

**DECENTRALIZATION AS DEVELOPMENTAL  
STRATEGY IN THE DENGIST ERA**

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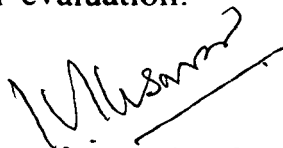



July, 1999

## CERTIFICATE

This is to certify that the dissertation entitled "**DECENTRALIZATION AS DEVELOPMENTAL STRATEGY IN THE DENGIST ERA**" submitted by **MR. G. VENKAT. RAMAN** in partial fulfilment of the requirements for the award of the degree of **MASTER OF PHILOSOPHY**, has not been previously submitted for any degree of this university or any other university. This is his own work.

We recommend that this dissertation may be placed before the examiners for evaluation.

  
**PROF. K.V.KESAVAN**  
(CHAIRPERSON)

  
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(SUPERVISOR)

***Dedicated to  
my beloved parents***

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# **INTRODUCTION**

## INTRODUCTION

The People's Republic of China (PRC) covers an area of 9,571,300 sq. km (almost 3.7 m.sq. miles) and extends about 4,000 km, from north to south and 4,800 km from east to west.<sup>1</sup> Owing to China's mountainous relief and the comparatively inadequate infrastructure in the more backward regions, distance creates major economic and political problems. For example, not only is it costly and technically difficult to build a dense communications network, but also repeated attempts to move industry inland and away from the established centers in the east have been seriously hindered by such factors as the long haul for new materials and markets.

China's land frontiers extend for a total of 20,000 km, and has been the source of some tension. China shares frontiers with Republic of Korea, Mongolia, Russia, Kazakhstan, Kyrgyzstan, Tajikistan, Afghanistan, Pakistan India, Nepal, Bhutan, Myanmar (formerly Burma), Laos and Vietnam China's eastern sea-board is 14,000 km in length.<sup>2</sup> Its territorial waters are dotted with 5,000 islands, ranging from provincial sized Hainan down to minute atolls, which include the strategically significant, but disputed Xisha (Parcel) and Nansha (Spratly)

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<sup>1</sup> Michael Freeberne, *Physical and Social Geography of the People's Republic of China. The Far East and Australasia, 1999*. Europa Publications Ltd., Thirteenth Edition, pp.228-233.

<sup>2</sup> *Ibid.*

Islands.<sup>3</sup> Rich in fish and also petroleum reserves, these waters make a significant contribution to the output of marine and fresh water aquatic products. China lacks an important seaforming tradition, however, partly because the relatively smooth coastline is largely without good natural harbors.

Administratively, the People's Republic of China is divided into 22 provinces, five autonomous regions and four municipalities, all of which are directly under the central government. There are more than 2,000 counties, which until the early 1980s were subdivided into more than 50,000 people's communes. As the communes underwent striking changes after their introduction in 1958, much of the effective economic and political organization in China was at production brigade and production team level, which frequently coincided with the natural village. In the post-Mao era, the communes have been superseded by the household responsibility system commonly centered upon the family unit. Other organizational structures, such as macro-economic and military regions, may embrace various provinces, whilst under Deng Xiaoping's economic reforms and the 'open door' policy several Special Economic Zones have been established (including Shenzhen, Zhuhai, Shantou, Xiamen and Hainan).<sup>4</sup> In the urban areas, tiny neighbourhood street committees keep a watchful eye on day-to-day activities.

China's fourth national census of 1 July 1990 revealed that the population

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<sup>3</sup> *Ibid.*

<sup>4</sup> *Ibid.*



had grown to 1,130,510,638 compared with 1,008,180,738 at the time of the third census in 1982 and with 582,602,417 at the first census in 1953.<sup>5</sup> These figures, which represent more than one-fifth of the world's population, are formidable in view of both the pressures which the population has exerted historically and the contemporary problems in the physical environment already outlined. There is for instance, a striking imbalance in the distribution of population, which is heavily concentrated in the plains and the riverine lands of the south-eastern half of the country, while most of the north-western half is, by comparison, thinly populated. This results in very high densities of population in the richest areas for settlement, such as the Changjiang Delta or the Red basin of Sichuan. Indeed, 90% of the population inhabit little more than 15% of the country's surface area.

Some 91%-96% of the population is Han Chinese. The remaining 8.04% belong to the national minority groups.<sup>6</sup> Altogether there are over 91 million non-Chinese living within China, chiefly, the peripheral areas beyond the Great wall in the north, the north-west and the south-west. There are 55 different minorities scattered throughout 60% of the country. Between 1982 and 1990, whilst the Han Chinese population increased by 102 million, or 10.80% (1.29% annually), the national minorities grew by 24 million, or 35.52% (3.87% per

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<sup>5</sup> As cited in *ibid.*

<sup>6</sup> *Ibid.*

year).<sup>7</sup> Although so-called autonomous regions have been established, the larger minority groups have presented the central government with serious administrative difficulties. Racial, religious and linguistic problems as in Muslim Xinjiang and Buddhist Tibet, have resulted in several anti Chinese uprisings since 1949; these have been forcibly suppressed.

Linguistic differences among the seven main Chinese dialects as well as between Chinese and minority languages, have proved an intractable issue, despite a) the adoption of Mandarin as the national language and b) attempts at the simplification of the written language by reducing the number of strokes in individual characters and by romanization, and c) literacy drives.

In 1995, almost 352 million people in China lived in cities or towns, but this is still predominantly a rural country, with nearly 71% of the population living in the countryside. The inequalities in living standards between the cities and the rural areas confront the Chinese with some of their most urgent ideological and economic problems even today.

Since 1978, when China began reshaping its domestic economy and opening up to the outside world, the national economy has been developing at such a rapid speed that it has boosted "comprehensive national strength"<sup>8</sup> and has enabled the country to become one of the fastest growing economies of the world. Official

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*Ibid.*

\* Justin Yifu Lin, Fang Cai and Zhou Li, *The China Miracle: Development Strategy and Economic Reform*, The Chinese University Press, 1996, p. 170.

statistics show that the annual GNP growth rate averaged about 10 per cent from 1978 to 1994, a rate which calculated according to comparable prices, is far higher than the world average of 3 per cent during the same period.<sup>9</sup> The annual increase in the national income averaged 9.25 per cent in 1978-93, 61 per cent higher than the average annual growth rate of 5.74 per cent in the 1952-77 period.<sup>10</sup>

In the period from 1978-1994, the per capita annual income of China's rural residents rose from 133.57 yuan to 1,220.98 yuan, with annual real growth averaging 8.25 per cent (3.5 times the average annual growth rate of 2.38 per cent) during the period from 1952-1978.<sup>11</sup> The per capita income of urban residents increased from 316 to 3,179 yuan, with the real annual growth averaging 6.5 per cent, which, calculated according to comparable prices, was 11.2 times the average annual growth (rate of 0.58 per cent) in the 1957-78 period.<sup>12</sup> The peasants' per capita consumption during the same period increased from 138 to 1,087 yuan, with the annual growth of the consumption index averaging 6.8 per cent.<sup>13</sup> Calculated according to comparable prices, this was more than the three times the average growth rate of (1.8 per cent) during the period from 1952-

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<sup>9</sup> *Ibid.*

<sup>10</sup> *Ibid.*

<sup>11</sup> *Ibid.*, p. 172.

<sup>12</sup> *Ibid.*

<sup>13</sup> *Ibid.*, pp. 172-173.

1977.<sup>14</sup>

Against the above backdrop it is quite obvious that the most crucial question faced by the Communist party of China (CPC) is the question of good governance. Closely linked to this question was the strategy of development that was to be followed by the CPC to make the People's Republic of China economically strong and satisfy the hopes and aspirations of its people and fulfil its promises (made during the revolutionary period) to improve the living conditions of the people and make the PRC a powerful country. Here, the question of good governance is being used to refer to the developmental strategy to be adopted in the context of the debate over centralization and decentralization.

## **CENTRALIZATION AND DECENTRALIZATION**

The terms centralization and decentralization are often used with reference to the incompatibility in their respective exercise of authority, as if to suggest that an organization which is characterized as centralized, is completely devoid of decentralized characteristics and vice - versa. In a stable organization, centralization and decentralization are complementary and not antithetic. However, depending on the degree of concentration or diffusion of authority, they are labelled as centralized or a decentralized system. In this dissertation we are

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<sup>14</sup> *Ibid.*, p. 173.

concerned with the question of distribution of authority with reference to governance and as the chief basis of developmental strategy of the PRC and the various factors which determine the ruling elite's choice in opting for a specific strategy, namely, centralization or decentralization, as well as its defining characteristics.

One of the most significant factors favouring centralization in most developing countries was the legacy of colonialism - including the centralization of colonial administration and the centralization of the nationalistic movement as a reaction.<sup>15</sup> This is true of all colonial situations, African or Asian. Another significant factor underlying centralization of authority is the attempt to promote economic development through centralized economic planning.<sup>16</sup> This was based partly on the Soviet experience of democratic centralism in planning and partly on the obvious plea that all resources can be utilized in a co-ordinated manner only by centralized planning. A contrasting force developed through local demands, and local participation was sought to be secured through some local institutions. But this tendency had been more than offset in the sixties (of this century) by the nature of the world economic order and the growing accumulation and

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<sup>15</sup> V. Subramaniam, "The Rhetoric of Decentralization and the Reality of Centralization", *The Indian Journal of Public Administration*, Quarterly Journal of the Indian Institute of Public Administration, July - September 1978, p.767-769.

<sup>16</sup> *Ibid.*

centralization of international capital. Moreover, the power of technology had led to centralization in two ways. First, performance following instructions at the local level was hindered by the low levels of mechanization and technological development, almost primitive, in some countries of Asia and Africa. These two hindrances have led to concentration of authority in a few hands. Second, the larger amount of information that needs to be processed by an authority in making decision, compared to the amount of local information processed by any local authority was a major obstacle. Cybernetics and the computer have progressively reduced these hindrances to manageable proportions but such facilities have not spread uniformly or evenly. This two-fold contribution of technology towards centralization varies in importance from one country to another. But there is also a demonstration effect in that once a possibility is realized in one country, the same possibility is taken up for consideration by most other countries and this increases the tendency towards centralization. In this sense, even less developed countries are exposed to the centralization possibilities of technology.

Effective state action requires a minimum coherence and coordination within and among different state organizations, and that in turn presupposes a minimum autonomy from forces of civil society. Equally and perhaps more important, is the responsiveness of the entire organizational parts of the state apparatus to internal guidance and co-ordination of state action rather than to outside interests and demands. These problems are made more serious by the fact that many types of

state action require decentralization for maximum efficiency. The issues of inadequate knowledge base for developing and implementing rational policies are exacerbated in highly centralized bureaucracies by the loss of information and distortion of commands involved, as both pass through various levels of the hierarchy. Moreover, subordination to a highly centralized chain of command deprives sub-units from taking initiatives on their own and thus exploiting to advantage local conditions. Besides, there is the necessity of negotiating with threatened vested interests and building support among potential constituents at a lower level. The more the state wishes to penetrate the social and economic life, the less can the leaders of lower level operative units afford to act simply as subordinates in a bureaucratic chain of command. These considerations, led to a need for some form of decentralization. With its ethical base in democracy, decentralization has come into use as an evocation of popular appeal against all forms of authoritarianism and excessive centralization. Excessive centralization can be neutralized when there is decentralization of administration, both along geographical and functional parameters Hence, there is a demand for democratic administration, self - determination, community control, neighbourhood government, individual initiative or participatory management.

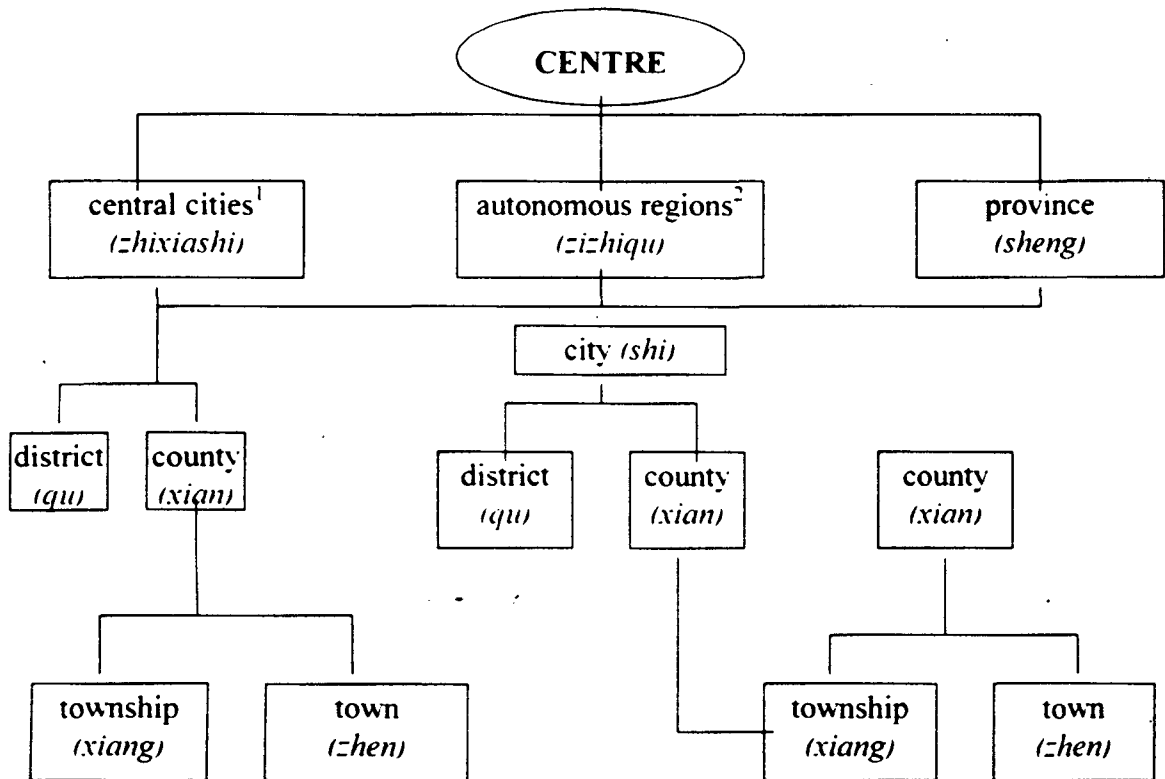
The growth of the welfare state, the planning and social engineering of developing societies have added a new dimension to the debate on centralization versus decentralization. The various services of the welfare state could not be

performed from the Center unless, of course, service by computers and advanced means of technology. Normally the local bodies, employing their own personnel with adequate resources available for mobilization at the local level, ensures success of the concept of welfare state. But, in no welfare state is this happening. Those who pay for the provision of services, also keep a watchful eye upon the quality of the service rendered and the personnel and procedures through which the service is provided. Detailed supervision may interfere with the flexible approach to the provision of service. Ultimately, therefore, in a welfare state, decentralization in administration should mean divesting of decision making at the top and investing it in the local government. Thus, irrespective of the ideological foundations or level of intervention, the contemporary state must localize its governmental apparatus. Thus, decentralization has become an idealistic concept suggesting a system in which people will be given an opportunity to perform their individual goals, assisted and guided by local autonomy at the local government levels.

Against the above backdrop its worth examining the system of governance the Chinese leaders decided to establish. As mentioned earlier, one of the biggest problems that all Chinese leaders have faced historically has been to determine how to administer a vast territory and large society, like China. The following diagram shows that a territorial division of power in China means that a decision made in Beijing passes through many layers of authority before it reaches the



## The Structure of China's Governmental System



### Notes:

1. There are three large cities which are directly administered by the centre (Beijing, Shanghai and Tianjin) and thus equivalent to the province.
2. These are the equivalent of the province in the national minority areas. These are similar differences in labelling at lower levels but these have been omitted for the sake of simplicity.

Source: Gordon White. *Riding the Tiger - The Politics of Economic Reform in Post-Mao China*. The Macmillan Press. Ltd. 1993, p. 19.

public. The administrative distance between the making of a policy decision and its implementation on the ground has been an important factor in the determination of decentralization and political authority in the PRC.

The Chinese Communist leaders did not decide on the decentralized model of government right from the inception of the PRC. Three months before the formal proclamation of the Chinese People's Republic, Mao Zedong set forth the new principles in accordance with which the new government was to be established - thereby providing an ideological rationale for communist political supremacy. Beginning with the premise that "bourgeois democracy" was bankrupt in a China so long oppressed by the imperialism of the bourgeois democracies of the West, Mao announced that the new state was to be, not a bourgeois republic, but a "people's republic". And more precisely, the new "people's republic" as to be "a state of the people's democracy dictatorship, a state under the leadership of the working class and based on the alliance of workers and peasants."<sup>17</sup> Moreover, the new political order was to rest on an even broader social base, for the workers and the peasants were to be part of a "national united front" which included the petty bourgeoisie and the "national bourgeoisie". In accordance with this framework, indigenous Chinese capitalism (capitalist forces and classes not tied to the external imperialist order) was to be allowed to develop in order to meet the

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<sup>17</sup> As cited in, Maurice Meisner, *Mao's China - A History of the People's Republic*. The Free Press, Collier Macmillan Publishers, 1977, p.67.

need for modern economic development. As Mao put it, "China must utilize all elements of urban and rural capitalism that are beneficial and not harmful to the national economy. ...our present policy is to control, not to eliminate capitalism". Nevertheless, Mao repeatedly emphasized that the people's democratic dictatorship was to be firmly "under the leadership of the working class and the Communist Party", for, its ultimate goal was to transform China from a "new democracy" into a socialist and communist society.<sup>18</sup>

The political task that confronted the victorious communists in 1949 was to forge a new political structure which had to be undertaken under very difficult conditions. In 1949, the PRC was an economically backward country which possessed only the most primitive system of communications and transportation, in a land where the persistence of strong traditional localistic and regional loyalties had retarded the development of a modern national consciousness and where the dominance of largely pre-capitalist forms of economic life provided only the most fragile material basis for national integration.<sup>19</sup> To realize the goal of modern political unification under such conditions and in the world's most populous country and territorially one of the largest, was a task of staggering proportions. The CPC under the leadership of Mao Zedong was very much prepared for the difficult task ahead. "On the People's Democratic Dictatorship", where he

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<sup>18</sup> *Ibid.*, p.68.

<sup>19</sup> Maurice Meisner, *op. cit.* p.71.

discussed the two most important problems to be tackled by the communist party (CPC), one was, to quote Mao, "our present task.... to strengthen the people's state apparatus - mainly the people's army, the people's police and the people's courts in order to consolidate national defence and protect the people's interests." The second problem to which energies were to be devoted was "the serious task of economic construction (that) lies before us".<sup>20</sup>

Thus Mao set forth the two overriding objectives that were to mould the nature of state and society in China for the next five years: establishing a strong state power and a strong state power and a strong economy. The realization of these objectives demanded highly authoritarian means of social control and centralized bureaucratic forms of political and economic organization, measures which were to be introduced with extraordinary rapidity and efficiency.

It is not surprising that the communist leaders should have given priority to the need for a strong state and to economic development. In a huge country where traditional forms of political authority had long ago disintegrated, where modern forms of government had existed only incompletely, where during most of the modern times and in most places, the Chinese people had been "governed" by warlord armies, by foreign invaders and occupiers and by the corrupt and inefficient Kuomintang (Guomindang) bureaucrats and militarists; in such a

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<sup>20</sup> Mao Tse-Tung. (Mao Zedong). "On the People's Democratic Dictatorship", in *Selected Works of Mao Tse-Tung* (Peking, 1967), pp.417-18.

situation the establishment of a viable national political order and an effective administrative apparatus was the first and the foremost task.<sup>21</sup>

Alan P.L. Liu, in his work "How China Is Ruled",<sup>22</sup> has categorized the political traditions inherited by the communists into four major factors, namely, (1) The Revolutionary Tradition, (2) Regionalism, (3) Bureaucratic Centralism, (4) and Alien Rule. In keeping with our requirements in this dissertation, we would limit our discussions to only two of them, namely: "regionalism" and "bureaucratic centralism".

Most of the China analysts have observed that Chinese since ancient times have accepted disunity and regionalism as facts of life. The popular Chinese novel *The Romance of the Three Kingdoms*, written some five hundred years ago, begins with the observation that a period of unity is always followed by a period of disunity, after which a period of unity will return once more. It has been pointed out that this "political tradition" of China persists even today in the post liberation era.<sup>23</sup> It was especially visible, as will be seen in the latter part of this dissertation, in the Maoist era where there was constant debate and implementation of the style of administrative functioning from centralization to decentralization. The problem of regionalism brings into focus the question of center-province

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<sup>21</sup> Maurice Meisner, *op. cit.*, p.59.

<sup>22</sup> Alan P.L. Liu, *How China Is Ruled*, Prentice Hall Inc., Englewood Cliffs, 1986.

<sup>23</sup> *Ibid.*

relations which this dissertation has tried to address.

The problem of "center" versus "region" has exercised Chinese governments for centuries. In the early 1950s, the Chinese Communists thought that the Soviet-style of centralized planning could resolve this problem by a straight line span of control from top to bottom.<sup>24</sup> By the mid 1950s, it was clear that this would not work. The CPC tried administrative centralization in order to bring about political unity in a country that had been disunited for fifty years. Administrative centralization achieved its aims, for it permitted the establishment of a uniform governmental system throughout China. However, administrative centralization created rigidities at the middle and lower levels of the system. This meant once again the acceptance of a difference between center and region. Its worth quoting at length an editorial of the *Renmin Ribao* (People's Daily) to see how it described this problem for the pre – 1949 period.

"The local political system under the rule of the KMT reactionancy forces and other reactionary forces was oppressive of the people. The reactionary rulers made use of a bureaucratic system from top to bottom, but they also relied on small and big landlords rotten gentry, and warlords to create a hierarchical system of control weighing on the heads of the masses. The further one got down to the basic level, the more they directly enslaved and trampled the people. But because the reactionaries who controlled the so-called central power quarrelled over self-interest with reactionary cliques who controlled the regional power, they regarded the center and the regions as mutually juxtaposed. The consequence could only be the

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<sup>24</sup> Franz Schurmann, *Ideology and Organisation in Communist China*, University of California Press, 1966, p. 210.

unity of despotic rule on the divisiveness of regional feudalism."<sup>25</sup>

The rulers in the national capital before 1949, were faced with the dilemma that the more bureaucratic rule was imposed from the center, the more regional co-ordination broke down. This presented the ruler with the choice of using "whimsical" and "despotic"<sup>26</sup> approaches of arriving at some compromise with regional interests. Earlier dynasties had tried alternative solutions. During the Sung period, "special imperial commissioners" were periodically sent to the provinces to enforce policy orders and shake up the web of mutual involvement at the regional level. This they did without destroying these networks which formed once again as soon as the commissioners left.<sup>27</sup> The Mongols further expanded the procedures by setting up "mobile bureaus".<sup>28</sup> But no dynasty was ever able to create a continuing nation-wide organization under the effective control of the center which was *outside* both of the formal bureaucracy and of regional power groups. The use of special commissioners, even when permanently appointed, was still an *ad hoc* device designed either to counteract bureaucratic rigidity or vagaries of local power interests.

Despite the power of the new administrative system, the Chinese

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<sup>25</sup> As cited in Franz Schurmann, *Ideology and Organization in Communist China*, University of California Press, 1966, p.213.

<sup>26</sup> *Ibid.*, p.214.

<sup>27</sup> *Ibid.*

<sup>28</sup> *Ibid.*

Communists still faced problems of center versus region, similar to the pre-1949 period.

Coming back to the question of political traditions inherited by the CPC, bureaucratic centralism was another important legacy. The formal appearance of the "traditional Chinese bureaucracy impresses one with its rationality and efficiency". According to Alan. P. Liu, the bureaucracy exhibited all the necessary qualities of Max Weber's "ideal" bureaucratic organization, namely: (1) organization of official functions bound by rules; (2) officials having a specified sphere of competence; (3) hierarchical organization of offices; (4) official conduct regulated by explicit rules; (5) strict separation between offices and the personal property of officials; and (6) administrative acts, decisions, and rules formulated and recorded in writing.<sup>29</sup> At the national level traditional Chinese bureaucracy typically comprised a Prime Minister who was directly responsible to the Emperor and a central government consisting of six ministries on boards. The Prime Minister along with a set of officials advised the Emperor on major policies and were responsible for day-to-day administration of the empire. A majority of officials were remitted through civil service examinations, a procedure that is regarded as unique in traditional political systems for its universalistic standard and open accessibility. Through a system of local governments, the power of the

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<sup>29</sup> Max Weber, "The Essentials of Bureaucratic Organization: An Ideal Type Construction", in Merton et al; *Reader in Bureaucracy*, pp.19-20. As cited in Alan P.L. Liu, op. cit. p.10.



Chinese national government was extended to every part of the empire. This highly centralized and formalized administrative system was designed to enable the emperor to control the officials. In many ways, these two political traditions discussed above continue to influence the way the PRC is administrated even today.

As the title of this dissertation suggests, and as mentioned earlier, decentralization was adopted been adopted as a key factor in the developmental strategy after the First Five year Plan in the PRC. But, as will be seen in the second and third chapters, the decentralization in the Maoist era was completely different from the one in the Dengist era. Before going into the question of development strategy with special emphasis on the model of decentralization followed, is important to establish a link between decentralization and developmental strategy.

All contemporary states today seem to need some form of decentralization or other. Even the smallest of states have some kind of local government with some degree of autonomy. With the advent of the welfare state, the number of functions to be performed by the state and with the expectations from it having become manifold, the modern state seems to have no other option but to decentralize its administration. Whether it is for reasons of practical application, operation of the modern state at local levels or the collection of taxes and enforcement of tax laws, decentralization seems to be the *sine qua non* of good

governance. In short, whatever its ideological foundation or level of intervention, the contemporary state must localize its governmental apparatus.

In different regions of the world, national governments are using decentralization as a strategy for coping with the political instability which is threatened by secessionist elements and demands for greater regional autonomy. Decentralization, along with economic development of backward regions constitutes a vital ingredient in curbing secessionist demands. Moreover, as the pressures for larger organizational units, minimum national standards and central planning capabilities mount, so the concern for local autonomy grows.<sup>30</sup> Besides, one of the most disturbing characteristics of contemporary society is said to be the concentration of power in fewer and fewer organizations/individuals. Few governmental functions are the exclusive responsibility of local institutions. Local needs outstretch local resources in both developed and developing societies. The threats, and in some cases the reality, is of a large, remote impersonal administrative reaction dominating the life of the individual.<sup>31</sup> The above account evidently points out that any effective functioning of the modern state has to be punctuated with a link between administration and decentralization as a development strategy.

The above account clearly highlights the importance of decentralization as

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<sup>30</sup> B.C. Smith. *Decentralization - The Territorial Dimension of The State*. George Allen and Unwin Publishers Ltd., London. 1985. p.4.

<sup>31</sup> *Ibid.*

an effective means of governance of any country and China being a multi-ethnic society with vastly diverse geographical conditions and population distribution, the need for decentralization becomes all the more necessary. As mentioned earlier, the attempt to establish an efficient and effective relationship between central and local authorities in the context of implementing economic strategy and building state socialism had been an ongoing problem for the authorities since 1949. Initially the issue revolved around deciding what was the best way of organizing territory to facilitate decentralized control. Subsequently, as the tasks of nation building and development gathered momentum, the question was, how much power should be devolved to the lower-level units. Unable to find satisfactory and conclusive answers to these questions, PRC government policy on organizing space and decentralizing decision making changed (often radically) on a number of occasions since 1949. Such policy vacillations in part reflect the changing priorities of the central leadership regarding the administration of a vast and varied entity like the People's Republic of China.

