

Chapter 4

China's Opening-Up: Idea, Process and Logic



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Abstract China's opening up since 1978 has been a historical process of continuous expansion and deepening. In the course of this process, Chinese policymakers and the mass of the people have gradually deepened their understanding of reform and opening up, and China's relations with the world, especially its role in the world, have been constantly adjusted. At the beginning of reform and opening-up, China adapted to and was integrated into the international economic system; it then became engaged in the participation and improvement of that system, and then became an advocate and leader in the reform of the international system. Moreover, in practice, an incremental series of coherent open economic policies and theories with Chinese characteristics that facilitate an open economy have come into being. Under the guidance of Deng Xiaoping Theory of reform and opening up, China's practice of opening up to the outside world is not only a good fit with China's traditional trade theory, the *Huainanzi*/Sima Qian Theorem, from which people benefit by exchanging their surplus goods for those that they lack, but also is explicable in terms of modern economic trade theories. With the entry of socialism with Chinese characteristics into the new era and profound changes in the international environment, China still needs to open further to lead and promote mutual and shared openness for all countries in the world, so as to create good international conditions for promoting the construction of a shared future for mankind and building a world of lasting peace, universal security, common prosperity, openness, inclusiveness, cleanliness and beauty.

Keywords Opening to the outside world · Historical process · Economic logic

In the forty years of reform and opening-up, China has achieved remarkable achievements in various fields. Opening up to the outside world has become China's basic national policy. This is not only a major choice made by the leaders of the older

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generation after summing up domestic and foreign historical experience, but also an internal requirement for developing national prosperity.

Deng Xiaoping, the chief designer of China's reform and opening-up policy, clearly pointed out at the beginning of the policy that "The present world is an open one" and "Without reform and opening-up, it will be hard to develop the economy."¹ Deng Xiaoping's idea of opening to the outside world covered building special economic zones, actively utilizing foreign capital, developing foreign economic cooperation and foreign trade, spreading opening up from coastal areas to the hinterland, correctly handling the relationship among independence, self-reliance and opening to the outside world, and so on. The fundamental goal of reform and opening up is to liberate and develop the productive forces, improve labor productivity, and ultimately achieve the high-quality development of the Chinese economy. In short, reform and opening up is designed to rationalize the government/market relationship through the reform of institutional mechanisms so that the market can play a leading role in resource allocation; strengthen the protection of property rights; accelerate the accumulation of human capital and encourage scientific and technological innovation; and reduce transaction costs, further the international division of labor and specialization, and expand market scale. Reform and opening-up are mutually independent and complementary and constitute a dialectical unity. Domestic reform covers economic, social, political and cultural fields. Reform in each field involves opening up and at the same time provides an institutional guarantee for the promotion of opening up. The continuous expansion of external opening-up on the basis of trade, direct investment and financial cooperation is itself a reform, which in turn will promote and deepen reform in various fields at home. Since the 18th National Congress of the Communist Party of China, opening-up in the new era has stepped up to a new level in terms of concept, form and content. On the basis of this historical process, this paper seeks to sum up the basic content of opening-up and to explore the economic principles and theoretical logic underlying its great achievements.

4.1 Background and Awareness of Opening Up

China's implementation of reform and opening-up has a profound and complex historical background. At home, the Cultural Revolution that started in May 1966 and continued to October 1976 caused the People's Republic of China to suffer the most serious setbacks and losses since it was founded in 1949. In conclusion, the country urgently needed a change that would bring order out of chaos and allow the whole nation to regain confidence and hope. In terms of bilateral relations, at the end of 1978 and the beginning of 1979, as the central figure in the second generation of collective leadership, Deng Xiaoping visited Japan and then the United States. These two visits strengthened his conclusions about the great disparity between world advanced industrial and technological levels and those of China, and confirmed

¹Selected Works of Deng Xiaoping (1993), pp. 64, 367.

his determination to open-up and development of the country. In terms of the global situation, the Soviet Union had invaded and occupied Afghanistan in December 1979, and the US-Soviet struggle for hegemony was white-hot. One could say that it was these complex internal and external changes that prompted the Chinese leadership of the time to seriously consider the future direction of the country's development. After reviewing the situation, they ultimately determined to promote reform and opening-up and integrate China's economy into the globalized world.

