

# Macroeconomics with a Socialist Conscience: A Quest for Chinese Characteristics

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Throughout China's economic history the central government has invariably played a leading role. Modern scholarship on Chinese economic history, though, has yet to discover a common set of macroeconomic policy instruments which previous dynasties applied consistently; rather, macroeconomic theory was rudimentary at best. Nonetheless, it is the consensus that the government had significant influence over the course of development (or stagnation for that matter).

Past governments were highly concerned with the availability of productive factors and the circulation of goods, the most critical productive factors being land and labor. Dynastic rulers regularly relied on conscripted labor for public construction and to provide services for the emperor. In certain periods commoners were permitted to substitute taxes for labor obligations, as such obligations were generally more despised and feared than taxes. Historical texts note a wide variety of methods for evading labor requirements. Land policy, on the other hand, impacted upon the peasant's work incentives in the field, and hence reflected upon government revenue, leading to a constant struggle among dynastic officials over proper policies in this area.

With regard to the circulation of goods, dynastic rulers invariably adopted a form of nationalized economy. Nationalized commerce was considered the solution to mercantile exploitation of the peasant class. The scope of nationalization included salt, iron, alcohol, "natural" resources (mountains and rivers), and so on, which, in conjunction with labor obligations, were crucial factors in determining the rate of accumulation. The court resorted at times to printing money for short-term financial crises; at other times, they went as far as collecting taxes on razors (for shaving the head) to catch those who sought to avoid labor obligations by taking refuge in the monasteries.

Another popular economic tool of dynastic rulers was the establishment of commodities banks, especially food banks. Almost all dynasties had some sort of food bank in order to control food prices by selling in

times of scarcity and buying during times of over-production. In reality, however, food banks never really worked as expected because of poor system design and corruption. Such problems were exacerbated by the standard practice among regional nobles of undermining and seeking to benefit from the court's taxation in kind, and that of landlords and merchants who made economically detrimental land purchases. The competition between regions and center was equally acute as each dynasty entered its inevitable phase of decline.

The court itself spent chiefly on activities which did little to stimulate economic accumulation: housing and feeding troops and bloated staffs, building city walls, upgrading imperial residences, traveling and recreation. Mid-level and local officials took advantage of the loosely-structured command system to squeeze resources from below and keep them from above. Their enrichment was more a result of manipulation than of market operation. Most detrimental to the development of capitalism was the fact that these local forces rarely engaged in economic activities outside the scope of land purchases. The rise and scope of commerce was determined by the limited capacity of local banking and confined to sectors such as rice and textiles; profits were generally invested in land.<sup>1</sup>

The communist regime which came to power in 1949 did not transform the traditional economic style from the very beginning. The regime, like its dynastic predecessors, emerged from a split political system composed of local strong men. Economic control through command was reinstated gradually as the regime consolidated its political power. In one sense, however, the communist regime was historically innovative in that it was highly concerned with capital accumulation. This emphasis on economic growth did not negate egalitarian concerns, but stimulated a dispute as to whether the central or local authorities were more appropriate as the locus for development initiative. The decentralizing pull was already apparent during the Great Leap Forward and the Cultural Revolution. After a short interlude, reform economists began to publicly encourage economic actors in the lower echelons to take the initiative. The following discusses whether or not the deeply-rooted philosophy of the command economy has undergone an irrevocable reformation (Shih, 1990).

### **Macroeconomics under Market Socialism**

What the aggressive planners of China's command economy did was directly extract resources from the agricultural sectors and redistribute them to support industrialization. There are three forms of extraction. First, the planners arbitrarily kept agricultural prices low and prices for manufactured goods and machinery high, and the price differential pro-

moted capital accumulation in industry. This practice is untraditional to a limited degree since the past rationale for the existence of food banks was to prevent food prices from dropping too low. Nonetheless, the bank also had the traditional function of thwarting price inflation and dissuading commercial interests from profiteering in food exchanges. The dynastic authorities must have theoretically considered profiting from such market manipulation just as their contemporary communist counterparts have done, only not for purposes of industrialization.

Secondly, the planners requested taxes in kind, including both foodstuffs and raw materials for light industry. Thirdly, the planners regularly employed agrarian labor to build dams and roads, and to engage in small-scale labor-intensive production. These two latter forms of extraction are typically traditional in style. Like its dynastic predecessors, the communist regime intended to regulate the use of land and labor, but in this case it was able to achieve more due to its enlarged and effective political authority. In the cities, the planners directly manipulated worker wages. Since most workers had a peasant background, the wage control was another kind of extraction, kind of extraction, though to a lesser degree, of agrarian resources. In short, the scope, the willingness, and the capacity of the economic planners dramatically surpassed that of the dynastic court. The continuity lies in the regime's moral and selfless gesture to ward public welfare and the suppression of private commercial activity.