### **The Centralized Planned Economy**

The PRC's experience with totally centralized planning came from its decision to adopt the Soviet type system, or more specifically, the Stalinist model of development, under which the central government translated its broad economic objectives into a set of specific output targets for individual industries. The objectives of matching supply and demand required the establishment of various

balances; material balance for production and distribution of goods, labour balances for the allocation of available labour suppliers, energy balances for fuel and power production and allocation. Corresponding to the material balances were financial balances consisting chiefly of arrangements for the incomes and expenditures of the population, the state budget, the cash and credit plans of the banking system, and the income and expenditure of plans of economic sectors, compiled from those of individual enterprises. The central plan not only encompassed economic sectors *per se*, but extended as well to the development of the health care, educational and cultural systems.

Central plans were vertically organized; the plan for each economic sector was supervised by the relevant central ministry and was national in scope. In addition, provinces and localities also made plans that were horizontally organized on the territorial principle and covered all sectors within the relevant jurisdiction but only those enterprises that were under provincial (or local) control. In the early 1950s the predominance of and small privately owned firms among industrial and commercial enterprises caused a large share of non-agricultural output to remain in the horizontal planning system. But the heavy commitment of the First Plan to develop central state owned enterprises increased the center's share of total industrial output to almost one-half by the end of the plan. Moreover, the central government increasingly encroached upon the nominal authority of local governments to plan the activities of their own enterprises.



The pronounced centralization that developed in the course of the first plan had its advantages. Structural change was the order of the day. The rapid shift in the relative proportions of consumer goods and producer goods in total output, and in the geographic disposition of industry from the coastal regions to the hinterland, arguably required highly centralized allocation of resources. There was also the consideration for equity: the party was committed to reducing the sharp regional inequalities in the level of development and distribution of services: central control over resources was effectively used to this end during the first plan period. A greater degree of regional and local autonomy would very likely have pushed Chinese development along the path of widening distributive inequality. Nonetheless, the Chinese did not continue along these lines: the first five year plan (FFYP) constitutes the only time such a highly centralized policy was adopted and exercised in their development strategy.

## **MAOIST DECENTRALIZATION**

The cost of centralization in Mao Zedong's estimation were higher than the benefits, and as the designed structural shifts were brought about, and the size and complexity of the economy rapidly increased such a high degree of centralization brought inevitable consequences: excessive bureaucratization which occurred almost simultaneously within party and government structures, elitism and a widening of the socio-economic and cultural gap between the rapidly developing

urban areas and the largely stagnant rural hinterland. An extensive discussion on the costs of centralization took place after the circulation of Mao's "Ten Major Relationships" speech in April 1956. Mao advocated enlarging the powers of the provinces and the localities and also dealt with the issue of increasing the authority of the individual enterprise. He discussed the relationship between the center and the regions in terms of a contradiction - central control and direction could only be effectively consolidated if genuine decentralization measures were adopted and the interests of the regions were attended to. As he put it, "(We) must fight for "the region" not from the point of view of regionalism or localistic interests, but from the point of view of the interests of the nation as a whole". In order to resolve this contradiction, what was needed, according to Mao, was to consider how to arouse the enthusiasm of the regions by allowing them to "run more projects under the unified plan of the center." For Mao, the building of socialism in the PRC was inextricably linked with emphasizing "self - reliance" for the localities, which in effect meant strengthening the collective/co-operative sector at the local levels; in other words, decentralization measures should allow "an appropriate degree of power "to the communities, the cooperatives and the labouring masses.

In the wake of this speech, an entire range of crucial problems of motivation, control, and reputation were also revealed as consequences of excessive centralization. Often, local and central authorities would duplicate each

others' effort within a region, leading to waste, redundancy and competition for materials. The problem of "local initiative" was particularly severe; under the consolidated state budget system, local expenditures were determined by the center and bore no relation to local revenue. This weakened the incentive of the localities to increase their revenues and to engage in local development efforts.

There was by and large agreement on the need for some kind of decentralization; however, what was being debated was the nature of the proposed decentralization. The second chapter would look into the sort of decentralization that was pursued in the PRC during the Maoist era.

Administrative decentralization contained an answer to some of the problems facing the Chinese economy after the First Five Year Plan (FFYP): social mobilization and the propagation of correct ideological virtues which would ensure appropriate distribution, effective incentives, the right use of local powers, and therefore, adequate central control. The State Council decisions announced on 18th November 1957 embraced the organizational underpinnings of this strategy endorsing administrative decentralization.<sup>32</sup> The decentralization from center to provinces was matched by an analogous handing down of power from the latter to sub-provincial units. Administrative districts and counties now found themselves controlling small enterprises that had previously been under provincial jurisdiction.

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<sup>32</sup> Carl Riskin, *China's Political Economy - The Quest for Development Since 1949*, Oxford University Press, 1987, p.104.

The trend marked by the November 1957 reforms towards increasing the scope of horizontal (or territorial) planning at the expense of vertical control was considerably strengthened by additional measures announced in September 1958, which gave the provinces the power to plan for all enterprises within their territory, including those operated by the central government.<sup>33</sup> Although vertical and horizontal decentralization were to proceed nominally in co-operation with each other, the horizontal element was now predominant. The Great Leap Forward (GLF) in late 1957 and 1958 and a series of state council directives concertized Mao's strategy of decentralization of the planning and management system for industry, commerce and finance in the shape of the rural peoples communes. Although further changes occurred subsequently, including another major decentralization in 1970, the reform of the late 1950s was believed to have inspired the principal outlines of the planning and management system that endured until the reforms of the late 1970s began.

### **Inauguration of Market Reforms and Dengist Decentralization**

The market reforms initiated under the leadership of Deng Xiaoping gave top priority to the goal of modernization as the most important task of the CPC. He compared the realization of the "Four Modernizations" to a profound revolution which should be led by an "emancipation of minds" claiming that without an immediate significant economic and political reforms and emancipation

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<sup>33</sup> *Ibid.*, p.106.



of minds, China's "modernization programme and socialist cause will be doomed".<sup>34</sup> Second, Deng introduced the concept of economic democracy and discussed it at two levels - (1) There should be a decentralization to give full play to the initiative of every region, every factory and every production team; (2) It was essential to safeguard the 'democratic rights' of workers and peasants, including "the right of democratic election, management, and supervision" so that every worker and peasant would have the incentive to work for China's modernization. Third, Deng deviated from the Maoist stress on building socialism by a progressive reduction in socio-economic inequalities; in the view of the reformers this had reduced the people to the level of common poverty. Deng claimed that some people and some regions should be encouraged to get rich first as models for others to emulate. The chief planks in the new economic programmes were: attacking the over-concentration of authority in economic management; reforming the commune system in agriculture multiple and improving farm incentives; and raising living standards. These objectives were seen partly in terms of another decentralization to both local governments and enterprises. Clearly however, this decentralization was going to be of a different sort.

### **Plan and the Market**

In attempting to locate the underpinnings and impetus of decentralization in

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<sup>34</sup> Deng Xiaoping, "Emancipate the Mind, Seek Truth from Facts and Unite as One in Looking to the Future. (December 13, 1978). *Selected Works of Deng Xiaoping*. (1975-82) Beijing, Foreign Language Press, 1984. p.161.

the Dengist period, it becomes necessary to examine the debates regarding the market reforms and the views on the role of planning. The present dissertation would seek to establish that it is these debates and the requirements of market functioning which largely shaped the contours of decentralization in the post-Mao period.

The consensus which was emerging in the early eighties, regarded the Chinese economy as "a commodity economy combining planning regulation with market regulation".<sup>35</sup> Deng Xiaoping's view on the market economy were however more positive as was revealed in his answer to a question from a delegation from Encyclopedia Britannica Inc.: "(It) is surely not correct to say that market economy is only confined to capitalist society. Why cannot socialism engage in a market economy? A market economy existed already in the feudal society. Socialism may also engage in market economy". Deng seemed to suggest that, (1) a market economy should be ideologically acceptable in socialist China; (2) socialist public ownership need not necessarily conflict with the workings of the market; (3) experiments in applying a market economy in China should be tolerated.<sup>36</sup>

Despite such utterances by the paramount leader, the issue of whether China's economic reforms should be market oriented or not, continued to be

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<sup>35</sup> Wei Wei Zhang, *Ideology and Economic Reform Under Deng Xiaoping - 1978-1993*, Kegan Paul International, 1996, p.60.

<sup>36</sup> *Ibid.*

contentious one. Amidst opposition from the conservatives and the prevailing conventions, reformers were able to adopt two moderate but significant steps. First, they protected and encouraged various local experiments of market economy to continue; and second they took initiatives to reform those areas of planning which the ideological consensus had permitted. With the Chinese economy being characterized as a "socialist market economy," the Chinese proceeded to explore the scope of the market under socialism. Between 1974 and 1988, dominant Chinese debates on the ways to combine plan and market have gone through four periods of change: 1979-83, 1983-84, 1984-86, and 1986-88. These debates will be thoroughly examined in the third chapter.

In contrast to Mao's view of development as a dialectical activity encompassing a number of contradictions, Deng's view of development as a linear progression towards modernization gave an entirely different basis to the latter's decentralization policies and processes. The relationship between the state and the market that has emerged in a vastly changed global scenario as well, contributed to this difference. One may therefore suggest that the shift from 'restrictive planning' to 'guidance planning' has been both influenced by and in turn further encouraged market driven decentralization and greater institutionalization of the party-state in contemporary China with the dispersal of power from the center to the provinces and this aspect has been looked into in this present work. To accelerate the transformation of centre-local relations, the Chinese may need to

review and profoundly rearrange the functional division between the center and the localities, and to establish systematically relevant laws and regulations which institutionalize the central-local relations. The present dissertation seeks to examine how the Chinese are managing this process. The dissertation would also attempt to investigate the factors and the motivation (ideology and politics) underlying the change in decentralized governance in the Dengist era. In order to highlight the salient features of Dengist decentralization, the question of agricultural reforms with the Household Responsibility System (HRS) as the focal point has been taken up for detailed examination in the final chapter. The main objective in this dissertation is to understand the basic premises and characteristics of the developmental strategy introduced by Deng Xiaoping since 1978. It is felt that without a thorough grasp of the strategy which was in effect during the early years as well as the changes brought about by Mao Zedong, the post-Mao period would not be adequately comprehended. Hence the first two chapters will provide that historical backdrop to the Dengist developmental strategy.

# **CHAPTER I**

## **The First Five Year Plan (FFYP) and the Beginning of the Planning Process.**

## **THE FIRST FIVE YEAR PLAN (FFYP) AND THE BEGINNING OF THE PLANNING PROCESS**

On October 1, 1949, before a large crowd gathered in Beijing's Tiananmen Square, Mao Zedong, Chairman of the Communist Party of China and at that time also Chairman of the Chinese People's Government, announced the establishment of the People's Republic of China (PRC). After more than three decades of devastating civil upheaval and foreign wars, the PRC embarked on the task of reconstruction and development under a new dispensation. To make the country strong and the people rich was the ideal of China's Socialist revolution. Many members of the Chinese Communist Party toiled very hard for this ideal. When the change in the political regime took place in 1949 and the PRC was established, the new national leaders faced the problem of selecting an appropriate development strategy and choosing the proper administrative institutions to organize China's economic construction in order to quickly accomplish their goals. This gigantic task had two aspects: physical reconstruction and institutional reform.<sup>1</sup> The Communist revolution was not at that stage an ordinary affair, its aim was not merely to patch up shattered physical assets; rather, it was to restructure Chinese society and introduce a new political, cultural, and economic order. The new order was to be based on the ideological premises of Marxism - Leninism which was

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<sup>1</sup> Jan. S. Prybyla. *The Political Economy of Communist China*. International Textbook Company. 1970. p.11.

earlier tested by the Communists under Mao's leadership in the Jiangxi Soviet (1931-49), northern Shensi (1935-47), the rural areas of Manchuria (1946-49), and other Communist controlled regions of China.

## **DEVELOPMENTAL STRATEGY IN THE FIRST FIVE YEAR PLAN**

Communist China's first long-range economic plan covers the years 1953 through 1957. In actual fact, the plan was not approved until April 1955 and the original draft underwent far-reaching revisions in mid-1956.<sup>2</sup> It could, therefore, be argued that during twenty-seven months (1953 - March 1955) the economy was run on the basis of annual plans, the original version of the First Five Year Plan was applied over some fourteen months, and during the remainder of the plan period (mid 1956-57) a modified rendering of the original plan was in force.

The question that faced the Chinese leaders around 1952-53 was what kind of planning was to be pursued, or to put it differently, what blueprint for modernization was to be followed? The leaders in China found an answer in the heavy-industry oriented development strategy which has been described as the "Leap Forward Development Strategy" by scholars like Justin Yifu Lin, Fang Cai and Zhou Li. The term leap forward development strategy is to describe the

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<sup>2</sup> With Soviet assistance, a State Planning Committee was set up in the autumn of 1952 (headed by Kao Kang) and paralleled by planning bureaus in economic ministries and government offices concerned with economic problems. The committee was recognized in 1954 as the State Planning Commission and placed under the direction of a new organ, the state council.

government's attempts to pursue an industrial structure which deviated from the optimal structure based on the comparative advantage of the economy's endowments.<sup>3</sup> The adoption of the capital-intensive heavy industry oriented development strategy in a capital scarce economy is an example of the leap forward development strategy.<sup>4</sup> The strategy was arrived at not only by taking into consideration the surrounding political and economic environment both in China and in the world at that time, but also reflected the political leaders' wishes of making China a strong economy. Besides, and most importantly the Chinese looked to the planning experience of the Soviet Union, for the following reasons.<sup>5</sup>

1. The Soviet (Stalinist) model of Socialist economic development was the only one readily available, ideologically acceptable, and tested in practice. It had shown itself effective insofar as its stated priorities were concerned, in spite of many drawbacks.
2. The adoption by China of the "economics of Stalinism"<sup>6</sup> also apparently made sense from the standpoint of expected foreign aid. The Soviets could, (and that time would), send to China equipment for heavy industries.

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<sup>3</sup> Justin Yifu Lin, Fang Cai and Zhou Li, *The China Miracle: Development Strategy and Economic Reform*. The Chinese University Press, 1996, p.32.

<sup>4</sup> *Ibid.*

<sup>5</sup> Jan S. Prybyla, *op. cit.*, p.111. It may mentioned here that this section on the FFYP draws on the research and analysis of Prybyla.

<sup>6</sup> *Ibid.*



complete plants, and so on. The technical assistance which the Soviet Union was capable of giving was geared to long experience in the ways and means of the Stalinist model.

3. From available sources, it seems that the Chinese Communists do not appear to have had a workable alternative of their own: their economic theorizing and practice did not go much beyond the stage of new democracy.<sup>7</sup> But there were a number of other general theoretical and practical reasons that contributed to its widespread selection.

First to play a part in the selection of a developmental strategy was the strong desire of governments in developing countries to catch up with and overtake advanced economies. After World War II, a large number of colonial or semi-colonial countries became politically independent. The question of how to independently develop their economies so as to achieve rapid economic growth and eliminate poverty and backwardness was an urgent one for every national government. At the time, however, developing countries lagged far behind advanced ones in the areas of economic and social development. Compared with advanced countries, these developing countries had an extremely low economic growth rate and per capita GNP, high birth and death rates a low educational level, an insufficient number of capable managers, and a rigid political system. To

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E.F. Szczepanik, "The Economic Policy of Marxism" in E.S. Kirby (ed.) *Contemporary China: I*, 1955, pp.50-65, and Werner Handke, "The Law of Proportional Development", *Contemporary China: II*, 1956-57, pp.100-104, as cited in *ibid*.

transform these conditions quickly, a large number of developing countries were strongly drawn towards the path of rapid industrialization.

The radical view of economic development in developing countries also affected their development strategies. Most developing countries were used to being colonies or semi-colonies. Their leaders were influenced by the views held by the radical economists at that time. They believe that the market system would lead to serious polarization of their economies and to economic backwardness, and that foreign trade would result in the loss of valuable resources. Based on these assumptions, they expected that the terms of trade for the primary products which constituted their major exports would deteriorate continuously. Therefore, national leaders and economists in developing countries tended to think that under the very imbalanced economic conditions of the world, development and non-development were two sides of the same coin. If developing countries did not establish their own independent industrial systems, but merely depended on the export of primary products, they would be on the peripheries of advanced economies and would remain in a state of backwardness.<sup>8</sup>

The idea prevalent in development economics at the time advocated state intervention for developing economies. This view, which was born in countries with advanced economies, also had an important impact on developing countries'

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<sup>8</sup> Andre Gunder Frank, et al., "The Issues of Economic Development and Underdevelopment from a Historical Perspective", in *The Political Economy of Development and Under-development*, Part 2, edited by Charles K. Wilber (Beijing: China Social Science Press, 1984).

choice of a development strategy. Under the influence of Keynesian economics, mainstream development economics at that time held that the market contains insurmountable defects and that the state was a powerful means which could be used to supplement it and accelerate the pace of economic development.<sup>9</sup> Looking at prevailing realities of developing countries from the viewpoint of development economics, many economists opposed conventional economics; emphasized market imperfection in developing countries despite the role of the market and price mechanisms; and advocated the implementation of centralized and detailed planned management so that the national economy could operate smoothly and reasonably. Because of academic exchanges, the hiring of economists from developed countries such as the World Bank in the formulation of development policies in developing countries, this tendency greatly affected the choice of development strategies in the developing countries, which had only begun to construct their own economies independently.

### **The Heavy Industry Development Strategy**

The extremely backward state of the Chinese economy was an important factor in the selection of its development strategy. When the PRC was founded in 1949, the total output value of industry and agriculture in China was only RMB 46.6 billion and the per capital GNP was RMB 66.1.

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<sup>9</sup> Until the mid - 1970, most development economists were anti-price system, pro-planning, pro-intervention and anti-trade. When they conducted positive analysis, they advocated intervention. See Deepak Lal, *The Poverty of Development Economics*, (Cambridge, Mass: Harvard University Press, 1985), pp.5-16.

Within the total output value, agriculture accounted for 70 per cent and industry made up 30 per cent. Heavy industry contributed only 7.9 per cent of the total output value.<sup>10</sup> Meanwhile, owing to the disquiet over the Communist Party's takeover of the Mainland, Western countries, led by the United States, launched a series of campaigns to politically isolate and economically obstruct China. As a consequence, China had poor international political and economic relations, and had to be prepared for war at any time. The leaders realized that the economy had to be quickly developed and made independent. In light of China's development and the available knowledge at that time, calls for building the national economy and for eliminating poverty and backwardness were almost synonymous with the call for industrializing the economy.

China's industrial foundation was very weak at that time. The modern industrial sector accounted for only 10 per cent of the national economy, whereas the agricultural and handicraft sectors accounted for ninety per cent. Nearly ninety per cent of the population lived and worked in rural areas.<sup>11</sup> Under these conditions, the national leaders encountered the problems of how to mobilize capital and of what kind of development strategy to adopt in order to accelerate industrialization. They selected the heavy industry - oriented development strategy.

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<sup>10</sup> China Economic Yearbook Editorial Board (ed.), *China Economic Yearbook 1987*. (abridged edition, Beijing: Economic Management Press, 1982), p. VJ-4.

<sup>11</sup> Liao Jili, "On China's Reforms of Economic System", in *China Economic Yearbook 1981*, p.III-37.

## **Plan Strategy Defined**

The main objective of the strategy of economic development adopted by the Chinese from the Soviets and adopted by them to the Chinese conditions was rapid growth of output. Concentration on the increase in the volume of the output involved some sacrifice of quality. Workers', peasants' and managers' performance norms. ("success indicators") were geared to the physical output criterion expressed in weights and measures.

Components: The strategy of economic development adopted in by the Chinese from the Soviets and adapted by them to the special conditions of China may be described as 'selective growth under conditions of austerity'.<sup>12</sup>

Selective growth means:

1. Resources are channelled primarily into modern, capital-intensive, heavy industry which is expected to lead to rapid economic growth per unit of invested resources in the long run. The absolute size of the modern industrial sector is seen as the main determinant of national power.
2. Investment in human capital (education) of a particular type, i.e. development of scientific and technical skills.
3. Application of up-to-date technology to certain segments of both the priority and non-priority sectors, together with intensive use of under employed

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<sup>12</sup> Anthony M. Tang. "Agriculture in the Industrialization of Communist China and the Soviet Union". *Journal of Farm Economics*. (December 1967), p.18. As cited in Jan. S. Prybyla. op. cit., p.113.

labour ("technological dualism")

4. Attitude towards agriculture ranging from relative neglect to outright exploitation for the benefit of industry, especially producers' goods industry. Investment in agriculture is made primarily in order to increase the position of marketable agricultural output going to the state. The real costs incidental on this procedure are borne by the peasants, and, to a lesser degree, by urban consumers. In the special circumstances of China this particular component of developmental strategy was - as will be discussed later - significantly modified.
5. Relative neglect of domestic trade and services, and of residential housing construction and maintenance.
6. Reliance on domestic sources of capital formation rather than an foreign trade and assistance.

"Conditions of austerity" mean two things :

- 1) The economy starts from low per capita income levels, low productivity, modest educational standards and a small degree of inter-sectoral integration.
- 2) The rate of investment is high. In the backdrop of an underdeveloped economy this means that consumption, while regarded as the ultimate goal, is seen during the development process as an intermediate activity of secondary significance, except in so far as it affects worker morale and

productivity, and thus the fulfillment of the plan.

"Selective growth under condition of austerity" is not the easiest thing in the world to achieve within a framework of political democracy, and social pluralism as understood in the west, even on the assumption that democratic and pluralistic traditions existed in the country undergoing the process of austere selective growth. Implicit in the strategy is a bias in favour of totalitarian modes of behaviour.<sup>13</sup> The nation, and that means the poor - and that, for all practical reasons, means the peasants - has to be made to save out of meager income, save at high rates, that is trim its already modest consumption standard, or at the very least, postpone consumption increases and surrender to the state, produce where there is hardly enough to cover minimal needs. The resources so extracted are channelled into projects which reflect planners preferences, or more exactly, the preferences of the top leadership imposed on the planners. The projects, moreover, have to be built quickly in a climate of impatience and hurry. Everyone, from the planners all the way down the line to command, is set high targets which cannot reasonably be reached with the allotted inputs and which, therefore, calls for extra effort and ingenuity, if only to circumvent the regulation. This "planners tension" is "abnormal feature" of the model.<sup>14</sup>

The system is socially stratified, although social mobility through approved

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<sup>13</sup> Alec Nove, *The Soviet Economy: An Introduction*, (New York: Praeger, 1961), pp.303-306.

<sup>14</sup> Jan S. Prybyla, *op. cit.*, p.115.

channels (the party, governmental bureaucracy, science, enterprise management) is encouraged.<sup>15</sup> The system blends advancement based on merit (especially technical merit) and allegiance to the party line, the latter bring the more important ingredient. Income differentials, while significant, are less decisive than privilege which depends on access to sources of decision-making at the top.<sup>16</sup>

### **Plan Strategy and China's Economic Reality: An Antithesis**

When China chose heavy industry-oriented development as its strategic goal, heavy industry's character arising from its capital intensive nature was in direct conflict with China's resource endowments and ability to mobilize resources at its stage of economic development at that time.

First, there was a conflict between the long time period required for constructing a heavy industry project and the scarcity of capital in China at the time. Heavy industry is a sector for supplying productive means or productive materials. It requires a much longer period for basic construction than does light industry. Moreover, due to the high capital intensity of heavy industry on the one hand a huge amount of capital has to be added continuously throughout the process of basic construction, and on the other hand, the period before capital return can be expected is significant. Therefore, during the process of heavy industry

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<sup>15</sup> Milovan Djilas, *The New Class*. (New York: Praeger, 1957); Isaac Deutscher *Stalin: A Political Biography*. (New York: Vintage, 1949, 1960), pp.338-40.

<sup>16</sup> Abram Bergson, *The Economics of Soviet Planning*. (New Haven's Yale U.P., 1964), pp.106-126, 178-200.



construction, a large amount of capital is tied up for a long period of time, and the interest burden is heavy. In the early period after the founding of the PRC, China's economic development was at a very primitive stage. GNP per capita was only RMB 104 in 1952. Such a low income level hampered capital accumulation. Therefore, capital was the most scarce factor of production. The scarcity of capital implied that the market-determined interest rate was very high. In the early 1950s, the monthly interest rate was around 2 to 3 per cent. No heavy industry project could afford such a high cost of capital.<sup>17</sup>

The second conflict was between the source of heavy industry equipment and the scarcity of foreign exchange. Given that heavy industry development was the core component of industrialization, a large amount of machinery and equipment had to be imported, thus implying a strong need for foreign exchange. At that time, China was basically a closed economy. The products that could be exported were limited in variety and quantity. Therefore, the ability to trade and earn foreign exchange was very low. In addition, the relationship between China and other advanced, capitalist countries was not normal. The ability to obtain foreign exchange was thus further circumscribed. This situation made developing heavy industry in China even more difficult.

The third conflict was between the funds required for a heavy industry project and the economy's ability to mobilize such funds. A heavy industry project

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<sup>17</sup> Justin Yifu Lin, Fang Cai, Zhou Li. *op. cit.*, p.30.

not only requires a longer period for construction, but also requires a larger initial investment than do projects in other industries, due to heavy industry's economies of scale. This is true for a single project, and especially true when a whole series of industrial projects are undertaken simultaneously. In such a case, it is very important that the nation be able to mobilize funds and other resources. In the early period of China's economic development, not only was capital scarce, but the economic surplus was small and was scattered in rural areas throughout China. The economy had little power to mobilize funds. For example, in 1952 state-owned banks' year-end total asset value was only RMB 11.88 billion, and the total deposit was US \$9.33 billion. They accounted for only 20.2 per cent and 15.8 per cent respectively of the GNP in that year.<sup>18</sup> Thus, it was impossible to develop heavy industry spontaneously in China at that time.

### **THE FIRST FIVE YEAR PLAN: THE CASE OF AGRICULTURE**

The basic purpose of reforms was to put the leadership in position to effectively implement the strategy of "selective growth under conditions of austerity". It meant the "quasi-total nationalization" or collectivization of the private sector in agriculture, industry, and trade, and a corresponding

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<sup>18</sup> Sheng Bin and Feng Lun (eds.), *Report on China's National Conditions*. (Liaoning: Liaoning People's Press 1991), p.521.

strengthening of governmental and party machinery.<sup>19</sup> Reconstruction and reform - Mao's "new democracy" - was merely a phase to be gone through before the inauguration of socialist modes of production and distribution.<sup>20</sup>

The top leadership of the Communist Party of China (CPC) was greatly influenced by the Soviet precedent of collectivisation of agriculture and there was complete unanimity among them to adopt the same for agriculture in China. But some leaders like Peng Duhai, Chen Yun, Sun Yefang were more wary about how collectivization was to be carried out, more fearful of the possible immediate consequences than others. There was no telling how the "rich" peasant class with large ownerships of land might react, how much violence and destruction co-operation might bring with itself. To the leadership in China, Stalin's way of dealing with peasant problem was both an inspiration and warning.<sup>21</sup>

Like the Soviets the Chinese started with land reform which gave land to individual peasant households. Both embarked on collectivization via lower level, transitional co-operative arrangements in which for a time voluntary participation by peasants played a dominant role.

The transitional arrangements in China consisted of (a) mutual aid teams, and (b) lower level agricultural producers' co-operatives. These arrangements

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<sup>19</sup> Jan S. Prybyla. *op. cit.*, p.146.

<sup>20</sup> *Ibid.*

<sup>21</sup> *Ibid.*, p.147.

lasted from about 1950 to 1955. Mutual aid teams were of two kinds : seasonal and year-round. "Peasants joining mutual aid teams worked together, while their land, draught animals, farm tools and other means of farm production remained their own private property, the farm produce of each piece of land went to the family that owned it...At the very beginning the organization of such mutual aid teams was temporary and seasonal, they were later developed into round the year mutual aid teams in which there was, on the basis of working together, a certain degree of division of labour and line, and a small amount of collectively owned property".<sup>22</sup>

The lower level (or elementary) agricultural producers' cooperatives "pooled land and practiced unified management and distribution of income. The principle followed in their distribution was that a smaller part of the income was distributed as land payment proportionate to the land pooled by the members, which was an expression of the continued private ownership of land (the land payment share varied from 30 to 60 percent of the crops harvested) while the greater part of the income was distributed as work payment according to the quantity and quality of the work done by the organizational form... put in practice in China's countryside from 1953 to 1955."<sup>23</sup> Each household was allowed a "retained plot" of arable land for private use. These plots were located in the pooled fields, the plot area

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<sup>22</sup> Liao Lu-yen. "Agricultural collectivization in China". in *Socialist Industrialization and Agricultural Collectivization in China*. (Peking: FLP, 1964). p.28.