At the beginning of reform and opening up, China basically relied on the planned allocation of resources or factors of production; there were multiple restrictions on transactions involving voluntary contracts, and market scale was under extreme pressure. Reform and opening-up was designed to leave all this behind and allow socialist China to integrate into the world of economic globalization by comprehensively adopting market mechanisms. In terms of the domestic environment, the policy makers of reform and opening-up had eliminated a heavy historical burden with the extensive political resources at their disposal; but at the same time, the government was under considerable financial pressure, full employment was hard to achieve, and the standard of living was very low. In terms of the international environment, China had become the "third pole" that the two hegemonic powers, the US and the Soviet Union, sought to win over; most of the other planned economies had started on and made progress with reforms, and those East Asian countries with open economic models had been very successful. In this context, the time was ripe for China to take the initiative in opening its doors to the outside world, with a view to a speedy exit from these difficulties that would enable the economy to return to the right track and maintain long-term stable and rapid growth.

The successful experience of the open Asian economies played a key role in opening the door for China's reform and opening-up. On the basis of the historical development of the Japanese cotton textile industry, the Japanese economist Akamatsu Kaname had put forward his "flying geese pattern of development" in 1932. On the subject of technology gaps, this theory states that latecomers can achieve industrialization and develop heavy industry and highly processed products by introducing advanced technology from technological front-runners that allowed them to produce, process and export goods at home. Those countries that first emulated innovative developed countries could also develop through trading with those that come later to imitation, forming a trade and industry chain that corresponds to that of the innovative countries. This makes for the rapid development of the national economy.² In the 1960s, the emerging industrial economies represented by the "Four Asian Dragons" followed by Japan as the "lead goose," actively pursuing an export-oriented economic development model and participating fully in the international division of labor, with a focus on the development of labor-intensive processing industries. In a relatively short time, they achieved rapid economic development, leaping over the middle-income trap. All this provided valuable practical resources for China to draw on in carrying out reform and opening up. Summing up the successful development experience of these economies, we can see that opening up is a key prerequisite for

²Kaname (1994), pp. 93–108.

achieving rapid development. In conjunction with a high savings rate, encouragement of exports, attracting foreign investment (advanced technology, management, etc.), and emphasizing human capital investment, opening up promotes economic growth.

After the Third Plenary Session of the Eleventh Central Committee, the second generation of collective leadership headed by Deng Xiaoping came into being.³ Faced with the great changes in the world economy and politics at the time, Deng Xiaoping had a keen insight into the way the themes of the times had begun to change from war and revolution to peace and development. He first put forward the idea that “For quite a long time to come, it is possible that there may not be a large-scale world war.”⁴ Later, he concluded that peace and development were the two main themes of the contemporary world.⁵ Based on these scientific judgments, the Central Committee of the Communist Party of China decided to shift the focus of national work to economic construction, and established a policy of invigorating the economy at home and opening-up to the outside world.⁶ At the Twelfth National Congress of the Communist Party of China, Deng Xiaoping said “We are unswervingly dedicated to implementing the policy of opening-up and actively expanding foreign exchanges on the basis of equality and mutual benefit.”⁷ The report of the Twelfth National Congress of the Party clearly pointed out that implementing opening-up was China's unswerving strategic policy. Opening to the outside world was in line with the theme of the times and the general trend of world development. It is an inevitable choice for China's modernization drive and a basic national policy that must be followed for a long time.

Like other major theoretical principles and policies of the Communist Party of China, opening-up has the theoretical quality of keeping pace with the times, and its connotations have been continuously enriched and perfected in a series of important conferences. The report of the Thirteenth National Congress of the Party proposed to further expand the breadth and depth of opening to the outside world and continuously develop economic and technological exchanges and cooperation with foreign countries. The Third Plenary Session of the Fourteenth Central Committee proposed “making full use of internal and external markets and resources and optimizing resource allocation... and developing an open economy.” The report of the Fifteenth National Congress proposed to perfect a multidimensional, multi-level and wide-ranging opening up arrangements and develop an open economy. The report of the Sixteenth National Congress pointed out that the focus of developing an open economy in the next five years should be to adhere to the combination of bringing in and going out. The report of the Seventeenth National Congress held that China's open economy had entered a new stage, and for the first time put forward “an open economic system.” Following the outbreak of the global financial crisis in

³Party Central Committee Literature Research Office (2004), p. 1295.

⁴Selected Works of Deng Xiaoping (1993), p. 127.

⁵Selected Works of Deng Xiaoping (1993), pp. 96, 104.

⁶Selected Works of Deng Xiaoping (1993), pp. 135, 237.

