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**READJUSTMENT AND REFORM IN
THE CHINESE ECONOMY**

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UNIVERSITY
of
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READJUSTMENT AND REFORM IN THE CHINESE ECONOMY

BY JAN S. PRYBYLA

Preliminary Remarks*

In an article "China in the 1980s" published in the May-June 1980 issue of *Challenge* I discussed various problems troubling the Chinese economy and the policy responses of the post-Mao leadership. This paper continues the review in the light of information obtained since that time.

Since the death of Mao Zedong (September 1976) and the arrest of his leftwing associates (October 1976), two steps forward and one step back have been taken in the matter of economic planning. In February 1978, Hua Guofeng unveiled a grandiose Ten-Year Plan for the Development of the National Economy flanked by a Ten-Year Plan for the Development of Science and Technology for the period 1976-85.¹ The plans suffered from two major defects: they were too ambitious in their objectives and too flimsy in their methodology. They were scrapped in 1980 and replaced by three sets of plans: a transitional three-year plan of "Readjustment, Restructuring, Consolidation, and Improvement" (1978-80); a five-year plan (1981-85); and a ten-year plan (1981-90).² This paper concentrates on the transitional plan (1978-80) and on policy intentions for 1981.

For the sake of expositional convenience I make a distinction between policies of "readjustment" and those of "reform." Readjustment refers to measures taken to improve the operation of the existing system of administrative command without, however, affecting the basic operational principles of the system. Reform refers to policies which change the system in fundamental ways. While one

* Condensed version of a paper given on November 6, 1980 to the Economic Planning Workshop, University of Pennsylvania. Jan S. Prybyla is Professor of Economics at Pennsylvania State University and Visiting Professor, University of Arizona at Tucson.

1. Hua Guofeng, Report on the Work of the Government to the 1st Session, 5th National People's Congress, February 26, 1978, *Peking Review*, March 10, 1978, pp. 7-40. I have analyzed this plan in "Changes in the Chinese Economy: An Interpretation," *Asian Survey*, Vol. XIX, No. 5, May 1979, pp. 409-435.

2. Hua Guofeng, Report on the Work of the Government to the 3rd Session, 5th National People's Congress, September 7, 1980, *Beijing Review*, September 22, 1980, pp. 12-29, and Yao Yilin, Report on the Arrangements for the National Economic Plans for 1980 and 1981, *ibid.*, pp. 30-43.

should not build a conceptual great wall between the two, the distinction is useful. I believe that the changes in the economy effected so far, as well as those contemplated for 1981-85, fall predominantly into the "readjustment" category. The possibility of more important systemic changes to come is not excluded at this stage.³ As I see it, the system of administrative command that had been in place from 1961 to 1966 (in essence, modified Stalinism) has been cleansed during the last four years of most of its leftist accretions acquired during the Cultural Revolution of 1966-76, and it has been modernized, that is, adapted to changed historical circumstances.⁴ The question now is where to go from here.

To date, the changes have been of two kinds: controlled experiments in selected economic units and locations (of which the so-called "Sichuan experiment" in enterprise management is the best known), and nationwide measures. In general, the controlled laboratory experiments are potentially more reformist than have been the measures thus far adopted nationwide. As with earlier such experiments elsewhere (e.g., the "Bolshevichka" and "Mayak" management changes in the U.S.S.R. of the 1960s), several problems have surfaced in connection with the Chinese experiments. First, the enterprises selected for experimentation were, by and large, not typical of enterprises in their branch or sector. More often than not the pilot firms were above the average to begin with, which, of course, has