At some point in the 1980s, the communist regime formulated a theory of a commodity economy in the belief that the command economy was incapable of promoting productive forces. The continued use of the traditional command economy in its first few decades enabled the regime to put its development policy into action, yet ironically it exposed inherent weaknesses. Decentralization was first tried in the 1950s when it appeared that the production of raw materials had reached a bottleneck. Decentralization, though, is not the same as using the market. The experience of the Great Leap Forward suggests that decentralization can lead to highly centralized local plan centers. The implication of decentralization was therefore not how efficiency could be improved, but how the regime could deliberately encourage decentralization without its political control first in decline.

Reform in the 1980s gave birth to the idea of using the market to cure efficiency problems caused by over-centralization in each region. In this way the ability to regulate from the center has been further weakened. This is completely at odds with traditional practice, since the dynastic authorities never surrendered economic command without having first lost political control to regional strongmen; in contrast, the current regime remains the only supreme political authority despite the gradual decline in command economy. One must note the possible political

effects here. In an extreme case, if the market alone could provide for public welfare as the regime originally intended, then it would no longer matter in which fashion the regime chose to present itself to the public, for the intention of the regime is no longer germane to public welfare — the moral integrity of the regime is irrelevant.

Without being politically subdued, the regime has taken voluntary action in decentralizing financial power, and, later, letting market pressure reflect the change of political economic logic. Although decentralization and deregulation have so far been limited to the economic arena, it is precisely this separation of economics from politics which deserves attention, for the regime has moved beyond the constraints of millennium-old economic thought as a newly invoked socialist theory of the command economy revokes the tenets of that system. Theoretically speaking, as the regime constructs a theory of “decentralization and relinquishment” (*fangquan rangli*) to oppose the planner’s sovereignty, it permits the separation of economics from politics (discussed below).

*Fangquan rangli* has been the synoptic slogan for socialist macroeconomics since the 1980s. *Fangquan* refers to financial decentralization and *rangli* to the actual receipt of profits by people. However, a close examination of so-called socialist macroeconomics reveals ubiquitous parallels with neo-classical economics in the West. An economics textbook published by the CCP Central Party School (*Zhonggong zhongyang dangxiao*) details at least four necessary foundations (Guo and Li, 1989, pp. 91-92). First, major efforts must be made to achieve equilibrium between aggregate demand and supply, in consideration of such issues as inflation, sectoral balance, and balance of foreign exchange. Second, the government should promote the development of productive forces in society and enable the national economy to grow steadily. Thirdly, the government should attempt to improve economic efficiency. Finally, the government should make sure people can gradually raise the standards of their material life.

This material life includes one’s consumption capability and such basic necessities as food, clothing, shelter and transportation. There is also a cultural aspect of material life, comprised of education, recreation, and sanitation. Social security is also considered a key element which should be measured by indicators such as rate of employment and life expectancy (Guo and Li, 1989, pp. 100-102). In terms of goals, these concepts are certainly not unique to socialist or command economies.

A relatively effective way to achieve equilibrium is to allow the market to operate on its own and this is why economic reform must begin by restricting the planning system. The new economic philosophy is so entirely different from that of the command economy that the authorities are able to direct that only “in a specifically determined period should the state maintain direct control over a small number of priority projects,

specialized industries and precious but scarce goods.”<sup>2</sup> The new philosophy holds that guidance provided by the authorities should at most be advisory in nature, and hence theoretically non-binding. Regulation by the planners should accordingly be executed indirectly through managing economic levers well known in the West such as the discount rate, tax rates, interest rates, budgeting, etc.

Even these levers themselves must be possessed by decentralized economic units. It is argued that the best guarantee of scientific macroeconomic management is democratization of policy making, for “centralized policy making is often subject to the detrimental intrusion of individual planners’ prejudices (Tan, 1989, p. 191).” In practice, democratization refers to the notion of separation of management from ownership. The rationale of democratization is the belief that the enterprise knows the market best and should be encouraged to adjust its investment policy accordingly, so that national resource allocation at the macroeconomic level may satisfy the requirements of efficiency. To take the argument one step further, democratization in its ultimate form would mean consumer sovereignty:

[We] cannot help but make the market choice made by consumers an increasingly important constraining factor in resource allocation. In a sense, under the conditions of the commodity economy, the sum of market choices made by consumers reflects the movement of societal demand which ultimately prescribes the direction of movement in national resource allocation. Although the degree to which consumption demand guides resource allocation varies with periods and types of state, the general requirement that resource allocation must comply with consumer choice is irrefutable. Therefore, research on the relation between resource allocation and economic system under socialism must embark upon the search for the behavioral pattern of consumers in the socialist context. Consumer choice defines the goal of resource allocation.... In this way, resource allocation effectively accommodates consumers’ choices (Liu et al., 1989, p. 8).