⁷Selected Works of Deng Xiaoping (1993), p. 3.

the United States, Europe and other developed economies, China and other emerging economies played a prominent role in the global governance arena. In 2008, at the G20 summit, China put forward important reform measures, including promoting the reform of international financial organizations and improving the international monetary system.⁸ This implies that the emerging economies represented by China no longer passively integrate and adapt the existing international system, but are beginning to become more active in participating and improving the system. The Eighteenth National Congress of the Communist Party proposed that the level of the open economy should be improved in an all-round way. In order to adapt to the new economic globalization, China needs to carry out a more proactive opening-up strategy and make the open economic system one that is mutually beneficial, win-win, pluralistic, balanced, safe and efficient. General Secretary Xi Jinping further pointed out that “China will improve the level of the open economy to give it a wider scope, broader field and deeper level,” “will improve the open economic system making it mutual beneficial, win-win, with a diverse balance, and safe and efficient” and “will jointly maintain and develop an open world economy.”⁹ The Nineteenth National Congress took opening up to new heights. It proposed firmly implementing the developmental concepts of innovation, coordination, green, open and sharing, developing the open economy at a higher level and promoting the formation of a new pattern of comprehensive opening up. This reflects the fact that since the Eighteenth National Congress, China has begun to take the initiative more often and adopt an active approach to leading the construction of a global open economic system and the reform of global governance. In summing up the evolution of reform and opening up policy, it is easy to see that China’s opening to the outside world permeates all stages of national economic development from its initial adaptation to participation and thence to advocacy and promotion of improvements. China’s opening up has always maintained its vigor and vitality, forming an open theoretical system with a stronger initiative and its own characteristics.

At the Second Plenary Meeting of the Fifth Plenary Session of the Party’s Eighteenth Central Committee, Xi Jinping analyzed the outstanding contradictions and problems in current national development, including innovation, coordination, green, open and sharing.¹⁰ These contradictions and problems have become the main obstacles to the transformation of China’s economy from “high-speed growth” to “high quality development.” It is on the basis of these judgments that the Party Central Committee vigorously promotes innovative development, coordinated development, green development, open development and shared development, and takes them as a whole as being the material road to the realization of the Chinese Dream of the Chinese nation’s great rejuvenation. Among the “Five Great Developments” mentioned above, open development has obvious systemic importance. As part of the basic contents of innovation and development, scientific and technological innovation involves not only independent research and development but also the full use of

⁸Selected Works of Hu Jintao (2016), p. 139.

⁹Xi (2014), pp. 114, 347, 335.

¹⁰Xi (2017), pp. 197–200.

the advanced scientific and technological achievements and beneficial management experience created by human society. In a world of unprecedented interdependence, no coordinated internal development can take place without effective interaction with the outside world. When global problems such as climate change have a serious effect on human survival, green development is itself a topic that requires the joint action of all countries in the world. The ultimate goal of development is the development of all; the achievements of development should be shared by the peoples of the world.

It is particularly worth emphasizing here that the understanding of property rights protection, as one of the cornerstones of China's socialist market economic system, has also gone through a long process. On the eve of reform and opening-up, Deng Xiaoping had already noticed the importance of kindling the enthusiasm of producers; he criticized the view of people who "go on about 'Raising just a few ducks is socialism; raising a few more is capitalism.'"¹¹ However, moving from keeping producer morale up to establishing a relatively complete property rights system and market mechanisms and implementing them strictly and efficiently cannot be achieved overnight. The report of the Twelfth National Congress emphasized that "China implements a planned economy on the basis of public ownership" and at the same time put forward the principle that "the planned economy is dominant and market regulation is supplementary."¹² The Third Plenary Session of the Twelfth Central Committee proposed "developing the socialist commodity economy."¹³ At the beginning of 1992, Deng Xiaoping put forward the important point that capitalism also has plans and socialism also has markets.¹⁴ This sundered the ideological shackles that had hindered the market from playing a leading role in resource allocation. Subsequently, the Report of the Fourteenth National Congress clearly put forward the idea of "establishing a socialist market economy."¹⁵ In 2004, a constitutional amendment clearly stipulated that "Citizens' lawful private property shall not be infringed upon." In 2007, China's first Property Law formally went into force, a full 25 years after the Party's Twelfth National Congress.

4.2 The Main Content of Opening-Up

In the past forty years, policy and institutional reforms related to China's opening up have come in an array of different forms and covered a variety of areas. Having analyzed and reviewed these, we now summarize the main reform measures involved in implementing the basic national policy of opening to the outside world under six heads.

¹¹ Xiaoping (2004), p. 238.

