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Econ 493

China's Economic Reforms in 1978

Introduction

In 1978, the Chinese government made tremendous economic reforms in the bid to turn the country into a market-oriented economy. The changes were introduced through a radical reform movement by the government and had essentially been described as successful owing to the results that have been noticed from the associated changes. During the first two decades after the introduction of the reforms, China realized over 10 % of economic growth rate of the country's annual GDP (Chow 2004). These data are available in the world economic statistical trends of various countries' economic growth or movements. There are various reasons that inspired the introduction of these reforms which are discussed in detail in this project proposal. The study also covers the major components of China's economic reforms over three decades as well as the distinct characteristics of the reforms introduced in the country to transform it into a competitive market. Essentially, the major reform areas affected by the rapid change that would be highlighted in this project include the agricultural sector, changes experienced among the enterprises owned by the state and introduction of the open-door policy.

Reasons for the Introduction of the Economic Reforms in 1978

There are some reasons as well as enabling environment that made it necessary and possible for the Chinese government to introduce the economic reforms in 1978. It should be noted that economic changes and reforms in China started to be implemented earlier than 1978, however, they were slightly different from that brought up in 1978. The first five-year plan to transform the Chinese economy covered the period between 1953 and 1957 (Chow 2004). The plan was initiated by the Chinese Communist Party (CCP) and had a socialist approach to economic policies and transformations. In 1978, the government felt the plans were stalling the desired rate of growth and thus major changes were inspired by the Deng Xiaoping. There initial plan had to be abandoned, achievable as it may have appeared, due to the slow economic rate.

One of the major reasons for the economic reforms initiated in China by 1978 was the unpopularity of the Cultural Revolution that was introduced and implemented between 1966 and 1976 (Chow, 2004). The Chinese people did not fully support the Cultural Revolution and that made the Chinese Communist Party and as well as the government feel isolated. Therefore, there was an urgent need for policy reforms that would be supported by the people of China. The CCP national chairman Mao Zedong, the official behind the unpopular Cultural Reform, lost his life in 1976 and with that the enthusiasm behind the implementation of the reforms vanished. With the support Deng Xiaoping had among the party members, he was elected as the leader of China with a daunting task to initiate a popular economic change that would have the support of every citizen.

The second reason was the realization by various economic planners that it was very challenging to manage a planning system and it required lots of resources that the economy

could not afford at that time (Chow 2004). As a result, there was a need to come up with policy measures that would inspire economic growth and creation of resources that would facilitate effective and efficient management of economic planning and execution.

Thirdly, the Chinese planners studied the economic performance trends of the neighboring economies and realized that a more market-oriented approach would lead to the achievement of better performance (Chow 2004). Taiwan, Hong Kong, and Singapore are some of the countries that were taken as an example and further motivated China to shift its economic policies. Further evidence of the effectiveness of the open market approach was drawn from comparing the economic growth of two distinct economies in the same region. For example, North and South Korea performed differently in terms of the economy and so was West Germany and their Eastern counterpart. With these statistics, the Chinese government was determined to change its approach to the market and inspire a faster economic growth and development.

The fourth and major reason is that the Chinese citizens desired an economy with market-oriented policies and were willing to support the rise of such policies (Chow 2004). People were the major victims of consequences suffered as a result of the failed central planning policies. The latter brought about such effects as food shortage across the country, and there was a very small variety of goods of better quality in the Chinese market. Motivated by these effects, the Chinese people were in need of a market-oriented economy that would guarantee a significant level of improvement of living standards in various households.

The economic reforms that were introduced in China around 1950 were inspired by the model and the planning system introduced by the Soviet Union (Chow 2004). The plan was

implemented by the country between 1953 and 1957, but considerations were made to change the model and adopt a more market-oriented approach that would allow the country to achieve better economic reforms. 1978 was a premier year for the introduction of the economic reforms because it was the same year in which the communist party was beginning to initiate its four pillars of economic reforms.

The major pillars that were promised by the communist party that were to be implemented included the changes in the agricultural, industrial, scientific, and technological sectors (Chow 2004). The plan should have been implemented earlier, but it faced a major hindrance and had to be implemented in 1978. Essentially, the obstacle was caused by the cultural change that took place in China between 1966 and 1976 (Chow 2004). Therefore, the period that followed after the introduction of the changes led to tremendous increase in agricultural production as the policies influenced a positive transformation.