In order to empower enterprises to respond flexibly to the market, the state must allow them not only to use resources based upon their own market judgment, but also to generate enough resources to enable them to grab market opportunities. This requires a looser financial policy whereby enterprises can acquire easier credit from banks. In fact, up until 1984, the four specialized banking systems had generated three times as much credit as the central bank (Chen, 1989, p. 36). Later, suspicions arose that the specialized banking systems were subject to administrative interference from their superiors, and were using their newly acquired

power to grant credit to provide improperly approved loans to well-connected enterprises. One solution considered is to have banks accountable for their own profits and losses, thus forcing them to be cautious in their selection of patrons. In reality, establishing such accountability remains difficult after decades of extreme centralization. Political interference in financial affairs was standard practice long before these specialized banks were opened under the reforms. As a result, abuse of credit sparked serious inflationary pressure on several occasions in the 1980s.

One easy answer lies the liberation of interest policies. Scholars criticize past interest controls as consistently "rigid" and "highly centralized." This deprived the planners of the freedom to implement a stable monetary policy. Reform, accordingly, requires a floating rate. They contend that a floating interest rate policy would serve to absorb funds in the private sector and compel enterprises to think twice before using their connections with banks to rescue money-losing businesses. Their new slogan is "self-regulation" (*ziwo jingying*) and "self-renovation" (*ziwo gaizao*) (Guo and Li, 1989, pp. 228-229).

Closely associated with *fangquan* in the banking system is the theory of regionalism. Regional economic development under the socialist command economy was formerly subject to two forms of constraint. One constraint originated in the regional strategic preoccupation with autarky over specialization. The other constraint is related to a sectoral strategic concern which reflects the departmentalist interests of each state ministry. The former constraint appears to be a natural tendency which has survived, even flourished, across dynasties and regimes. The communists subdued regionalism for a brief period, only to have it explode during the course of the Great Leap Forward. The latter constraint is said to be rational, as China lacks economic managers, and has therefore had to depend on a small number of technocrats to lead it out of underdevelopment (Guo and Li, 1989, pp. 46-47).

Under reform, economists maintain that regionalism should be recognized to the extent that regional specialization utilizes regional strengths. Obviously, local elites are in a better position than the central planner to realize regional strengths. The central planner apparently appreciates this approach and has established new localized plan centers which belong to both the sectoral/ministerial and the regional/provincial plan systems. The new plan centers are primarily cities, while some are mammoth enterprises. They currently receive planned materials directly from the central plan without going through regional or sectoral planning boards. In fact, it is required, at least theoretically, that these traditional planning boards assist these new plan centers to develop independently.

Specialization is often a critical element in realizing market efficiency. The communist regime fully utilized its power as a central planner by first enforcing decentralization and then moving beyond decentraliza-

tion in search of specialization. The regime henceforth constricted its own capability, symbolized by sectoral technocracy, in favor of a locally-based elite-oriented development route. Likewise, the central bank establishes branches in each local plan center just to guarantee that the new plan center is equipped with sufficient financial instruments to initiate plans, lead industry, and construct supporting facilities and other basic infrastructure. The thinking behind such economic philosophy is akin to that which prompted the establishment of an economic axis in some Latin American [check with author] countries (Chilcote, 1984, pp.24-48).

Apparently, the Chinese state has no intention of giving up its socialist commitment to both development and egalitarianism. The aforementioned goal of macroeconomic management mentions the material life of the people. Will *fangquan rangli*, which encourages decentralization and regional specialization and recognizes consumer and enterprise sovereignty, lead to results in direct opposition to the overall, long-term goal of equilibrium, growth, and equality? More importantly, why should low-level economic units regard the regime as a relevant actor in the market?

### **Moral Confinement of *Fangquan Rangli***

China's guiding economic principle during reform has been the credo that "the state regulates the market and the market directs enterprises." In other words, the levers available to the state in the market should be economic in nature and indirect in process. This would make China appear capitalistic, and, in fact, Deng Xiaoping's public plea in 1992 to boldly adopt capitalist measures has inspired reform-oriented officials and scholars to proclaim a more liberal interpretation of socialism. In this regard, socialism can no longer be indicated by economic measurements and has to be identified somewhere else, for example, by the intention of its economic actors. The communist regime is fully aware of the importance of rectifying people's preferences and intentions as a unique way of preserving socialism.

