2011. In this paper, he sorted and analyzed a large amount of historical data and classified relevant countries into five types on the basis of the order of economic takeoff, development strategy, economic system and development type and course. He believed that the radical reason why some countries fell into middle income trap laid in that there were serious defects in their basic industrialization framework so that industrialization process could not continue, high growth could not be retained, and “abnormal drop” occurred. But some other countries successfully got over middle-income trap and also “high walls” and entered the rank of high-income countries. At that moment, economic growth speed would drop inevitably but such drop was a kind of “natural drop”. He analyzed the mode and strategy of economic development of China and believed that China could successfully get over middle income trap. But there were some tough challenges for China to get over “high walls” and enter the rank of high-income countries. First, once growth speed lowered, the problem of low efficiency, which was covered up for a long time in the past, would be exposed and become prominent. And second, the expansion of market was limited under the current development mode. There were increasingly prominent issues such as insufficient market incentives for supply, slow accumulation of human capital, and inadequate channels for workers to participate in modernization. Therefore, he suggested that people should promote the transformation of development mode with “participation-promoted reform”.

III. Establishing the Economics with Chinese Characteristics—Socialist Market Economics and the So-Called “China Model”

In China, the historic process of creating the new system of socialist market economy required the Chinese people to establish their own transition economics and socialist market economics and provided sufficient possibility for them to achieve it. China established socialist market economy under the condition of concurrently carrying out three transitions. Compared with the developed capitalist market economies in the West, China’s transition economy and socialist market economy showed large difference and gap in terms of economic structure and market maturity. In the report of the 17th CPC National Congress, President Hu Jintao proposed that “the outlook of scientific development has been proposed through taking the basic national situation of the primary stage of socialism as the start point, summarizing China’s development practice, drawing from foreign development experience, and adapting to new development requirement.” In order to establish China’s transition economics and socialist market economy, it was important and necessary to draw from the practical experience of western countries and western economics. But what was more important was to take the basic national situation in China as the start point. It was impossible to find ready answers about the issues that China faced from western economics.

In the above, the author said that China borrowed many useful things from western economics. But borrowing was not equal to copying or replicating. The borrowed things could grow and yield results only when they were combined with China's national situation. In the 1990s, some people in the international community boasted about the so-called Washington Consensus proposed by John Williamson, research fellow of the Institute for International Economics in the USA, in 1989. These people peddled ideas filled with neoliberalism and preached privatization. Their views were completely incompatible with China's national situation. There were also international personages with good will who valued China's special road and experience. For example, Joshua Cooper Ramo, former editor of the *Time* magazine in the USA, established the Beijing Consensus in 2004. But he seemed not to have sufficient understanding on China's complicated national situations. Chinese people could and should not expect foreign masters to fulfil for them their own historical mission of establishing transition economics with Chinese characteristics and socialist market economics. The historic mission was put by the history onto the shoulders of the workers in theoretical and practical economic work in China. This was a mission that Chinese economists could and should not shirk.

Some famous Chinese economists, such as Xue Muqiao, Yu Guangyuan, Ma Hong, Liu Guoguang, Gao Shangquan, Dong Fureng, Liu Shibai and Gu Shutang, already called for establishing economics with Chinese characteristics. Some scholars were making efforts in this aspect. For example, the China Institute for Reform and Development, led by Gao Shangquan and Chi Fulin, committed themselves to the study on China's transition economy and proposed that the characteristics of China's transition economy were "market orientation and progressive mode". And in 1995, they published the book *Research Reports on China's Transition Economy* with the Reform Publishing House. Over a dozen of very insightful research reports were published on the theory of transition economy and relevant important economic issues in the book. For another example, Wu Jinglian, Zhou Xiaochuan and Rong Jingben published the book *The Road to A Market Economy: Comprehensive Framework and Working Proposals* with the Central Compilation and Translation Press in 1996. They carried out systematic research on the basic thought, general design and various reform supportive measures of China's transition from planned economy to socialist market economy. These research results positively pushed forward the study on transition economics and made fundamental preparations for establishing socialist market economy in the area of empirical study. Chen Dongqi and Li Maosheng wrote *On Socialist Market Economy* as an academic attempt, which was used as the textbook of the postgraduate students in the Chinese Academy of Social Sciences.