¹² Hu (1986), p. 22.

¹³ Central Party Literature Research Office (1996), p. 349.

¹⁴ Selected Works of Deng Xiaoping (1993), p. 373.

¹⁵ Selected Works of Jiang Zemin (2006), p. 228.

First, we should reform systems and mechanisms and support opening-up. The applicability or coverage of institutions is bounded. Market scale can be expanded by the practice of strengthening the applicability of effective institutional arrangements and increasing their coverage, or by setting up institutional arrangements that enable transactions to be achieved on a larger scale. This means that the promotion of opening to the outside world is inseparable from relatively complete institutional guarantees. Opening-up is closely connected to economic reforms that cover the rural economy, the ownership structure, state-owned enterprises, the price, financial and fiscal systems, taxation, foreign trade and so on. In the case of the reform of foreign trade, the Decision of the State Council on Further Deepening the Reform of the Foreign Trade System issued in January 1994 clearly defined the objectives of the reform: policy unification, open operations, equal competition, self-financing of profits and losses, integration of industry and trade, implementation of an agency system, and establishment of an operational mechanism adapted to the prevailing rules of the international economy.¹⁶ The purpose of institutional reform was to make the system more effective in terms of respect for and protection of property and contractual rights and reduction of transaction costs. All this undoubtedly helped further opening up and the formation of a single or unified market.

Second, the introduction and absorption of advanced science and technology was not only one of the original intentions of China's opening-up, but also a key factor in promoting its rapid economic development. Technological progress, as a direct driver of improved labor productivity, played a crucial role in promoting long-term economic growth. In the early stages of reform and opening up, China faced a grave shortage of funds and of ideas and experience to do with advanced technology and scientific management; going all out to attract foreign investment was aimed at adopting the strong points of others and making them our own. As early as April 1979, the central authorities put forward the policy of "readjustment, reform, rectification and improvement." At the time, the import of technology was mainly reflected in two "shifts": firstly, the shift from new projects to transformative technology, and secondly, the shift from importing complete sets of equipment to trading under license, cooperative production, advisors and consultancies, and technical services. The Decision on Scientific and Technological Reform issued in March 1985 stated that modern science and technology is the most dynamic and decisive factor in the new productive forces. In 1988, Deng Xiaoping put forward the famous assessment that "Science and technology are the primary productive forces." In May 1995, the Central Committee of the Communist Party officially put forward the strategy of "rejuvenating the country through science and education." With the advent of the 21st century, a large number of policy documents have been issued in support of the national plan for medium and long-term scientific and technological development; this played a large part in driving innovation and encouraging scientific and technological innovation.

Third, in line with the idea of "crossing the river by feeling for the stones," a policy was adopted whereby the experience of pilot schemes and trials, if successful,

¹⁶Central Party Literature Research Office (2008), p. 638.

would be extended to a larger scope region, with a view to expanding the domestic and international markets. Closely related to this were two major measures, the first of which was the establishment of special economic zones. In July 1979, the Central Committee decided to adopt a “special policies and flexible measures” approach to setting up pilot special economic zones in Shenzhen, Shantou and Zhuhai in Guangdong and in Xiamen in Fujian. In April 1984, the Central Committee approved the opening up of a further fourteen cities, including Dalian, to the world, to encourage the creation of economic and technological development zones. In 1988 and 1990, it approved the establishment of Hainan Special Economic Zone and Shanghai Pudong New Area. These special zones attracted foreign investment by creating a favorable investment environment, accompanied by preferential measures such as tariff reduction and exemption, and also introduced advanced science and technology and scientific management concepts and methods that drove and facilitated regional and national economic development. The second measure was the establishment of free trade pilot zones. China's first free trade pilot area, the Shanghai Free Trade Pilot Area, was formally established in September 2013. It centered on institutional innovation, transformed government functions, deepened financial reform, facilitated investment and trade, created a favorable business environment involving internationalization, the rule of law and facilitation, turning the relevant experiences and practices into a national system which is carried out countrywide.