Intention produces goals. Theoretically speaking, capitalist states are run by the bourgeoisie and their market operation must, by definition, serve bourgeois interests. In socialist China, by contrast, economic regulation in the name of all laborers cannot possibly be aimed at anything but than public welfare, owing to the fact that China's bourgeoisie perished decades ago. In practice, though, intention may hardly matter. Since the price of a product is largely determined by the market, laborers must abide by the iron law of prices. They cannot glorify their preference simply by arbitrarily setting prices low. In actuality, they would have instead to pay more to reveal their preference, and, as a rule, restrain their

preference as prices climb (Hsu, 1989, p.55). The intentions of economic actors before entering the market and policy goals which meet such intentions are therefore not pertinent to market operation.

Nonetheless, socialist producers must logically differ from bourgeois producers. If one believes that the latter breed of businessman is constantly conscious of the need to accumulate capital, and this affects his market behavior, one with socialist goals should be able to do the same, simply with opposing preferences. A socialist state may actually satisfy its preferences better than a bourgeois government, which has access to materials and profits only through the market, because the socialist state itself is both economic manager and owner of raw materials. Exactly because no bourgeoisie controls the means of production, the socialist state is constantly able to bear in mind its most important mission of reconciling individual and collective interests and short-term and long-term causes. It is in charge of the overall direction of state development:

[The state] prescribes the guiding strategy, principle and policy of economic and social development; systematically executes the specific economic and social goals of enriching resources, technology, industries and knowledge; organizes and accommodates the endogenous and exogenous needs of regions, sectors, and enterprises to grow and cooperate; reconciles interest relationships among the state, enterprise, and individual; provides information, consultation, technology exploration, education and training, social security, etc.; stipulates, supervises, and executes economic laws and regulations; and establishes fundamental economic order (Guo and Li, p.21).

At first sight such remarks may appear to be from one of East Asia's other developing capitalist-oriented states. One might wonder if China's socialism is more Asianistic than socialist. Thanks to public ownership of the major means of production, though, the Chinese socialist state may actually get involved in economics to a much greater extent than other Asian states. At least it is assumed natural for the state to think so as Jiang Zemin remarks:

We have the confidence, ability and methodology to resolve all difficulties and problems on our way to moving forward... We will concentrate on eight aspects. The first is to constrict investment in local capital, as the center has requested, and adhere to the principle of the collective interest prevailing over parochial interests. So we must curb the inclination to overly invest in local capital. The second is to control consumption pressures, the growth of which must be



kept below the growth of productivity. The third one is to perform well in our tasks of inspection of tax records, financing, pricing and crediting, and correcting malfunctions of enterprises. The fourth is to secure the supply of necessities. The fifth is to continue to strengthen reform efforts, enliven dormant national enterprises, and form self-regulative mechanisms inside each enterprise while enforcing reform, inspiring economic initiatives, and improving economic efficiency. The sixth is to actively carry out pioneering housing reform in preparation for an overall reform of the existing housing system. The seventh is to maintain unity and stability in order to create conditions favorable for economic management and regulation. The eighth is to intensify the "double-growth, double-savings" campaign in order to incite laborers to work and complete economic projects with a competitive spirit (Jiang Z., 1989, p. 15).

The aggressiveness of the planners does not promise that economic actors in society will comply, since planners would also like to protect the integrity and independence of a market in which a plan has no legitimate role. Advanced economic scholarship thus focuses its attention on the socialist conscience as well. The rationale of plan management noticeably shifts. Some point out that a plan should impact not by legally, administratively and politically restraining economic actors' market behavior but by molding their preferences and values. There are two approaches to successful preference management. First, the planner gives up his traditional practice of directly issuing plan commands to the enterprise. Instead, he simply proposes options. The plan is therefore a "soft plan" and budgeting therein is "soft budgeting." Theoretically, it is up to the enterprise to decide to what extent it will follow the proposal thus delivered. Secondly, the Communist Party empowers the enterprise to instill a sense of socialist duty in the laborer. Enterprises acquire their mandate to persuade workers to engage in projects which best satisfy long-term collective interests.