<sup>23</sup> *Ibid.*, pp.28-29.

per head being fixed at a maximum of 5 per cent of the average arable land per head in the village.

The final step was the advanced agricultural producers' co-operatives or fully fledged collective farm in which land payment was abolished. "The co-operative members' privately owned draught animals, farm tools, and other major means of production were pooled and their money value turned into the collective property of cooperatives. After setting a part of the value of the draught animals, farm tools, etc., against the cost of shares necessary for membership, the rest of their value was repaid by the cooperatives in installments. After deducting the costs of production and management, reserve funds, public welfare funds and agricultural tax, all income of the cooperatives was distributed among the members according to the socialist principle "to each according to his work, and more income for those who work more".<sup>24</sup> Private plots were allocated to members of the collective according to the 5 per cent rule.

One of the striking similarities between Chinese and Soviet collectivisation was that, both, up to the last moment, assured the peasants that advanced collectivization was reserved for a fairly distant future, that for the time being individual agriculture would remain dominant, and that joining the collectivisation process would always be a question of the individual household's voluntary and unconstrained decision. Both reneged on the promise. Like the Soviet

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<sup>24</sup> *Ibid.*, pp.29-30.

collectivisation, the Draft First Five Year Plan (FFYP) stated that "by 1957, about one-third of all the peasant house-holds in the country will have joined the present agricultural producers' co-operatives of elementary form... The individual peasant economy still possesses a certain amount of latent productive power which should in suitable ways be brought into play as fully as possible to raise the yield per unit area".<sup>25</sup> As early as March 1953, and again in the spring of 1955, the moderate segments of the party such as Liu Shaoqi, (Liu Shao-Ch'i) Deng Xiaoping openly opposed hasty collectivisation. The left wing elements led by Mao Zedong, however, counterattacked in June, 1953. In November they consolidated their position in the course of the Third National Conference on Mutual Aid and Co-operativization. The Central Committee "Decisions on the Development of Agricultural Producers' co-operatives"<sup>26</sup> adopted in December 1953 said that "it is absolutely impermissible to try and carry out the socialist transformation of small peasant economy merely by issuing a call from above... compulsion, commandism, and expropriation of the peasant's means of production are criminal acts".<sup>27</sup> This was to be interpreted in a somewhat different manner two years later. After all, it was argued, a collectivization is not expropriation but merely a

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<sup>25</sup> First Five Year Plan for Development of the National Economy of the People's Republic of China in 1953-57. (Peking: FLP, 1956) p. 119-120.

<sup>26</sup> Jan. S. Prybyla, *op. cit.*, p. 152.

<sup>27</sup> Hsiao Shu, "The Peasant Question in the Socialist Revolution", Hung Ch'i (Hong Qi), No. 6, 1964 in *Peking Review (Beijing Review)*, (May 26, 1964), p.15.

change from individual to group ownership, and since each individual is part of the group, he is also part owner, and b) by definition, "collective ownership is established voluntarily by the peasants and handi-crafts men under the leadership, and with the assistance of the Party and the state power of the proletariat".<sup>28</sup> Those who reject that leadership and assistance and balk at proletarian power, are enemies of the people, bourgeois elements, freaks and monsters who do not count in the reckoning.<sup>29</sup>

In a decision adopted on March 3, 1955, the State Council spoke of insufficient experience and preparation in the matter of running collective farms, restiveness of the peasants, and loss of livestock and forest land resulting from both.<sup>30</sup> Mao answered his critics with a speech on July 31, 1955, which he referred to those who wanted to slow down the collectivization process as "tottering along like a woman with bound feet, always complaining that others are going too fast."<sup>31</sup> Even then, however, the Maoist program scheduled the absorption of half the peasant households in lower level co-operatives by 1958. The rest were to be absorbed between 1958 and 1960. As late as December 1955

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<sup>28</sup> *Ibid.*, p. 15.

<sup>29</sup> Jan S. Prybyla, *op. cit.*, p.152.

<sup>30</sup> Liu Shao-chi, "The Victory of Marxism-Leninism in China" (September 14, 1959), in *Collected Works of Liu-Shao-Ch'i 1958-1967*, (Hong Kong: URI, 1968), p. 55.

<sup>31</sup> Mao Tse-Tung, "On the Question of Agricultural Co-operatives", *People's China*, (November 1, 1955), pp.3-17.

Mao reiterated his conviction that collectivization would come in three or four years, i.e., by 1959 or 1960.<sup>32</sup>

Due to the heavy industry development strategy, except some institutional changes, nothing spectacular was achieved in agriculture. The neglect of agriculture and its low level of development got the communist leaders into a dispute. For instance, one of the accusations made against Lio Shaoqi (Liu Shao-Ch'i) and his group during the Cultural Revolution of the late 1960s was that they opposed the collectivization of agriculture arguing that mechanization should precede rather than follow the establishment of collective farms.<sup>33</sup> Liu was alleged to have held that agricultural machinery should be manufactured in series, in large, specialized, modern plants. Mao's position was that less complex equipment should be produced in local factories (artisan workshops), using what material there was, and turning out small and medium-size farm tools and sets of equipment.<sup>34</sup> It is pertinent to note that beneath these debates there was the question of power struggle between the "leftists" and the so called "rightists" in the CPC which culminated in GPCR with Maoist ideas dominating the course of various developments during this phase.

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<sup>32</sup> Mao's Preface to Socialist Upsurge in China's Countryside (Peking: *FLP*, 1957), p.8.

<sup>33</sup> Jan. S. Prylsyla, *op. cit.*, p. 163.

<sup>34</sup> "Struggle Between the Two Roads in China's Countryside," *China Pictorial*, No.3, 1968, p.2-7.



## **OUTCOME OF THE FFYP**

The preponderant stress of the First Five Year Plan on heavy industry had both internal consistency and a certain relevance to China's most acute needs. The Soviet model of development along with its complements - highly centralized mode of command planning, a hierarchical "one-man management" system, and a highly articulated structure of individual material incentives in industry answered China's pressing national needs. After decades of internal chaos and centralized authority was a national imperative. The unbalanced location of industry in the preliberation era as well as its unsatisfactory composition, reinforced the urge for centralization.

Rapid development of heavy industry also made sense in Chinese conditions of the early 1950s. The inherited industrial structure was highly skewed towards consumer goods production. Yet increasing the living standards of the population as a whole, which required above all the technological transformation of agriculture, could not be imagined without construction of the fuel, power, metallurgical, machine building and chemical industries which had a lot to do with considerations of military security reinforced this demand. Much that China was able to accomplish later, when priorities and strategy had changed, rested on the heavy industrial achievements of the FFYP.

Besides, the pronounced centralization that developed in the course of the FFYP had its advantages. Structural change was the order of the day. The rapid shift in the relative proportions of consumer goods and producer goods in total

output, and in the geographic disposition of industry from the coastal regions to the hinterland, arguably required highly centralized allocation of resources. There was also the question of equity: the party was committed to reducing the regional inequalities in the level of development and distribution of services; and central control over resources was effectively used to this end during the FFYP. A greater degree of regional and local autonomy would have pushed Chinese development along the path of widening distributive inequality. Yet, despite the advantages that accrued to the Chinese economy, there were major social and political consequences which didn't augur well for the People's Republic of China (PRC) in the long run.

Socially, the most significant result of the FFYP was the emergence of new patterns of inequality. The imperatives of rapid industrial development, or at least the manner in which it was pursued, gave rise to two bureaucratic elites, one was a political elite of communist leaders and cadres rapidly becoming administrators and functionaries in the growing state apparatus that presided over the industrialization process; the second was a technological elite of engineers, scientists, and managers necessary for the development and operation of the expanding modern economic sector. These newly emerging social groups tended to become increasingly motivated by professional and vocational ethics, rather than by Marxist goals and communist values, which had increasingly separated them from the masses of workers and peasants by virtue of status, power, and material

benefits.<sup>35</sup>

For the workers, the FFYP brought increasingly repressive conditions of life and work. Whether the factories were run by professional managers or party functionaries, the workers were subjected to increasingly repressive forms of control at the places they worked and, through the urban neighbourhood resident committees, at the places they lives as well. Besides this, inequalities within the working class grew itself as a result of wage differentials and monetary rewards based on skills and productivity were introduced.

Inequality was apparent in sharpening distinction between town and countryside. The industrialization of the urban areas was at the cost of exploitation of the countryside. While material conditions in the cities improved, the rural economy was largely stagnant, thus widening the economic and cultural gulf between the modernizing cities and the backward countryside.

The new educational system, heavily influenced by Soviet methods and curricula, tended to reinforce these tendencies towards social inequality and stratification. Moreover, to meet the needs of industrialization, the educational system in general and university education in particular, overwhelmingly emphasized science and technology which led to creation and perpetuation of a privileged technological intelligentsia.<sup>36</sup>

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<sup>35</sup> Maurice Meisner, *Mao's China: A History of the People's Republic*. The Free Press, 1979, p.135.

<sup>36</sup> *Ibid.*, p.136.

The political fallout because of the adoption of the Soviet model was grave as well. This model necessitated the development of Soviet forms of political organization and state administration. Centralized economic planning demanded the rapid bureaucratization and routinization of state and society.<sup>37</sup> The Maoist preference for simplicity gave way to complex and increasingly specialized structures; the cadres of a revolutionary party were transformed into administrators and bureaucratic functionaries; workers in factories were subjected to increasing control by factory managers; the revolutionary ideal of the "guerilla" generalists was replaced by a new-found faith in the virtues of specialization and the technological specialist; old egalitarian ideals clashed with a new hierarchy of ranks and the emergence of new patterns of social inequality; the revolutionary faith in the initiative and spontaneity of the masses and mass movements faded as industrialization demanded authoritarian discipline, social stability, and economic rationality; socialist goals were postponed and partly ritualized in favour of the the immediate and all-embracing goal of economic development.<sup>38</sup>

Another political result of the FFYP was the centralization and expansion in 1954 of central agencies. The general political structure that began to emerge in China in the mid-1950s increasingly resembled the Soviet state structure of

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<sup>37</sup> *Ibid.*, p.125.

<sup>38</sup> *Ibid.*

centralized "vertical" forms of bureaucratic rule and control.<sup>39</sup> As the formal state bureaucracy grew in size and power, the political and ideological authority of the CPC was diluted and its functions underwent significant changes.

As can be deduced from the foregoing, the radical changes in mainland Chinese society had, by the end of 1956, created numerous contradictions. The situation in the countryside was particularly tense. The exaction from the "advanced co-operatives" and the newly instituted "unified purchase and sale system" had resulted in food shortages and peasant demonstrations.<sup>40</sup> Communist cadres often made peasants work excessively long hours.<sup>41</sup> In August 1956 the Chinese press reported of wide-spread accidental deaths of rural infants in the countryside due to their mothers' being compelled to work in the field.<sup>42</sup> Elsewhere, the purge of Gao Gang of northeast China and Rao Shushih of east China in the suppression of dissent within the Communist Party over collectivization had a chilling and demoralizing effect.

Economically, there was the inadequate growth of agricultural production and procurement: a stagnation of grain output because of poor incentives had been

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<sup>39</sup> *Ibid.*, p.126.

<sup>40</sup> Wang Xuewen. "Critique of Certain Mistake Views on the System of Compulsory Purchase and Sale", *Xuexi*, no.7 (1956), pp.25-27.

<sup>41</sup> Yang Jiao. "Why We Should Not Neglect Individual and Current Interest of Labourers" *Xuexi*, no.7 (1967), pp.25-27.

<sup>42</sup> "We Should Not Allow Accidental Deaths of Women and Infants to Happen Again in the Countryside", *Renmin Ribao (People's Daily)*, August 12, 1956.

averted by the 'three-fix' policy in mid-1995, but at the cost of a decline in state procurement of food grain. Some means had to be found around the unhappy choice between too little growth and inadequate procurement. Moreover, the industrialization strategy of the FFYP had proved incapable of solving the unemployment problem. It was compounded by the continuing flow of rural migrants escaping poverty, natural disasters, and the turmoil of collectivization, and seeking secured and better-paying jobs in cities. Neither the capital intensive strategy of the FFYP nor the administrative capacity of the government was capable of responding adequately to the problem.

Lastly, planning and administration, in their highly centralized form, had become increasingly ineffective as the economy grew in size and complexity, and especially after virtually all industry and commerce came under direct state control in 1956. The decentralization measures of 1957-58 were supposed to deal with this problem by giving provincial authorities more scope for planning regional development. China's leaders were looking to a rather different distribution of authority between centre and localities during the Second Five Year Plan.

Thus, what was needed, was a strategy that in comparison with the First Five Year Plan would give greater attention to agriculture, negate the evils of centralization, give greater initiative to localities (and/or to enterprises), and turn China's redundant labour force into a strength instead of a weakness. Such objectives fitted very nicely with the CPC's preference under Mao's leadership for a mobilizational strategy based on administrative decentralization.

## **CHAPTER II**

### **Maoist Decentralization: The Great Leap Forward (GLF)**

## MAOIST DECENTRALIZATION: THE GREAT LEAP FORWARD

At the end of the First Five year Plan, the People's Republic of China was characterized by various problems in the social, political and the economic spheres. This led to the development of an indigenous model of economic development as a solution to the various ills that gripped Chinese economy. There was a growing realization of the limitations of the Soviet model.

According to Gordon White, the failure of the Soviet model led to the development of two different varieties of "Maoisms", namely "developmental Maoism", and "radical Maoism".<sup>1</sup> The former, which emerged during the mid-1950s reflected to a considerable extent Mao's own diagnosis of defects in the Stalinist model. This was the motive behind the the Great Leap Forward and the formation of the "rural people's communes" in 1958. This brand of Maoism drew on his experience in the 1930s and 1940s in the northern revolutionary base area of Yenan during the war against Japan. The latter variety which developed during the early and mid-1960s led to the development of this new paradigm of socialist development. In this view, the "socialist" society already established in China, the Soviet Union and other "socialist" countries embodies certain vested interests and

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<sup>1</sup> Gordon White, *Riding the Tiger - The Politics of Economic Reform in Post-Mao China*, The Macmillan Press Ltd., 1993, p.22. (For two Classic statements of radical Maoism in the 1970s, see Yao Wengyuan, "On the Social Basis of the Lin Biao anti Party Clique", *Peking Review*, (*Beijing Review*), 10, 1973, pp.5-10 and Zhang Chunqiao, "On Exercising all round dictatorship over the bourgeoisie", *Peking Review*, (*Beijing Review*), 14, 1975, pp.5-11.



incipient class forces which obstructed the volume of genuine socialism and threatened a "reversion to capitalism". Thus institutions and people needed continually to be transformed alongside economic and technical modernization. This transformation involved a prolonged political struggle waged by a "proletarian" party conducted under the banner of "the continuation of class struggle in socialist society" in a process of "continuing revolution" – this was this was the ideological basis of the Great Proletariat Cultural Revolution in 1966.

## **DEVELOPMENTAL MAOISM**

Developmental Maoism levelled a double critique at the Stalinist approach to development. First, in terms of development strategy, Soviet planners had given priority to industry over agriculture heavy or light industry and capital or labour intensive technology. By contrast, Mao argued in the mid-1950s that the state should give greater attention to agriculture and light industry which were more appropriate for an under developed country like China and which, over the longer term, would generate funds to be ploughed back into heavy industry. In choosing technology, Mao emphasized the need to "walk on two legs"<sup>2</sup> towards industrialization, using intermediate and "native" as well as advanced foreign technology, and encouraging (small-scale) industrialization by local collectives as well as in the state sector, in the countryside as well as in the cities.

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<sup>2</sup> *Ibid.*, p.23.

Second, in terms of political and economic institutions, Mao criticized the Soviet model for being overcentralized and "top-down" and argued for greater decentralization of power to local governments and collective institutions (notably the communes) according to the principles of local "self-reliance" and "two enthusiasms are better than one".<sup>3</sup> The distinctive role of the party was to galvanize the state's administrative machine and mobilize the population for developmental purposes through wave after wave of mass movements. This was a "revolutionary" state in the sense that its role was to lead an "uninterrupted revolution", a developmental process marked by qualitative "leaps forward" in a continuing struggle against economic backwardness.

### **Developmental Maoism and the Yanan Model**

The economic philosophy of Mao was shaped to a great extent by the context of the "New Democracy" which he envisaged in the pre-liberation days. "New Democracy" was the system which replaced the "Soviet system during 1937 in line with the united frontage principles"<sup>4</sup>. New electoral laws were proclaimed in May 1937 which were based on universal suffrage and the right of all political parties to nominate candidates. These good laws envisaged a hierarchy of elected councils at township, district, county, and regional levels, each supervising the work of an executive body. The goal was an alliance of diverse classes, all defined

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<sup>3</sup> *Ibid.*

<sup>4</sup> Andrew Watson (ed.), *Mao Zedong and the Political Economy of the Border Region*, Cambridge University Press, (CUP) 1980, pp.13-14.

as revolutionary in the context of a colonial or semi-colonial country fighting against imperialism and the vestige of feudalism<sup>5</sup>. In sum, the New Democracy was that which laid the groundwork for the maximum programme which envisaged the transition to socialism. The gain for the communist party was the broadest base of support possible.

Mao was concerned with a mixed economy and with the welfare of the masses of ordinary peasants who made up the private sector. The party, Mao opined, would only win their support if it could its practical ability in economic management. In order to have a sound economic management, "self-reliance" and "primitive accumulation" had to compensate for the lack of capital resources. There was no alternative to organizational reform, intensive use of labour to exploit available land and resources, and improved use of traditional techniques. Mao promoted innovations along these lines so long as they did not undermine the stability of the existing economic structure and thus weaken peasant support. The most radical experiment was the introduction of self-supporting production in the public sector. This brought immediate financial returns, created some key public enterprises, and provided a model of decentralized economic growth. In all the policies put forward, Mao argued that success depended on positive action by the Party and government, and on the stimulation of mass enthusiasm. Innovations should build on existing practices but not go beyond what was acceptable to the

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<sup>5</sup> *Ibid.*

peasants. The model of economic development just described, formed the starting point for Mao's approach to economic problems on the eve of the establishment of the People's republic.

Mao's position on many of the issues involved in the New Democracy model started changing around 1953 and his concern with rural problems was already pointing towards the development strategy he would expound from 1955 onwards. It is often noted that Mao made many positive comments on learning from Soviet experience and that his aim of achieving rapid industrialization inclined him towards the centrally controlled, heavy-industry oriented strategy that characterized the First Five Year Plan.<sup>6</sup> He later said that the First Five Year Plan was "essentially correct".<sup>7</sup> Nevertheless, Mao's willingness to adopt the Soviet experience must be seen in the perspective of his earlier differences with Stalin and the Comintern, and his growing criticism of Soviet methods and Stalin after 1953.<sup>8</sup> Furthermore, his involvement in an agricultural collectivization programme which differed markedly from Soviet practice soon led him to raise important questions about the balance of investment between industry and agriculture, the

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<sup>6</sup> C. Howe and K.R. Walker, "The Economist", in D. Wilson (ed.), *Mao Tse-Tung in the Scales of History* (CUP, 1977), pp.185-86.

<sup>7</sup> "Speech at the Second Plenary Session of Eighth Central Committee, 15 November 1956, *Selected Works of Mao Tse-Tung*, vol.5, p.333.

<sup>8</sup> Stuart Schram, *The Political Thought of Mao Tse-Tung*, Penguin Press Ltd., 1969, pp.415-18.

implications of that balance for overall development, and its ultimate effects on the political alliance between workers and peasants on which the Party depended. In addition, the formal, the centralized bureaucracy and professional decision-making implicit in the Soviet model, contrasted sharply with the principles of decentralization and mass-line operation which had distinguished Mao's approach to political and economic leadership before 1949.

One of the most significant factors which contributed to the development of Mao's economic policies was his thinking on the relationship between the relations of production and the productive forces and between the superstructure and the economic base. Although in Yen-an Mao had proposed organizational reform such as the establishment of cooperatives and exchange-labour teams as a means of expanding production, such innovations were not at the time seen as a shift from "capitalist" relations of production to "socialist" relations. Similarly the changes in organization and ownership associated with the new-democratic model were intended to facilitate the growth of a modern industrial country on the basis of which the transition to socialism would be made.<sup>9</sup> Thus, changes in the relations of production might lead to growth in the productive to forces but it was changes in the economic base as a whole that would enable the eventual transformation of society.<sup>10</sup> For many Chinese leaders, similar assumptions about the need for

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<sup>9</sup> Andrew Watson (ed.), *op. cit.*, p.43.

<sup>10</sup> *Ibid.*

building up the economic base as preconditions for further advance in the superstructure, underpinned the Soviet model of the First Five Year Plan. Nevertheless, Mao's experience and his military philosophy which saw the role of morale, ideology and commitment as more decisive than the actual weapons used,<sup>11</sup> indicate that he was not mechanical in his conception of the relationship between material and social conditions. That is, he did not assume that the economic base automatically determined the superstructure but that the latter could also affect the former. Indeed, he later claimed that the Yenan cooperatives did contain the "sprouts of socialism"<sup>12</sup> and he criticized Stalin for not considering the role of the superstructure in helping to change the economic base.<sup>13</sup> During the early 1950s, Mao was already stressing such points when he linked changes in the system of the productive forces and "socialist industrialization" with the "cooperative transformation of agriculture".<sup>14</sup> Subsequently, the practical and theoretical issues

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<sup>11</sup> "On Protracted War", May 1938, *Selected Works of Mao Tse-Tung*, vol.2, p.143.

<sup>12</sup> "Talks at the Cheng tu Conference", March 1958, *Wansui*, 1989, p.175. Translated in Stuart Schram, *Mao Tse-Tung Unrehearsed* (Penguin 1974), p.117.

<sup>13</sup> Speech on the book, "Economic Problems of Socialism", November, 1958. *Wansui* (1969), p.248. translated in *Miscellany of Mao Tse-Tung Thought*, [Joint Publications Research Service (JPRS)], pp.129-32.

<sup>14</sup> "Two Talks on Mutual Aid and Co-operation in Agriculture", October and November 1953. *Selected Works of Mao Tse-Tung*, vol.5, p.134.

involved became the center of debate within China on the questions of whether agricultural mechanization should precede or follow collectivization, and of debate between China and the Soviet Union over the nature of people's communes and their implications for the building of communism.<sup>15</sup> If Mao was correct, China could move quickly towards a socialist society than either the new democratic or Soviet model allowed. And practical economic policies could reflect that goal. If he was wrong, he was guilty of attempting the impossible and might hinder the development of that country. The division between Mao and his colleagues on this issue and its practical implications contributed substantially to the evolution of what Gordon White calls "radical Maoism" which culminated in the Great Proletarian Cultural Revolution (GPCR).

In sum, Mao's analysis of the stage of development in China after 1949, his concern with the relative importance of the economic base and the superstructure in the transition to socialism, and his experience of the Soviet model in the early 1950s, resulted in the evolution of economic policies that increasingly diverged from Soviet practice. And as part of that process he turned to the experience of Yanan and stressed its applicability to the economic problems China faced.<sup>16</sup>

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<sup>15</sup> Jack Gray, "The two Roads: Alternative Strategies of Social Change and Economic Growth in China", in Stuart Schram (ed.), *Authority, Participation and Cultural Change in China*, (CUP), 1973, pp.139-144.

<sup>16</sup> *Selected Works of Mao Tse-Tung*, vol.5, pp.184-207.

## **RADICAL MAOISM**

"Radical Maoism" offered a critique of Stalinist institutions and advocated ways to reform them. At the ideological level it called for a struggle against forms of Marxism-Leninism which allegedly fostered capitalism, notably Soviet "revisionism"; at the institutional level, the target was bureaucratism which was to be attacked through constant ideological education of officials, their repeated involvement in manual labour or visits to the grass-roots to practice "the mass line", and their participation in institutions which contained mass representatives<sup>17</sup> (such as the "revolutionary committees" set up to run units during the Cultural Revolution or the "three in-one" innovation groups set up in factories which combined workers, technicians and managers). Besides, in the context of the early and mid-1960s, it also sought to defend them against those in the Soviet Union and other Eastern European countries who were moving in the direction of "market socialism"<sup>18</sup>. "Revisionist" ideas about the need to encourage market mechanisms, provide economic incentive for workers and grant more autonomy to productive enterprises – elements of an embryonic version of what was later to become a more fully fledged "market socialist" paradigm were current in China in the early 1960s and had attracted the attention of key leaders like Chen Yun and

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<sup>17</sup> Gordon White, *op. cit.*, p.23.

<sup>18</sup> *Ibid.*



Deng Xiaoping in the CPC. It was against this ideological trend that the Cultural Revolution was directed. Maoists were violently opposed to any hint of market socialism and vociferously denounced what they saw as "bourgeois" innovations, such as individual material incentives to spur productivity, profits as an index of enterprise performance, the play of supply and demand as a stimulus to greater economic efficiency, and expanded links with capitalist economies abroad.

## **DECENTRALIZATION AND THE GREAT LEAP FORWARD**

Mao's answer to the problem of rigid over centralization and bureaucratism inherent in the Stalinist system of planning and management is usually seen as achieving its structural foundation as in the 1957-58 reforms. Although further changes occurred subsequently, including another major decentralization in 1970, the reform of the late 1950s was until recently, generally taken to have established the principal outlines of the planning and management system that endured until the reforms of the mid 1980s began.

The Eighth party Congress of 1956 called for a strengthening of dual rule in all agencies of government. This put an end to the development toward centralized vertical rule of the early 1950s. But it also paved the way for decentralization in 1957, on the eve of the Great Leap Forward. The Eighth Party Congress initiated a discussion of decentralization that mainly found expression in academic particularly economic journals. The discussion intensified greatly in

1957, partly because of legitimization by the great economic recognitions carried through by the Soviets in May 1957. Decentralization was one of the major topics discussed in the meeting of the Third Plenum of the Central Committee which lasted from September 20 to October 1957. The length of the meeting indicates that basic changes in policy were discussed.<sup>19</sup> Some of the most critical policies leading to the Great Leap Forward were decided during this meeting. However, there was complete unanimity regarding decentralization. But, decentralization can take two different paths: either decision making powers are put into the hands of the producing units themselves. (decentralization I) or they are put into the hands of lower echelon administrative units (decentralization II)<sup>20</sup>. There were sharp cleavages of opinion among the members of the politburo as to what "correct" economic strategy should be.

The question of decentralization led to two different views, of which one was headed by Mao, who advocated a policy of social mobilization in order to achieve rapid economic growth. Another group, headed by Chen Yun advocated a policy of material incentives in order to achieve a more balanced, though slower, economic growth. These divergent opinions had different consequence for the

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<sup>19</sup> Franz Schurmann, *Ideology and Organization in Communist China*. University of California Press, Ltd., 1966, p.195. The following discussion has benefitted greatly from this work.

<sup>20</sup> *Ibid.*, p.196.

centralization-decentralization problem. There were some members of the politburo like Hsueh Mu-ch'iao (Xue Muqiao), head of the State Statistical Bureau, who called for a policy of simultaneous centralization, decentralization I, and decentralization II. The central economic agencies would retain planning controls only over a small number of vital products. The central ministries and provincial governments would be allowed to impose planning controls over a long range of products not covered by central economic controls, but considered important for the production programmes of these administrative agencies. Production planning for all other products would be determined by the enterprises according to supply and demand, that is, the market. Thus, the central branch agencies provincial government, and individual enterprises would each acquire greater decision - making powers.