Agricultural Reforms

Several policies have been formulated that led to the transformation of the agricultural sector in China. One of the major landmarks in this sector is the adoption of “Household Responsibility System” in operation of agricultural activities (Yeh 2001). Household operation in agriculture required that agricultural activities be carried through a communal system aimed at improving agricultural produce. Farmers were organized into teams of forty people, and the entire group would share their additional production achieved from additional efforts. Upon realizing that the farmers would be more productive if they worked alone, they were allowed to enjoy the extra production that they realized after meeting the required unit for national circulation; farms were subdivided among individual farmers. That move led to a tremendous

increase in the agricultural produce achieved by the country to the point of being a major agricultural produce supplier in the world (Chow, 2004). The agricultural improvement was an important aspect of the country and its population because it enhanced productivity and brought about food security in the country, leading to stability.

Aggregate or communal cultivating under the Cooperative Framework presented by Mao in 1958 in his move to initiate forward agricultural development was a positive move towards establishing changes in the agricultural sector. Agriculturists acted as a group comprising of somewhere in the range of forty people and in that respect, the level of cooperation was effectively enhanced as well as worker motivation. A farmer could not get an additional reward by working harder because all individuals from the group would share the extra yield because of his extra work (Chow 2004). Chinese farmers merited credit for starting a change in farming to ensure they increase their production capacity and in the process, realize the potential of their work regarding the yields. This was a massive improvement from the central planning policies that were initially being used. Consequently, that drained the resources and energy of the farmers and in the end, they had very minimal gains from their investment of time and efforts (Yeh 2001).

A few ranchers and farmers understood that on the off chance that they cultivated independently the group could create more altogether and still conveyed a similar measure of yield needed by the obtainment framework for state dispersion of economic agricultural items (Ho and Young 2013). Such feelings among the individual farmers meant that the household agricultural system was highly motivational on farmers' attitude towards agricultural production. Over a period of five years following the introduction of the farming and agricultural policies,

China had already become one of the major exporters of agricultural produces within the Asian market, the European market, and other parts of the world such as America and Africa.

The Cooperative framework was reorganized as the group was rearranged by dispersing its territory to various families to cultivate independently, each receiving the extra pay for additional work. The portion earned was after delivering a settled measure of yield to the group for conveyance to the agencies responsible for procuring items for the government that had been created to purchase various proportions of what had been produced by the farmers within China (McMillan and Naughton 1992). Such practice was presented and spread in numerous areas of the nation with individual farmers realizing the tremendous increase in agricultural production. In 1978, the president perceived its helpful impacts and relized it as a state strategy and called it the "Household Responsibility System." Production in agriculture expanded at tremendously high rate across different regions in the country and China soon began to enjoy stability in food security, contrary to the situation during the policies utilized before the 1978 period.

The economic capacity in the form of the financial stability of the farmers relatively increased as the farmers who were initially poor became wealthier due to the opportunities presented by the new economic system. The achievement of change in horticulture filled in as the establishment of the change in different divisions by expanding the supply of sustenance as well as by influencing a change of ideology among the members of China's ruling party.

The initial modifications in the 1978 economic change process focused on agriculture with attempts to inspire balance economic relations. The government was interested in empowering the individual farmers so that their hard production work could count. To ensure this was achieved, the economic policies proposed an increase in the procurement prices for the

agricultural producers that were purchased from the farmers by the government (McMillan and Naughton, 1992). With the increase in procurement prices, farmers aggregate earning per season improved, and they had extra resources to plow back into agriculture to realize more production capacity. The better prices made farmers view the industry as an important investment project that guaranteed the financial return, and thus the number of households engaging in farming activities also increased tremendously. In the process, food production increased in China leading to food security and increased foreign exchange earnings as the country traded on the surplus with foreign countries across different regions.

Another critical improvement in the agricultural sector was the introduction of crop diversification encouragement of specialization (Garnaut, Song and Yao 2006). Crop diversification led to a significant improvement of various types of food produced within the country. Most of the food was consumed locally while others were exported in a bid to enhance foreign trade relation with other countries. Availability of numerous food types also increased the country's nutritional capacity compared to the initial times.

Agriculture thrived because the new economic policies introduced under the 1978 reforms relaxed and lifted some of the restrictions that initially existed on trade fairs. With improved chances of making agricultural practices relatively profitable, more people were willing to take part in agricultural activities, leading to a tremendous increase in agricultural production. Special economic zones (SEZs) were introduced, on which preferential foreign trade policies were conferred to encourage or attract foreign investment, enhance incorporation of technology in agriculture, and promote the export of surplus products to other countries.

Reform of Chinese State-Owned Enterprises

There are three major components in the Chinese state sector that were defined under the economic transformation reform that was introduced in 1978. One of the components is the enterprises that are under full ownership of the state. These enterprises are managed by the state through the “State-owned Assets and Supervision and Administration Commission (SASAC)” both at the state, provincial, municipal, and county government levels (Garnaut, Song and Yao 2006). These groups of SOEs are effectively and fully controlled by their owners who make all the necessary managerial decisions that affect the directions to be taken by such organizations. The third components are the group of business entities that are owned and managed through the use of subsidiaries attached to various SOEs and are located within the country as well as outside China. Due to the wide spread of this group of entities across China and various other places in the world, their actual size is not easy to tell.