Fourth is increasingly active participation in regional economic, trade and financial cooperation. In the international arena, opening to the outside world is mainly reflected in the following three areas. (1) China's active participation in Asia-Pacific regional cooperation. In November 1991, China was formally admitted as a member of APEC. In 2000, it participated in the Chiang Mai Initiative, which played an important role in promoting the construction of financial cooperation mechanisms and regional integration in East Asia. (2) The establishment of the China-ASEAN Free Trade Area. This marks a new level in China's participation in regional cooperation. The establishment of the FTA will help expand bilateral trade and investment, accelerate the flow of funds, logistics and information among countries in the region, promote the cultivation and development of regional markets, and raise the level of China-ASEAN economic integration. (3) The Belt and Road Initiative. In September and October 2013, Xi Jinping proposed the major initiative of building a “Silk Road Economic Belt and a Maritime Silk Road for the Twenty-first Century” during a foreign visit. The initiative is based on the basic principles of joint consultation, construction and sharing; deepening the “Five Links” of cooperation is a key pillar and building a new pattern of comprehensive opening up is the direction of effort. The active expansion of a new space for international cooperation through intensified trade and investment cooperation, the promotion of infrastructure links and the strengthening of open cooperation in innovation capacity and global economic governance, will bring benefits to countries along the route and even to the whole human race everywhere in the world.¹⁷

¹⁷Communist Party of China Central Committee, Publicity Department (2018), pp. 298–307.

Fifth, we should steadily promote the internationalization of economic and trade cooperation and broaden its scope. China's currency, the RMB, has become the pricing, settlement and reserve currency of international economic and financial exchanges, thus lowering exchange rate risks, reducing transaction costs, promoting economic integration between China and its trading partners, sharing in the pricing power for bulk commodities, promoting diversification of the international monetary system, restraining irresponsible behavior on the part of policy makers in key monetary centers, and obtaining seigniorage tax. In December 1996, China took the lead in implementing the current account convertibility of the RMB. After years of effort, the RMB was approved to join the IMF's Special Drawing Rights currency basket in November 2015. This was formally implemented on October 1, 2016, enabling the RMB to take an important step on the road to becoming one of the world's key currencies. Of course, we should also be soberly aware that the internationalization of the RMB is still a long way off, and there is still a big gap between the RMB and the key international currencies.

Sixth, we should participate in and promote the reform of the international structure, improve global governance and reduce the non-neutrality of global rules.¹⁸ China resumed its membership of the IMF and the World Bank Group in 1980, formally joined the World Trade Organization in 2001, and established the Asian Infrastructure Investment Bank (AIIB) in 2015. These actions constitute successive milestones in China's adaptation and integration into the international system during its opening-up. The global financial crisis that began in the United States had severe negative consequences throughout the world, clearly exposing shortcomings in financial regulation and the drawbacks of international financial organizations. To maintain international financial stability and promote world economic growth, China has actively promoted reform of the World Bank and the IMF. In April 2010, World Bank voting rights reform made China the third largest shareholder. The IMF share reform, which came into effect in January 2016, has raised China's voting power from sixth to third place, and has also strengthened its international influence and voice. Promoting the joint construction of international financial institutions such as the BRICS New Development Bank and the Asian Infrastructure Investment Bank marks the first steps in China's initiative as a leader at the center of the world stage. The BRICS New Development Bank focuses mainly on financing long-term development of infrastructure and sustainable projects. BRICS emergency reserve arrangements focus on financial stability, providing short-term liquidity support to members facing balance of payments pressure. The Asian Infrastructure Investment Bank focuses on supporting investment in infrastructure construction and other productive areas in order to promote sustainable economic development in Asia. In the course of its

¹⁸Institutional non-neutrality means that the same institutions mean different things to different people; that is, under the same system, different people or groups often get different things. Those individuals or groups who have benefited from the established system or may benefit from some future institutional arrangement will undoubtedly do their best to maintain or strive for it. See Zhang (1994).

continuing opening-up, China's role is also changing from adapting to or participating in the international system to being an indispensable advocate, leader and promoter of reform.

China's practice of opening up to the outside world is a historical process of continuous expansion and deepening. With the dramatic changes in the late 1980s and early 1990s in the former Soviet Union and the East Europe, the confrontation between the Soviet Union and the United States and the coexistence of "two parallel markets" collapsed, a wave of marketization sprang up worldwide, and with it the deepened development of economic globalization. China's opening up process also accelerated and intensified, and ultimately achieved the five changes outlined below. First, in terms of countries to which the open door applied, it has moved from "determination to open to the developed world" to "a better combination of opening to developed and developing countries." Second, in terms of areas for opening, China has moved from manufacturing industry and trade in goods to a variety of industries including energy, aviation, the automobile industry, agriculture, finance, insurance, education and consultation. Third, in terms of space for opening, the services trade has changed from coastal opening to coastal plus border opening and thence to comprehensive opening; fourth, in terms of the direction of opening, China has moved from opening-up to the outside world to bilateral opening and joint opening. Fifth, in terms of opening up claims, it has moved from introducing foreign capital and advanced technology and management experience to promoting the joint construction of the global value chain.