3. "Generally speaking the break with the old has not been sufficient and we are still a long way from the goal of the reform. Over the past year or so, only a breach has been made in the old system, but we must advance on the crest of this victory. . . . We can during the next few years only make minor reforms to create conditions for major ones." Xue Muqiao, "Some Opinions on Reforming the Economic System," *Renmin Ribao*, June 10, 1980, in *Foreign Broadcast Information Service (FBIS)*, June 25, 1980. "All the economic reform measures of 1978-81 . . . are aimed at promoting the readjustment of the economy. . . . But these measures are only of a preliminary nature. The overall restructuring of management of our economy calls for further investigation and study, the summing-up of experience, deeper theoretical exploration and the absorption of the strong points of other countries which are relevant and useful." Yao Yilin, *op. cit.*, pp. 42-43

4. The 1961-66 system is associated with the formerly disgraced, now rehabilitated Liu Shaoqi. The name given to it was strikingly similar to that given to the current transitional plans. It was called "Readjustment, Consolidation, Filling-Out, and Raising Standards." It came in the wake of the damage inflicted on the economy by the leftist Great Leap Forward (1958-60). By and large, the people in charge of the 1961-66 system were the same as those in charge of the post-Mao economy (1977-81). The 1961-66 system is described in my *The Political Economy of Communist China* (Scranton: International Textbook Company, 1970), Chapter 9.

biased the results. Second, even with generally positive results, "quite a few new problems have cropped up in the process of experimentation."⁵ Third, "pilot projects in some units conflicted with the existing overall administrative system." In other words, the pilot projects operated in a hostile or, at least, uncongenial systemic environment. Fourth, "many reforms were conducted individually and were not coordinated with one another." Fifth, "many comrades' ideological consciousness could not keep pace with the conditions. They dealt with new problems on the basis of their old experiences."⁶ In other words, there has been something less than perfect professional competence in implementing the changes (most managers are simply not used to making decisions by themselves), and there has been ideological foot-dragging due to the cadres' fear of possible future retribution by a reborn left.⁷ The experience of other socialist countries with readjustment and reform (especially Hungary) suggests that the longer reform is put off, the smaller are the chances of its ever being introduced.

The paper examines two areas of readjustment and possible reform: balanced development (the planning system) and management of the firm (including incentives to firms and workers).

Balanced Development Planning

According to the post-Mao analysis the Chinese economy suffers from several inter- and intra-sectoral imbalances (which I have listed and described in the *Challenge* article). Here I review the latest information on how some of these imbalances are being put right.

Imbalance Between the Performance of Industry and Agriculture

In line with the guideline that "agriculture is the foundation of economic development," the following measures have been adopted:

5. Yao Yilin, *op. cit.*, p. 33.

6. Xue Muqiao, *op. cit.*

7. Next to popular cynicism, cadre immobilism ("passivity toward the four modernizations") remains a major problem for the readjusters. Making mistakes on the right, which cadres are in effect now asked to do, may be lethal for individual cadres in the future, should the present regime collapse under pressure from a resurgent left, or simply change its political color.

1. *State budgetary investment* in agriculture rose from 10.7 percent of budgetary investment expenditures in 1978 to 14 percent in 1979. By 1985 at the latest, this proportion is to rise to "around 18 percent." The bulk of these outlays goes to state farms and other state-related projects (e.g., large water conservancy and forestry works). State budgetary outlays on "agricultural undertakings and appropriations in support of the communes, production brigades and teams" are to rise "step by step" to about 8 percent of the state's total budgetary expenditures, presumably also by 1985 at the latest.⁸ In 1979 such outlays amounted to 9 billion yuan, or 7 percent of total state budgetary expenditures. They were used mainly to purchase key industrial inputs (chemical fertilizer, machinery) and for the development of livestock raising and fisheries. If only direct state budgetary appropriations for capital construction in agriculture are considered, agriculture receives nowadays some 14-15 percent of total state budgetary expenditures on capital construction. However, such direct appropriations do not tell the whole story. In addition, as we have seen, there are sizeable allocations to the commune sector of additional working capital and funds earmarked for fixed capital construction. In 1979 these represented 17.5 percent of total state budgetary expenditures on capital construction.

All in all, it would not be far wrong to say that directly and indirectly agriculture nowadays receives perhaps as much as one-third of all state budgetary expenditures (direct and indirect) on capital construction.