It should be noted that the contribution of the SOEs is very important to the Chinese economy as it accounts for nearly 50 % of the China’s GDP (Ho and Young 2013). The approximation of the fiscal contribution of this economy is inclusive of the SOEs owned by the government, foreign investment firms that lack the essential connection to China, and the aggregate financial impact is reflected in the economic gains of the country. The previous government leader adopted policies that were less expansive, and this made it difficult for China to access foreign markets and initiate progressive changes in various sectors. Growth and development in any country are contingent to the relationship that the country builds with the other nations regarding international trade and foreign investment.

The reforms introduced in the state-owned business enterprises were a classic example of a slow and gradual process that turns out to be very successful. The process was carried out or implemented on an experimental basis to project the level of success and the possible challenges

(Collins and Gottwald, 2014). At the time of the introduction of the progressive economic changes, every aspect of the economy that could inspire a significant growth was explored. To initiate the change process, the state enterprises were offered a significant level of autonomy in various aspects of production to ensure that the productive capacities increased massively (Yan & Yudong 2003).

Autonomy was also granted in other areas such as marketing and investment. The autonomy in this category allowed the enterprises to be proactive and expansive regarding business operations, including venturing into foreign markets (Naughton, 2006). The preserved or facilitated level of autonomy introduced and enjoyed by these entities explains their increase in number and operations within and even outside China. This was necessary for the bid by the government to empower the Chinese population which would then inspire economic growth and development across the rest of the sectors in the country.

Investment decision could now be made separately in different state-owned enterprises without depending on the central planning process as before. This is a representation of one of the many preferences that SOEs benefited from the Chinese government. Such preferences include the preferred access to bank capital so as to encourage more people to engage in the opening and management of the SOEs. One of the major things identified by the Chinese leaders in 1978 was the importance of access to capital in the bid to come up with new business ventures that have the potential for growth.

Another step that was taken by the government to enhance the chances of improving the SOEs was enabling them to access loans at a rate lower than the operational market rate (Ho and Young 2013). These loans were provided by banks owned by the state; thus it was easy for the

government to subsidize the cost of loans that could be accessed by various organizations in the SOEs sectors. Other than that, the organizations also received a favorable tax treatment compared to other sectors of the economy. This provided them with the opportunity of making significant amounts of profit and expanding rapidly and in the process, increasing the availability of other opportunities such as jobs for the growing population in China. At that time, the SOEs could not thrive in the Chinese market unless the government intervened in the situation, created a competitive environment for them about other larger firms that were already operational.

The experiments that led to the total transformation of the operations in the state-owned enterprises were introduced in 1978 in six designated enterprises in one of the provinces in China. About ten years later, productivity in various sectors had been noticed to the tune of over 40 % among 6000 government enterprises that were allowed the freedom to make important business decisions (Chow, 2004). The increased productivity indicated that autonomous decision-making process is very important in developing efficient and thus more productive business organizations. The autonomy allowed on decision making meaning that the previous bureaucratic tendencies that negatively affected the decision-making processes through structural delays were eliminated. Quick decision-making processes enjoyed by the enterprises led to speedy operations and thus, more efficiency and effectiveness.

The introduced changes also targeted the need to make the government enterprises achieve financial independence and become flexible in making decisions that would affect the financial tendencies of the organizations. The financial reforms allowed the enterprises the freedom of keeping the extra earnings after the enterprises paid taxes to the authorities (Chow 2004). This measure gave the enterprises an opportunity to increase the level of operation through reinvestment of profits realized and thus increase the chances of expansion. It was a

measure meant to further broaden the capital capacity of the SOEs and increase their financial power needed for the purpose of venturing into other sectors that organizational management identified.

The third reform introduced the level of communal responsibility, as was in the case of the agricultural sectors, aimed at making the success of the enterprises become the responsibility of the individual employees within the business sectors. Various other reforms were introduced into this sector to ensure that the cost of operating businesses by the government went down, but the level of productivity increases significantly. This process led to the expansion of various business organizations or enterprises that were owned by the state, and this was a major contributing factor in the expansion of business activities in the Chinese economy.

Introduction of the Open-Door Policy

The Open-Door Policy is also one of the famous economic reforms that were introduced in China during the reign of President Deng Xiaoping in 1978. The policy was meant to inspire foreign direct investment in various countries including the United States. It was motivated by the need to keep China open to trade with other nations in an equal capacity. The number of countries that were interested in trading with China was fast increasing led by the US with the aim of protecting the sovereignty of China as well as the integrity of its territories (Ho and Young 2013).

