

The Economics of China

A little bit of History Part 2



Fall 2020

The Socialist Era, 1949–1978

- Global historical context around the 1949 revolution.
 - The end (in case of Japan) and decline (in case of Britain) of old empires.
 - Two main victors emerged from World War II which ended in 1945: USA and Soviet Union.
 - USA became leader of the "capitalist bloc".
 - Soviet Union became leader of the "socialist bloc".
 - Korean War (1950-1953).

The Socialist Era, 1949–1978

- What is Socialism?¹
 - "...the elementary stage of communism" (p.14).
 - "...is a stage of development when the direct producers gain control of the means of production" (p.14).
- Does state-ownership and government planning/intervention in the economy exist only in socialist economies?
 - "State ownership simply means that the state has effective control over the means of production" (p.15).
 - "State ownership exists both in a capitalist system and in the transition period toward communism" (p.14).
 - "Like state ownership, the state in the capitalist system also uses planning as an instrument to steer the direction of the economy" (p.15).

¹ the following quotes are from: Hsu, D. Y., & Ching, P. Y. (2010). Rethinking Socialism: What Is Socialist Transition?.

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- The table below² shows government spending as % of GDP in a sample of "capitalist" countries in 2018 or the latest available year.

Location ▾	▾ Latest
France	55.86
Finland	53.24
Belgium	52.15
Denmark	50.94
Sweden	49.87
Norway	49.16
Austria	48.65
Italy	48.39
Greece	46.96
Hungary	46.69
Germany	44.41
Slovenia	43.55
Portugal	43.37

² OECD (2020), General government spending (indicator). doi: 10.1787/a31cbf4d-en (Accessed on 15 September 2020)

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³ Mao Zedong, n.d. photograph, viewed 16 September 2020,
< <https://www.history.com/.image/tshare/MTU3ODc5MDg0MDE5ODlwMjU1/mao-zedong-2.jpg> >.

The Socialist Era, 1949–1978

- The 1949 revolution inherited lots of problems.
- In addition to hyperinflation and damage from the war, main challenges facing the Chinese Economy in 1949 were as follows:⁴
 - Inequality and poverty that needed "immediate action".
 - "overwhelming majority of the Chinese population could neither read nor write" (p.72).
 - Low life expectancy at birth.
 - Poor infrastructure.
 - "the growth of modern industry was constrained by the abject performance of an agricultural sector incapable of supplying the wage goods and raw materials required" (p.72).
 - "And although China had a long coastline, the scope for international trade was to be limited by the American trade embargo" (p.72).

⁴Bramall, C. (2009). Chinese Economic Development. London: Routledge, <https://doi.org/10.4324/9780203890820>.

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- To address these challenges, the development strategy during the Socialist period had the following elements (although with varying prevalence in different years):⁵
 - "Greater 'self-reliance'" (p.277).
 - "Distribution is inseparable from growth" (p.277).
 - Balanced economic growth:
 - "sectoral 'balance' between heavy industry, light industry and agriculture" (p.277).
 - "Development should be 'balanced' between regions" (p.277).
 - "Both modern and traditional technologies should be utilized" (p.277).

⁵Paine, S. (1976). Balanced development: Maoist conception and Chinese practice. *World Development*, 4(4), 277-304.

The Socialist Era, 1949–1978

- Industrial policy in the early years after 1949:
 - High levels of investment.
 - In the early stages, the focus was on developing heavy-industry.
 - "heavy industries are technologically challenging and hard to master".
 - "This approach fits easily with a strategy of national self-reliance and limited openness to the outside world."
 - "These industries can be considered 'strategic,' in the sense that they have the most linkages with other industries."
 - "the beginning of planning in China also meant the beginning of regional redistribution and the attempt to move the industrial center of gravity away from the coastal enclaves".

The Socialist Era, 1949–1978

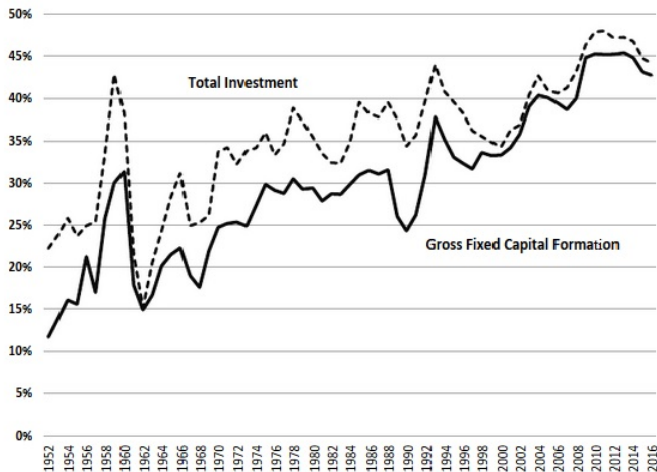


Figure 4.1

Investment as a share of GDP.