The divergent approaches to decentralization obviously raises questions regarding what was at stake when the policy of decentralization was to be adopted. The issues which went a long way in contributing to Mao's administrative decentralization are mainly four: a) the issue of *control* b) the question of *distribution*, c) the question of *values* and d) the *incentives*.

First at stake, was the question of *control* - how much direct control the party should continue to exercise over economic affairs. The market socialist option (which Schurmann calls decentralization I) involved a loss of direct control by the Party as a whole, the administrative decentralization approach (Schurmann's

decentralization II), meant a redistribution of party control from centre to regions. Second, there was the question of *distribution*. Both kinds of decentralization were likely to increase the relative access of resources to more advanced provinces and localities, in comparison with the highly centralized system under which resources were routinely transferred from richer to poorer regions. There was also a question of *values*: centralized control could be exercised according to broad political criteria (control by the state council) or according to narrower economic criteria (control by the ministries). Decentralized control would clearly be less political in nature under a market oriented variant, but even administrative decentralization would give rise to a range of possible objectives, from the "purely" economic (e.g. maximizing local growth) to the largely ideological, and including the desire to enhance local bureaucratic power. Finally, there was an *incentive* problem to consider: how could workers, managers, and local planners be motivated towards diligence and efficiency while gearing their work to the central plan?

After intense debates and discussions what came out of the Third Plenum was a clear cut decision for decentralization II. Mao's chosen strategy – administrative decentralization contained an answer to the questions raised above : social mobilization and the intense propagation of correct ideological values would ensure appropriate distribution, effective incentives, the right use of local powers and therefore, adequate central control. The State Council decisions announced on 18 November, 1957 embraced the organizational underpinnings of

the GLF strategy by endorsing administrative decentralization.<sup>21</sup>

### **The Great Leap Forward (GLF)**

The Great Leap Forward (GLF), which gathered momentum in the winter and spring of 1957-58 epitomized Mao Zedong's response to the complex set of problems left by history and, more immediately by the First Five Year Plan strategy. The early stages of the Leap involved experiments with larger scale units of organization during the agricultural slack seasons of winter 1957-58. Several co-operatives were encouraged to work together on projects such as dam building and other water-control work. The idea was to rely on local people and resources in preference to asking for state aid.

In industry, ambitious slogans appeared on factory walls, urging the workers on to new goals. At first these were realistic; "Overtake England in steel production in fifteen years" was a plausible target. However, the time period of the slogan was progressively reduced from ten years to five and even, in couple of areas, to three years. The slogan "More, better, faster, and cheaper" appeared everywhere.

There was also an intensification of a campaign begun somewhat earlier to send young urban intellectuals to the countryside to "take root, flower, and bear fruit." Known as the *xiaxiang*, or "sent-down" youth, they were expected to share

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<sup>21</sup> Carl Riskin, *China's Political Economy - The Quest for Development Since 1949*, Oxford University Press Ltd., 1987, p.104.

their intellectual knowledge with the peasants while at the same time learning agricultural techniques that would enable them to raise more food for China. This fit in well with Mao's desire to reduce the differences between city and countryside.

Another slogan associated with the GLF was "walk on two legs" with one leg representing the modern sector (as, for example, heavy industry with its need for expensive machinery, or, in the health field, up-to-date Western medical procedures) and the other leg representing the traditional (labour-intensive spinning and weaving techniques in the textile industry, and traditional Chinese medicine in the health field). The scientific method and research projects of all sorts were castigated as bourgeois.

In August 1958, large -scale agricultural units called the Rural People's Communes were formed by combining several co-operatives. These communes played a very vital role in the economic social and political life of rural China since 1958. Emerging as an amalgamation of collectives trying to mobilize enough labour for the unprecedented mass irrigation campaign of winter 1957-58, they were quickly seized on and popularized by the Party. A Chinese commune was not only a large agricultural co-operative, but a composite unit of local government that encompassed the whole range of economic, social, administrative and political functions for the rural community. Its essential purpose was to organize and mobilize the rural population to develop their land and other resources in order to

meet their essential needs on the principle of "self-reliance" while at the same time reducing social inequalities and creating a rural society based on justice and equality.<sup>22</sup>

## **ORGANIZATION OF COMMUNES**

A Commune was divided into a number of production brigades, which were further sub-divided into production teams. As for the size of a Commune there were wide differences in the number of brigades and teams in a Commune. In some densely populated areas, a Commune could have thirty, to thirty five brigades and three hundred to four hundred production teams, but some had only five to ten brigades and only fifty to hundred production units.<sup>23</sup>

A production team of ten consisted of a natural village or cluster of houses with twenty, thirty or forty families or hundred to two hundred members, cultivating anything from ten to forty hectares, depending on population density in relation to available land.<sup>24</sup> The production team was the basic production and accounting unit which owned the land and was responsible for all the decisions

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<sup>22</sup> Sartaz Aziz, *Rural Development - Learning from China*, Macmillan Press Ltd., 1978, p.47. The Section on Communes has benefitted greatly from this work.

<sup>23</sup> *Ibid.*, p.48.

<sup>24</sup> *Ibid.*

involving the deployment of available manpower, managing production and distributing the income generated by the production team. The overall planning of production was subject to certain guidelines such as quotas for grain and basic commodities which had to be sold to the state at fixed prices and minimum or maximum quotas for certain other agricultural products such as fruit, vegetables, fish or meat, but the production team had some flexibility or discretion in meeting different quotas. Similarly, the production team had substantial autonomy in making investment decisions involving its own labour and savings, such as buying agricultural machinery, planting an orchard or improving its irrigation facilities. In practice, the production team was the most important unit of rural organization in China's countryside.

The production brigade co-ordinated the annual production plans of the teams on the basis of quotas assigned by the Communes and allocated certain agricultural inputs such as fertilizers and pumps. But its more important functions were to undertake investment and development activities on a scale that was too large for the production team. The brigades may set up livestock farms, Vegetable gardens, fruit orchards and small scale industries. In addition, it provided certain social services like primary schools and health clinics. Brigades could also organize credit co-operatives or militia units; in some cases, they served as the accounting unit, but these were not common. The brigade also served as the seat of the party branch and is thus the lowest level at which the party operated through



direct contact with the rural population.

The commune not only co-ordinated, supervised and guided all these activities of production teams and production brigades, but also discharged supplementary functions which were beyond their capacity or scope. It undertook larger projects requiring a considerable work force or substantial financial resources, such as large water conservancy projects or rural roads and industrial units. In addition, it provided supplementary social services, particularly secondary education and hospital facilities. The main political function of the commune was to supervise and implement the political and administrative policies of the government and to strengthen the ideological and political basis of the rural society. The communes performed certain other functions, such as military training, control of the movement of population and the collection of government taxes. The next higher level of state government - the county, would maintain certain offices in a commune, but these were largely, supervised by the communes and some were being absorbed by the communes. Thus, while in its political role the commune was responsible for implementing governmental policy at the local level, its economic role was to provide leadership, guidance and assistance for agricultural and rural development through production planning, provision of essential inputs, the diversification of the rural economy and provision of certain social services. The extent to which a commune would perform these economic functions effectively depended on its initial success in mobilizing resources, either

through brigades and teams or through its own projects and enterprises.

### **The Working of the Commune System**

The commune system was the direct outcome of Maoist decentralization and so enjoyed autonomy in the performance of its essential functions within the overall political framework and national policy on the use of national resources or the pattern of rural institutions. The communes had a wide measure of autonomy for a whole range of economic and developmental functions. The communes and its constituent units were free to decide the best use of their land, water and human resources and how to distribute, save or invest their income. Even in the case of production planning, which was geared to certain national targets and quotas, the communes had in practice a great deal of flexibility in altering or exceeding the quotas.

The various factors working in favour of commune system were as follows. First, the surplus labour force available in the rural areas was greatly facilitated by its policy of collectivization and that success in turn created the impetus and the resources for the next stage in China's rural programme. Second, the success of the Chinese communes was its ability to diversify the rural economy, first within the agricultural sector, to forestry, fisheries and livestock and then to small industries, based on local raw materials or tools producing machinery and other inputs for agriculture. Third, the system of rural education and training in China was geared to educating and training the rural population for work within the

commune. Four, the success of the system was its role in planning. The system of communes provided a very effective mechanism of local planning, in accordance with the simple philosophy "from the bottom, up and from the top down". The merit of their system was its emphasis on maximum exploitation of local resources for meeting local needs. Finally, the transition from agricultural to rural developmental is not complete until the rural community had established effective links with higher political and administrative levels and integrated its planning and development activities with national targets, goals and policies. This becomes increasingly important as a rural community moves into more advanced stages of agricultural and rural development. Requirements of inputs have to be co-ordinated at the provincial and national levels and surpluses and deficiencies had to be absorbed or provided for. The Chinese commune, while fairly autonomous and decentralized on questions of land use, relative priority of locally financed projects and distribution of the income generated by it, was on the whole, well integrated in the process of planning at the county, provincial and national levels.

#### **MAO'S TEN MAJOR RELATIONSHIPS AND THE GLF**

The rejection of the Soviet model led to a new developmental strategy under Mao's leadership. The rejection of the Soviet models, and the new Maoist developmental strategy was implied in Mao's speech *On The Ten Major*

*Relationship* ~~On April 1956.~~<sup>25</sup> Mao called for greater attention to agriculture and linkages between industry and agriculture. Mao expanded this analysis of sectoral balance in "on the ten major relationships".<sup>26</sup> Successful development, said Mao, depended on correctly understanding the interdependence between industry and agriculture.<sup>27</sup> Light industry was an important mediator between heavy industry and agriculture. By producing consumer goods it helped to raise peasant standards and this, after all, was one of the goals of development and one of the proofs that socialism was better than the traditional economy. It also accumulated funds for investment in heavy industry through its trade with the agricultural sector. Thus the correct way to develop heavy industry was also by stimulating light industry and agriculture. Although technological change through increased inputs from modern industry was essential in the long run, initially agriculture had to be accumulated within that sector, and such accumulation could only be achieved through co-operative transformation. Mao's political concern for building socialism in the countryside cementing the worker peasant alliance was thus closely integrated with his economic analysis.

Mao emphasized on a mixture of technologies in agriculture with reliance

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<sup>25</sup> Mao Tse-Tung (Mao Zedong), "On the Ten Major Relationships", (April 25, 1956), in *Selected Works of Mao Tse-Tung*, vol.5, (Peking: [Beijing] FLP, 1977), pp.292-95.

<sup>26</sup> See *ibid.*

<sup>27</sup> Andrew Watson, (ed.), *op. cit.*, p.46.

on traditional methods, wherever effective, which was reflected in his insistence that industrial policy should include the development of large, medium and small factories using a mixture of labour, capital and technology to local conditions.<sup>28</sup> Reliance on large plants using modern technology required human and capital resources in short supply. If all resources were to be tapped, it was necessary to be more flexible in the means used.

Two other factors also permeated Mao's approach. One was a concern with the well being of people and improvements in their livelihood. The peasants should not be "squeezed" as they had been in the "Soviet Union".<sup>29</sup> Furthermore socialism should raise their standard of living, not decrease it, nor simply maintain it. Mao insisted that each stage of co-operative transformation should and would result in an improvement in the peasants' material conditions. The second factor was emphasis on "self-reliance". This was at first a policy for development within agricultural co-operatives or within localities, but later it came to apply the country as a whole.

One of the major aspects which Mao stressed during his speech *On the ten major relationships*, was the question of regional balance. While it was essential to develop industry in the backward regions in land, Mao advocated, it was also

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<sup>28</sup> *Ibid.*, p.47.

<sup>29</sup> *Ibid.*

important to make full use of the infrastructure in the relatively developed coastal areas. While it was necessary to build national unity and central discipline, it was necessary to allow local authorities, some independence and initiative. Mao argued that in the FFYP coastal industry, particularly light industry, had been relatively neglected, and there had been too much centralization.<sup>30</sup> Excessive centralization had two bad effects. First, it restricted the possibilities for developing resources in the localities. Second, since central control was expressed through a variety of agencies and their local branches, there were often considerable problems of coordination and many computing demands were made on local authorities.

Mao saw greater consultation and the handing over of some responsibilities to lower levels as ways of combating the above mentioned problems. He wanted a form of regional decentralization rather than decentralization by economic sectors or economic units.

As early as 1956, Mao Zedong pointed out that under the centralization system, the relationship between the center and localities was a "contradiction". The main problem was, he explained, that the local powers were too restricted. It was necessary to enlarge local power and grant localities certain independence under the central plan, because, Mao argued, "two enthusiasms" (which referred to enthusing of both central and local governments), were more beneficial than

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<sup>30</sup> *Ibid.*

only central control.<sup>31</sup> In order to stimulate local authorities enthusiasm and creativity in socio-economic construction and to reduce the central government's heavy administrative and financial burdens by shifting certain economic controls to the provinces, Mao launched adjusting programmes three times between 1957 and 1970. These programmes represented attempts to resolve the troubling dilemma in central-local relations. The results, however, were not satisfactory. When the center interested more power to local authorities, the local governments used every means to extract profits from the enterprises in their regions, leaving the central government with a revenue shortage; meanwhile, the redundant construction projects in regions and unreasonable competition among provinces worsened. Troubled by these difficulties, the center was forced to take back some power which had been transferred to the localities previously. As a result, however, local enthusiasm for economic development was severely damaged again.

The first attempts at decentralization came during the GLF. On November 18, 1957, the state council announced three regulation on changes in the system of industrial, commercial and financial administration. These can be briefly detailed as follows. First, on industry the most important change was the transfer to provincial governments of a broad range of industries. This included: almost all

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<sup>31</sup> Refer footnote no.25.

light industry, non-strategic heavy industrial enterprises, the timber industry, ports, some enterprises under the jurisdiction of the Ministry of communications, and construction enterprises. The principle of dual rule was to be universally implemented in industry. Enterprises still subject to central jurisdiction were henceforth to be linked to regional authorities through dual rule. Regional authorities acquired greater powers over allocation of materials. They now got a greater share of above budget production, as well as share of enterprise profits. Regional authorities, also acquired greater control over personnel, including those working in central state owned enterprises.<sup>32</sup> The planning system was greatly simplified, with greater leeway given to factory managers to practice flexibility. The system of profit-sharing made it possible for enterprises to derive some of their investment funds directly from enterprises' profit.

Second, on commerce. As in industry, a broad range of commercial agencies and enterprises were placed under provincial control. The big "specialized commercial corporations", which earlier had acquired needed goods, for central government agencies, were abolished. Wholesale trading stations, formerly entirely under central control, now partly come under provincial control. The planning system was greatly simplified. A profit sharing system was introduced, and provincial authorities were given greater control over enterprises' profits (this to

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<sup>32</sup> Control of Personnel was one of the major aims of Party Organization in Economic Units.



be done "gradually" and "experimentally"). Provincial authorities were given the right to set some prices in their areas of jurisdiction, although here too "the regulations indicated that great care had to be exercised, and all efforts, made to achieve co-ordinations in price setting between the center and the provinces. As in industry, the principle of dual rule was universally introduced into the commercial network.

Third, on finance. Unlike in the other two sectors, no structural rearrangements were made, and no mention was made of dual rule.<sup>33</sup> The regulations on finance laid down general lines of revenue division between the center and the regions, with the latter given a greatly increased share of budgetary revenue. The regulations on financial administration indicates no major structural changes in contrast to the regulations on industrial and commercial administration.<sup>34</sup> This conservatism undoubtedly reflected the great sensitivity which the Chinese communists have always shown for financial matters, and the fear that decentralization of monetary and credit controls might have adverse consequences, such as inflationary pressures.<sup>35</sup>

The regulation on the decentralization of industrial administration consisted of two parts. One was called "suitably enlarging the authority of provinces.

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<sup>33</sup> Franz Schurmann, *op. cit.*, p.208.

<sup>34</sup> *Ibid.*, p.209.

<sup>35</sup> *Ibid.*

autonomous regions and directly attached cities, over the management of industry"<sup>36</sup> the other was called "suitably enlarging the managerial authority of personnel in charge of enterprises over the internal (affairs) of the enterprise".<sup>37</sup> The first clearly constituted decentralization II, the latter, at least, constituted a degree of decentralization I. If both had been carried in spirit and in letter, a kind of checks-and-balance conditions would have been created, marked by the juxtaposed authorities of provincial cadres and enterprise managers. This would have increased centralization of power at the regional level. However, since actually decentralization II took place, says, Franz Schurmann, a rapid process of province level centralization set in. An example of local centralizing tendencies was provided by the communes formed in the summer of 1958. Far from allowing the actual producing units, namely brigades and teams, to enjoy the fruits of decentralization, commune headquarters tried to manage them centrally, much as earlier the ministries had managed the agencies and enterprises under their jurisdiction. What happened in the communes was repeated at the level of the provinces.

The implementation of decentralization II had a profound effect on the functions of government in communist China. Provincial government emerged as a powerful level of administration with great control over the economic system.

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<sup>36</sup> *Ibid.*

<sup>37</sup> *Ibid.*

specifically over supply, production, and sales. The GLF's unrealistically high targets, their hasty implementation, and the extreme emphasis on the growth of iron and steel production encouraged the local authorities to irrationally use their power in blind extension of local iron and steel industry. The resulting serious economic dislocation and resource scarcities caused the national economy to fall into great disorder and imbalance in the first half of 1959.

In order to restore the national economic order, beginning in the second-half of 1959, the central government gradually took back most of the power which had been transferred to the localities during the period 1957-58. By 1961, central-local relations returned to the old situation in which the central planning controlled all the local production and allocations, consequently, local development declined sharply soon thereafter.<sup>38</sup>

Two further attempts to change the *status quo* occurred in 1964 and 1970. In 1964, the local governments were granted greater power to allocate revenue resources and products on materials. They also gained more power to decide the scale and pattern of investment. In 1970, local controls over economic development were further reinforced. The power to manage about two thousand large and medium-sized industrial enterprises, construction companies, and other

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<sup>38</sup> Zhong Zhu Ding, "Mainland China's Dilemma: Central-Local Conflicts in Economic Management". *Issues and Studies*, September 1995, p.21.

economic entities was shifted from the central level to the local level.<sup>39</sup> To stimulate local potentialities, the provincial power of capital allocation was institutionally ensured by the central policy. The system allowed the provincial authorities to distribute autonomously a considerable ratio of local revenue allocation for local development. The provincial government were also granted the right to participate in decision making for the division of national revenue allocations. Under this system, the provincial authorities had power to control 30 per cent of capital construction investment; another 30 per cent was agreed upon jointly by the central government and the provincial government; and the remaining 40 percent was directly controlled by the central government.<sup>40</sup>

The reformed system effectively stimulated local governments' enthusiasm to enlarge their local industries and promote socio-economic development. However, it also brought crises and disorder to the national economy from unbalanced local industrial development and redundant construction projects. The system remained in operation until a new strategy was launched in 1972 by the central authorities following adoption of the policy of "readjustment, restructuring, consolidating, and improving the national economy". Under the new strategy, central planning was reimposed in many economic areas. This new policy favoured

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<sup>39</sup> *Ibid.* p.22.

<sup>40</sup> Ren Luosun, "Changes in China's Economic Management". *Peking Review*, (*Beijing Review*), vol.23, (Feb. 1980), p.22.

light industry as opposed to heavy industry. The related policy of narrowing the scope of capital construction created problems, particularly because the demand for machinery decreased, leaving many engineering concerns with insufficient work to do. Factories which had found themselves in this position were forced to explore other channels, such as producing for export or manufacturing accessories and spares. In these circumstances, the national economy suffered another period of inactivity.

Until 1978, all attempts at modifying central-local relations focused on readjustment of control limits between the central and local governments, with almost no attention paid to the economic relations between the state and enterprises. Consequently the real problems remained unresolved during that period.

Central-local relations seemed to be caught in a vicious circle: once the center transferred economic authority to the localities, the national economy would fall into disorder; the central government would then be forced to resume rigid control by restricting local power; consequently local development would decline and the national economy would become stagnant again.

The approach of the leap to technology and management was consistent with the concept of "politics in command", as was the formation of the people's communes. The critical link between political direction and economic organization, however, is the incentive system, which directly affects the distribution of

incentives underlying social relations, as well as the individual's perception of how just the system is. The GLF's attack on functional inequalities in organization and management were reflected in incentive policies that encouraged collective solidarity and mass responsibility by greatly reducing individual income differentiation.<sup>41</sup>

The GLF provided for external as well as internal incentives – specifically, those related to job enlargement and worker participation in management. Workers who were part of "triple combination" technical teams or acquired managerial responsibilities, and who were attending spare time factory schools to upgrade their skills, were expected to identify more closely with their enterprise and to internalize its interests as their own. The collapse of central planning in 1958, probably enhanced this incentive for a while by leaving enterprises and localities with considerable autonomous authority, in which their workers shared.

### **Evaluation of the GLF**

Mao's answer to the various problems (created as a result of the FFYP) in the form of the GLF and its main innovation, the communes; saw human initiative as the key to success in all great endeavour and the conditions arousing greatest initiative were those that promised greatest success. Much human initiative was indeed aruced during the decade, and was invested in the building of rural

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<sup>41</sup> Carl Riskin, *op. cit.*, p.119.

industries, the terracing and irrigation of farmland, the establishment of co-operative medical insurance programmes and the like.

However, despite these various achievements the quality of central planning, to quote Carl Riskin, "deteriorated under the ideological assault of the anti-bureaucratic agenda and the political assault on many of the planners themselves". Allocative decisions became arbitrary, unpredictable, and subjective forcing individual enterprises, and localities to take measures that were irrational. With neither market nor central planners to co-ordinate the economy, Mao sought to minimize the need for co-ordination by means of "self reliance".<sup>42</sup> Some notable success was achieved at the county level and below, but, in general, appropriate institutions and political conditions proved difficult to identify and establish, and "self-reliance" raised as many problems as it solved. At what level it should be achieved ? How much self sufficiency did it imply ? How should it be combined with "socialist co-operation" between enterprises and localities to capture economics of comparative advantages? Perhaps most fundamentally, self-reliance did nothing to correct the inherent weaknesses of administrative planning—especially its weakness in motivating efficient and innovative performance.<sup>43</sup> Only at the lowest-level perhaps that of the production team, might the link between self-

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<sup>42</sup> Carl Riskin. *op. cit.*, p.137.

<sup>43</sup> *Ibid.*

reliant production and community income be direct enough to provide such motivation. At higher levels it was apt to be a case of arbitrary decisions made not by central bureaucrats but by local and provincial ones, possessing even less planning skill.

Under the GLF, the regional party committees acquired supreme decision making powers for all regional economic activities. Since the scope of regional economic activity had greatly expanded, this meant greater economic power. This resulted in regional Party committees launching ambitious projects. However, in order to do so, they had to have capital and labour. As for capital, the decentralization decision gave provincial governments control over a broad range of industries formally under Central jurisdiction. However, in addition to that, provincial governments acquired the right to place orders with enterprises still under central jurisdiction. The provincial governments also received a much greater share of control over the supply system. Provincial governments also acquired power to re-allocate scarce capital equipment assigned to regional areas as long as they observed the state plan. As for labour, the decentralization decisions explicitly granted provincial governments power to shift labour in all industries in the provinces, including those that remained under central jurisdiction. The only exceptions were highly skilled individuals who could only be moved with the permission of the state council. Since labour mobilization was the key device of the GLF, the provincial governments, though the party



apparatus, had a great labour force at their disposal for the projects, in which they were investing.<sup>44</sup> The GLF was thus made possible by the full implementation of decentralization II.

From the above account one can come to the conclusion that the Maoist strategy of development which took place in the shape of the GLF led to many problems and the Chinese economy suffered from various drawbacks. With the emergence of Deng Xiaoping as the paramount leader of the PRC in the post-Mao era a new developmental strategy was to be followed. In the next chapter the Dengist Strategy of Development with a special emphasis on his market driven decentralization and other related questions will be looked into.

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<sup>44</sup> Franz Schrumann, *op. cit.*, p.218.

## **CHAPTER III**

### **Market Reforms and the Beginning of Dengist Decentralization**

## MARKET REFORMS AND THE BEGINNING OF DENGIST DECENTRALIZATION

The Third Plenum of the CPC Central Committee, held in December 1978, signalled a watershed in China's polity and economy. The re-emergence of Deng Xiaoping as the paramount leader of the PRC in the post-Mao era led to what is now known in the available literature as the era of "reforms". It is worth noting that the "reforms" refer to those set of political and economic issues which were initiated and implemented since the Third Plenum. Henceforth, in this dissertation, the term "reforms" will mean the policies initiated by the Third Plenum and the group of leaders who supported Deng by and large, will be referred to as "reformers" (though it must be kept in mind that there were different factions within this large group). The "reforms" era came into being not only as an answer to the various problems which China was facing as a result of the "Maoist mobilisational approach"<sup>1</sup> to development, but also because the previously unchallenged predominance of the Soviet model of development (which was characterized by central planning) was also being questioned. Elements of the reformist critique had already appeared in China as early as the mid-1950s when Chen Yun, for example, had advocated greater use of indirect planning methods

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<sup>1</sup> Gordon White, *Riding the Tiger - The Politics of Economic Reform in Post-Mao China*, The Macmillan Press Ltd., 1993, p.29.

and a more market-oriented pricing policy.<sup>2</sup> Economists such as Xue Muqiao and Sun Yefang had also voiced pro-market proposals and there were short-lived experiments to grant enterprises greater power to act as autonomous entities outside state controls. (Decentralization I, according to Franz Schurmann) But these and other similar policy proposals were submerged by various events which finally culminated in Great Proletarian Cultural Revolution (GPCR). In the earlier periods of reformist thinking, the various problems identified by critics may have been real enough, but there was not enough political impetus to convert reformist ideas into sustainable policies. It is here that Deng Xiaoping and his group of supporters made a significant departure. Deng and other "reformers" went beyond a mere attack on Maoism to include a thoroughgoing critique of China's developmental experience over the past three decades. This led to laying of a new basis for China's economic future, a process of 'economic structural reform' leading to a new model of development in which market would also have a say in the shaping of Chinese economy.

## **ORIGINS OF THE REFORMS**

Prior to the reforms China adopted a centralized planning system which was moulded with the Maoist strategy of development according to Chinese conditions

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<sup>2</sup> *Ibid.*

(as perceived by the CCP under Mao's leadership). The origins of the reforms can be traced back to the pressures for change which had gradually been building up since 1957.<sup>3</sup> Given the party leaders' emphasis on rapid economic growth and their intent to catch up with the world's most advanced economies as soon as possible, the most important cause of the reforms was the declining rate of growth of the economy since the FFYP (1953-57). Economic growth in China in terms of net material products in comparable prices had been fairly rapid during the FFYP period, reaching on average almost a per cent a year.<sup>4</sup>

Given China's emphasis on modernization and its ambition to catch up with the technology of advanced countries, another important reason for economic reforms emanated from the worsening technological backwardness of Chinese industry. Under the old economic system and trade policy, China's capacity to import technology was severely limited. In the 1950s the source of China's imported technology was limited to the communist bloc because of the economic boycott of China by western countries and the subsequent 'lean-to-one-side' foreign (and trade) policy adopted by China at that time. During the period of "self-reliance" in the 1960s and the early 1970s, China's capacity to import foreign technology was constrained by its inability to increase its manufactured exports to

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<sup>3</sup> Joseph. C. H. Chai. *China: Transition to a Market Economy*. OUP, Clarendon Press, 1997, pp. 2-5.

<sup>4</sup> All the Statistical data in this portion. C. F. Joseph, C. H. Chai. *ibid*.

earn foreign exchange, for, under the old economic system enterprises were neither interested in, nor capable of, producing competitive exports were neither interested. In, nor capable of, producing competitive exports for overseas markets. Furthermore, under the import substitution trade policy, there was built-in incentive bins against export production.