The way China's opening up to the outside world changed from partial to general and rose from a low to a high level can be explained by changes in the operation of Sino-foreign joint ventures. Initially, all joint ventures had to produce for export, mainly because the Chinese labor force had entered the international division of labor or global market via commodity exports. They were subsequently permitted to sell to the domestic market, resulting in a growing proportion of domestic sales. The domestic and foreign markets have become increasingly integrated. Foreign capital as a factor of production was initially allocated in relatively narrow and specific areas and fields, with the host country imposing relatively strict limits on equity and "life cycle." Later, with the continuous relaxation of restrictions, the scale, type and conditions of available foreign capital have undergone tremendous changes. Initially, China's domestic products lacked standards or had standards that were relatively low, but later, with the increasing scale of processed exports, the domestic market became more and more conscious of international standards and especially developed market standards, so that the standard of domestic products began to align with those of developed markets.¹⁹

¹⁹Lieberthal (2010), pp. 262–263.

4.3 The Theoretical Logic of Opening-Up to the Outside World

Opening up to the outside world promotes economic and social progress and national prosperity and development. This is a profound truth that has been proved by economic theory and development practice both at home and abroad. Marx explicitly included international economic relations in the research framework of political economy. In discussing the methods and systems of political economy, he wrote: "... (4) International relations of production. International division of labor. International exchange. Output and input. Exchange rate. (5) World markets and crises."²⁰ According to Marxist political thought, technological progress and the development of the productive forces will inevitably lead to the expansion of exchanges and the deepening of the division of labor. The latter will improve production efficiency, thus promoting the development of the national economy and profoundly affecting the world economy.²¹

The practice of China's opening-up to the outside world is highly consistent with traditional Chinese ideas on trade. As early as two thousand years ago, Chinese thinkers and historians had a profound understanding of the relationship between free trade and economic prosperity. Sima Qian wrote in the *Shi Ji: Biographies of Merchants* of "exchanging one's surplus for something one lacks."²² The *Huainanzi-Customary Proverbs of Qi* further states that, "On marshes and coastlines, nets were woven. On hillsides and slopes, fields were plowed. People use what they have to exchange for what they lack and use what they are skilled into exchange for what they cannot do."²³ Sima Qian talked about "production for trade or profit" or "chres-matics," which is equivalent to the "returns" or "growth" of modern economics. The essence of ancient Chinese thought on trade is "exchanging one's surplus for something one lacks," or "using what one has to exchange for what one lacks and using what one is skilled into exchange for what one is unable to do." They concisely point out that trade is one of the fundamental sources of economic growth. Accordingly, we can call this the *Huainanzi-Sima Qian Theorem*. Other sayings based on the idea of obtaining economic development and gains from trade through exchange include "adapting measures to local conditions," "capitalizing on strengths and avoiding weaknesses" and "exchanging needed goods." It can easily be seen that across the millennia of Chinese civilization, economic prosperity and social stability flourished when economic policy accorded with this theorem.

Although the *Huainanzi/Sima Qian Theorem* appeared more than two thousand years ago, it concisely crystallizes the basic principles of the modern open economy, i.e. the principles of the three main trade theories. In his enduring work, *The Wealth*

²⁰Selected Works of Marx and Engels (2012), p. 709.

²¹Pei and Liu (2018).

²²Sima (1959), p. 3262.

²³Gu (2009), p. 179.

of Nations, Adam Smith focused on the logic of a country's prosperity and development. He saw economic development as being characterized by an increase in per capita income that could only be obtained through an increase in labor productivity, which in turn could fundamentally be brought about by the division of labor and specialization. The basic conditions for these desiderata was the expansion of market scale. This gives us a theoretical model of economic growth: expansion of market scale → reinforcement of division of labor and specialization → higher labor productivity → rising per capita income → economic growth.²⁴ Simplifying this logic, we arrive at the axiom that economic prosperity comes from expansion of market scale, in what is termed the "Adam Smith theorem" or "theory of absolute advantage." David Ricardo's theory of comparative advantage holds that differences in countries' labor productivity reflect differences in technology which result in different costs of production. When a country has no advantage in the production of commodities, it should concentrate on producing for export those commodities where the productivity gap with its trading partner is smallest, on the basis of the principle that choosing the better of two benefits and the lesser of two evils improves the welfare of both countries. This is known as the theory of comparative advantage.²⁵ The theory further develops the idea that free trade promotes economic prosperity. Marx also holds a positive attitude towards this view. He argues that countries with low productivity in international exchanges, i.e. economically underdeveloped countries, "pay more for objectified labor in physical form than they get, but the goods they get from it are cheaper than they can produce themselves."²⁶