2. *Agricultural Bank loans* in general are expected to play a more important role in capital financing than they had done in the past. (This had also been the expectation of the Soviet readjustment measures of the 1960s). Agricultural loans from the state banking system are to more than double between 1980 and 1985 (Table 1).

Two problems have emerged: (a) the banking authorities have not made adequate studies of the borrowers' creditworthiness, and (b) the question "how to use the minimum amount of funds to achieve maximum economic results" has not been resolved. The first problem has apparently three causes. One is that over the past thirteen years or so "loans for the rural areas have often been regarded as relief funds for distribution. . . . As of the end of 1979, the country's

8. "The Agricultural Development Programme" (Outline of Decision on Some Questions of Agricultural Development), approved in September 1979 by the 4th Plenary Session of 11th Central Committee of the Communist Party of China, *Beijing Review*, March 24, 1980, p. 17.

Table 1
**AGRICULTURAL BANK AND CREDIT COOPERATIVE LOANS
 TO COMMUNES AND COMMUNE MEMBERS**
 (Billion yuan)

	Jan.-Sept. 1979	Jan.-Sept. 1980	Percent Increase
Agricultural development and commune industry loans to communes, brigades, teams	10.2	19.84	45
Loans to commune members for development of sideline occupations	0.34	0.66	94

Source: *Beijing Review*, November 3, 1980, p. 4.

agricultural loans which could not be reclaimed when due or overdue, exceeded 10 billion yuan.”⁹ In Inner Mongolia, “out of some 54,900 production teams which had received bank loans in the past, 43,900 are unable to repay their loans.”¹⁰ The second cause seems to be the continuing problem of overlap between banking and Party authorities, with an influential Party lobby pressing for the old egalitarian solutions. The third cause is that the financial cadres themselves are not, as of now, terribly competent. Of the country’s financial cadres only about 25 percent are familiar with financial work and their age is over 50. Only about 12 percent are professionally trained in financial affairs. The charge that the banking authorities fail to make proper studies of the effectiveness with which loans are to be used is somewhat weakened by the fact that the current state of Chinese economic science, the structure of prices, interest rates, and so on, do not provide an adequate foundation for such studies.

3. State *procurement prices* for a number of key farm products have been raised and *prices charged by state industrial enterprises* for some products used by agriculture have been lowered. The idea is to improve agriculture’s terms of trade with industry and thus help the commune sector’s capital accumulation funds as well as raise the income potentially available for distribution to commune members.

The compulsory quota purchase prices paid by the state for 18 products were raised in the summer of 1979. The products involved

9. Beijing Radio, Xinhua, June 17, 1980, in *FBIS*, June 18, 1980.
 10. Hohhot, Nei Monggol Regional Service, May 28, 1980, in *FBIS*, June 4, 1980.

were: grains, oils and fats, cotton, pigs, beef cattle, sheep and goats, eggs, aquatic products, sugar beets, sugarcane, hemp, ramie, castor oil, silkworm cocoons, timber (in the south region) bamboo, and cattle hides. The national average purchasing price increases are shown in Table 2.¹¹ The policy of paying higher prices for above-quota deliveries of grains, edible oils, and cotton was instituted.

Table 2
NATIONAL AVERAGE INCREASES IN QUOTA AND ABOVE-QUOTA STATE
PROCUREMENT PRICES OF EIGHTEEN AGRICULTURAL
PRODUCTS, SUMMER 1979
(Percent)

Product Group	Quota	Above-Quota*
Grains	20	50
Oils and Fats	25	50
Cotton	15**	30
Pigs	26	
Remaining 14 products	20-50	
Average for 18 products	24.8	

Source: *Renmin Ribao*, October 25, 1979, p. 1, in *FBIS*, October 25, 1979, p. L-12.

* On top of the quota price.