China's ability to diffuse imported technology was also severely limited because the old economic system did not offer sufficient price and income incentives to enterprises which successfully adopted new technology. The result was that by the late 1970s, Chinese industrial technology lagged approximately 10 to 20 years behind world levels with a gap of 20 to 40 years in some fields.<sup>5</sup>

Another important cause for the reforms was the growing disequilibrium in the economy. Not only was the old economic system incapable of delivering long-term sustained growth but also it was incapable of maintaining an equilibrium in the economy. The use of plans to co-ordinate supply and demand proved to be very costly and ineffective because the cost of information gathering was very high and rose with the growing complexity of the economic structure. The problem was exacerbated by the imbalances generated by the Stalinist growth strategy adopted in the past. This gave preference to the development of heavy industry in general and the machinery industry in particular, to the neglect of agriculture and other

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<sup>5</sup> Joseph C.H. *op. cit.*, p.4.

complementary industrial branches. The Stalinist system of planning adopted by other planned economies tended to give rise to bureaucratism and administrative over-centralization. To counter these problems, Mao introduced widespread administrative decentralization within the Chinese planning system. The basic idea was to establish relatively independent localities with discretion to allocate resources and distribute income according to broad criteria enunciated from the centre, but implemented in constant consultations with lower levels.<sup>6</sup> Though this idea was commendable, it was difficult to put into practice. The result was a severe weakening of Chinese planning capacity to co-ordinate the economic activities.

The growing disequilibrium of the economy manifested itself in increasingly serious shortages of transport facilities, energy, and industrial and construction materials. In the late 1970s it was estimated that one-quarter of China's industrial production potential remained unutilized because of electricity shortages.<sup>7</sup> At the same time, the transport system was able to satisfy only 50 to 70 per cent of the country's transportation needs.<sup>8</sup> Similarly, the supplies of steel, cement and timber

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<sup>6</sup> Carl Riskin, *China's Political Economy - The Quest for Development since 1949*, OUP, 1987, pp.82-84.

<sup>7</sup> Joseph C.H. Chai, *op. cit.*, p.4.

<sup>8</sup> *Ibid.*, p.5.

fell short of their respective demand by 60 to 70 per cent in the late 1970s.<sup>9</sup>

By the late 1970s, the political costs of these economic deficiencies were mounting. This not only fuelled social discontent but, more importantly, created a situation which lacked incentives leading to economic passivity which held back improvements in productivity which dampened growth in real incomes and so on.<sup>10</sup> Since the legitimacy of the CPC regime, even in the Maoist period, rested heavily on its ability to improve the living standards of the population, such disappointing performance posed a serious challenge to the party leadership. Persistent poverty, technological backwardness, and pervasive economic inefficiency were a source of great concern to Deng and other senior leaders of the CPC and provided the basis for supporting the proposals of reform economists. In economic terms the political appeal of market reform was, in the eyes of significant sections of the Party elite at least, for recouping the Party's political credibility by demonstrating its capacity to raise living standards and make China a strong economy.

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<sup>9</sup> *Ibid.*

<sup>10</sup> *Ibid.*



## THE ECONOMIC REFORM PARADIGM

This section of the chapter is greatly influenced from Gordon White's work - the Tiger - The Politics of Economic Reform. The new economic strategy which emerged over the late seventies and eighties was an attempt to correct certain basic imbalances in the economy which originated from the Maoist model of development and the Soviet model.<sup>11</sup> These readjustments were to be accompanied by a thoroughgoing structural reform *of the system of economic planning and management*. The main element of the structural reform are as follows.

"A Redefinition of the Socialist Development State": In the previous system, the spheres of politics, administration and economics were intertwined in practice: "the state apparatus dominate the economy and the Party pervaded both".<sup>12</sup> Reformers have regarded this situation as objectionable, first, because direct politicisation of state bureaucracy (through party organizations) impedes the emergence of a more professional form of modern administration and second, because excessive involvement by either the party or the government administration in the affairs of production enterprises is considered economically

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<sup>11</sup> Gordon White. *op. cit.*, p.43. This section of the chapter is greatly influenced by Gordon White's work *Riding the Tiger - The Politics of Economic Reform*. (Refer footnote no.1).

<sup>12</sup> Gordon White. *op. cit.*, p.43.

harmful. The latter objection though contested by the pro-state advocates, is a viewpoint of liberal variety. The intention, therefore has been to separate the institutional spheres of politics, administration and economy, to define their respective functions more precisely and to redefine the relationships between them.

White has discussed three areas of separation here: between politics and administration, between politics and economics and between administration and the economy. The first of these relates to the question of political reform of the state apparatus. The second involves the attempt to depoliticize economic decision-making at all levels. Ideologically, the reformers emphasized the need to treat "politics" and "economics" as distinct spheres and avoid subordinating the latter to the former. At the institutional level, this separation implies a more limited role for the party in the everyday process of economic management. The system of "interlocking directorates", whereby party officials "wear two hats"<sup>13</sup> by holding office as administrators or managers, would have to be reduced. Ultimately this means that party organizations in economic bureaucracies and enterprises would either be removed or restricted to narrowly defined political work which does not involve them in the day to day operation of the unit. This implies greater role specialization, more groups in their own areas of expertise, and changes in occupational recruitment criteria, from "redness" to "expertise". At the motivation

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<sup>13</sup> *Ibid.*, p.44.

level, there was far greater emphasis on the importance of "material" as opposed to "moral-ideological" incentives in motivating labour. In practice, this meant a move away from Maoist style "egalitarianism" which stressed collective material incentives and restraint on income differentials, towards greater use of individual incentives and a positive view of income inequality as a way to stimulate efforts.<sup>14</sup> The third area of separation was between government administration and the economy: the latter was to be characterized by its anti-bureaucratic nature. Previously, argued the reformers, the economy was run as an administrative system through a complex system of central ministries and local government departments. As mentioned in the first chapter, it was prone to the problems of complex, centralized bureaucracies which systematically impaired economic performance. The problem was not merely of administrative subordination; but also the fact that the enterprise's managers were neither uniform nor consistent: there were numerous higher organs, functional and regional, and their functions often overlapped, with the result that state enterprises were subject to too many superiors. Economic management requires economic methods, argued the reformers, enterprises should be released from the grip of their, "superior departments"<sup>15</sup>. While the state should still retain an important economic role,

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<sup>14</sup> *Ibid.*

<sup>15</sup> *Ibid.*, p.45.

planning was henceforth to be based on "guidance"<sup>16</sup> rather than "directive" methods and economic management was to be conducted largely by means of policy regulation rather than administrative fiat. Rather than abolishing the "socialist developmental state", therefore, the reforms aimed at changing its character and functions, moving in the direction of the kind of economic regulation characteristic of capitalist "mixed economies" while retaining basic socialist features, such as the predominance of ownership.

### **Economic Decentralization and the "Socialist Commodity Economy"**

The redefinition of the Chinese state set the context for a programme to decentralize economic decision-making power and revive market type relations between individuals and enterprises.<sup>17</sup> Whereas the Maoists had sought to reform the planning system by decentralizing power from central to local governments, the new thrust was to devolve power from any layer of government to the enterprise itself: this could be described as a transition from "administrative to economic decentralization".<sup>18</sup> Gordon white has pointed out that post-Mao economic reformers tended to view administrative decentralization with suspicion:

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<sup>16</sup> Guidance Planning and Mandatory Planning will be discussed in the latter part of this chapter.

<sup>17</sup> As mentioned earlier in this chapter, pro-market policies were adopted in the early sixties.

<sup>18</sup> Gordon White, *op. cit.*, p.45.

as an expression of the "Maoist" approach to reform which lost some of the advantages of centralization while at the same time creating both, dislocation and duplication in the planning system and maintaining the economically irrational principle of bureaucratic domination over enterprises.<sup>19</sup> In the opinion of the reformers, the direct subordination of enterprises to government was unwise, regardless of the level of government involved. The key link in meaningful reform, therefore was economic decentralization. It is pertinent to note that the reformers didn't abandon or rule out the importance of administrative decentralization. However, they emphasized that administrative decentralization should not be accorded the prime priority and, to the extent that it did take place, should be accompanied by a process of economic decentralization at the local level, so that local governments should exercise their economic powers in a new way, indirectly, rather than directly, using economic policy mechanisms, not administrative fiat.

The Maoist emphasis on local "self-reliance", it was argued did reduce some of the problems of over-centralization in Soviet-style planning but only at considerable economic cost: for example, it tended to encourage local governments to establish irrationally comprehensive local industrial systems which violated the need for specialization and exchange between areas as was seen during the GLF.

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<sup>19</sup> As cited in *ibid.*

Moreover, it did not challenge the principle of administrative subordination of the enterprise: it merely relocated its source.

In the new system, the state would act to achieve its plan objectives by seeking to influence enterprise behaviour in certain directions, rather than by issuing administrative orders.<sup>20</sup> This new relationship between state and enterprise would, it was argued, allow most micro-economic decisions to be taken at the enterprise level where they belonged.<sup>21</sup> The enterprise was to gain greater power in decisions about investment, output, wages and salaries, pricing, procurement and marketing and was to behave more directly in pursuit of its "independent financial interests". This new system meant a change in the nature of economic linkages, away from "vertical" relationships between enterprises and the supervisory state organs above them, towards "horizontal", market-type links between enterprises regulated by contracts and prices which reflected real conditions of supply and demand.<sup>22</sup>

The underlying assumption behind this new type of economic system is that planning and markets are compatible principles: markets can be utilized to serve

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<sup>20</sup> *Ibid.*

<sup>21</sup> Xue Muqiao, "A Study in the Planned Management of the Socialist Economy", *Peking Review (Beijing Review)*, 26 October 1979, p.43.

<sup>22</sup> Gordon White, *op. cit.* p.46.

the aims of socialist development.<sup>23</sup> Reform economists such as Li Guoguang, Chen Jiyuan, He Jiangzhang argued that a socialist economy, cannot operate without markets. Markets are an objective economic necessity, a response to the complexity of any economic system, the separation between economic actors within it and the differences in their economic interests. In the words of one reform text, "the state plan can only reflect the needs" of society in totality but cannot reflect correctly and flexibly the kaleidoscopic needs of our economic life".<sup>24</sup>

While initial thinking about the need for markets focussed mainly on product-markets, as the reforms progressed, the argument was extended to include markets for capital, labour and land. In regard to capital, said the reform economists, the previous system for mobilizing and allocating investment funds had been too cumbersome and monolithic, the financial system should be diversified and commercialized, to promote a more flexible and productive flow of funds. This meant greater autonomy for state owned banks and a wider range of financial institutions and assets, including the emergence of markets for bonds and shares. For the more radical reformers, the ultimate character of the "socialist commodity economy" was a fully-fledged market system in which a wide range of market for

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<sup>23</sup> *Ibid.*

<sup>24</sup> Liu Guoguang, et. al., "The Relationship Between Planning and Market as Seen by China in Her Socialist Economy", *Atlantic Economic Journal*, no. 31, 1974, p.15.

all factors of production prevailed. But the desirable extent of "marketisation" was to become a bone of contention between conservatives and the reformers as the reforms actually took their course.

### **Ownership**

Reformers challenged the previous Stalinist/Maoist notion that economic entities undergo an inexorable transition from "lower" to "higher" levels of ownership in the process of socialist development. They argued that this contravenes the Marxian "law" that the relations of production must conform with the level of productive forces.<sup>25</sup> In other words, in China's conditions of economic underdevelopment, large-scale state enterprises are often inappropriate, thus the role of private, small-scale co-operative/collective and various forms of hybrid or joint-ownership enterprises should be encouraged for the foreseeable future.<sup>26</sup> At the same time, most reformers have tended to concede that state ownership should still remain dominant in the economy.<sup>27</sup>

### **The Open Policy**

Reforms in the domestic economy were to be accompanied by a greater openness to, and a wider range of linkage with, the international economy. The

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<sup>25</sup> Gordon White, *op. cit.*, p.48.

<sup>26</sup> *Ibid.*

<sup>27</sup> *Ibid.*



previous Maoist emphasis on national "self-reliance" was criticized on the ground that it denied China the benefits of participation in the international division of labour through foreign trade and of infusions of foreign capital which could spur domestic development. Economic theorists advocated an increase in the ratio of foreign trade in the economy, the acceptance of foreign credits from both governmental and private sources, encouragement of direct foreign investment through wholly-owned or joint ventures, and the establishment of "special economic zones" and "open cities" to foster foreign participation in the economy.<sup>28</sup> This did not mean that the Chinese economy would be thrown completely open to, and dependent on, the outside world: the state would still play a crucial role in setting foreign trade policy and defining the terms of foreign participation to serve the broader interests of the national economy.<sup>29</sup>

## **AN OVERVIEW OF REFORMS**

In the above account, we have seen four vital characteristics of the reforms but as the title of this work suggests, we will limit our inquiry into the reform era by studying the policy of decentralization as adopted in the post-Mao era after the Third Plenum. But before discussing the Dengist decentralization *vis-a-vis* the Maoist decentralization, it will be appropriate to have an overview of reforms in

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<sup>28</sup> *Ibid.* p.49.

<sup>29</sup> *Ibid.*

the first two decades of economic reforms. At the risk of appearing digressive, the following section is necessary to clarify the debates and the various arguments regarding the role of the market among/within reformers. Considering the fact that "market" lies at the heart of Deng's reforms as well as the core of his strategy of decentralization, this would be necessary, even crucial for our understanding.

Most of the debates revolving around the economic reforms in the post-Mao era can be divided into two periods. The first can be labelled as the period between two crucial events: from their official launch at the Third Plenum in December 1978, to the Tiananmen crisis of June 1989. The second period is the period from the Tiananmen square incidents to the present times. In this work, we would limit our discussions of the debates revolving around the question of "market" as they took place after the initiation of economic reforms till the Tiananmen square incident. This period can be divided into two main phases, each with its own fluctuations and sub-phases. The first ran from the Third Plenum (of the 11th Central Committee) held in December 1978, to the Third Plenum held in October 1984. The second phase ran from late 1984 to the Tiananmen incidents of June 1989. Broadly speaking, the first was dominated by a sweeping transformation of rural economic institutions; in the second phase, attempt was made to accelerate reform in the urban-industrial sector, but the reform process as a whole ran into increasing problems as the economy ran out of control, popular discontentment mounted and fissures started appearing among the reformers.

culminating in the upheaval and repression of mid-1989.

The reform consensus within the CPC leadership began to break into two broad groups, usually called the "conservatives" and the "reformers". This is a misnomer because the arguments of both the sides were "pro-reforms" insofar as they saw the need to change the old system of central planning and give more scope to market mechanisms. According to Joseph Fewsmith, "conservatives", though strong believers in planning, felt that there was room for market forces, particularly with regard to China's rural areas and consumer goods.<sup>30</sup> This approach to planning recognized the limitations of planning in China. The two categories "conservatives" and "reformers", have been used with the clear understanding that for the most part these denote differences among reformers as a whole. Further, it is more sensible to see these two terms as referring to broad "tendencies" or attitudes, held to greater or lesser degrees by individual leaders, rather than to well-defined groups with some internal coherence and a shared programme. The dominant leadership group at any given time will include a particular mix of these tendencies. However, this simple dichotomy is helpful analytically, in that it enables us to point out the various opinions and disagreements over the conduct and aims of the reforms. The scope of discussions on economic reforms is very vast and keeping this very fact in mind, the debates

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<sup>30</sup> See Joseph Fewsmith, *Dilemmas of Reform in China - Political Conflict and Economic Debate*, M.E. Sharpe, Inc. 1994, pp.88-116.

on economic reforms are limited to two key issues, namely. The debates revolving round the introduction of market in a socialist economy and then the question of decentralization. In the next section there would be an analysis of these debates as and when they unfolded.

### **The "Conservative" and "Reformist" Attitudes to Economic Reforms.**

Before knowing the viewpoint of the "reformers" and the "conservatives" towards economic reforms, it is quite appropriate that one knows the prominent leaders of these two factions of the CPC. The main "conservative" leaders were Chen Yun, Yao Yulin, Wang Jiye, Wu Jinglian, Wu Kaitai and their supporters. The main reformers were leaders like Zhao Ziyang, Deng Xiaoping, Hu Qili, Hu Yaobang and their supporters.<sup>31</sup> The two groups "conservatives" and "reformers" differed in their views on four key questions: planning, markets, ownership and the overall character of the post-reform "socialist commodity economy". The conservative view was that planning (both "directive" or/and "guidance") is a fundamental defining characteristic of "socialism" and should continue to play a dominant role in the economy. In their view, central planning was both desirable and feasible. Reform of the planning system was possible by increasing the scope of "guidance planning", particularly through the use of fiscal and financial controls

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<sup>31</sup> This section and the following sections have been influenced by Gordon White's *Riding The Tiger - The Politics of Economic Reforms in Post-Mao China*; Joseph Fewsmith's work, *The Dilemmas of Reform in China - The Political Conflict and Economic Debate*; Robert Hsu's work, *Economic Theories in China, 1979-1988*.

to achieve macro-economic balance, by reducing the scope of directive planning to concentrate more publicly on key sectors; by improving the quality of information and personnel, by devising better incentive systems and the like. Markets, on the other hand, are seen as potentially anarchic and destabilising; they are incapable in themselves of achieving the aims of a socialist economy, but have certain benefits in balancing supply and demand and creating pressures for greater efficiency at the enterprise level.<sup>32</sup> The market can thus play a valuable role in a socialist economy, but a role which is supplementary to the plan. As for the international market, the conservatives were willing to recognize the economic benefits of foreign trade and finance, but again saw this largely as a useful supplement to a basically "self-reliant" economic strategy and were reluctant to allow the Chinese economy to become too dependent on the outside, especially given the fact that the "open door" let in "unhealthy" cultural and political influences. In terms of the system of membership, moreover, "conservatives" insisted that the public sector should remain dominant in the economy, although admitting that private and other 'non-socialist' sectors could play a valuable supplementary role, particularly in providing services and non-basic consumer goods.

For the conservatives, therefore, there are certain points beyond which

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<sup>32</sup> Gordon White, *op. cit.*, p.64.

market oriented reforms cannot go. Their picture of the ultimate "socialist commodity economy" would seem to be of an essentially dual economy: central planning would dominate over a market sector.<sup>33</sup> The operation of markets would be kept within tight limits and would largely be confined to commodities. Markets in capital, labour and land threaten to undermine the very bases of a "socialist" economy and have to be treated with great caution. This model is an amended form of the Stalinist model (which also allowed for a market sector); though the market sector has been enlarged and institutionalized as a long-term component of a "socialist" economy. As such, there are important institutional continuities between the old and the new models.

By contrast, the reformist model seeks a more radical break with the past. Rather than a central pillar of socialism, it is argued, centralized directive planning is an impediment to socialist development since it is incompatible with economic efficiency; economic institutions should be defined as 'socialist' to the extent that they contribute to 'developing the productive forces'. In an advanced economy, only markets are capable of guaranteeing a rational allocation of economic resources and they should become the prime mover of the economy. The traditional planning system should be dismantled and, to the extent that state planning remains (to achieve long-term national objectives or correct certain

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<sup>33</sup> *Ibid.*, p.65.

negative effects of the market), it should be redefined mainly in terms of a regulatory framework of macro-economic policy, operating through economic levers such as interest rates, taxation and tariffs. In the words of Zhao Ziyang, whose report to the Thirteenth Congress of the CPC in 1987 can be considered as the official statement of the reformers' position, "the state regulates the market and the market guides enterprises".<sup>34</sup> The exchange of commodities would largely be governed by a competitive price system, and markets would gradually emerge for basic factors of production - capital, labor and land-leading to comprehensive "marketisation" of an economy which would also become extensively integrated into the international economy. Since private and other non-socialist forms of ownership were dynamic and efficient, they should be encouraged and not fettered by politically inspired restrictions; moreover, traditional forms of state and collective ownership should be fundamentally reformed. The endpoint of the reforms would be very different from the conservative model it would essentially be a market economy, though perhaps one with a relatively large residual public sector and substantial state regulation of the economy.<sup>35</sup>

### **The Market Under Socialism**

The central underlying strategy of Deng Xiaoping's economic reforms was

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<sup>34</sup> As cited in *ibid.*

<sup>35</sup> *Ibid.*

to combine socialism with the market mechanism in order to import greater economic incentives and flexibility to the economic system, thereby raising productivity in all sectors of the economy. To understand Deng Xiaoping's strategy of decentralization, its very important to know how the introduction of market was viewed in a socialist state. The introduction of market mechanism into a society that had been hitherto ideologically opposed to it was not an easy task. For it to succeed, fundamental attitudinal changes had to be brought about and the market oriented changes had to be theoretically justified. In the mid-1970s, the market was considered to be the embodiment of capitalism and the anti-thesis of socialism; even minor rural market activities and peasant sideline production for local markets were criticized as the "tails of capitalism".<sup>36</sup> By 1982, the dominant attitude towards the market had been transformed, so much so that the 1982 state "ensures the proportionate and coordinated growth of the national economy through overall balancing by economic planning and the supplementary role of regulation by the market" (Article 15).<sup>37</sup> During the preparation of the third plenary session of the Twelfth Central committee of the CPC held in 1984, when the Decision on Reform of the Economic system was being drafted, the theoretical debate on the objective of reform again concentrated on "socialist commodity

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<sup>36</sup> Robert C. Hsu, *Economic Theories in China - 1979-1988*. CUP, 1991, p.26.

<sup>37</sup> As cited in *ibid*.



economy". Thus Zhao affirmed that "A socialist economy is a planned commodity economy", proposing that "the planned economy suited to China should operate in accordance with and in application of the law of value" and that "our policy should be to gradually reduce mandatory planning and extend guidance planning".<sup>38</sup> In the Decision on Reform of the Economic system<sup>39</sup> adopted by the Third Plenary session of the Twelfth Central Committee held in October 10, 1984 "socialist commodity economy" was clearly affirmed.

The Third Plenary session of the Twelfth Central Committee created a new situation for economic reform and development. In 1985, there was a significant turn in the mode of thinking and study on China's economic theory. Along with the accumulation of experience and progress in theoretic study on reform, the concept of socialist commodity economy continually deepened and developed in theoretical implications of reform conception. This found expression in the report of the Thirteenth National Party Congress held in 1987. The report fully endorsed the view that "A socialist economy is a planned commodity economy based on Public ownership", which was advocated by the Third Plenary session of the Twelfth Central Committee. However, the report also pointed out: "The socialist planned commodity economy should be a system that integrates planning with the

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<sup>38</sup> In a letter dated September 9, 1984 to the standing committee of the Political Bureau of the CPC Central Committee regarding the reform of the economic system.

<sup>39</sup> Robert. C. Hsu. *op. cit.*, p.26.

market". This led to paving the way for the establishment of the "Socialist market economy" in that the Party gave a greater role to market forces than offered by any other ruling communist party to date. The State, the report said, will retain the capacity to make "macrolevel adjustments and control" but market forces are to eradicate poverty, while the laws of supply and demand are to ensure the rational allocation of commodities throughout the economy. Indeed, at one point, Jiang put forward the use of price levers and competition to improve efficiency and "realize the survival of the fittest" (*Shixian Yousheng Lietai*). In the Fifteenth Party Congress, 1998, Jiang Zemin while delivering the report, said "We (the CPC) should accelerate the process of building a complete market economy.. We shall continue to develop all kinds of markets for capital, labour, technology and other production factors and the mechanism for pricing these factors..."<sup>40</sup>

The above account portrays the unfolding of the socialist market economy in China in various discussions and debates among/between the "pro-plan" faction and "pro-market" faction phases. However, this evolution has not been an automatic one. On the contrary, the socialist market economy in today's China is a product of various debates that took place in various phases during the last two decades.

The dominant Chinese views on the ways to combine the market and the

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<sup>40</sup> Jiang Zemin. "Report delivered at the 15th National Congress of the CPC on September 12, 1997. *Beijing Review*, October 6-12, 1997.

plan took shape in the first decade of economic reforms. This period can be broadly sub-divided into two periods; 1) 1979-84 and 2) 1984-1989.

**1979-84:** The first and most significant conceptual development occurred in 1979-80 when, as a reaction to the problems of the past planning practices and emboldened by the euphoria of political change, a number of economists published their ideas on combining the market with socialist planning. He Jiangzhang, Wang Jiye, and Wu Kaitai (1980) advanced the "permeation" thesis, in which the market and the plan permeate each other. The reasoning is that the plan needs to be consistent with and supported by the market to make it flexible and conducive to incentives, whereas the market needs to be guided by the plan to ensure the unity of interests among the state, the collective and the individual under socialism. Thus, the plan and the market are complementary, correcting each other's imperfections. This perspective became widely accepted by reform economists in the early 1980s constituting a watershed in the evolution of China's economic reforms.<sup>41</sup>

Many veteran planners and top party cadres, however, resisted this talk of the market; they wanted to "reform" the legacy of the Cultural Revolution and return to the 1950s. This sentiment came into the open in late 1981-82. For example, You Lin talked of dividing the economy into two sectors, according to

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<sup>41</sup> Robert C. Hsu, *op. cit.*, p.34.

the importance of the products, and wanted important products to be planned by the state in terms of production, prices and distribution, minor products should be regulated by the market. In refutation, pro-market reformers argued that in this model, the two regulatory mechanisms as well as the two sectors are separate and uncoordinated and that the model will not work because each sector will ignore the needs of the other.<sup>42</sup>

As part of the conservative reaction against the pro-market activist, Chen Yun reiterated in early 1982 his priority for reforms - "planned economy in the main and market regulation as the supplement" - which was popularized by the government in early 1982 into a policy of slogan.<sup>43</sup> As a result, proof the permeation model and of the socialist commodity economy were criticized in government circles.<sup>44</sup> Subsequently Liu, He and other leading "radical" reformist economist such as Sun Yefang and Wu Jinglian were pressured into expressing support at a forum for this conservative emphasis on planning.<sup>45</sup> Pro-planning government economists such as Deng Liqun, Wang Renzhi and Gui Shiyong

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<sup>42</sup> *Ibid.*, p.35.

<sup>43</sup> *Renmin Ribao (RMRB)*, (*People's Daily*), January 26, 1982, as cited in *ibid.*

<sup>44</sup> He Jiang Zhang in an interview to Robert C. Hsu, (Author of *Economic Theories in China, 1979-1988*), July 15, 1988.

<sup>45</sup> *RMRB*, Feb. 22, 1982, as cited in Robert C. Hsu, *op. cit.*, p.36,

became more influential in government councils as market oriented theorizing became temporarily muted in published materials.<sup>46</sup>

In spite of the conservatives' attempts to restore the planning system of the 1950s, it was no longer possible to do so in early 1980s because the problems of the past central planning were well known, and because the impressive results of the rural reform had strengthened the leadership's commitment to, and power to implement, additional market-oriented reforms. Thus, starting in late 1983, discussions on ways to combine the market with the plan were renewed, there were also related discussions on how socialist planning itself can be made more flexible and effective so that it will be compatible with reforms. The discussions centered on whether or not the scope of "mandatory planning"<sup>47</sup> should be reduced and that of "guidance planning"<sup>48</sup> expanded, as He Jiangzhang proposed.

As mentioned earlier, the debates revolving around the question of market versus plan might appear to be incongruous but as the introduction of market had

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<sup>46</sup> He Jiangzhang in an interview to Robert C. Hsu, on July 15, 1988, as cited in *ibid.* p.36.

<sup>47</sup> Mandatory planning (*zhiling jihua*) is the orthodox type of Socialist planning, with compulsory target for production and distribution. Definition as given in Robert C. Hsu.