Sources: NBS (1999, 6–7); SAC (2017, 36).

The Socialist Era, 1949–1978

- Agricultural policy in the early years after 1949:
 - First, land reform (redistribution of land ownership) so that "holdings were largely equalized among households" (textbook).
 - However, another problem still needed to be addressed:
"Among the poor and lower middle peasant households, which were 60 percent 70 percent of China's peasantry, many did not even own a plough, let alone other farm tools or draft animals" (Hsu & Ching, 2010, p.18).
 - "Collective farming was seen as the answer to the problem of low productivity in farming" (Bramall, 2009, p.286)
- Command-Economy System:
 - "By 1956, [China] completed both the nationalization of industry and the collectivization of agriculture" (Hsu & Ching, 2010, p.15).

The Socialist Era, 1949–1978

- Early achievements after 1949: (textbook)
 - "economic growth was jump-started after the stagnation and disruption of the depression and war years."
 - "By 1952, industry and agriculture surpassed their highest prerevolutionary levels, and the stage was set for a new phase of development."
 - "industrial production had expanded 17% annually between 1952 and 1957".
 - "Virtually every sector of the economy had been rehabilitated".
 - "massive investments in education and training".
 - "inflation under control by the end of 1950."

The Socialist Era, 1949–1978

- The Great Leap Forward (GLF): several institutional innovations (textbook).
 - 1. “Communes” were established in the countryside. A commune was a large-scale (bigger than any collective) combination of governmental and economic functions. It was used to mobilize labor for construction projects, provide social services, and develop rural small-scale industries.
 - 2. Material incentives and monetary rewards were rejected.
 - 3. Control over economic decision-making was decentralized.
 - 4. A “walking on two legs” technology policy was established, in which simple technologies were to be combined with advanced industrial technology.
- In the communes, new social services, including communal dining halls and child-care facilities, were initiated on a large scale; mass poetry-writing sessions were held.

The Socialist Era, 1949–1978

- GLF: textbook approach.
 - "Indeed, the essence of the GLF was the attempt to resolve contradictions by doing everything simultaneously".
 - Problem: Given the resource constraint, "the most basic economic outcome of the GLF was a massive increase in the rate at which resources were transferred from agriculture to industry".

The Socialist Era, 1949–1978

- GLF: alternative approach.⁶
 - "the industrial sector grew far more rapidly than the agricultural sector in the period from 1952 to 1957" (p.99).
 - "The disparity between the industrial and agricultural sectors in rates of growth could be maintained for some time, especially as the growth in agricultural output did outpace, if by a narrow margin, the growth of population" (p.99).
 - However, "bottlenecks were bound to appear and the ability of the agricultural sector to support industrialization was bound to be undermine" (p.99).
 - This meant the following problems:
 - Shortage of food supplies and raw material supplies to light industry.
 - "overcrowding and unemployment in urban areas" .(p.99)
 - Less agricultural exports means less foreign exchange which puts an additional constraint on importing from abroad.

⁶ Unless mentioned otherwise, the discussion and quotes in slides 14-17 are from Lippit, V. D. (1975). The Great Leap Forward Reconsidered. Modern China, 1(1), 92-115.

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- GLF: alternative approach.
 - "This means that agriculture, far from contributing to the growth of industry in financial terms, was increasingly acting as a drag on it." (p.102).
 - "Given the growing imbalance between the agricultural and industrial sectors in China in the course of the 1950s, a continuation of the policies which marked the 1950s could not assure a continuation of China's rapid economic growth" (p.102).
 - "Further, the continued tensions in relations with the United States as well as with the USSR made self-reliance a necessity as well as a virtue, and a rapid increase in output appeared especially urgent" (p.106).
 - "These conditions together set the stage for the GLF" (p.102).

The Socialist Era, 1949–1978

- GLF: alternative approach.
 - "A common and somewhat casual criticism of Chinese policies in the 1950s is that China simply did not devote a large enough share of her planned investment to the agricultural sector.
 - While many critics who take this view do not take account of the lack of historical precedent (no other country, developed or developing, had based its modernization effort on massive government investments in the agricultural sector), the principal objection to this critique stems from the limited investment capabilities of industry vis-a-vis agriculture.
 - The modernization of agriculture requires mechanization (tractors and the like), electrification, and chemical fertilizers.
 - None of these can be provided without the prior establishment of an industrial base for the economy.
 - In the absence of such a base, investments in the agricultural sector would have had to have been made in less productive ways, if at all" (p.102-103).