Soft planning is nonetheless a kind of planning and inconsistent with the logic of the market. Chinese scholars hence struggle to distinguish the difference between a soft plan and the traditional hard plan. Accordingly, a soft plan is said to provide direction and be "the prime foundation of healthy national economic development."<sup>3</sup> More importantly, its major contents comprise "proposals which forecast, refer, and guide according to the laws of commodity exchange and price." Their function, therefore, is to assist in "reconciling the activities of individual economic actors with the overall bearing of national plans by persuading and influencing those economic actors to hedge against market uncertainties (Tan, 1989, p. 184)."

The intriguing aspect of soft planning is precisely its non-coercive

nature. The enterprise receiving a soft plan is encouraged to revise the plan according to market information it collects in the process of executing the plan. In other words, a plan tells what the planner thinks feasible and agreeable. The enterprise cooperates with the planner because the planner has a grasp of the overall economic picture and supposedly knows more about market trends, based upon his capacity for information collection. Ideally, following the soft plan gives the enterprise an edge in the marketplace since individual enterprises do not usually have the capability to collect, systematize, and interpret broadly scattered market information.

Before a plan is assigned and all available tax privileges are granted the planner and the enterprise must negotiate. This tedious process, however, may enhance the socialist conscience of the enterprise as it strives to internalize the plan's rationale. Of greatest importance is the recognition that the planner may make mistakes, or at least the market trends he spots may shift. The planner thus depends on the enterprise to take the pulse of the market by generating information through revisions to the original plan. The soft plan raises the annual objectives of the enterprise and the enterprise revises such goals via implementation. The soft plan is soft because the planner realizes there is an objective limitation of knowledge and he cannot possibly have sovereignty in the market as traditionally assumed; so he must rely on the enterprise to detect current market trends. While each individual enterprise is concerned only with its own profits and revising the part of the soft plan related to its own production lines, the planner has the advantage of a comprehensive communication network in the soft plan system.

Whether or not the enterprise is obliged to negotiate with the planner if the former has access to market information and, more importantly, resources seems not to be exclusively an economic, or even legal, issue. Preference management, therefore, cannot simply go through the soft planning system alone, but must be conducted on the condition that the soft plan is morally irresistible. The planner is a legitimate, though indirect, actor in the market because he cannot be an exploiter. Just imagine what pretexts an enterprise could enlist to justify its rejection of a plan without incurring a lethal, negative image.

To preserve socialism, the planner must enhance the socialist conscience and guarantee that the enterprise is endowed with a socialist world view. For this purpose, there must be mechanisms which serve to bring together interest conceptions held by the state, the enterprise, and its laborers. In the past this was the exclusive domain of the Party leadership. The state has recently endeavored to consolidate the convergence of all these interest conceptions as the market becomes more germane to decision making in the enterprise, and as the Party's role of indoctrinator fades. The idea is to have the enterprise internalize the

state's interest conceptions. The enterprise is expected to bear in mind socialism while making investment and bonus decisions. This is what Chinese scholars repeatedly cite as "the principle of self-consciousness" (*zijue yuanze*). Several methods are employed to rectify *zijue yuanze*.

First of all, the plan must be written according to market information and there should be no predetermined agenda as when to when the final stage of communism will be reached. There is therefore no need to demonstrate one's dedication to communism by rapid advancement in that direction. That the planners are not exploiters is alone considered sufficient evidence of socialism in China. Nowadays, neither economic backwardness nor temporarily sluggish growth can be used to insinuate the failure of socialism. With this understood, the planner can proceed to collect as much information as possible to assist in objective economic forecasting. Ostentatious reporting of achievement ceases to be the most reliable legitimating technique.

For this reason, factual statistics are now considered one of the most important foundations of policy analysis. The state statistics Bureau and its regional divisions are employing UN statistical systems which enable the planners to analyze the vicissitudes of consumption and investment throughout the banks' accounts. China has also taken advantage of modern satellite facilities to link itself with numerous international science and technology information centers (Guo and Li, 1989, pp. 65-67). These statistics are the sum total of individual economic decisions taken in the market. As long as the planner faithfully reflects the market situation, his proposals to the enterprise will likely contribute to the enterprise's capacity for profit. In actuality, enterprises and consumers in the market ultimately determine the contents of the plan. The planner performs the role of an inductive medium.