** In north China 20 percent. The quota price was subsequently increased by another 10 percent.

Ex-factory prices and marketing prices for farm machinery, chemical fertilizers, insecticides, plastics used in farming, and other industrial goods used by the farms are to be lowered gradually. A price reduction in these items of between 10 and 15 percent has been reported.

These two measures are similar to those taken by the Soviets in respect to their agriculture at the time of the industrial wholesale

11. A more detailed breakdown of procurement prices (1978, 1979) for grains and oils has been published in *Shichang* (Market News), No. 2, 1979, p. 1. It is reproduced in Appendix Table 14 of the U.S. Department of Agriculture, *People's Republic of China: Agricultural Situation, Review of 1979 and Outlook for 1980* (Washington, D.C.: June 1980). In 1976 a survey carried out in 1,300 production teams revealed that the average cost plus tax of producing 100 catties (50 kilograms) of six kinds of foodgrains was 11.6 yuan, while the state purchasing price of these same items was on the average 10.75 yuan. In 1977 a survey of cotton production in 302 production brigades revealed that the average cost of production was 2 percent higher than the state purchasing price. *China News Analysis* (CNA), Hong Kong, No. 1178, April 11, 1980, p. 2.

price reforms of 1967. As in the Soviet Union, there have been some problems connected with relative prices. (In the Soviet Union for a while after the procurement price adjustments, peasants started massively feeding bread to their pigs).

It should be noted that state retail prices of grain products, edible oil, cotton cloth, and sugar sold to urban consumers (and physically rationed) were to remain unchanged despite the procurement price hikes, while the retail prices of other agricultural products "indispensable to the masses in their daily life" (e.g., salt, vinegar, matches) were to remain "basically the same," or could be changed only with the permission of the State Council or of province-level authorities. To lighten the burden on the state of the agricultural subsidy, retail prices of eight food items were raised quite sharply on November 1, 1979 (Table 3). At the same time it was promised that retail prices of meat, eggs, and milk would not be raised again for some years and special subsidies to state sector workers and employees (amounting to 5 yuan per head per month) were granted.¹²

Table 3
STATE RETAIL PRICE INCREASES FOR SOME AGRICULTURAL
PRODUCTS,* NOVEMBER 1, 1979
(Percent)

	State Regulations	Beijing
Pork	33	32
Fresh eggs	32	{ 33 low season 22 high season 11 hot weather seasons
Chicken	?	35

Source: *Renmin Ribao*, November 1, 1979, p. 1, in *CNA*, No. 1178, April 11, 1980, pp. 2-3.

* Other products the state retail prices of which were raised: beef, mutton, milk, and vegetables.

In 1979 the subsidy paid by the state to cover the increase in the quota delivery prices of the 18 commodities and the above-quota prices instituted for grains, edible oils, and cotton, amounted to 7.8

12. The allowance applies only to state sector workers and employees, that is, to a small percentage of the labor force. Allowances for those working in collective sector enterprises are to be authorized by province-level authorities and for soldiers by the Central Committee's Military Committee.

billion yuan, or 1.3 billion yuan over the budgeted figure. In 1980 state subsidies directly or indirectly connected with agriculture were estimated by the authorities at more than 20 billion yuan or roughly 18 percent of total budgeted state expenditures for that year. The rough breakdown is given in Table 4. "The total figure will be much bigger if subsidies for house rent, transport, and other items are included."¹³

Table 4
AGRICULTURAL SUBSIDIES, 1980
(Billion yuan)

Subsidized basic procurement quota prices for grain, edible oils, meat, eggs, vegetables, and coal for household use	12
Subsidized above-quota procurement prices for grains, edible oils, and cotton	5 +
Subsidy for ensuring preferential prices of the means of production for agricultural and industrial products which aid agriculture	3
	20 +

Source: Wang Bingqian, "Report on Financial Work" to 3rd Session, 5th National People's Congress, *Beijing Review*, September 29, 1980, p.16.