<sup>48</sup> Guidance planning (*zhidao jihua*) is a more flexible type for planning, concerned with the micro relativities of most enterprises, with the key enterprises excepted. It's important to note that there is no unanimity among Chinese economists on the proper scope for guidance and mandatory planning.

a direct fallout in terms of Deng's strategy of decentralization, its necessary to lay the ground work in understanding Dengist strategy of development. Coming back to the question of planning, most Chinese economists have concluded that "mandatory planning" produces rigidity and disincentives, and therefore "mandatory planning" should be limited to the major macro proportions and balances of the economy, and to the production and distribution of essential products and the key enterprises that produce them. The role of market is minimal in this type of planning. In the case of "guidance planning", enterprises are given a large degree of autonomy in their production for the market. They are to be guided by the planners in achieving the suggested targets. These targets are not binding, and the enterprises can adjust them in accordance with changes in the market or in supply conditions. Thus, in this type of planning, the market mechanism plays a dominant role and planning, a minor and indirect role. By October 1984, when China's leaders decided to reform the urban industrial sector, Chinese economists had widely accepted guidance planning as the ideal strategy to raise the productivity of enterprises and to make their production more attuned to market demand.<sup>49</sup>

The October 1984 decision of the party leaders to reform urban industries is regarded by Chinese economists as another important turning point in China's

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<sup>49</sup> Robert C. Hsu. *op.cit.*, p.36.

market oriented reforms. As a result of that decision, economists' theoretical discussions of the market entered a new phase because now it could be taken for granted that the reformed economy would be predominantly market-oriented. Ideologically, it was now officially proclaimed that the socialist economy was a "planned commodity" economy and that the commodity economy needed to be expanded in China.<sup>50</sup> In addition, it was held that the commodity economy was also a market economy; hence the experience of the capitalist' countries concerning the market might provide useful lessons. This led to a rapid decline in the scope of "mandatory planning" and a rapid expansion in that of "guidance planning".<sup>51</sup>

In addition, a new way of combining market flexibility with planning in some sectors of the economy was introduced. Previously, both Chen Yun's "big plan and small market" and pro-market economists' "guidance planning versus market planning" represented a particular type of dual system. The economy was conceptually divided into two separate sectors in which planning and the market mechanism respectively predominate. As an integral part of this dualism, state-set prices would prevail in the planned sector, and floating prices (flexible within state-set limits) and free prices would prevail in the other sector. In 1984-85,

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<sup>50</sup> *Ibid.*

<sup>51</sup> *Ibid.*

however, a different type of dual system was introduced to further expand the role of the market.<sup>52</sup> For many industrial materials previously covered by mandatory planning, a certain level of input was subject to plan quotas at low controlled prices; excess output over and above the quotas could be sold in the market at higher market prices. The same two-tier price system also applied to grains-lower purchase prices and market prices for the additional output sold to the market.

This method of combining planning and the market was introduced to facilitate the transition to a predominantly market oriented system following a thorough price reform. Conceptually, this dual system presumed that planning and the market mechanism within the same industries would be compatible and complementary, as did the advocates of the permeation and rubber-glued models in 1979-80.

**1986-88:** This period saw the continuation of the same trend to combine the market with the plan. One significant development was that a central idea which was implicit in the discussions of the previous periods, was made explicit in this period so that it became firmly established and widely accepted. The idea is that the market and the plan are comparable under socialism because they are merely two alternative methods of adjusting and developing the economy, and thus can be adopted and combined in accordance with the conditioning of the economy. Hence

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<sup>52</sup> *Ibid.*



a socialist economy is also a market economy, and a capitalist economy can also be a planned economy according to this view. Jiang Yiwei of the Institute of Industrial Economics, the Chinese Academy of Social Sciences, likens both planning and market to basketball rules and economic systems to ball teams. The same rules are to be observed by all teams, capitalist and socialist alike. It is the nature and organization of the teams - that is, the ownership and production relations - that distinguish the socialist teams from the capitalist ones.<sup>53</sup> As of mid-1989, most Chinese economists agreed with Jiang Yiwei and Gao Shangquan that both socialist and capitalist systems can utilize planning and the market as the adjustment mechanisms of the economy, and that it is the nature of ownership of the means of production that is the hall mark of an economic system, even though they have no consensus as to the best form of socialist ownership.

Such an approach has been criticized by many scholars. Kornai, a Hungarian economist, characterizes this approach as a naive "supermarket shopping" approach to economic systems in which disparate items are taken from different shelves as one wishes. He argues that such an approach will not work in socialist reform and that in real life an economic system has to be considered a "package deal", with all its good and bad features taken together Kornai may have overstated his case because, taken literally, his package deal approach permits no

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<sup>53</sup> Ibid.

reforms in any economic system and no possibility of a successful mixed economy - but his statement does contain a valuable insight. Along the same time, Prybyla contends that techniques of the market system cannot be used disjointly. "They must be applied as a system their organic interconnections unbroken"; otherwise, "they either atrophy or work in a perverse way".<sup>54</sup>

Prybyla implies, in the view of Robert Hsu, that market reforms in a socialist economy can be viable if, and only if, the essential organic interconnections of the market system are introduced and fostered together, and are safeguarded against arbitrary infringement by the government. These organic interconnections include the depoliticization of economic activities, the safeguarding of personal liberty and property rights, and the existence of a free, competitive environment. From this, the Chinese conception of the market and of planning as merely managerial techniques for adjusting the economy misses an essential dimension of the market mechanism and is therefore, not conducive to the creation of the necessary market environment.

## **DECENTRALIZATION IN THE DENGIST ERA**

Before dealing with the nature and characteristics of Dengist decentralization, its worth quoting Deng Xiaoping:

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<sup>54</sup> *Ibid.*

"Under our present system of economic management, power is over-concentrated, so it is necessary to devolve some of it to the lower levels without hesitation but in a planned way. Otherwise it will be difficult to give full scope to the initiative of local as well as national authorities and to the enterprises and workers, and difficult to practice modern economic management and raise the productivity of labour. The various localities, enterprises and production teams should be given greater powers of decision regarding both operation and management. There are many provinces, municipalities and autonomous regions in China, and some of our medium-sized provinces are as big as a large European country. They must be given greater powers of decision in economic planning, finance and foreign trade - always within the framework of a nationwide unity of views, policies, planning, guidance and action".<sup>55</sup>

As mentioned in the introduction, China is not only a large country covering vast territory and inhabited by an enormous population, it also has a complex political and administrative machinery. As the CPC explored the best way of organizing and administering territory from 1947 to 1976, so it experimented with different degrees of centralized control with varying success. As discussed in the second chapter, the first experiments in decentralization came in 1956-57 as a response to the evils of central planning in the FFYP. Although power was recentralized between 1961 and 1964 as part of Chen Yun's strategy to facilitate economic recovery after the failure of the Great Leap, there was another round of decentralization by 1964. This was followed by a further transfer of economic control to the provinces after 1969, when the centre gave up direct

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<sup>55</sup> Emancipate the Mind, Seek Truth From Facts and Unite as one in Looking to the Future (December 13, 1978). Selected Works of Deng Xiaoping (1975-1982). Foreign Language Press, Beijing, 1984.

management of over 2,600 key enterprises, including the massive Anshan Iron and Steel Complex and the Daqing Oilfield.<sup>56</sup> Local controls over material and financial resources were also introduced to facilitate the policy of developing local self-sufficiency in grain production, light industrial production, and machinery supplies to heavy industry.<sup>57</sup> The result was duplication of production and waste of materials and investment capital. As the decentralization measures transferred profit-making light industrial production to lower level authorities but kept major and expensive projects under central control, it also led to increased pressure on central government coffers. The reformist leadership in post-Mao China sought to resolve these problems and other ills of the Chinese economy by introducing market reforms. When one talks of decentralization in the Dengist era, it is important to recognize that market reforms themselves present a form of decentralization. Where previous experiments in decentralization simply transferred power within the party-state framework, market reforms devolved decision-making powers to producers and enterprise managers. As stated earlier, Shurmann distinguishes between these two forms of decentralization by terming them decentralization I and decentralization II. According to Kenneth Lieberthal, real decentralization has occurred in China only after the introduction of market

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<sup>56</sup> Shaun G. Breslin, *China in the 1980s- Centre-Province Relations in a Reforming Socialist State*, St Martin's Press Inc., New York, 1996, pp.89-90.

*Ibid.*

reforms. The territorial governing bodies at provincial, municipal, county, and township levels have gained enormous initiative at the expense of the vertical functional bureaucracy that reach to Beijing.<sup>58</sup> Moreover, the state no longer promotes either revolution or ideological orthodoxy.<sup>59</sup> Rather, it promotes economic growth by any means that do not produce massive social and political instability. In order to facilitate our understanding of Dengist decentralization and how it is different from Maoist decentralization, this section deals with strategy of decentralization pursued in the Dengist era in terms of a) Centre-Province Relations b) Decentralization and inter-provincial competition; c) Decentralization as it took place in the case of enterprises.

## **CENTRE-PROVINCE RELATIONS**

The issues revolving around Centre-Province relations are very important in China's reform process. When the post -Mao leadership initiated the reform of the economic system in 1978, it also set in motion a process of political reform. Political reform here refers to the significant changes in the processes of political power within the framework of existing party rule. Arguably, these changes were more keenly felt in central-provincial relations than in many other arenas.

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<sup>58</sup> Kenneth Lieberthal, *Governing China - From Revolution Through Reform*. W.W. Norton and Company Inc., 1995, pp.315-317.

<sup>59</sup> *Ibid.*

The drive for economic growth impinged on virtually every aspect of centre-province relations: the state-planning process was partially dismantled; the role and scope of market forces were increased; more central powers were devolved; and a new regional development strategy was adopted.<sup>60</sup> In the old system, political and economic channels were so inextricably linked, that economic reforms could not take place without generating some changes in the political relationship between centre and province.

Although the old planned economy may not have been very efficient, participants in the decision-making process knew their roles and understood the rules of the game.<sup>61</sup> With the weakening of this system and its gradual replacement with more market-oriented mechanisms, many of these certainties disappeared.<sup>62</sup> Moreover, new economic and political relationships were continually being created. According to Shaun Breslin, the pace and extent of economic reform created a dynamism and uncertainty in the politico-economic system. Furthermore, the reforms were uncoordinated and frequently in conflict. Although such a lack of coordination is excusable given the extent of the changes

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<sup>60</sup> Shaun G. Breslin, "Centre and Province in China", in Robert Benewick and Paul Wingrove. (ed.), *China in the 1990s*, Macmillan Press Ltd., 1995, pp.63-72.

<sup>61</sup> *Ibid.*

<sup>62</sup> *Ibid.*

that have taken place in post-Mao China, they nevertheless made a significant contribution to the emergence of new forms of centre-province relations.

During the 1980s, sinologists researching on centre-province turned to study the importance of institutions in addition to their previous emphasis on leadership and elite preferences. The literature during this period considered the centre as the locus of policy formulation and the provinces that of implementation. Centre-province relations were pictured as involving intense inter-agency bargaining. Important studies during this period were made by Barry Naughton, Goldstein and David Bachman. In the late eighties and early nineties, scholars like Susan Shirk and Linda Chelan Li have made new contributions to the centre-province studies in the PRC where the centre-province relations have been portrayed as "non-zero sum".<sup>63</sup> As Tang Tsou (1991) has noted, in the earlier studies, political conflicts in China have been characterized by a total victory versus total defeat' situation in which the winning side retains "all real power to make decisions, whereas the other side is totally defeated". The studies of the nineties have pictured centre-province relations as an inter-active process in which the centre and the provinces struggle hard in order to attain their respective objectives. This section draws insights from this vast and varied research.

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<sup>63</sup> The non-zero sum view adopted here stresses the interdependence and thus mutuality of power between the centre and the provinces as constituent parts of the state. When both parties are mutually dependent upon one another, conflicts necessitate compromise. The more intense the conflicts, the bigger the compromise is required to be resulting in eventually, qualitative change in the relationship.

Reforming the state planned economic system created a number of important challenges for the CPC leadership. Chief among them was the need to replace old economic levers of control over the provinces with new mechanisms which reflected the decline in central planning functions. Although the changing nature of centre province relations in the 1980s was a gradual process, it is possible to identify four distinct phases in the evolution of these relationships: the emergence of a conflict of interests between centre and provinces, 1978-84; increasing local autonomy, 1984-86; a growing divergence of interests, 1986-88; and the failure to rein in the provinces, 1988-89.<sup>64</sup> This periodization has been done by Shaun Breslin in her work, *China in the 1980s - Centre and Province Relations in Reforming Socialist State* and this section is influenced by his work. However, there is also a fifth phase which for our convenience can be termed as the post-Tiananmen phase. The various periods can be accounted for as follows.

**1978-84: "The emergence of a conflict of interests between centre and provinces"**. The first sign that the reforms might generate conflict between the centre and the provinces came as early as March 1979. A mere three months after his accession to *de facto* power, Deng admitted that it was necessary to make a "partial retreat" and slow down the pace of reform. Although this was in part a response to the failures of Hua Guofeng's economic strategy, it was also prompted

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<sup>64</sup> Shaun G. Breslin, *op. cit.*, p.56.



by the explosion in capital construction investment in the provinces that had followed the devolution of controls over investment spending.

This proved to be just the first of many occasions in the 1980s when the issue of capital construction spending created centre-province tensions.<sup>65</sup> The growth in new locally funded enterprises was problematic for two main reasons 1) It contributed to the emerging financial crisis at the centre, with the 1980 deficit of RMB 12.75 billion over a third higher than the planned RMB 8 billion deficit more worryingly, the results of this expansion were disappointing. The new enterprises had not only absorbed large financial inputs, but they were also typically high consumers of raw materials.

The centre was posed with a serious dilemma. On one hand, they needed to curb the rapid expansion of investment to lay a sound financial basis for future reforms, and to answer the criticisms of more cautious leaders. But they had to be careful that the retrenchment did not result in a sharp economic downturn that could jeopardize popular support for the new leadership. In addition, if they placed too great an emphasis on the problems of the reform, then this would give a chance to the conservatives to attack the reform process. However, there was complete unanimity among central leaders when it came to criticizing the provinces and lower level units that placed local interests above national needs. Deng's

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<sup>65</sup> The growth in investment spending contributed to, or at least exacerbated, almost all the pressing financial concerns of the 1980s (inflation, budgetary deficits, etc).

vision of reform was one where the centre retained the power to exert overall economic control over a decentralized economic system. Adherence to central commands and instructions was essential if the reforms were to pass off as smoothly as possible. More specific criticism was reserved for those underdeveloped regions that had tried to boost their local economies and promote rapid growth. Increasingly freed from the constraints of "mandatory planning" and not yet regulated by macro-economic market mechanisms, many areas simply ignored the requirements of greater national goals and turned inward. Growing feelings of a envy and reactive deprivation exacerbated this issue as the 1980s progressed. Although such reproaches came from all central leaders, more conservative leaders such as Chen Yun, Yao Yilin, Song Ping, Chai Shufen and other key state planners did not miss the opportunity to call for a slower and more balanced pace of reform.

Whilst spending much time and energy in condemning such practices, central leaders did little to remove the economic irrationalities (and even incentives) which had prompted the moves towards localism.<sup>66</sup> Instead, they identified immediate problems and took remedial action to solve specific ills, leaving the fundamental causes of these instabilities untouched. With inflation rising and the budget deficit growing, the central leadership responded by trying

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<sup>66</sup> Shaun Breslin. *op.cit.*, p.58.

to take some of the heat out of the economy through a reinstatement of central control.<sup>67</sup> This was supported by a campaign to halt the construction of a number of badly planned large-scale projects or those which were taking longer than expected to be finished. However, in carrying out its retrenchment policies, the centre only had direct control over large state owned enterprises, and investment covered by the national budget. Local extra-budgetary investment proved much more difficult to control. Whilst investment covered by the plan decreased during 1981, extra-budgetary investment by local authorities actually increased. There was a definite reduction in investment in large scale capital construction, while the proliferation of smaller projects continued unabated. As a result, while the state was cutting production of some products, locally owned enterprises increased their production of those same goods. This trend clearly concerned even the most ardent reformers in the central elites.

**1984-86 : " Increasing Local Autonomy "**. The Third Plenum of the twelfth central committee marked watershed in the swing back from retrenchment towards further reform. Although the plenum addressed the economy as a whole, this section is only concerned with those factors relating to centre-province relations. The Planum's resolution identified the following five causes of economic instability in 1982<sup>68</sup> :

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<sup>67</sup> *Ibid.*

<sup>68</sup> CPC CC, 1984, p.iii. As cited in Shaun Breslin. *op.cit.*, p.63.

- 1) The lack of distinction between the functions of governments and enterprises
- 2) The existence of trade barriers between localities
- 3) Over-rigid administrative control over enterprises
- 4) The negation of market mechanics in economic decision-making.
- 5) 'absolute equalitarianism in distribution'.

In order to resolve these problems, the state (at all levels) had to step back from economic activity and allow market forces to play a much greater role. The state would simplify annual plans which would no longer contain mandatory commands but instead become more general guides of the aims of development. In addition, the plenum made a commitment to reforming the prevailing price system. Furthermore, a crucial component of the new reform agenda was an explicit and official commitment to a strategy of uneven development of regions.<sup>69</sup>

### **Impact of Reforms**

One of the most important consequences of the new wave of reforms after 1984 was their effect on the nature of intra provincial conflicts. Attacks on interior provinces for hoarding raw materials continued, but interior leaders' complaints of unfair treatment became increasingly vociferous. The centre's initial response to the growing resentment from interior provinces was a combination of promises, pay-offs and exhortations. Apparently aware that these would not be sufficient to

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<sup>69</sup> Shaun Breslin. *op. cit.*, p. 64.

pacify the interior regions, the central leadership also announced increases in its aid to the western Autonomous Regions and Yunnan, Qinghai, and Guizhou provinces by 10 per cent per annum. It leads one to the inference that although many of the advantages of the reforms accrued to enterprises and local authorities, the centre bore many of the costs. Throughout the reform process, the reformers were apprehensive of the effect of market reforms on geographical and sectoral groups. For example, in addition to subsidizing western provinces, urban workers received compensatory payments to offset the impact of the agricultural price rises. So, in order to ameliorate the negative effects of emphasizing coastal development, the centre took on extra budgetary commitments at a time when central coffers were under strain. This not only affected the long term investment considerations of the centre, but also to a shift in the financial balance of power between the centre and some provinces.

A second key consequence of the new reforms was a further expansion of local spending. Some Chinese economists like Deng Yitao, Luo Xiaopeng and Xu Xiaopo argued for a strengthening of central control rather than a further devolution of power. In addition, August 1985 saw the indictment of some local leaders who failed to place national interests above local concerns. Besides, some high ranking officials in Hainan, like Chen Yuji and Lei Yu, were dismissed from office for severe abuses of power. Hainan had been granted special tax free status to facilitate the development of island into a major economic base. Officials

imported tax-free cars, televisions, etc. and then resold them at twice or three times the initial price to less favoured areas (Chang, 1985). The resulting impact on local revenues was favorably received by the local population but not by central authorities.

**1986-88: "Losing Control - A Divergence of Interests"**. Throughout 1987 and 1988, the centre's ability to control economic affairs in the provinces steadily declined. A July 1987 SSB (1987, p.27) communique provided an example of problems which were not related to productivity increases; investment in capital construction outside the state plan had increased and prices of foodstuffs were rising so rapidly in some cities that real incomes had fallen. This situation coincided with Li Peng's appointment to the premiership, an event that marked an important turn in the reform process, and in central attempts to control the provinces.

Clear signs of the new direction in central government policy came in Yao Yilin's draft national plan for 1988. Although Li Peng had announced a new emphasis on developing the weak links in the economy - agriculture, energy, raw and semi-finished materials and transport and communications - it was Yao Yilin (1988) who outlined new financing arrangements. Provinces and lower-level local authorities would partially fund key development projects through the compulsory purchase of a special bond issue. Any locality that failed to comply would face financial sanctions from the centre, and localities could not launch any new

projects until the bond purchase was complete. Yao introduced strict controls on the expanding rate of local investment. Banks were to refuse loans for projects that would compete for energy and raw material supplies from state-owned enterprises and work on non-productive projects' (hotels, office buildings, etc) was to cease immediately. Central leaders also attacked the growth of institutional spending to improve the working and the living conditions of local level cadres.

By the autumn of 1988, the Chinese economy was facing severe difficulties like inflation, continued credit boom, food shortages and the 'energy crisis' etc. In responding to these problems, the central leadership tried to implement a retrenchment package which affected the provinces in two main ways. First, the package included a number of policies specifically designed to control provincial spending. Second, Li Peng initiated policies related to price reform and the scope of administrative controls which had indirect effects on both centre-provinces and province-province relations. In identifying the cause of these problems and taking remedial action, the central authorities were much more explicit in their criticisms of the provinces than even before.

Faced with a mounting economic crisis, the central authorities were quick to place the blame for many of the problems on the provinces. The main criticism was that local authorities had misused their powers to erect barriers (both fiscal and physical) to prevent goods leaving their territory. As this local hoarding and consumption reduced the available supply of raw materials for the national market,

it had helped generate intense competition between enterprises in richer provinces to pay inflated prices for scarce goods. Unable to compete with the richer competitors, large state-owned complexes had been starved of supplies.

**1988-89: "The Failure to Rein-In The Provinces"**. It was against the above background that the Third Plenum of the 13th Central Committee was held in Beijing in September 1988. This coincided with the conflict between conservatives led by Li Peng, Yao Yilin and reformers led by Zhao Ziyang. The preparations for the Third Plenum had been fraught with difficulties and conflicts centering on solving the growing inflationary prices. Zhao Ziyang pressed for further reforms in the form of price reform and wage reform to eliminate one of the causes of economic instability - the conflict between administrative and market control mechanisms. In contrast, Li Peng, Yao Yilin maintained that inflation was so high and instability so great that extending price reform would only exacerbate the problems. Instead they should take a step back to stronger administrative control rather than a step forward to greater market control. As party Secretary General, it fell to Zhao Ziyang to articulate the decisions of the preparatory central work conference, despite the fact that he opposed many of the new measures.

The speech of Zhao marked a definite shift in favour of restoring central control over the economy and bringing the provinces into line. Qiao Shi expressed sentiments which pointed to this new policy. While it was wholly correct to encourage decentralization and local initiative, Qiao asserted that it was wrong to



use these powers to disregard central authority.

The Third Plenum marked the beginning of a new central initiative to reinstate control over the new provinces. This was supported by a concerted campaign in the national press aimed at warning the Chinese public (and presumably the provincial leaders themselves) of the dangers of growing provincialism. One RMRB (28/9/1988) editorial even went as far as to warn against the emergence of what it termed "local parties".<sup>70</sup> Another editorial, on November 10 (RMRB, HWB, 10/11/1988), identified three degrees of illegitimate action that had to be stamped out.<sup>71</sup> In ascending degrees of severity, these were: publicly supporting central policy, but doing nothing concrete to enforce it; the adoption of counter-measures to deal with policies from above; and provinces which did 'every thing possible to counter the policy from the central authorities'.

More concrete attempts to restore central control came with the reintroduction of price ceilings, and a reinforcement of controls on capital construction investment. The centre also took steps to solve specific problems in particular areas. For example, in order to cut back on expenditure in the Special Economic Zones (SEZs), the centre revoked their 100 per cent foreign currency retention rights. Instead, they had to abide by the same 20:80 retention ratio

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<sup>70</sup> As cited in Shaun Breslin. *op. cit.*, p.73.

<sup>71</sup> *Ibid.*, p.74.

applicable elsewhere (Wen Wei Po 15/10/1988).<sup>72</sup> The centre also acted to prevent rich areas buying scarce produce at inflated prices.

**1989: The Rise of Institutionalism.** Before going into details in this section, it is necessary to be clear about what the term 'institution' means here. In this work, the term institution has been used in the way Kenneth Lieberthal has defined it in his book, *Governing China - From Revolution Through Reform*. According to Lieberthal, institutions are practices, relationships, and organizations *that have developed sufficient regularity and perceived importance to shape the behaviors of their members.* (emphasis in the original) In contrast, he defines organizations as coherent, internally interdependent administrative or functional structures. According to Lieberthal, organizations exist in abundance, even at the highest levels of the Chinese system. But in reality the top power elite, the twenty-five to thirty-five individuals who at any given time oversee all sectors of work and politics, personally redefine the real rules of the game on an ongoing basis, and they are constrained only by the views and actions of others within this inner circle.<sup>73</sup> But, it is only in the case of institutions that the PRC falls short and it is even far less institutionalized as a political system than was the imperial Chinese

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<sup>72</sup> This meant, that 80 per cent of any foreign currency earned was given to the centre, who would reimburse in RMB.

<sup>73</sup> Kenneth Lieberthal, *op. cit.*, p.184.

government.<sup>74</sup>

In the reform era, according to some scholars like Susan Shirk and Linda-Chelan Li, a major trend emerging from the intense conflicts and interactions between the centre and the provinces is a gradual move towards institutionalization.<sup>75</sup> This move is characterized by shifts in two aspects.<sup>76</sup> First, the emphasis shifted from an unscrupulous scramble for resources to a clearer definition of jurisdiction - whilst resources were still the ultimate concern in central-provincial relations, jurisdiction was regarded as the best means for securing new resources, as well as retaining existing ones. Second, the centre and provinces found that in order to protect their respective interests they would need a clearer specification and a closer observance of the rules. Clarity had to replace ambiguity in the definition of their relationship and in the conduct of their interactions.

Towards the late 1980s and early 1990s bargaining between the centre and the provinces was increasingly preoccupied with a better demarcation of jurisdiction.<sup>77</sup> Not only should the specific assignment of authority and

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<sup>74</sup> *Ibid.*

<sup>75</sup> Linda-Chelan Li, *Centre and Provinces: China 1978-93*, Clarendon Press, Oxford, 1988, pp.289-94.

<sup>76</sup> *Ibid* p.289.

<sup>77</sup> *Ibid*.p.290.

responsibility be fair and consistent, it was argued, but more importantly the demarcation of jurisdiction should be laid down in law, and even included in the constitution, to ensure its relative stability and security from encroachment on both sides.<sup>78</sup> These calls for a clearer demarcation of the jurisdiction of the central and provincial governments were unprecedented and went beyond mere requests for an adjustment to the existing distribution of power and resources. In calling for the institution of a regularized avenue through which to resolve disagreements in future, they embodied a new recognition of the need for a higher level of institutionalization within central-province relations.

A corollary development to the above happenings was the gradual move from ambiguity to clarity in central provincial interactions. Under the pre-reform political system, when the central power was stronger, provincial governments often sought to blur the clarity of central policies. Vague policies increased the space for provincial discretion during implementation. The ambivalence of central policies and the inconsistencies within different central policies also allowed provincial governments to play off one central prescription against another, as well as to escape responsibility for their discretion. The benefits of this ambiguity extended to the centre as well, because it facilitated the making of policies and their implementation in the form of experiments and minimize the political risk of

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*Ibid.*

failures. Notwithstanding the dominance of ambiguity in central-provincial relations, a new trend has started emerging. The shift from bargaining for resources to clearer demarcation of authority, called for a change in the nature of interactions. There would still be bargaining, but the nature of bargaining changed substantially.<sup>79</sup> Success and failure no more depended on manipulating ambivalence but in defining and clarifying the boundaries of jurisdiction to one's advantage, and make it binding on the other parties. This necessitated a greater regard for laws and regulations and for a more institutionalized manner of interacting.<sup>80</sup>

## **INTER-PROVINCIAL COMPETITION**

Closely related to the shift in centre-province relations as a result of Dentist decentralization was the question of inter-provincial relations. The most remarkable change in the area of inter-provincial relations came about in the form of inter-provincial competition. Not that such a competition was non-existent in the Maoist era, but this seems to have heightened in the post-Mao era. There are two important points worth noting here. First, the reconstruction of the economic system led to the emergence of new provincial winners and losers. For example, the concentration of heavy industrial complexes in the north-eastern provinces of

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<sup>79</sup> *Ibid.*, p.294.