Secondly, the state can make direct investment from the center. Each sizable investor that a state-owned enterprise makes in a locality spontaneously captures local attention. As local enterprises respond and start peripheral supporting industries, the economic effect of the state investment multiplies. State investment of this magnitude is referred to as "dragon-head" (*longtou*) investment which economists believe can stimulate local investors to more effectively "use their natural environment self-consciously and in an orderly fashion."<sup>4</sup> Also, the state owns mineral resources and is able to influence investment decisions of collective enterprises. Collective, private, and individual enterprises generally maintain contractual relations with state-owned enterprises. This guarantees that as long as general managers at state enterprises maintain a socialist conscience, actions taken by other enterprises cannot conceivably stray too far away from the socialist track (Tan, 1989, p. 257). The drawback, then, is that these market-oriented enterprises may not achieve socialist consciousness simultaneously.

Thirdly, there are numerous legislative, judicial, and administrative channels through which the planner can straightforwardly engage in preference management. The planner may make clear his own preference and simply direct the subordinate enterprise to enforce it. This approach violates the integrity of the market and it is believed that it should not be employed regularly. The availability of these channels, though, is "the essential hallmark of the socialist market as opposed to the capitalist market (Guo and Li, 1989, p. 82)." In short, the need to enliven enterprises does not justify complete freedom. Because it remains unlikely that an enterprise will be penalized for bad management by being declared insolvent, the planner must remain in ultimate charge lest the enterprise wastefully abuse the soft budgeting system.

Administrative interference by the state should be considered as an attempt to rescue the enterprise from illegal practices under general market failure, a condition which remains endemic in most state-run enterprises. Among these practices are the often cited problems of over-investment, investment overlap, generous bonus policies in loss-making enterprises, etc. The goal of such interference should be to restore market order, yet the difficulties it faces are monumental (Jiang Y., 1989, pp. 87-91). There is no guarantee, for example, that the state manager will respect the market any more than the enterprise manager. Likewise, administrative interference defeats the purpose of having enterprise managers be conscious of the market, though they may bitterly appreciate the existence of the omniscient socialist planner. Finally, interference of this sort stirs feelings of grievance among labor and is harmful to consolidation of regime legitimacy in the long run.

The most effective, although not necessarily most economically efficient, instrument to rectify *zijue yuanze* is moral leadership provided through the Party network in each enterprise. Successful moral rectification not only contributes to the socialist conscience of enterprise workers but may also enhance the profitability of the enterprise through tax breaks and the training of market-oriented managers. Obviously, the Communist Party holds the sole legitimate claim to be the supreme moralist and trainer in today's China, granted the general trend of moral decline in this society. Since the first introduction of reform, the Party's moral leadership in the market has become subtle and intriguing:

Generally speaking, the Party is the tool of ruling. However, only at the top level does this general rule completely show. Economic entities like enterprises do not perform the general political function of the state machinery, so the Party organization in the enterprise cannot be analogous to Party committees in the central and local governments, do they have a similar amount of influence. In the enterprise, it is the general manager who is in charge. He cannot

possibly leave the Party leadership behind, though. It does not matter how the general manager is selected in the enterprise, he will have to execute the state plan and state laws, orders and regulations... The general manager, totally responsible for business management and sometimes not even a Party member, cannot be a substitute for the leadership which the Party provides for the enterprise. What has changed is the style and content of that leadership (Qi, 1989, p. 205).

The most important task today for Party organs within enterprises is to produce good Party workers so that they can serve as models for emulation in factories. They must also work on the thought and ideology of enterprise cadres and workers. These Party members remind the enterprise that state regulations should be faithfully observed. Their task is "difficult but crucial (Qi, 1989, pp. 205-206)."

Although the planner remains a powerful actor in the market, his interference presumably requires economic justification under reform. The chief characters in the realm of central planning have witnessed stark transformation. The plan must represent more than a show of planner sovereignty and the assignment given the enterprise through bargaining. The soft planning system is a combination of material incentives (tax privileges), coercion (administrative interference) and persuasion (Party leadership), which is aimed at helping the enterprise internalize the plan and perpetuate its socialist conscience.

For thousands of years, Chinese regimes feigned no conflict of interest with the people in order to justify their command economy. They traditionally suppressed commercial interests and dreaded market calculation; it would only be natural today for reform in Communist China to begin to depart from this practice. The regime hesitates in the face of the market, preferring the enterprise to handle the market on its own. Past regimes pretended moral supremacy and economic selflessness to enforce the command economy; today's regime prepares to forego its total command while continuing to act with moral pretension. The task which remains is to prove that moral and economic command can be separated yet remain mutually congruent.