The *Huainanzi*/Sima Qian Theorem emphasizes the role of endowment in trade. Two thousand years later, the Swedish economist Bertil Ohlin, building on research by Eli Heckscher, pointed out that "Countries have comparative advantages in those goods for which the required factors of production are relatively abundant,"²⁷ thereby developing a theory of international trade based on factor differences that is known as the factor endowment theory or Heckscher–Ohlin theory. This theory posits that the production of goods requires different factors of production; beside labor, these include land, capital, technology, and knowledge. The production of different commodities entails differences in the factors of production required. Therefore, a country should export goods in which its factors of production are relatively abundant and import those in which its factors of production are relatively deficient. In other words, the relative differences in countries' factor endowments and in the intensity with these factors are used in production constitute the basis of international trade. Trade allows each participating country to improve its own level of welfare and thus promotes common prosperity and development.

²⁴Adam Smith believed that all countries benefit from the international division of labor. If one country uses less labor to produce wine and another uses less labor to produce wool, each should specialize in producing the products that cost it less labor and then exchange them for those of its trading partner. This allows both to save labor, increasing labor productivity and mutual benefit. See Smith (2009), p. 331.

²⁵Ricardo (2011), pp. 64–77.

²⁶Marx (2004), p. 265.

²⁷Ohlin, *Interregional Trade and International Trade*, p. 6.

The above trade theories prove to varying degrees that even without technological advances, as long as the market's micro-agents (individuals or enterprises) or countries focus on production in which they have an advantage and obtain from their trading partners what they produce less efficiently, they can achieve gains from trade that promote economic growth. One of the main sources of the economic miracle that China has witnessed in the past forty years has been the huge trading gains that have accompanied market enlargement. However, in reality, technological progress occurs in tandem with the expansion of market scale, as reflected in the course of upgrading the division of labor and level of specialization. At times, this may even determine the speed and limits of market scale expansion. Moreover, the "changes," "exchanges" or "transactions" mentioned above are all conditional. "Conditional" here, in short, refers to the laws of trade and the institutional arrangements based on those laws. A trinity of conditions made possible the realization of the Chinese miracle: "gains from trade," "gains from technological progress" and "gains from institutional upgrading." As far as the Chinese miracle is concerned, opening up to the outside world was a logical and practical preliminary.

There is an immense amount of literature on the contribution of technological progress to long-term economic growth, with Schumpeter's being representative. Schumpeter points out that growth comes from innovation, which manifests itself in new products, methods, markets, raw materials and ways of organization.²⁸ One can see from Schumpeter's summing up of innovation that he sees innovation as being closely related to technology. The motive force of technological progress is not only the innovative activity of market players pursuing profits, but also the way people learn or introduce the advanced technology and production organization of others. The theory is not particularly concerned about "new markets." It is precisely on this point that the emphasis on market size in the trade theories of Schumpeter, Smith and others converge. The emergence of new markets inevitably leads to a new division of labor and specialized production. The intensification of competition brought about by the expansion of market scale also forces market actors at all levels to engage in technological innovation or introduction. While emphasizing that specialized production and competition play a key role in promoting technological progress, Schumpeter also points out that an essential requirement for innovation is the existence of an effective financial market to provide the requisite financial support. Given that financial market is a classic institutionally intensive arrangement, the reform of systems and mechanisms or the establishment of effective systems are issues that cannot be avoided.

Progress in technology and trade can promote economic growth, but they depend on effective institutional arrangements. The core elements of these are clearly defined and protected property rights, respect for contracts by all players, and performance by government and the market of their respective functions without trespassing beyond their own sphere. The core elements of the above institutional arrangements constitute the conditions not only for the maintenance and expansion of market scale but also for the ultimate transmission of expansion of market scale to economic growth. The

²⁸Schumpeter (1991), pp. 73–74.

critical role is that of the government, since it is the government that is responsible for defining and protecting property rights, maintaining contracts and ensuring that the market plays a decisive role in resource allocation.²⁹ In other words, economic prosperity depends on the effective use of government power. Clearly, its functions are not limited to domestic arrangements. Inter-country exchanges are based on rules. The breadth and depth of coverage of international institutions or rules also determine the size of the market and the quality of trade, while the latter in turn affects the market size. For a country that has long been outside the international trade system, accepting and joining the established international system means not only enlargement of its own market but also the reform of those parts of its original system that are completely at odds with the existing international system. It also implies that the interests of domestic vested interest groups will be seriously affected. This is known as “coerced reform.”