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Jilin 54 and Heilongjiang, once the source of their wealth, has now become a liability for them.<sup>\*1</sup> Previously the major beneficiaries of central planning, state ownership and central investment, they now became the main losers of a strategy that favours small, non-state-sector light industrial enterprises. Second, there is resistance to the interior and the west to the preferential treatment granted to provinces in the south and east. There are three main points to be noted in this argument:

- 1) low state-set prices for raw materials and semi-finished products were retained, whilst finished products increasingly fetched higher, market prices. This has been irking many in the interior who produce raw materials.
- 2) Many leaders in the interior are also disturbed by special policies implemented in coastal provinces, especially in the Special Economic Zones (SEZs).
- 3) leaders in the interior appear skeptical that the much-promised "trickle down" of wealth from the coast will in fact occur, and fear that an extension of market forces will instead lead to a polarization of national wealth. These fears have reinforced the inclination to keep local resources within the province. Since this policy obstructs the expansion of inter-provincial trade, the suspicion that trickle down will not occur may become

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\*1 Shaun Breslin, *op.cit.*, p.68.

a reality.

Conversely, leaders in coastal provinces counter the complaints from the interior by arguing that too much of their income is used by the state for investment in the interior. They suggest that if they are allowed fully to exploit their economic strengths, then this will indeed aid the interior through the process of 'trickle-down'.

As mentioned earlier, competition between regions for preferential central treatment has always occurred in China but the potentially higher gains made possible under the market-driven decentralization strategy has enhanced this competition, and represent a heightened perception of provincial interests generated by the uneven central treatment of different provinces.

## **DECENTRALIZATION AND INCREASE OF ENTERPRISE AUTONOMY IN DECISION-MAKING**

Since 1980, industrial enterprises in the PRC, accounting for the most of the gross output value from state industries, have been granted the right to retain part of their profits instead of turning them over entirely to the state. Also, they have been given greater power to make their own decisions. The practice has given the management and the workers of these enterprises incentive to improve production and business operations, resulting in higher incomes for the workers, the enterprises, and the state.

Before the reform, producers did not have the right freely to sell their products. All products, including raw materials, facilities and machines, were allocated to enterprises according to state plans. Under the new system, the producers are encouraged to contract with buyers beyond state plans. For example, a mine is allowed to sell its iron directly to a steel works, and a textile mill can sell its cloth directly to a clothing factory. Breaking through the conventional lines of division between industries and trades, associations for various economic sectors have been established. The associations are composed of producers and buyers of particular products, such as steel or clothing. These specialized associations act very dynamically to promote business dealings in a market environment. The associations provide their members with updated information about market demand and supply for their products and organize marketing conferences to facilitate contacts and negotiations among producers, marketing agencies and buyers.

Mainland China's reforms had achieved significant success by 1984. This encouraged authorities to deepen and strengthen economic reforms, focussing on the changes of relationship between the state and enterprises, and between planned and market economies.<sup>82</sup> At the Third Plenum of the CPC's Twelfth Central Committee, one of the most important documents on economic structural reform

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<sup>82</sup> Zhong Zhu Ding, *op.cit.*,p.24.



was adopted on October 20, 1984.<sup>83</sup> According to the document, the goals of the reform to be pursued by Chinese authorities were:

1. To develop socialist market economy combining beneficial parts from both the state planning system and the free market system.
2. To revitalize enterprises, the key to restructuring the national economy, by granting them greater autonomy.
3. To establish a flexible price system to reflect demand-supply conditions and to facilitate economic resource allocation.
4. To separate government control from enterprises' operating processes, enabling them to make economic decisions independently based on market competition.
5. To create a new distribution system rewarding workers according to work performance, thereby stimulating production growth.<sup>84</sup>

As planned under the new system, enterprises bear the primary responsibility for undertaking production, construction, service, and commodity circulation.<sup>85</sup> The enterprises have been divided into industrial, transport and

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<sup>83</sup> As cited in *Ibid.*

<sup>84</sup> CPC Central Committee *China's Economic Structure Reform Decision of the CC Central Committee*. (Beijing: FLP, 1984) As cited in *Ibid.*

<sup>85</sup> *Ibid.*

telecommunications, construction, commercial, and service sectors. Since the enterprises are of great importance, they need great vitality to lead the economy.<sup>86</sup> The Chinese reformers understood that this vitality can only be built in two ways: enterprises need to be free from unnecessary state control and an organized internal vitality needs to exist between the managerial leadership and the workers and the staff under the new system, an enterprise has the power to adopt flexible and diversified forms of operation; to plan its production, supply, and marketing; to keep and to budget funds; to employ and remove its own personnel; to decide on how to recruit and use its work force; to set wages and rewards; and to set the prices of its products within limits prescribed by the state.

Under reform, each enterprise is gradually becoming an independent entity as both a producer and a seller of its products. The reformers believed that production strength and vitality would come from managerial efficiency and workers' initiative. Workers' initiative in turn would be encouraged by benefits.

From 1985 to 1988, the PRC government imposed three major reform measures on the urban economic structure. First, the authorities slowly reduced the central government's direct control of enterprises by perfecting a system of indirect control, under which the government levies taxes instead of having all profits. Second, the government transferred power to the publicly owned

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<sup>86</sup> State Statistical Bureau, *Zhongguo Tongji Zhaiyao* (China Statistical Digest) (Beijing: 1993), pp. 19-20.

enterprises. Of large and medium sized operations, such enterprises must become much more autonomous, self-managing, and responsible for their profits and losses as socialist commodity producers and managers. Third, under planning, the commodity market was developed further by allowing more products to be distributed through the market and allowing their prices to float.

The new system has granted the provincial and major municipal governments much greater power in economic management since 1985. Before the reform, the provincial governments functioned only as representative agencies of central authorities to transmit and implement central planning in managing local enterprises. They had no autonomy to formulate independent planning for local industrial development. Under the new system, the provincial and municipal governments have gradually been granted power to formulate independently their local planning of industrial development according to central guidelines.

By 1994, all the provincial and municipal governments had been granted the same power of autonomous industrial management enjoyed by the SEZS and ETDZs. The central government has now transferred the management power of most centrally controlled enterprises to the provincial or municipal governments, except for a few enterprises of strategic importance such as the railway industry, major coastal harbours, major steel and iron corporations, and the defense industry. There are still controlled by the central government.

As seen from the above account, the decentralization strategy in the

Dengist era had wide ranging ramifications. However, a study of Dengist decentralization is bound to be uncompleted without an inquiry into the agricultural sector, the area from which Deng's reforms started unfolding. In the next chapter, an inquiry into the question as to how market driven decentralization in the Dentist era affected agriculture reforms with the Household Responsibility System (HRS) as the focal point will be inquired.

## **CHAPTER IV**

### **Market-driven Decentralization and the HRS: Deng's Strategy for Agricultural Development**

## MARKET-DRIVEN DECENTRALIZATION AND THE HRS: DENG'S STRATEGY FOR AGRICULTURAL DEVELOPMENT

As mentioned in the last chapter, in the final section, we would attempt to examine the Dengist decentralization in the agriculture sector. As the agriculture sector is too vast an area to be covered, in keeping with the requirements of this work, we would limit our study to the Household Responsibility System (HRS) which formed the core of rural reforms in general and agriculture in particular. The choice of agriculture with focus on HRS to study Dengist decentralization is influenced by more than one reason. At the beginning of the reform era, China was still a predominantly agrarian society. In 1978, 82 per cent of the population lived in rural areas: of the total labour force then, about 76 per cent worked in the countryside, mostly in agriculture.<sup>1</sup> Despite substantial progress towards industrialization over the past four decades, and despite rapid diversification of the rural economy during the reform era, agriculture still remains the foundation of the Chinese economy. Thus, success in reforming agriculture is as essential as it was to be in any other sector. Agriculture is also important for our analysis because it is in this sector that the impact of the reforms, in terms of social and institutional change, have been the most profound.<sup>2</sup> The dismantling of the

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<sup>1</sup> Data as cited in Gordon White, *Riding the Tiger: The Politics of Economic Reform in Post-Mao China*. The Macmillan Press Ltd., 1993. p.85.

<sup>2</sup> *Ibid.*

communes and the introduction of the HRS was to leave a very big impact on the countryside. To quote Tang Tsou, "of all reforms, the most profound and rapid have been those in the policies, institutions, and practices in the countryside". He further opines that "in no other sphere has political control by the upper levels been relaxed to a greater extent; nowhere have relative autonomy and freedom in managing economic affairs on the part of the lowest-level units, the households, and the individual producers been restored more quickly; and nowhere have the market mechanism and individual incentives been given a more important place within the overall framework of national planning".<sup>3</sup>

The adoption and evolution of the HRS for agricultural production in the post-Mao era turned out to be a complete reversal of the Maoist strategy. The "learn from Dazhai" movement and to build Dazhai-type counties which was considered to be an attempt to revitalize the commune system and to encourage a trend towards increasing the size and functions of collective units and minimizing the role of the individual outside the strictly defined collective framework was now abandoned. The commune system was the hallmark of Maoist decentralization with its emphasis on mass mobilization to bring about economic development and equality. In contrast, the household responsibility system (HRS) was to be the hallmark of Dengist decentralization where it (HRS) would seek to appeal to the

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<sup>3</sup> Tang Tsou, et.al., "The Responsibility System in Agriculture - Its Implementation in Xiyang and Dazhai". *Modern China*, vol. 8, January 1982, p. 41.

economic self-interests of the individual peasants.

Before going on to discuss the HRS and its impact on Chinese agricultural development, it is appropriate to know the evolution of agriculture reforms in the Chinese countryside. For the sake of convenience, China's agriculture reform can be divided to the following three major stages:<sup>4</sup> the first stage was from 1978 to 1984, when China set up and gradually implemented the contract responsibility system based on the household and with remuneration linked to output in the rural areas.

The second stage was from 1985 to 1991, when China reformed the system of state monopoly purchases and quotas, and gradually lifted controls from the market and prices of agricultural products. The third stage was from 1992 to present times, when the country started the transition to the rural market economy in an all-round way. Even in the third plenary session of the 15th central committee of the CPC which was held in Beijing on October 12-14, 1998, it was held that agriculture, rural work and farmers, are important issues that have a vital bearing on China's reforms, opening up and modernization drive.<sup>5</sup> It was held that, to fulfil the "grand trans-century development goals" set forth at the 15th

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<sup>4</sup> Gao Shangquan, Chi Fulin (ed) *The Reform and Development of China's Rural Economy*. FLP, Beijing, p. 1. (The periodisation of agriculture reforms has been done in accordance with this work).

<sup>5</sup> *News From China*, October 21, 1998, p. 8.



National Congress of the CPC, efforts must be made to further strengthen agriculture as the main foundation of the national economy, maintain sustained agricultural and rural economic development.<sup>6</sup> Thus, agriculture and rural reforms continue to occupy a very prominent position in the overall framework of China's economic reforms even after two decades of market reforms. The various phases of agriculture reforms can be summarized as follows :

1978-84: "Setting up and extensively carrying out the contract responsibility system based on the household and with remuneration linked to output."<sup>7</sup>

The agricultural reforms started with the Third Plenary session of the CPC's 11th National Congress, held in December 1978. The session paid particular attention to agricultural problems : "The session held that the whole party must concentrate its main energies on the development of agriculture, because agriculture as the foundation of the national economy has suffered serious damage in recent years and as a whole is very weak [now]..... For this purpose, we must first mobilize the socialist enthusiasm of China's hundreds of millions of peasants, must be fully concerned with their material interests economically and truly guarantee their democratic rights politically"<sup>8</sup> In accordance with these ideological

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<sup>6</sup> *Ibid.*

<sup>7</sup> Gao Shangquan and Chi Fulin. *op. cit.*, p.1.

<sup>8</sup> As cited in *ibid.*, p.2.

guidelines the plenary session put forward a series of political and economic measures for developing agricultural production. The adoption of these measures was aimed at lightening the burden on peasants, mobilizing their initiative and freeing them from anxiety.

China's rural economic reforms started with the "contract responsibility system" based on the household and with remuneration linked to output, commonly known as the fixing of output quotas based on the household on the contract responsibility system based on the household. Setting up and carrying out the "contract responsibility system" and with remuneration linked to output, and the reform of, and eventual abolition of the people's commune were two major features of the first stage of China's agricultural reform. These two reforms advanced virtually side by side. This resulted in doing away with the highly centralized management system of the communes. The Commune system gave way to the HRS in which individual initiative was no more stifled. It leads one to the conclusion that in the Maoist era decentralization took place down to the collectives with stress on egalitarianism but in the Dengist era decentralization took place to spur individual initiatives with the attraction of material incentives.

1985-91: "Expansion of the agricultural reform from the micro to the macro dimension".

The extensive practice of the contract responsibility system based on the household and with remuneration linked to output in China's rural areas bought a

change in the life of the peasants in two aspects :1) property rights; and 2) status. Though these aspects were incomplete at first, the preliminary conditions started to emerge for the overall development of the rural commodity economy in China.

During the course of the rural reform, the peasants have gradually won more freedom to engage in economic activities, while obtaining more property rights. It is the basic guiding principle of the rural reform to show full concern for the peasants' material interests economically and guarantee their democratic rights.

The essence of the second stage of the reform was a profound adjustment of relations between the state and the peasants, which will be dealt in greater detail in the concluding part of this chapter. This led to further changes in the relations between urban and rural workers, workers and peasants, and in the relations among various sectors of the national economy. The aim of the unified and fixed state purchase was to redistribute the national income in the name of purchasing and selling commodities. Each portion of agricultural products sold by farmers to the state meant a contribution to the state, each agricultural product purchased by workers, staff or enterprises was equivalent to obtaining welfare from the state. Hence, the reform of the unified and fixed state purchase system, while focussed on exchanges at equal value, unavoidably affected the readjustment of the basic interests - of all urban and rural producers, consumers and operators, and will surely lead to profound changes of the overall economic set up and organizational forms.

1992-98: "Approaching the market economy in an all-round way" In the 1980s, China secured tremendous successes in agricultural reform as a whole, in spite of certain problems. First of all, agricultural production increased by a large margin and the land output rate and the production rate of agricultural labourers improved. At the same time the focus on grain as the "very link" was changed and the agricultural production structure was gradually optimized. Meanwhile, township enterprises,<sup>9</sup> which suddenly came to the fore, have played an important role in developing the rural economy, and farmers' incomes have increased by a large margin and their livelihoods have improved remarkably.

## **THE INTRODUCTION OF THE MARKET AND THE RURAL REFORMS OF CHINA**

The introduction of the market mechanism went a long way in changing the shape of the rural economy in the Dengist era. The achievements of China's rural reform in the Dengist era manifested in the growth of the market system, setting up of the HRS, and the emergence of township enterprises, among which there is

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<sup>9</sup> The term "township and village enterprises" first appeared in a party and government notice that confirmed the March 1984 "Report on opening of a New Phase for Commune and Brigade Enterprises of the State Council Ministry of Agriculture, Animal Husbandry, and Fisheries." This notice announced the breakup of the people's communes and a name change of the former "commune and brigade enterprises" to "township and village enterprises". This was followed by official acceptance of the individual peasant enterprises and joint capital enterprises that succeeded the commune and brigade industries in village society was greatly enhanced. Recently, they have also become remarkably active producers of goods for export.

an interconnection. Without the household contract system there would be neither the growth of the market nor the emergence of township enterprises.<sup>10</sup>

The fact that the HRS has become the core of the basic achievements of the rural reform in China has profound implications. First, the household contract responsibility system has led to profound changes in rural property relations. During the period of the people's communes, rural properties belonged to the farmers organized in collectives. However, such ownership was in name only. After the founding of the HRS, changes took place in the existing form of original collectively owned properties, i.e., though the farmers do not have ownership, they have occupation and use rights. On the other hand, they also have independent property ownership, including the right to make investment in the land and obtain added income therefrom. Farmers, enjoy complete ownership after they have paid taxes and handed in other necessary fees to the state. Farmers' property rights have thus been re-established, greatly spurring their enthusiasm for production. Second, the peasants enjoy considerable freedom after the introduction of the HRS. The people's communes adopted the system of management of paramilitary organizations, and farmers were restricted in their work and movements. But since the founding of the household contract system, they have not only obtained freedom for economic activities within the contracted fields, but also the freedom

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<sup>10</sup> Gao Shangquan and Chi Fulin, *op. cit.*, p.14.

of economic activities in the self-operated economic fields.

The market economy regulates economic life mainly with the market as guidance. The market is the total sum of exchange relations.<sup>11</sup> Exchanges are carried out by the market's main bodies, or economic entities. Not all economic units may become the main bodies of the market. The basic characteristics of the market's main bodies are distinct ownership related and independent operation rights.<sup>12</sup> The first and foremost contribution that the household contract system has made to the development of the market system is that the system has created a large number of market main bodies, thus enabling millions of peasants and rural households to enter the market. Peasants have started to organize and readjust their production and operation activities with the market as the center. The disposition of rural resources is being allocated more and more by the market. Hence the household contract responsibility system laid a micro organizational foundation for the market economy system in the rural areas.<sup>13</sup>

The appearance of the market led to an increase in the prices of agricultural products. the labour and the output of agricultural products has increased by a large margin. The increase in agricultural production has alleviated the long-

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<sup>11</sup> *Ibid.*, p.15.

<sup>12</sup> *Ibid.*

<sup>13</sup> *Ibid.*, p.16.

lasting shortage of agricultural products and provided the material conditions for the state to change the original planned and centrally controlled production, purchase and marketing of such products.<sup>14</sup> On this basis, the state adopted a series of measures : First, China replaced unified state purchase of grain, cotton and edible oil by contract purchase, lifted controls from the purchase and marketing prices of the overwhelming majority of agricultural products, allowed peasants to sell products not included in the purchase contract as they wished, and encouraged free competition through various channels. Now, of the total sales volume of agricultural and side-line products sold by peasants, that purchased according to contracts makes up less than one fourth; market regulation in the circulation of agricultural and sideline products occupies the dominant position.

After the first step was taken in the rural reform (the adoption of the contract responsibility system based on the house-hold with enumeration linked to output), the next step weakened the control by direct planning step by step, reduced administrative interference and constantly strengthened the growth of market mechanisms. Thus farmers were encouraged to decide their own economic activities according to market rules. Consequently, the rural market economy developed vigorously.

The scope of the rural economy regulated by the market has constantly been enlarged. Of the total volume of agricultural and side-line products sold by

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<sup>14</sup> *ibid*

farmers, those purchased according to state plans make up less than one fourth. This indicates that in the circulation of agriculture and sideline products, market regulation plays the leading role.<sup>15</sup> A rural system is being formed. Since 1979 the number of China's rural markets has doubled; the business volume increased by fifteen times, the average market sale has grown sevenfold; and wholesale markets and various specialized markets for agricultural and sideline products have been set up and expanded to over 1,600 or a more than four fold increase over the 1983 figure.<sup>16</sup> Besides, more farmers have entered the market and circulation fields. Now they are not only producers of agricultural and sideline products, but also important forces to enliven commodity circulation and boost the market. A new commodity circulation order was formed. The rural markets not only bring about tangible benefits, they also bring about intangible benefits through their influence on price and their roles in opening business, collection and distribution, information exchange, balancing supply and demand, improving business efficiency and cutting circulation costs. They have made circulation links tighter, doing away with the traditional, isolated and multi-planned circulation system. Lastly, the township and village enterprises (TVEs) epitomized the market nature of the rural reform. The TVEs made the following three important contributions to the

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<sup>15</sup> *Ibid.*, p.20.

<sup>16</sup> *Ibid.*



founding of the socialist market market economic system. a) During their development, TVEs struck powerful blows at the old highly-centralized and unified planned economic system, thus pushing forward the transition of the rural economy, and that the nation as a whole in the direction of a market economy. b) They have clearly verified that a socialist country can pursue a market economy, and that the market economy can work better and more efficiently than the planned economy in a socialist country.<sup>17</sup> c) TVEs have provided rich practical experience for deepening the reform and setting up a socialist market economic system.<sup>18</sup>

#### **THE HOUSEHOLD RESPONSIBILITY SYSTEM (*BAOCHAN DAOHU*)**

The adoption of the contract system under *bao chan dao hu* is, as seen in the above context, a transitional form towards a fully-fledged system of private household farming. Initially, under *bao chan dao hu*, the production team was formally retained as an accounting unit. Collective work, however, was abandoned, and land was allocated to each household in accordance with the active number of workers per household. The production team established an output contract with the individual household; in turn, the brigade and commune levels established output quotas for the production team. Whereas the output contract

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<sup>17</sup> *Ibid.*, p.21.

<sup>18</sup> *Ibid.*

arrangements remained, in principle, under the "unified management" of the production team, in practice the tendency was for the production team to disappear as a unit of collective work and ownership of farm machinery.

In 1978-80, the HRS took on different forms: 1) land and production quotas were allocated to individual households (*ba gan dao hu*); 2) Tasks and land (as opposed to production on quotas) were assigned to households (*bao gan dao hu*); 3) output quotas instead of being assigned to individual households were assigned to individual labourers (*bao chan dao lao*).<sup>19</sup>

According to official Chinese sources, 'the household responsibility system' had been applied to nearly 90 per cent of production teams by 1982.<sup>20</sup> Dazhai production brigade in Xiyang county, Shanxi province, once considered a model of "socialist efficiency" in the "learning from Dazhai" campaign, shifted to the HRS in 1980.<sup>21</sup> "Learning from Dazhai" began as a campaign to promote local 'self-reliance' and putting 'politics in command'. 'Learning from Dazhai' was abandoned by Dazhai in 1980. In some areas the system of 'large scale

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<sup>19</sup> H. Yamamoto. "Three Forms of the Agricultural Responsibility System". in C.K. Leung and S.S.K. Chin (eds.), *China in Readjustment* (Hong Kong: Centre of Asian Studies, University of Hong Kong, 1983), pp. 129-130.

<sup>20</sup> Michael Chossudovsky. *Towards Capitalist Restorationism? Chinese Socialism After Mao*. MacMillan Education Ltd., 1986, p. 45.

<sup>21</sup> "Learning from Dazhai" began as a campaign to promote local "self-reliance" and putting "politics in command" in the fifties and sixties. "Learning from Dazhai" was abandoned by Dazhai in 1980.

responsibility for production' was applied. Under this system the peasants signed output contracts directly with the township government (which replaced the commune); the three level collective structure collapsed, and the township appropriated the agricultural surplus directly from the individual 'tenant' households. Alternatively the production team or groups of peasants or producers' cooperatives contracted directly with the state marketing board.

### **The Dismantling of the Rural People's Communes**

According to China's 1982 constitution, the People's commune *formally* ceased to exist as an integrated unit of self-government. Its political and administrative functions have been transferred to the township (*cheng*) and village (*xiang*) bureaucracies, which in turn are integrated into the broader administrative hierarchy of the provincial bureaucracy. So-called "village committees", which replace production brigades, essentially deal with community affairs and social services. Each committee administers one or several villages whereas the township administers up to a dozen villages. By 1984, more than 22,000 township governments had replaced the commune administration in more than half of China's rural counties. The establishment of township and village government was completed in most parts of the country in 1984.<sup>22</sup>

Collective work broke down, land was subdivided into household tracts, farm machinery acquired collectively by the brigade or the production team was

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<sup>22</sup> Michael Chossudovsky, *op. cit.*, p. 46.

either subdivided, sold, leased or distributed by the collective to individual peasant house-holds. Where the peasants failed to agree on *how* to divide the means of production acquired collectively, farm machinery either stood idle or was simply withdrawn from agricultural production. In some other cases though rare, collective buildings and machinery were dismantled or destroyed.<sup>23</sup>

In many regions of China the three-level structure of the people's commune was dismantled and administrative functions were transferred to the township (*cheng*) and village levels (*xiang*) as early as 1980. The disintegration of the production team as a unit of both collective property and collective work was conducive in some regions, to the re-emergence of mutual aid teams and agricultural producers' cooperatives, similar in form to those (of the less advanced type) which developed in China in the early 1950s. These new co-operative schemes enable several households to acquire farm machinery which they are not in a position to purchase individually. In other cases, machinery is purchased individually and owned privately by rich peasants. In the rich farming areas, the formation of producer's co-operatives is dominated by the well-to-do peasantry.

New patterns of co-operation initially emerged after 1978 in small-scale rural industries, workshops, and so on. In this context, *small work groups*, involving the participation of several households, developed in activities such as

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<sup>23</sup> *Ibid.*

carpentry, repair workshops, brickmaking and handicrafts, and so on.<sup>24</sup> In the workshops, two or three households participated on a co-operative basis whereas in small-scale industries, 10-15 households were involved. The smaller units were owned and managed directly by the peasants. In Henan province, for instance, households were initially share-holders in that they participated in the earnings of small-scale industry in relation to their relative contribution to the investment fund. Under this system household earnings were based partly on work performed (in terms of work-time) and partly on ownership of real capital assets.<sup>25</sup> These ownership structures were in many respects transitional towards fully-fledged private ownership; inasmuch as they created a situation where earnings were based on ownership of real assets, they encouraged the development of private appropriation and accumulation. The underlying structure enabled individual peasant households to enrich themselves at the expense of those who 'participated' in terms of work-time rather than capital assets.

The new co-operative schemes should be distinguished from those which developed in the fifties. While they are similar *in form*, the 1950s mutual aid teams and elementary producers co-operatives developed *historically* within the context of the agrarian revolution as *transitional forms* which were subsequently conducive to the formation of more advanced forms of collective property and collective

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<sup>24</sup> W.H.Hinton. "More on China's New Family Contract System". *Monthly Review*, XXXV:11 (1984), pp. 114-46.

<sup>25</sup> *Ibid.*, p. 146.

work. This restoration of elementary co-operative forms, therefore, does not constitute a repetition of the institutional set-up of the 1950s.<sup>26</sup>

Inasmuch as the new co-operative schemes may indeed be interpreted as *transitional* forms, in the economic and social process of change since 1977, they are in no way *transitional* to more advanced forms of collective work and collective property. These new co-operative schemes are often characteristic of the producers' and marketing co-operatives which exist in many capitalist Third World countries and which essentially serve the interests of the farmer-entrepreneur.<sup>27</sup>

The reforms have led to the private marketing of agricultural output in the form of marketing co-operatives in which peasants are shareholders.<sup>28</sup> In practice, the rich peasants and so-called 'specialised households' dominate the marketing co-operatives because they control a large proportion of the co-operatives' stock. The co-operative will pay dividends to shareholders. surplus income is "used to give financial and technical support to rural producers".<sup>29</sup>

### **De-collectivisation and Ownership of Land**

The Communist Party initially stated in 1980-81 that "the public ownership

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<sup>26</sup> Michael Chossudovsky, *op. cit.*, p. 47.

<sup>27</sup> *Ibid.*

<sup>28</sup> *China Daily*, 22 January 1984, p. 7.

<sup>29</sup> *China Daily*, 18 January 1984, p. 4.

of the means of production will not change. The peasants only have the right to use, not to buy, sell or transfer the land, farm machinery, [and so on] owned by the production team".<sup>30</sup> Despite government "guidelines", however, there were numerous reports of so-called "illegal land deals" where land was bought, sold or exchanged. These transactions took place without the existence of legal titles of ownership.

The main issue here is not whether private ownership of land is reinstated or not. The private farmer need not own property in the form of land; he has, however, the *private use* of agricultural land. Under the contract system, land allocated to households 'will remain under their management for at least 15 years' with the possibility of transferring the land to their heirs.<sup>31</sup> These provisions (adopted by the Central Committee in 1984) are conducive in practice to the privatization of land in that they establish *de facto* property rights.<sup>32</sup>

### **The Privatization of Farm Machinery**

The ownership status of movable means of production is far more decisive than ownership over land because it defines the nature of social production

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<sup>30</sup> *Beijing Review*, 24:34 (1981), p. 18.

<sup>31</sup> See CCP Central Committee "Circular on Rural Work in 1984", *China Daily*, 4 February 1984.

<sup>32</sup> Michael Chossudovsky, *op.cit.*, p. 48.

relations.<sup>33</sup> Whereas the CPC initially stressed in 1978-80, collective ownership of farm machinery and draught animals, it nonetheless officially sanctioned the private purchase of the means of production, including the extension of bank credit to individual farmers. In other words, the agricultural system allows for private forms of appropriation which depend not only on the amount of land allotted by the 'collective' to each household, but increasingly on the existence of privately-owned means of production.