Some economists carried out more theorized exploration on transition economics and socialist market economics. For example, Zhang Shuguang, Sheng Hong, Fan Gang and Lin Yifu drew from neo-institutionalism and public choice theory, took transition process as an object of study in economics and the analysis of interest distribution as the lead in the study, and analyzed how different interest groups resolved their interest conflicts by means of public choice in the reform process. They took such interest conflicts as the cost of the transition process and carried out

cost-benefit analysis on transition process. They believed that progressive change would be a choice in which people would meet less resistance and paid less cost.

Dong Fureng and Wu Jinglian summarized socialist market economy at a higher and more abstract level. They used a simple formula to describe the essence of socialism: socialism = fairness + market economy or fairness + efficiency.²⁹ Obviously, this equation would become a main line always present in the socialist market economics that they designed. In his book *A New Theory of Economics*, Liu Guoguang explained socialist market economy as “a market system with macroscopic management and planned regulation”. In his eyes, the “socialism” in socialist market economy was embodied with “macroscopic management and planned regulation”. But in fact, modern market economy was already integrated with macroscopic regulation. The “socialism” in socialist market economy was mainly embodied with basic socialist economic system, namely “taking public ownership as the dominant one and achieving the joint development of multiple ownership economies”. In the long exploration of economic reform in China, people once proposed in the 1980s the conception of “combining planned regulation with market regulation”. In 1992, Deng Xiaoping proposed the target model of “socialist market economy”, which represented a large step forward from various explorations in the past. It emphasized that market mechanism should be taken as the fundamental instrument of the distribution and redistribution of social resources under basic socialist economic system.

For many years, the author advocated the study of socialist market economics and proposed another formula: Socialist Market Economy = Public Ownership Dominance + Market Economy. With the practice in reform for several dozens of years, the Chinese people achieved new development in their understanding on the basic economic system of socialism: It was not built solely on the foundation of completely dominating public ownership economy but would be built on the economic foundation of taking public ownership as the dominant one and achieving the joint development of multiple ownership economies. And taking public ownership as the dominant one was the kernel part of the basic economic system of socialism. The biggest difficulty in theory and in practice was the combination between this kernel part and market economy. Moreover, what was more important was that the maturity and development of socialist market economy would drive the successive establishment and quick growth of various social security funds controlled by the state, such as pension fund, medical care insurance fund and unemployment insurance fund, and also the constant emergence of various other public funds, such as investment fund, children welfare fund, disabled people fund, college fund and scientific research fund. These funds would become increasingly important institutional investors and also the main investors of more and more state-owned enterprises. This would create another form of realization of public ownership system—“fund ownership system” or “society ownership system”. This would be a form of public ownership system more complete than the current state ownership system or government ownership system because it provided the public with a new mechanism—“investor sovereignty”. The

²⁹*Economic Information Daily*, August 5, 1997.

above view was once called “financial socialism” or “fund socialism” by overseas scholars. The evolution of China’s state ownership system would generally follow the order of the following stages during the period of economic transition: state ownership system → state controlling system → fund ownership system or society ownership system. What was particularly important was that, as the author wrote a number of articles to elaborate, people could further realize the separation of administration from enterprise management with the public funds controlled by the state and the “fund ownership system”, with which these funds controlled and managed state-owned enterprises so that the government could thoroughly realize the transformation from an economic construction-oriented one to a service-oriented one.³⁰