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- The goals of the GLF.
 - "raise dramatically the output of agriculture and of newly-formed labor-intensive industries" (p.102).
 - "Rural industrialization would transform the countryside [and] facilitate the modernization of agriculture" (Bramall, 2009, p.286)
 - Close the gap between light and heavy industry.
- "In the absence of historical precedent, the GLF inevitably involved a high degree of risk" (p.105).
- "Two main points emerge from this discussion:
 - increasing production of agricultural producer goods was not a viable alternative to the GLF.
 - any disruption the GLF may have caused in the production of such goods was minor." (p.108)

The Socialist Era, 1949–1978

- The Great Famine:

- "A spectacular autumn harvest in 1958 comfortably surpassed those of the previous two years" (textbook).
- "In both 1959 and 1960, over a third of China's farmland was seriously affected by drought" (Lippit, 1975, p.93-94).
- "In some parts of the country not affected by the drought, mainly in South China, flooding was severe" (Lippit, 1975, p.94).
- "In all, approximately half of China's farmland was affected by the adverse weather" (Lippit, 1975, p.94).
- "As the system careened into 1960, local food shortages were ballooning into regional shortages, and China was facing a massive subsistence crisis" (textbook).

The Socialist Era, 1949–1978

- The Great Famine: Factors that made things worse.
 - " The impact of weather on agriculture was compounded by the impact on industry of the withdrawal of Soviet technical assistance and technicians" (Lippit, 1975, p.94).
 - In addition, it seems that there was "widespread overreporting of output by cadres" (Bramall, 2009, p.131).
 - The effect of the GLF: "Primary-sector employment fell by almost 40 million workers in 1959, almost a fifth of the agricultural workforce, because farmers were moved into rural industry" (Bramall, 2009, p.130).

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- The end of GLF:
 - "As a result, China finally did have to divert efforts from rapid industrialization in order to support the lagging agricultural sector" (Lippit, 1975, p.112).
 - "Existing production was reoriented, to the extent possible, to provide greater inputs into agriculture" (textbook).
 - "new draft plans envisaged rehabilitating existing industrial bases in the coastal regions and concentrating new investment in industries (especially chemical industries) that could support and bypass agriculture by producing fertilizer and chemical fibers" (textbook).
 - The agricultural sector performed relatively better afterwards: "as compared with 2.3% during the period 1952-7, the agricultural growth rate during the period 1963-70 was 3.9%" (Paine, 1976, p.295).
 - "This experience...ultimately led to self-sufficiency in foodgrain production and provided a firm foundation for economy-wide development and sustained industrialization" (Paine, 1976, p.295).

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- Third Front:

- With "increasing American involvement in Vietnam ...Mao pushed for the construction of the 'Third Front'" (textbook).
- The objective was, among other things, to "provide the basis for China's military security" (Bramall, 2009, p.286).
- "By building factories in remote and mountainous interior regions, Mao hoped to ensure that China's industrial base would not be vulnerable to American or Soviet military pressure" (textbook).

- Cultural Revolution:

- "From an economic standpoint, the Cultural Revolution (in the narrower definition) was, surprisingly, not a particularly important event" (textbook).
- "It produced much dramatic new political imagery but had relatively little effect on the economy" (textbook).

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- 1972 and after (textbook)
 - USA president Nixon visited China in 1972.
 - This eased tensions with the USA and other "capitalist" countries.
 - "Priority given to the Third Front was dramatically reduced".
 - Some investment was shifted to coastal regions.
 - "Economic relations with the capitalist world were re-established, and a decision was made to spend US\$4.3 billion to import industrial equipment".
 - "One of the largest items was a set of 11 very large scale fertilizer plants from a U.S.- Dutch consortium".

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- Long-run Achievements of the Socialist Era:
 - "Between 1952 and 1978, industrial output grew at an average annual rate of 11.5%" (textbook).
 - "The flow of resources into basic health and education was significant throughout the socialist period, and Chinese people were healthier and better educated at the end of the socialist era" (textbook).
 - "Moreover, these outlays [on health and education] were often made in ways that benefited lower-income members of society" (textbook).
 - In addition, "as a result of asset redistribution in the countryside and the creation of communes in 1958, per capita food consumption by the poor rose significantly, even though average food consumption rose only slightly" (Bramall, 2009, p. 295-296).
 - Average life expectancy at birth in rural China: around 25 in 1930s, 63-66 by mid 1970s (Bramall, 2009).