### **Irrevocable *Fangquan Rangli***

*Fangquan rangli* contributed to the rise of regionalism in the late 1980s, which critics call the "feudal lord economy" (*zhuhou jingji*). They claimed that such regionalism was splitting the national economy just as princes over two thousand years ago had split the feudal Zhou Dynasty. Feudal lord economy refers to local elites utilizing administrative barriers to protect the tax base of their respective region. These administrative

barriers to protect the tax base of their respective region. These administrative barriers prevent economic actors from purchasing goods outside their own provinces, so that all possible profits generated in the area remain in the area. Economists acknowledge that the feudal lord economy helps capital accumulation within the region over the short run, but is eventually "detrimental to regional development," for it "blocks the formation of a nationwide market" and thus limits the potential for growth in all regions (Dong, 1989, p. 127).

One solution is to establish new, lower-level plan centers, primarily in municipalities. It is predicted that these new plan centers will cut across traditional administrative demarcations. Once they receive independent assignments from the central planner and acquire stable institutional access to resources, rational enterprises may be expected to pursue new connections with these centers, and traditional regionalism would thus be rendered meaningless (Ma, 1985, p. 173). Others are uneasy about the possibility of the central planner losing control over these new municipal centers, which it is claimed will become new regional blocks to thwart national economic integration (Liu, 1986). Scholars may disagree on some details, but most concur in the opinion that problems arise from regionalism, be it provincial or municipal. One group of economists aim to thwart partial regionalism by encouraging comprehensive regionalism, believing it would compel regions to realize the merits of integration:

For a while, the boundaries between central and local government were obscure. The central government is reluctant to acknowledge that localities have relatively independent interest concerns. This leads provincial economic entities into oblivion. The center grabs everything and the localities follow heedlessly, creating colossal blindness and permanent imbalance in the evolution of local economic structures. Regional advantages are lost as a direct or indirect consequence. Henceforth, the local government must take over the central government's duties as director of local economic structural adjustment. This should be the approach. Local governments can develop their own economic resources more efficiently, reduce past blindness and avert massive periodical fluctuation and local economic imbalance (Liu et al., 1989, p. 240).

However, if the regime encourages localities to pursue purely economic interests in the name of government, it in fact violates the traditional expectation that the regime alone knows where the public interest lies. In fact, the creation of an office in charge of inter-provincial commerce illustrates the Chinese socialist planner's lack of trust in local judgment (Shirk, 1985, pp. 215-216). Partial decentralization allows localities the opportunity to abuse leeway thus gained in order to protect their

myopic, departmentalist interests; thorough decentralization negates the leadership provided by the regime in Beijing. Decentralization therefore reflects the moral predicament the regime faces:

Since reform started, all reform measures have been introduced under the promotion and recognition of the center. However, decentralization produces numerous competitors against the center. Consequently, in the arena of economic competition there is a never-ending battle between the local and central teams. The central team rarely triumphs as a competitor since it alone has to cope with all local teams. Although the central team sets the rules of the game and plays the role of referee, it always loses. The central team thus revises the rules and comes back again for another round of competition. This begets complaints from the local teams (Chen, 1989, p. 163).

The recommendation here is that the central team withdraw from competition and become a professional full-time referee, the idea being that the center can establish itself as an economic authority in such a manner. Only then can the regime keep the process of decentralization from "continuously splitting the government into parts (Chen, 1989, p. 164)." This solution does not provide an answer to the fundamental question of what is the source of economic authority. Whoever protects the market must himself enjoy a powerful economic position. If the center withdraws from the market, how can it thus protect it? Furthermore, without a position in the market, how can the center be influential in broadcasting socialist concerns?

*Fangquan rangli* is also reflected in the rise of rural enterprises. Villages and towns in which small enterprises have begun to thrive have a long way to go before reaching a level of prosperity — a full 70 percent of these locations are still below that level. This situation hinders the healthy development of the commodity economy since their products cannot possibly be sold outside their localities. This lack of integration among small localities means that rural enterprises invariably engage in investments which "blindly overlap" and seriously by lack quality. The goods they produce have no market in urban centers, and the local market is monopolized to such an extent that urban goods cannot penetrate. This conflict of interests between urban and rural enterprises has been described by many as "acute." (Hsu, 1980, pp. 72-73)

Rural businesses consume resources which are supposedly used more efficiently by urban industry. They dominate markets which rightfully belong to urban products, yet they are small and flexible enough to undermine all possible retaliations by more advanced and larger enterprises. Regardless, the government supports the continued development

of rural businesses and requests that Party and government organizations at all levels "actively provide guidance and support with enthusiasm (Zhang, 1988, pp. 47-48)." It seems clear that the damage these enterprises have inflicted on the hallmark of socialism, the state-owned enterprise, is intentionally tolerated. The government must encourage rural businesses in order to absorb surplus labor from the villages, preventing rural migration to urban areas which is a source of social instability. The political consequence is that the regime presents itself as unable to cope with the interest contradiction thus generated while still offering support to all sides.