Essentially, the Open-Door Policy is a term used to refer to equal trading rights offered to different countries in the world market (McMillan and Naughton, 1992). The introduction of this policy in China marked the introduction of the Special Economic Zones (SEZs) which included some cities earmarked to be so. Four major cities were affected by this

plan and that includes Shenzhen, Zhuhai, Shantou, and Xiamen. The four cities were chosen mainly due to their strategic locations that exposed them to other Chinese economies that were overseas such as Hong Kong, Taiwan, and Macau (McMillan and Naughton 1992). During that time, economies such as Hong Kong and Taiwan were performing very well due to their earlier adoption of the Open-Door Policy that allowed them the opportunity to trade with foreign countries and enhance foreign exchange in the process.

The Open-Door Policy was a complete contrast of the governance methodology implemented by Chinese leaders before the reign of Deng. Before his run began, China was mainly ruled through radical politics-oriented policies that tended to give much weight to self-sustained policies by the then president, Mao Zedong. Zedong's approach to the economy was much different and it closed the doors of China about foreign trade to the extent that even smaller neighboring economies performed better than the Chinese regarding Gross Domestic Product. The failures of this reign formed a major basis for the change in policies that would later be adapted by Deng Xiaoping. Instead of enhancing the beliefs and practices of his predecessor, he introduced the Open-Door Policy that ensured China had the opportunity to trade with other countries.

The Chinese government realized the importance of expanding its economy to external markets, and this motivated the introduction of the open-door policy. Before the advent of the reforms introduced in 1978, the Chinese economy was widely closed and rarely colluded with other countries concerning economic activities (Chow, 2004). By 1978, the total volume of the country's foreign trade regarding imports and exports barely hit 7 % in contribution towards the

national income. The changes introduced by President Deng Xiaoping encouraged foreign businesses, and this improved the total volume of income gained from the exports and imports of the country. The increase rocketed to about 25 % which is a very significant figure compared to the 7 % value that was achieved before the introduction of the economic reforms.

Due to the Open-Door Policy, the country has witnessed tremendous increases in foreign trade and investment. For example, in 1999, the Chinese government realized as high as US\$ 39 billion as a result of the direct investment inroads it had made in foreign countries (Leng 2009). The country has enjoyed a massive economic growth rate in the past two decades as a result of this policy that has also relatively lifted the living standard of the Chinese people. The Open-Door Policy proved to be China's way out of stringent poverty that had hit its population for decades. It not only improved the living standards of the people on about basic commodities only but also improved aspects of entertainment and leisure time as the market of popular culture was explored (Kornai, 1990). Globalization was enhanced to a great length through the Open-Door Policy as well as the increased use of the Internet by a majority of the Chinese people.

The introduction of the open-door policy required the availability of responsive regulatory policies that would support the implementation process. Therefore, the proponents of the change process initiated various constitutional changes and reforms to oversee the operationalization and institutionalization of the open-door policy (Kunrong & Jun 2002). The constitutional reforms introduced a strict control that was aimed at providing for exports that would cater for the payment of the goods and services that were imported by the country. The laws and policy regulations that were triggered in the constitution allowed various provinces within the country to promote exports a foreign trade in their capacity. Various trading companies within China were operated based on the products demanded in the different part of

the external or foreign market through the assistance of the government. Foreign trade is an important aspect of economic development, and it has been the major reason for the growth and rise of China as a major world economic power among the traditional world greatest economic powers.

The government introduced various measures regarding grants incentives to encourage different business organizations in various industries to increase their production. For example, the state provides special treatment for companies that specialized in exporting commodities from the Chinese market to other foreign markets across the world. The exporting companies were allowed to retain part of the profit that they made on their foreign trade attempts. Such steps increased the number of companies that were willing to operate in the foreign trade market, leading to an increase in the revenue gained from that sector.

Despite the numerous positive impacts, the Open-Door Policy has also brought about a certain level of negative changes that were unprecedented at the time of the policy was being introduced. For example, the policy led to increased industrial production which highly contributed to the emission of industrial wastes that led to environmental pollution in most of the cities across China.

Conclusion

The economic reforms affected different sectors of the Chinese economy along with several other aspects, such as the social welfare system which is also important to the national economy. The Chinese economy is now one of the leading powers in the market dealing with various goods and services. The Open-Door Policy exposed the Chinese market to the world and the country then made tremendous achievements through international trade by venturing into

different fields such as technology. China has managed to enter a lot of foreign markets through the use of electronic devices that are innovatively manufactured to have a low-cost effect on the final consumer. The reform process was characterized by major operational shifts that also had the political will and support from the leadership of the country. The reforms are attributed to the remarkable growth China continues to enjoy today in the foreign exchange market where it is a leading producer of various products.

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