Private ownership of farm machinery developed primarily as a result of the break-down of the People's Communes with the mechanics of privatization differing from one region to another.<sup>34</sup> Generally, with the adoption of the HRS there was a tendency for small farm machinery and draught animals belonging to the production team to be transferred to individual households or groups of households. In some townships, collective ownership of large tractors was initially maintained alongside the privatization of small farm machinery is related to the development of the farmer entrepreneur what the CPC Central Committee entitles officially the 'specialized household'. In some cases, collectively owned farm machinery was sold by the commune (or township), in other cases it was rented out on a concessionary basis to rich peasants who operated the tractors as private

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<sup>33</sup> *Ibid.*, p. 49.

<sup>34</sup> *Ibid.*, p. 50.



entrepreneurs by selling their services to other peasants for a fee. The concession was invariably granted to the highest bidder, that is, the household which guarantees the highest rent on the equipment to the village or township will be granted the concession.<sup>35</sup>

## CONSEQUENCES OF DECOLLECTIVIZATION

The dismantling of the communes and the introduction of the HRS had wide ranging ramifications. In this section an attempt will be made to highlight the consequences of the HRS in changing the face of the rural economy. According to a survey by the *Economist*, "Grain output grew by one third in six years, cotton almost tripled, oil bearing crops more than doubled, fruit production went up by half. Real incomes in the countryside grew even more spectacularly - threefold in eight years"<sup>36</sup> The success of the HRS led to the vast proliferation of markets, rural industries, and migration. Farmers obtained independent decision-making regarding diversity of crops, new industries, market activities, and the power of allocation of rural labourers and capital. Having mentioned all these achievements it will be the drawbacks of the HRS. It led to concentration of land in the hands of rich peasants, the emergence of the so-called "specialized households".

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<sup>35</sup> *Ibid.*

<sup>36</sup> "When China Wakes: A Survey of China". *The Economist*, (November 28-December 4, 1992), as cited in Kate Xiao Zhou, *How the Farmers Changed China - Power of the People*, Westview Press, 1992, p.175.

privatization and regional polarization, social inequality and further impoverishment of the poor peasantry. It led to the shortage of food grains and infrastructural bottlenecks. This has led to a situation where "self-reliance" which was once a vital part of Chinese developmental strategy has given way to a situation where the internal allocation of productive resources is increasingly subordinated to the laws of the capitalist world commodity market rather than to the principles of socialist planning.

The above discussion brings into focus the question of the effectiveness of decentralization in finding solutions to the ills faced by the Chinese economy in the Maoist era. The conclusion which one would arrive at is that, after two decades of dismantling of the previous planned economic system, the Chinese economy is better-off today. The market is playing an increasingly important role in the operation of the economy, economic growth has picked up speed and people's living standards are fast improving.

### **The Liberalization of Rural Market**

One of the most significant consequences of the HRS was the opening up of markets. Free markets were opened in few months after the Third Plenary of the Eleventh CPC Central Committee in late 1978.<sup>37</sup> Although prices of basic

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<sup>37</sup> Michael Chossudovsky, *op.cit.*, p. 70.

grain staples are regulated by the state, for non-grain commodities (for example, meat, poultry, fruits and vegetables) the tendency is towards complete price liberalization through a gradual convergence of the "regulated price" to the "free market clearing price".

The duality of the price structure characterized by the co-existence of free market and state-regulated prices, has had an important effect on land-use patterns in agriculture. This duality is, however, transitional in as much as Communist Party policy is towards the complete liberalization of prices in accordance with "the law of value".<sup>38</sup> State prices are either adjusted upwards to conform with the free market price or state controls over prices are lifted altogether. In agriculture, state regulated prices increasingly apply only to staple food products which are purchased with ration coupons.

### **Land-use Patterns**

The overall liberalization of agricultural prices, particularly in non-staple foods, has favoured a shift in land-use patterns which reduces the areas allocated to grain production. On the other hand, industrial cash crops such as cotton, tobacco, silk, oil bearing crops, and so on, have generally been favoured at the expense of grain. Vast agricultural areas have been transformed into tobacco and cotton fields, and in the vicinity of large cities extensive fruit - and vegetable -

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<sup>38</sup> *Ibid.*

producing areas have developed.

### **De-collectivisation and Open Door Policy**

With the liberalization of foreign trade in the post-Mao era, the structure of world commodity prices has had a decisive impact on the internal price structure. For instance, China imports both grain and cotton: the relative world price of these two commodities will influence the internal relative price structure, that is, an increase in the domestic procurement price of cotton (conducive to a corresponding shift in land-use patterns) enables China to "import substitute" cotton. Consequently, the domestic production of cotton is increased, foreign exchange is thereby saved by importing less cotton and more grain. Whereas this cost-revenue calculation is essentially sound from a strictly financial standpoint, the internal allocation of productive resources is increasingly subordinated to the laws of the capitalist world commodity market rather than to the principles of socialist planning.

The present grain policy is characterized by what might be described as "taking the world economy as a key link".<sup>39</sup> Despite an increase in the price of grain, the structure of relative procurement prices promotes regional and crop specialization and tends to destroy the structure of local self-sufficiency in grain. The concurrent increase in grain prices (along side the substantial increase in the prices of non-grain products) was largely motivated so as to avoid a massive shift

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<sup>39</sup> *Ibid.*, p. 72.

out of grain production. Whereas post-1978 grain harvests have been reasonably successful, the shift in land-use patterns at a regional level, the increased use of grain for animal feed and agro-industrial use as well as the liberalization of agricultural markets have resulted in localized patterns of "grain shortage".

### **The Emergence of Rich Peasant Class**

The de-collectivisation of agriculture resulted in the emergence of - rich peasant class. This phenomenon manifested itself in various forms like the emergence of "specialized households", the concentration of land in few hands, "proletarianization" of the poor peasantry and social inequality and the rural distribution of income.

The transition from collective to private and co-operative ownership of the means of production was initially conducive to the disengagement of farm machinery from production, particularly in the less affluent agricultural regions. The initial fragmentation of landholding under a system of 'equal distribution' of land gradually evolved, however, towards the **concentration of land** in the hands of the well-to-do peasantry. This in turn increased the size of the land-output unit and encouraged the use of privately-owned (and purchased) farm machinery by the "specialized household" farmer-entrepreneur. The adoption of the HRS by the CPC Central Committee in 1978 initially resulted in the fragmentation of collective land into household tracts. The transition from collective to private ownership of the means of production, however, created the social and material basis for private

appropriation and accumulation. In turn, this process led to the transformation of structure of land distribution. The system of "equal distribution" of land under *bao chan dao hu* was gradually eroded. Rich peasants and owners of the farm machinery (designated officially as "specialized households") were given larger tracts of farm land under the new principle of "contracting according to ability". The process of land concentration proceeded alongside the "proletarianization" or "semi-proletarianization" of the peasantry. Hired wage labour developed with the concentration of land and farm machinery and the formation of so-called "specialized households". The CPC Central Committee officially sanctioned the unequal distribution of land as an instrument of "socialist modernization".<sup>40</sup>

Support should be given to the rich peasant:

"The road to general prosperity was opened up by the Third Plenary Session.... The First [objective] is to wipe out egalitarianism and carrying out the socialist policy of distribution according to work.... To bring general prosperity to all peasants is our general objective. To allow some of the peasants to become well-to-do is our strategic way to reach that goal. To allow some of the peasants to become better off first, we can on the one hand encourage the poorer peasants. On the other hand it will enable the more prosperous peasants - who have experience in crop production, side-line production and various trades - to share those experiences with poor peasants".<sup>41</sup>

Rich peasants are now viewed as having management and scientific abilities.

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<sup>40</sup> *Ibid.*

<sup>41</sup> *China Daily*, 6 September 1983.

Their entrepreneurial skills are not seen as the basis of social division but as contributing to the promotion of the *peasants' general prosperity* and to the upward social mobility of the poor peasants. According to the CPC Central Committee, the rich peasants are the agents of "socialist construction" in China's countryside. "They are disseminators of science and agro-techniques as well as advanced builders of socialism."<sup>42</sup> At an ideological level, the emphasis is on individual initiative rather than on collective endeavours.

"Our policy is to encourage peasants to become more prosperous, we encourage some people to be very rich and that way others can learn the they can become rich later, those who have skills and technology may become rich earlier".<sup>43</sup>

## **THE DE-COLLECTIVISATION PROCESS AND SHIFTING OF STATE - PEASANT RELATIONS**

The de-collectivisation and the introduction of the HRS led to a distinctive change in the state peasant relations. Agriculture's performance, especially in the second half of the eighties highlighted some of the contradictions between the economic motivations and activities of peasant and state which had emerged in the wake of de-collectivisation and the move towards a more demand-oriented system of agriculture production and distribution. In a situation in which the economic goals of the state and peasant coincide, a shift of power from one constituency to

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<sup>42</sup> Statement by Wan Li, a member of CPC Politbureau, quoted in *China Daily*, 19 January 1984.

<sup>43</sup> *China Daily*, 6 September 1983.

other is bound to create tensions.

The post-Mao era reforms gave peasants much more control over production decisions than they had enjoyed since the early 1950s. For example, encouragement to sell more through markets and the institution of supposedly voluntary contracts for the delivery of grain and cotton, reinforced peasants' sense of independent decision-making. In so doing, it led them, in their search for income maximization, towards a structure of agricultural production which threatened to undermine the fulfilment of certain key goals, such as the maintenance of grain supplies for urban consumption and industrial use. As early as 1986, the government was in retreat and had effectively reintroduced mandatory quotas for grain. By 1990, "contractual procurement" of grain had given way to "state procurement", in apparent recognition of the failure of 1985 initiative to generate adequate food supplies for the cities. Besides, abandonment of the collective framework had robbed the government of a means of control and a mechanism for allocation of investment funds and other scarce resources. With state investment declining and no increase in private investment by peasants, infrastructural bottlenecks became a serious problem.

The relations between state and peasant underwent a change not only *vis-a-vis* the centre but also with regard to local governments. The power of the local governments was encroached upon by the increased power of the markets and rural merchants. When farmers' production became linked to market demands, the



farmers sought to maximize profits, they developed a drive difficult to contain. Because they were not organized, they could only be contained separately. Local cadres whose authority was challenged, tried every means to reverse the market trend. After 1985, a decrease in grain drove the market price up 10 per cent, but grain farmers tried to avoid the state plan system and tried to sell at the market price. In order to guarantee the purchase plan, the state set up regulations for every level of administration to enforce the purchase of cheap grain from farmers. Whenever one level of government failed to deliver the fixed quota, that government body would have to buy high priced grain to meet urban demand.

In order to provide lower level cadres with incentives to enforce the plan, the state allowed local cadres to control the sales money and allowed some control over the finances of farmers, the Deng regime restored some controls to limit the negative consequences of market in the agriculture sector. Local government's response was to close local markets, at the markets. To counteract the new impositions, farmers tried to sell their produce outside local markets. Many local governments had to use road blockades and repression to try to stop the flow of farm goods. This pattern of local anti-market behaviour tightened when the reforms decentralized power. But the farmers tried their best to move around the local government restrictions and sell their goods at a higher price. They had learned market participation.

# **CONCLUSION**

## CONCLUSION

China before 1978, by most accounts was essentially a command economy. The Maoist period, as seen from the first and the second chapters was initially characterized by the stultifying structure of centralized power that was copied from the Soviet Union in the 1950s and then became congealed by a multitude of bureaucratic interests. Under this system the most important activities of enterprises even those normally under collective ownership were controlled by the central plan, the enterprises had only to fulfil its allocated tasks. If it made profits, they reverted directly to the state: the losses were subsidized. But, as the Chinese economy grew and became more complex, the ability of the state to administer it effectively from the centre declined, and the irrational consequences of the system became more pronounced. The Soviet model of development had its own advantages in the initial years of the PRC after decades of internal chaos and exploitation by imperial powers, the establishment of a powerful centralized authority appeared to be a national imperative and as the only alternative. However, the Soviet model gave rise to various problems like "over bureaucratization" neglect of agriculture and over-centralization.

Mao Zedong was extremely critical of the over-centralization and bureaucratization of the FFYP. He felt that the CPC should devise a strategy of development which would negate the evils of the FFYP and turn the vast labour

force of China into a strength instead of a weakness. Such objections fitted with CPC's preference under Mao's leadership for a mobilizational strategy based on administrative decentralization. Rather than de-emphasizing political criteria governing the daily activities and replace them with what Deng Xiaoping would later term 'objective economic laws', Mao sought to mobilize localities precisely on the basis of political enthusiasm. It is because of this very reason that Mao's period is said to be characterized as one in which "politics (was) in command" for Mao, the alternative to the command economy based on "executive orders" was not the market, but rather social mobilization using "mass line" methods of leadership.

The proper environment for implementing this approach was an administratively decentralized one, with substantial control over economic activity wielded locally, primarily by the local party committees. In the ideal case, the localities and collectives on which economic authority would devolve would be small enough for their members to perceive personal benefit in economic success and therefore would be highly motivated. "Material interest" was thus a part of Mao's solution, although it operated chiefly at the group/collective level.

Mobilization depended much on direct communication between the political centre and the regions and localities, bypassing much of the state bureaucracy. Therefore, it leads one to the conclusion that Mao's strategy of administrative decentralization, while it heightened the authority of local areas in actual practice

it also simultaneously concentrated power at the very top.

The Maoist decentralization had severe limits. This was by no means an economy without central controls. In fact, central government was never prepared to allow local governments to operate in an independent manner before the reform era. The central government wished to maintain control over the general direction of local development, and it wished to maintain the basic parameters of the planned economy. These controls were designed to keep the economy from veering outside the bounds designated in Beijing. Three kinds of central control were particularly important: ideologically exerted controls over development strategy, tight controls over labour mobility and remuneration, and central control over commerce and agricultural procurement.

Ideological guidelines required that localities replicate central government development priorities (development strategy) at the local level. Local governments were instructed to develop heavy industries, particularly those that produced inputs for modernization of agriculture. This meant a stress on producer goods industries. Development strategies that emphasized production of consumers good with high markups were forbidden by strictures against 'putting profit in command'. Moreover, the government maintained monopoly control over agricultural procurement. In addition, China maintained strict controls over labour and remuneration. Migration to cities by rural individuals was forbidden. Only a modest intake of rural workers into the industrial economy was permitted through

tightly restricted recruitment programmes. This small flow into urban areas was more than overbalanced by sending down the youth to the countryside to work for indefinite periods. Within the cities, labour mobility was virtually non-existent.

The Chinese command economy traditionally operated with a strong centralized monopoly over commerce. Monopoly purchase of grain actually preceded agricultural collectivization in China, and even during the GPCR when much of the industrial management system was being decentralized, central control of agricultural procurement and distribution of key consumer goods continued interrupted. Virtually all commercial personnel worked for units organized into the state Ministry of Commerce System. In rural areas, most commercial transactions were carried out by the supply and marketing cooperatives - nominally an organization but in fact a heavily bureaucratized organization that functioned as the rural wing of the Ministry of Commerce. Peasants were forbidden to bring produce into the city to sell, and all urban free markets had been closed since the beginning of the GPCR.

The Maoist strategy of administrative decentralization which took the shape of the GLF resulted in many problems. With planning in disarray and market forces inoperative, much output was of too low quality to be used. Quality and variety were reflected in the rush to produce greater quantities. The Rural People's Communes, as it was argued by the "reformers" became a vehicle through which the state intervened directly and improperly in the affairs of agriculture, thus

depriving farmers of the incentive and authority needed to develop their local economies. The Maoist era in which "politics (was) in command" was used to override objective constraints. During the GLF, it came to mean that with the correct attitude any desirable goal could be achieved.

The above account leads one to the conclusion that Mao's administrative decentralization led to many problems. But the main reason behind its dysfunctioning and eventual failure, was not the strategy of decentralization *per se*, but its seemingly hasty formulation and poor implementation. Decentralization without clear principles for dividing authority led to chaotic authority relations. Throughout the Maoist era, China continuously sought a workable set of principles for decentralization, resulting in a restless shifting among different schemes and chaotic and conflicting authority relations at the enterprise level. The crucial point is simply that no stable or effective system for dividing responsibility between governmental levels was ever developed.

The chaotic state of the administrative system was exacerbated by the chronic factionalism of the Cultural Revolution. Both in the enterprise and higher up the administrative hierarchy, opposing factions had contended for control since the late 1960s. In many cases authority had see-sawed between different groups. Decision making had become more and more difficult, and the system was close to paralysis. Matters were made even worse by the absence of a system of material rewards that could be used to motivate workers and managers to meet planners'

goals. The Chinese economy was in a state of progressive devolution in which even the tasks to which the command economy was suited became difficult. Thus, by 1977-78, China's planners were struggling with a system that was carrying serious drawbacks.

The Third Plenum of the CPC Central Committee held in December 1978 signalled the dawn of a new era in the history of PRC. The reemergence of Deng Xiaping as the paramount leader of the PRC in the post-Mao period led to an era where an entirely new strategy of development was to be adopted. In the Dengist strategy, market was to occupy a pivotal position and as mentioned earlier in the third chapter, the introduction of the market in itself represents a form of decentralization. Deng's strategy has been termed "market decentralization" in contrast to Mao's "administrative decentralization". Ideologically, the reformers emphasized the need to treat "politics" and "economics" as distinct spheres and avoid subordinating the latter to the former. At the institutional level, this separation implied a more limited role for the party in the every day process of economic management. The system of 'interlocking directorates', whereby party officials 'wear two hats' by holding office as administrators would have to be reduced. This meant greater role specialization, more groups in their own areas of expertise, and changes in occupational recruitment criteria, from "redness" to "expertise". At the motivational level, there was far greater emphasis on the material incentives as opposed to the moral-ideological incentives in the Maoist



era. In practical terms, it meant a change in priorities from "egalitarianism" to "efficiency" where individual material incentives would stimulate effort.

Whereas the Maoists had sought to reform the planning system by decentralizing power from central to local governments, the new thrust was to devolve power from any layer of government to enterprise itself: this could be described as a transition from administrative to economic decentralization. Previously argued the reformers, the economy was run as a administrative system through a complex system of central ministries and local departments. As mentioned in the first chapter, the economy was prone to the problems of over-centralization and over bureaucratization in such a set-up. The problem was not merely of administrative subordination; but also the fact that enterprise's managers were neither uniform nor consistent: they were subject to commands from numerous higher organs, functional and regional, with the result that state enterprises were subject to too many superiors. Citing these reasons, the reformers came to the conclusion that enterprises should be released from the grip of their 'superior departments'. It's pertinent to note that the reformers didn't abandon or rule out the importance of administrative decentralization. However, it should not be accorded the prime priority and, to the extent that it did take place, should be accompanied by a process of economic decentralization at the local level, so that local governments should exercise their economic powers in a new way, indirectly, rather than directly, using economic policy mechanisms, not administrative fiat.

In the new system the state would act to achieve its plan objectives by seeking to influence enterprise behaviour in a certain direction, rather than by issuing administrative orders.

The Household Responsibility System (HRS) which has been discussed in the last chapter is another example of Dengist Strategy of development which is characterized as 'market decentralization'. The HRS went a long way in freeing the farmers from the control of the state bureaucracy, and enabled them to make the best use of the market.

Improvements in economic incentives and economic efficiency are the two factors contributing to the rapid economic growth since reforms were implemented. The improvement in economic efficiency on the basis of better utilization of comparative advantages, has constituted the main reason for the economy growing much faster after reforms were put into place. The reforms caused the incentive mechanism of state owned enterprises (SOES) to improve, by introducing reforms in the micro-management institution and the resource - allocation mechanism. Hence, these enterprises production and management efficiency improved as well. In addition, the deregulation of administrative control created the conditions necessary for the development of the non-state sector included urban collective undertakings, township-and-village enterprises and private enterprise in cities and rural areas. These enterprises had to survive and develop through market competition, because they could not get preferential

treatment from the government, and their workers were not eligible for government subsidies. But it was precisely this market competition which provided the impetus for these enterprise to optimize the allocation of resources, and which introduced the income distribution system that tied remuneration to output or contribution, a system that strongly motivated every labourer to achieve a higher rate of production. It was because of the market competition and incentives system that the non-state sector of the economy surged ahead.

The reforms have gone a long way in correcting the industrial structure. Before the era of market reforms, China's industrial structure was not in consonance with its comparative advantage. But with the reforms the bias against labour-intensive industries has been gradually alleviated. Before the onset of the reforms, the government through people's communes and the household registration system, tied the peasants to rural areas and firm production. After the reforms began, the government ceased to control both household registration and job choice in favour of controlling household registration alone, thereby no longer prohibiting peasants from engaging in non-agricultural activities. Once they had acquired the right to pursue non-agricultural employment, millions of peasants, induced by higher incomes, gravitated towards non-agricultural activities of their own accord, making a very valuable contribution to the economy. This also helped in solving the under-employment problem that continued to plague the agriculture sector.

Another important contribution of the reforms was that, with the 'open door' policy, foreign trade increased rapidly. This was supplemented with a big influx of capital. The changes mark the increasing introduction of the Chinese economy into the world economy and also indicate that since the introduction of reform, the nature of the economy has been gradually growing more outward-looking.

The current economic reforms in China has made the Chinese economy very dynamic but it has also given rise to many problems. The main reason for these problem is attributed to the fact that China began its reforms with the micro-management institution by allowing enterprises and farmers a greater degree of autonomy, but reforms in the macro-policy environment have lagged far behind the reform of the micro-management institution and the resource allocation mechanism.<sup>1</sup> This has led to various problems like overheating of the economy, inflation, consumption, and imbalanced regional development.

With such problems normal economic life is thrown into disorder and people grow discontented and lose confidence in the merits of the reform. Under such circumstances, the government interferes in economic operations by instituting compulsory retrenchment programmes. This leads to further problems. First, prices are strictly controlled and government uses its administrative authority

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<sup>1</sup> Justin Yifu Lin, Fang Cai and Zhou Li, *The China Miracle: Development Strategy and Economic Reform*, The Chinese University Press, 1996, p.193.

to curb inflation, stabilize prices of consumer and capital goods and interest rates. Second, authority which is delegated is centralized. In order to discipline enterprise behaviour and eliminate the deviation of investment from traditional strategic objectives, the government often reduces the autonomy delegated to enterprises and re-centralizes the authority it has given to lower-level resources administrative departments. Third, credit control is tightened and irrespective of the efficiency of the enterprises, there is uniformity in imposing a light quota on credit. Fourth, development of non-state sectors is suppressed. Hence, the economy is paralyzed once the retrenchment programme is introduced. After a period of slow growth, voices advocating for further decentralization at the micro level become louder. Reform featuring decentralization at the micro level and liberalization of resource allocation is advocated, launching another round of decentralization and re-centralization. This policy dilemma has been continuously witnessed in the PRC time and again since the onset of the reforms<sup>2</sup>.

One of the most serious drawbacks of the economic reforms has been the imbalanced regional development. There has been widening of income disparities between urban and rural areas, disparities among coastal and inland regions. Not only this, there have been instances where there has been imbalanced growth at sub-provincial levels within a province. For example, in Jiangsu province, the Sunan sub-province is one the wealthiest areas in China, but the Subei sub-

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<sup>2</sup> *Ibid.*, p. 193ff.

province is among the poorest areas in China. Further, Jiangsu expresses inability to solve the problem because of lack of resource, the same reason cited by central authorities when it comes to addressing the problem of regional imbalances at a macro level.<sup>3</sup>

The above discussion of the costs and benefits leads one to the conclusion that the Chinese economy has become more vibrant and dynamic in the post Mao era. Despite the various shortcomings, the Chinese economy has responded very well to the market driven decentralization of Deng Xiaoping. It has been two decades since the market reforms have been introduced and it's too early to make a judgement on the capacity of the CPC leadership to handle the contradictions posed by the 'socialist market economy.' The conclusion of some Western China scholars of a China disintegrating in the future is too hasty a conclusion to be made. The Chinese leadership, has been curbing localism and regionalism with various institutional devices which helped in curbing location and enhancing central control. The Dengist decentrazation if seen in terms of "state versus market" debate, leads one to the conclusion that Deng's policy of "economics in command" has led to a situation China where the role of politics and economics has been envisaged and treated as separate categories unlike the earlier fusion of the two. The CPC leadership under Deng Xiaoping has managed to demarcate the arenas

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<sup>3</sup> J. Bruce Jacobs, "Uneven Development: Prosperity and Poverty in Jiangsu". in Hans Hendrichke and Feng Chengyi (eds). *The Political Economy of China's Provinces: Comparative and Competitive Advantage*. Routledge, London, 1994, p.143.

of politics and economics, but sooner or later the post-Deng CPC leadership has to face the problem of maintaining the correct balance between plan and market. In his Government work Report to the Third Session of the Eight National People's Congress on March 3, 1995, Premier Li Peng announced that since severe inflation still troubles mainland China's economy and overheated growth still exists, the State's macro-economic co-ordinating capacity is therefore needed to strengthen and improve the Chinese economy. Li Peng seems to be right when he advocated State intervention, for the market, even at its best, is not a panacea. As J.S. Mill discussed in his *Principles of Political Economy*, markets are subject to failure. They also raise delicate ethical problems, some of which can be addressed only through the judicial agency of the State. In its absence, the market system dissolves into a stateless and lawless society or libertarian anarcho-capitalism.<sup>4</sup> *Laissez faire* does not advocate the absence of state intervention in the market, but merely the limitation of such intrusion.<sup>5</sup> However, the main problem is that state control usually impedes the market mechanism's ability to allocate resources based on demand and supply. Therefore, to what extent state control can enhance the market mechanism is a difficult question which Chinese reformers

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<sup>4</sup> James Buchanan, "Man and State" in Svetozar Pejovich, (ed.), *Socialism: Institutional, Philosophical and Economic Issues*, Dordrecht, Lancaster, Kluwer Academic Publishers, 1987, p.3-9.

<sup>5</sup> Ibid.

must face.

Discussing China's future possibilities, Liu Guoguang considered three courses of action advocated by different groups of Chinese economists.<sup>6</sup> The first is that given China's "confused economic order", it is difficult if not impossible to move ahead with reform and that it is therefore preferable to "exercise strict macro-economic control by administrative means". According to Liu, there are apprehensions that such an approach would lead to "economic deflation" and would not necessarily yield a "free economic environment" as claimed by its advocates, who assert that they are merely cautious, and not against reform.

The second course is "stabilization of the economy..... by deepening the reform, specifically by restructuring enterprise management and developing the contract responsibility system, followed in two or three years by price reform. According to Liu, economists who support this solution argue that "the new system would occupy a dominant position in approximately eight years".

The final course is an in-between approach. It combines retrenchment with "well-devised reforms to promote stable, sustained economic growth" and aims at improving the instrumentalities of macro-economic control, strengthening the enterprise contract responsibility system "in preparation for a transition to a joint stock system", and clarifying property relations "so as to switch macro-economic

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<sup>6</sup> Liu Guoguang, (Vice-President of the Chinese Academy of Social Sciences) "A Sweet and Sour Decade", *Beijing Review*, Jan. 2-8, 1989, pp.22-24.



management from direct [administrative command] to indirect [indicative market-type] control and regulation."

Of the above three alternatives the third alternative seems to be the course which is most likely to be followed. But, how effectively and efficiently this will be done, only the coming years will be able to say.

One final area of consideration is whether decentralization in the Dengist era was an end in itself, or a means to other ends. Clearly, a dominant aim of policy-makers was to stimulate economic development. In this sense, market decentralization can be seen to be an end of policy-making. However, it is also the case that decentralization policies were means to attaining other political and economic ends.

The devolution of power to lower-level authorities was in part an attempt to undercut the authority of more conservative central planners who were seen as being a serious obstacle on further reform, and to simultaneously build a reform coalition with provincial leaders. This leads one to the conclusion that Dengist decentralization measures were a means of facilitating the expansion of market decentralization.

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