The lifting of *fangquan rangli* to the status of official policy opens its own Pandora's box and decentralization takes on a momentum of its own. Despite the tremendous socialist legacy, the regime, together with local governments and enterprises, cries out for further decentralization as if the central plan were the source of all evil. It was the Great Leap Forward of 1958 which attempted to penetrate the countryside and recruit local leaders to serve central interests. Ironically, local elites gained the opportunity to expand local interests and precipitate regionalism (Nee, 1983). The stress on market mechanisms during reform furthers regionalism as *fangquan* empowers local governments and enterprises. While central planning was originally blamed in order to introduce market mechanisms, actual developments have made regionalism the biggest winner.

The government is unable to rein in already decentralized financial power for two reasons. First, the government does not have a theory which can convince the central planner himself that this would resolve the problem of economic stagnation, which plagued the nation before the 1980s. Second, local forces which enjoy access to resources are no longer totally dependent on the center; hence they are ready and willing to resist any attempts at recentralization. It is at least logically correct to assume that the use of market mechanisms does not have to harm the socialist character of the regime as long as the means of production are still theoretically in public hands. Regionalism, however, undeniably damages the sense of being socialist, since the pretension that the regime represents one proletarian class and symbolizes a harmony of interests within that class is shattered in the face of regionalism. *Fangquan rangli* is morally destructive because this policy invites regionalism through the market.

### Conclusion

In Chinese history, it was rare for a regime to voluntarily give up economic power when its hold on political power was firm. Economic levers were always considered essential to successful ruling not just



because commoners responded to economic carrots and sticks, but also because the regime did not want to encourage the pursuit of commercial interests in society. Since the regime did not pursue selfish interests, challengers who did so were forced to first deny the regime's moral superiority, thus undermining its political legitimacy. In the 1980s, the Communist regime voluntarily granted command of economic development to lower economic units and initiated an irrevocable process of decentralization.

The current regime has struggled to avoid the moral implications of reform, instead striving to separate economics from politics. This has been achieved through the assumption that labor with a socialist conscience could continue to honor the leadership provided by a Communist Party whose power has been seriously curtailed in a market now subject to the preferences of labor. The irony is twofold. The regime cannot be certain that labor indeed possesses this socialist conscience unless the workers are willing to forego market interests in certain cases and support state plans at their own expense. This would position the state against labor and offset any demonstration effect which labor could provide. Secondly, the state still relies on economic strength to enforce its socialist plan, but this incurs certain responsibilities if the plan fails to bring development. Although responsibility for economic failure can now be transferred to economic actors who make initial economic decisions, this would imply that the regime is now unable to lead.

From the local perspective, the market has been introduced to resist state interference. This is not necessarily a negative mindset as long as each locality does not also impose regional barriers to hinder economic integration. It is therefore interesting to note that macroeconomic textbooks are filled with the term "self-consciousness" as a reminder to economic actors of the existence of the market as well as their socialist duty. It is interesting to note that in enhancing one's socialist conscience, the Communist Party never advocates the separation of Party and enterprise even as it lauds the separation of politics and economics, and government and enterprise. The crisis which the Communist Party faces today is therefore much more complicated than a fight against capitalism, as most commentators have assumed. It is a matter of regime legitimacy in terms of maintaining the moral relevance of the Party in the arena of market socialism.

### Notes

1. Concerning Chinese economic thoughts, see the classical readings of Sa Mengwu, *Chinese Social Political History (Zhongguo shehui zhengzhi shi)* 1-4 (Taipei: Sanmin Press, 1980) and Ho Chiachu, *History of Chinese Economic Thought (Zhongguo jingji cixiang shi)*

- (Taipei: Chinese Cultural Renovation Commission, 1982).
2. Report on the Thirteenth National Congress of the Chinese Communist Party, 1987.
  3. See *Collection of Conference Documents of the Fourth Meeting of the Sixth National People's Congress* (Diliujie quanguo renmin daibiaodahui disici huiyi wenjian huibian) (Beijing: People's press, 1986), p.31.
  4. Yue Fubing portrays the dragon-headed state investment as the head of an airplane, see *On Commodity Economy in the Primary Stage of Socialism* (*Shehuizhuyi chujī jieduan shangpin jingji lun*) (Beijing: China Prospect Press, 1989), pp. 99,105 and 241. I:National Enterprises II:Collective Enterprise III:Other Enterprises

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