In recent years, there was a great hype about the “China Model” in China and abroad. This was because China’s high-speed growth over 30 years shocked the world and people all explored and discussed the radical reasons of China’s success. Yu Keping and Dong Ping edited and published the book *China Model and the Beijing Consensus* in 2006. Pan Wei edited and published the book *China Model* in 2008. Hong Kong scholar Ding Xueliang published *Debating the Chinese Model* in January 2011. There were also a great multitude of articles discussing China model and most of them explored the reasons of China’s economic success from different aspects. But the author paid more attention to the opinions that held a negative or prudent attitude toward the formulation of China model. One type of such opinions believed that there was no “China Model” at all. For example, Prof. Chen Zhiwu, who taught abroad for a long period of time, published the book *Chen Zhiwu Talking about Chinese Economy* in 2010. He believed that China’s success eventually was determined by “the freedom of the people, private property right and market economy and the rule of law. This is a model common to the mankind. It is not some China model.” In his eyes, China did not have any choice other than taking the road of western capitalist market economy. The other type showed a prudent attitude toward the formulation of “China Model”. For example, Zhao Qizheng, former director of the State Council Information Office, and John Naisbitt and Doris Naisbitt coauthored and published the book *The China Model: A Dialogue between East and West* in 2010, in which he specifically disagreed with the boasting about the China model. He believed that, although China succeeded in realizing high-speed economic growth over a long period of time at present, there were still serious issues of embezzlement, corruption, environment pollution and polarization of wealth. It was still too early to talk about the China model. Zi Zhongyun published an article entitled “People Should Better Find the China Road rather than Boasting the China Model” in the fifth issue of *Internal References on Reform* in 2011. In the paper, he pointed out that

³⁰See Huang (2002); “Socialism with Chinese Characteristics—The Combination of Public Ownership System and Market Economy (Public Ownership System + Market Economy)”, *Economist*, Issue 5, 1998; “Shareholding System—A Good Form of Socialist Whole People Ownership System”, *Economic Research Journal*, Issue 4, 1989; Robert (1991); Huang (2000); “The Separation of Administration from Enterprise Management: Government System Reform under Socialist Economic System”, in *China Economic and Social Development Report in the Five Years in the Future*, CPC Party History Press, 2006; “Establishing Transition Economics with Chinese Characteristics and Socialist Market Economics”, *Economic Perspectives*, March 2009.

“foreign people only pay more attention to China’s current economic aggregate and competitiveness. They do not truly care about the wellbeing of all the Chinese people and they have never felt the problems and pains of the Chinese public. ... As Chinese citizens, should we become self-content and complacent about the praise about China model from foreign people?” The author himself agreed very much with the prudent attitude in the second type. As he explained in the above, the system and theory of socialist market economy with Chinese characteristics were still in its infancy. The problem of “mixing up the functions of government and enterprise”, in which the government possessed dual identities and functions of economic entity and political entity, was the system origin of planned economy in the past. And now it became a system hotbed for power-for-money deal, embezzlement and corruption. All these needed to be resolved through government system reform. The outcome of this reform would determine the outcome of the institutional and theoretical innovations in “socialist market economy with Chinese characteristics”.

IV. Responding to the World Financial Crisis on the Basis of the Characteristics of Chinese Economy

(I) Clearly Understanding the Nature of the World Financial Crisis and the Characteristics of Chinese Economy and Endeavoring to Make China Embark on the Road of Recovery First

Most Chinese economists believed that the financial crisis this time was in fact the crisis of virtual economy. It was caused by the excessive spreading of virtual economy in the USA and European countries. In China, real economy still dominated. So, it was not proper for people to assert carelessly that China was also in the crisis. What China suffered was only the slowdown of growth speed. The growth rate was still positive rather than negative. China did not take the direct attack from the financial crisis in the USA and European countries while the crisis directly caused another crisis in the real economy in these countries. This seriously affected China’s import and export. Therefore, Wu Jinglian believed that the financial tsunami overseas aggravated the economic difficulty in China.

Taking the basic national situation in China, namely the primary stage of socialism and socialist market economy, as the start point of their discussion, some Chinese scholars further believed that, as long as China responded properly, Chinese economy would recover first. For example, Zuo Xiaolei proposed in the article published in *China Securities Journal* on February 2, 2009 that “there are three major factors that support Chinese economy to recover first”. These factors were that China’s real economy had solid and steady basic advantages. China had substantial financial strength. It also had stable and reliable financial system and took smaller impact from international financial crisis. Huang Fanzhang published the article “Reviewing the Tendency of Chinese Economy with a Prudent but Optimistic Attitude” in *China Economic Times* on March 7, 2009. There were five reasons to such attitude. First, real economy dominated in China. Virtual economy was of smaller scale. And the opening up to the outside world in financial area was carried out at a steady pace. Second, most of China’s exports were the basic life supplies necessary to the residents in developed