The basic approach underlying the economic logic of opening to the outside world provides an explanation of how opening-up can promote long-term economic growth by expanding market scale. This expansion has five dimensions. (1) An increase in the number of people involved in the transaction; (2) Improvement of participants' wealth creation ability due to the accumulation of human capital and technological innovation; (3) Expansion of the scope of tradable products; (4) Increase in the degree of monetization; (5) Expansion of the coverage of effective institutional arrangements and the strengthening of the enforcement. The five complement each other and work together, which eventually leads to the expansion of market scale.³⁰ Combining the expansion of market scale with the theory of long-term economic growth, we can get a concise model. Its key variables and logical connections are as follows: expansion of market scale → emergence or increase of potential “gains from trade” → property and contractual rights duly protected by the government → the transaction becomes possible and can be successfully completed → the division of labor and the enhancement of specialization → technological progress brought about by innovation and learning → improvement of labor productivity → economic growth (per capita income growth). The discussion in the first two sections of this paper indicates that logical framework above helps to deepen our understanding of the theory behind China's opening-up.

Here, there is a need for some supplementation of global governance. Global governance is essentially a strongly “non-neutral” set of rules used to regulate games among state or non-state actors. Current international institutions and systems have been created and led by the developed West; they reflect the interests of the developed economies. Clearly, emerging economies and developing countries' voice and representation have long been unsatisfactory. Given the substantial changes in the comparative power of the major gamers, some emerging economies are becoming indispensable to the solution of global problems. Their stake in the current international system has increased significantly, as has their desire to safeguard and expand

²⁹See Olsen (2005), p. 10.

³⁰Zhang and Feng (2017), pp. 89–121.

their own interest claims through global governance.³¹ In this context, at the same time as we balance rights and obligations, we should actively promote the reform of global governance, on the principle of “doing everything within our power but acting judiciously,” rather than revamping the old system or starting something new and separate. We should circumvent or water down the “non-neutral” institutional arrangements in the global governance system. If, when conditions allow, a country seeks to improve its position in the established international system, either alone or jointly with other stakeholders, this is undoubtedly a rational choice. This logic can be said to give a precise explanation of China’s actions in the field of global governance.

4.4 Conclusion

China’s opening up since 1978 has been a historical process of continuous extension and deepening. In the course of this process, Chinese policymakers and the mass of the people have gradually deepened their understanding of reform and opening-up, and China’s relations with the world, especially its role in the world, is undergoing constant readjustment. At the beginning of reform and opening-up, China adapted to and was integrated with the international economic system; it then participated in it and sought to improve it, and then strove to become an advocate and leader of the reform of the international system. Within Chinese practice, an incremental series of coherent open economic policies and theories with Chinese characteristics have come into being. Under the guidance of Deng Xiaoping’s reform and opening-up theory, China’s opening-up practice not only is a good fit with the traditional Chinese trade theory of the *Huainanzi*-Sima Qian Theorem, but also coincides with the explanations of modern trade theory and long-term growth theory.

As socialism with Chinese characteristics enters the new era and profound changes occur in the international environment, especially following the election of President Trump, Sino-US relations have begun to enter a period of qualitative change. It remains true that China needs to use its own opening-up to lead and encourage other countries to pursue mutual and joint opening-up, and needs to actively participate in the reform of global governance and regional economic and trade cooperation to create the conditions for a community of shared future for mankind and the building of a world of lasting peace, universal security, common prosperity, openness and tolerance, and cleanliness and beauty. The tremendous achievements of China’s economy have benefited from the continuous reform and opening up of the past forty years. The high quality sustainable development of China’s economy remains inseparable from the further deepening of reform and opening-up to the outside world. More than thirty years ago, Deng Xiaoping said, “If our opening-up policy remains unchanged in the first fifty years of the next century, then in the last fifty years, our economic

³¹Zhang et al. (2017), p. 11.

contacts with the international community will become even more frequent, interdependent and inseparable, and the opening up policy will be even less likely to change.” Over the past forty years, China’s policy of opening to the outside world has been consistent. Especially since the Party’s Eighteenth National Congress, Xi Jinping has repeatedly stressed on many occasions that China’s open door will never close; it will only open wider and wider.

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