countries. The tendency of dropping export volume would soon be contained or turned around. Third, there was huge potential in China's internal demand. Spurring up internal demand would become the main point of strength in responding to crisis. Fourth, China had huge domestic reserves and USD two trillion foreign exchange reserves, so it could adopt the strategy of "purchasing externally and promoting internally". And fifth, China faced the great opportunity to adjust industrial structure and implement the industrial gradient transfer from coastal regions to inland regions and thus develop inland economies. On July 31, 2009, Lin Yifu, deputy president of the World Bank, indicated to the reporter of the *Global Times* that China had huge financial potential and foreign exchange reserves and could get out of economic recession first. And he predicted that China's GDP growth that year would reach 7–8%.

(II) Drawing from the Framework of Macroscopic Regulation in the West on the Basis of China's National Situation and Proposing and Implementing a Series of Measures in Response

Facing the menacing international financial storm, the central authorities made resolute decisions and timely adopted proactive fiscal policies and moderately easy monetary policies. They also kept enriching, consolidating and improving the package plans for guaranteeing growth, expanding domestic demand, adjusting structure and benefiting the people's livelihood. These measures mainly included the following: The central authorities implemented the plans for the four trillion yuan investment program, structural tax reduction, home appliances going to the countryside and moderate adjustment of export tax rates. In addition, they also implemented ten major industrial adjustment and rejuvenation plans and the policies to develop high technology industrial clusters and enhance enterprise technological transformation. They also stabilized and developed agriculture and promoted the increase of the income of peasants. They formulated and implemented the policies to stabilize and expand employment policy and the measures to raise the retirement allowance and pension of retired cadres and employees and raise the standard of subsistence allowances and minimum wage. Obvious effects were achieved in the first half of 2010 in the implementation of such package plans.

Chinese scholars also drew from western theories and practices and proposed some meaningful views. For example, some scholars, such as Li Yiping, considered that the USA once was obsessed with the expansionary policy in Keynesianism so that stagflation occurred in the 1970s and warned that Chinese people should pay attention to preventing such Keynesianism dependence. Li's article was published in *China Economic Times* on July 14, 2009. Some scholars, such as Song Li and Wang Yuan, proposed that "it is necessary to make structural fine tuning to monetary policy" so that people could prevent asset bubble while expanding credit so as to promote the independent growth of economy. Song and Wang's article was published in *China Economic Times* on July 28, 2009.

After the World Financial Crisis passed, American economy was still in recession, unemployment rate stayed at a high level, and the so-called expansionary “quantitative easing monetary policy” implemented by the Federal Reserve caused huge inflation pressure to emerging economies including China. China’s CPI index exceeded 5% and 6% respectively in May and June 2011. Many workers in theoretical and practical economic work in China drew from the disinflation experiences and theories in western economics to make suggestions and proposals. For example, Wei Jianing pointed out in his article “China Faces Three Risks in Its Current Economic Tendency” published in *China Economic Times* on July 11, 2011 that there were three kinds of risks: The first one was stagflation risk. The second was hard landing risk. And the third was the risk of making the bubble bigger because people might worry about stagflation and ease monetary policy once again. Because of these risks, he advocated that China should draw from the policy of “monetarism” + “supply-side school” that the Reagan Administration had implemented in the USA in the past. The so-called “monetarism” policy mainly referred to raising interest rate and controlling currency and the so-called “supply-side school” policy mainly referred to lowering tax rate and invigorating enterprises.

(III) Positively Participating in the International Cooperation on Macroeconomic Policy and the Reform of International Monetary System

Before 1970s, western countries mostly followed Keynesian methods in macroeconomic regulation so that their economies avoided crises like the Great Depression in 1930s. Later, crisis or risk transmission mechanisms were also globalized as economic globalization process was quickly pushed forward. Under such circumstance, not a single country could keep its economy clear of a crisis, the only choice was to make international cooperation on macroeconomic policies across the borders. In the past, the author published articles for a number of times to formulate such international cooperation.³¹ And such international cooperation could be bilateral, regional or global in its size and be gradually pushed forward and enhanced from a primary level to an advanced level in its form. The countries could start with dialogue and information communication to increase the transparency of each other’s systems, policies and legislations. Then they could carry out policy consultation and policy coordination and then reach agreements or take joint actions. China positively participated in and carried out the international cooperation on macroeconomic policy. There were bilateral cooperation, such as the Sino-US Economic Cooperation Dialogue Mechanism, regional cooperation, such as China-ASEAN Finance Ministers and Central Bank Governors Meeting, and global cooperation, such as the participation in the G20 Finance Ministers and Central Bank Governors Meetings in Washington and London.

In the recent several years, the author further realized that such form of macroeconomic policy cooperation was not just a kind of meeting but a new mechanism

³¹See Huang (1998c); “Financial Globalization Needs International Cooperation on Macroeconomic Policy”, *China Economic Times*, June 29, 2002, “Economic Globalization Needs International Cooperation on Macroeconomic Policy”, *Macroeconomics*, July 2009.

required by economic globalization. In 2011, the heads of the state of the USA and China signed the Sino-US Joint Communiqué and called such meeting “macro-economic policy cooperation” for the first time. And it was written into an official document as a new mechanism. In recent years, the author also further proposed in his articles that, while the macroeconomic policy cooperation of the G7 was the breakthrough of old world economic order, the macroeconomic policy cooperation of the G20 meant the “incubation” and “embryo” of new world economic order.³²

Finally, it should be mentioned that China’s undertakings in building socialist economy were not completed at one go during over 30 years of the process of the reform and opening up. It was not a smooth journey, either. Rather, it was a profound revolution. Some people advocated taking the road of western market economy, implementing privatization and comprehensively practicing the withdrawal of state-owned enterprises and the entry of private enterprises. Some people even felt reluctant to drop traditional theories and planned economy. Therefore, in over 30 years in the past, three major debates on reform occurred. The first one occurred from 1980 to 1984. The second occurred from 1989 to 1992. And the third occurred from 2000 to the time before the 17th CPC National Congress in 2007. The first two debates centered round the themes of “planning and market” and “being capitalist or socialist in nature”. The third one was caused by some doubts or negations on prioritizing efficiency and the direction of market economy, which was triggered by the enlarging of the gap of wealth in the society. The indignation about “unfairness” was understandable. But turning back was absolutely not a way-out. In addition, people needed to pay attention to another potential danger or threat. It was the problem that the issue of the mixing up of administration with enterprise management and economic functions was yet to resolve in China’s state-owned enterprise reform. This problem left room for the collusion between government and businessmen so that it was difficult to control the emergence of corruption. The vested interests or crony capitalists were once the supporters of reform in the early period of the reform. Now the vested interests would be damaged when people needed to realize the thorough separation of administration from enterprise management and economic functions. These vested interests were once the driving power of reform but now they might become the resistance to further pushing forward and improving reform. All the issues above could only be resolved through further pushing forward reform and, in particular, through relying on resolutely pushing forward thorough government system reform. Such reform would determine the final outcome of China’s development. The Chinese people should hold high the great banner of socialism with Chinese characteristics, practically implement the outlook of scientific development under the guidance of the Deng Xiaoping theory and the important thought of the Three Represents, and continue to push forward the construction of socialist market economy.

In summary, the construction of socialist market economy in China was the unprecedented institutional and theoretical innovation carried out by the Chinese people through liberating the thought, advancing with the time, and breaking through

³²See Huang (2009); “Examining the Important Meaning of Macroeconomic Policy Cooperation from Sino-US Joint Communiqué”, *Economic Perspectives*, Issue 4, 2011.

the dogmatism of traditional Marxism and western economics under the great banner of socialism with Chinese characteristics. The author believed that, when China completed its triple transitions after several decades and also the moment when it completed the construction of socialist market economy, a brilliant banner would be flying high on the ancient lands of China on the horizon of the world's east end, with "socialist market economy and socialism with Chinese characteristics" written on it. China would write new magnificent chapters into the world's thesaurus of economics with transition economics with Chinese characteristics and socialist market economics.

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