Production teams are encouraged to sell to the state any grain or oil they may have after fulfilling their compulsory and above-quota deliveries, at "negotiated" (contractual) prices directly to state food departments or on the "free" village fairs. The interesting thing is that such "first category" goods as grain and edible oils are now no longer subject to the state's "unified purchase," i.e., any surplus left over after quota and above-quota sales to the state may be disposed of on rural or urban fairs at market or negotiated prices. (Products subject to "unified purchase" by the state — e.g., cotton — cannot be sold by production teams at market or negotiated prices; they can be disposed of only within the quota and above-quota system).¹⁴

13. Wang Bingqian, "Report on Financial Work," *Beijing Review*, September 29, 1980, p. 16.

14. Cotton fabric which an individual may have in surplus (i.e., above his rationed allocation) may be sold on the urban markets. An estimated 5 million tons of foodgrains were traded on the free markets in 1979, in addition to oil, vegetables, poultry, piglets, eggs, and fruit. Fruit used to be sold under the "unified state purchase" system. State commerce was unable to cope with this, and peasants fed their

4. *Payment for procurements.* Under a new policy, production teams must receive from the state procurement agencies (usually county-level commercial departments) 80 percent of the above-quota price for that portion of grain delivered in excess of the summer grain base procurement figure. (Beginning in the summer of 1980 the grain base procurement figure was to be decided on at the time of the summer grain harvest on the basis of the figure for the whole year's grain procurement.) In the past production teams were obliged to wait until the autumn harvest for calculation and payment of the above-quota price for their summer grain deliveries. The measure is expected to (a) "increase the revolving funds of communes and brigades for autumn production," and (b) "enable the peasants to increase their income because of the summer harvest redistribution."¹⁵

5. *Taxes on agriculture.* Two kinds of taxes are involved: (a) the agricultural tax, mostly collected in the form of grain ("grain tax"), and (b) commercial and industrial taxes levied on commune, brigade, and team commercial and industrial undertakings.

(a) As regards the agricultural tax, the following measures have been adopted. (i) The tax will henceforth be "stabilized," which means two things: first, it will be assessed — as it always was supposed to be — on the "set" (that is, estimated "normal") yield of the land rather than — as had been the practice in the last several years — on actual yield; second, the tax rate will remain stable over an extended period of time (at least five years). This will enable the production teams to better plan their activities and to benefit from increases in output due to gains in land and labor productivity. (ii) The rate of the agricultural tax in 1977-78 was around 5 percent of actual yield. This is to be reduced and the reduction is to be flexible. "You should consider the masses' grain ration first, before you collect grain taxes or buy surplus grain from them. If the situation warrants, it is all right if you collect only 1 percent of what they produce."¹⁶ (iii)

apples to pigs. Since 1979 fruit can be traded on urban and village markets and state shops can purchase fruit directly from production teams and peasants at negotiated prices. *Renmin Ribao*, December 23, 1979, p. 2. State shops can also now purchase at negotiated prices a variety of other agricultural goods. However, the retail sale prices for these goods and for similar goods supplied by the state through its quota and above-quota procurements differ. The shops are not allowed to reduce the volume of goods sold at "ordinary" prices, i.e., at the lower state-fixed prices. However, they are now expected to make profits and are judged accordingly.

15. *Renmin Ribao*, June 13, 1980, p. 3, in *FBIS*, June 23, 1980.

16. Lhasa, Xizang Regional Broadcasting Service, June 14, 1980. in *FBIS*, June 17, 1980.

Low-yield and grain deficit production teams are granted exemptions from the agricultural tax below a certain level. This exemption may be extended to whole regions. For example, Tibet has been exempted for two years (1979-80 and 1980-81) from all taxes on agriculture and animal husbandry.¹⁷ In the fiscal year ending March 31, 1980 the agricultural tax remitted to poor production teams came to 2.35 million tons of grain worth 746 million yuan, or about 18 percent of the total agricultural tax levied for the year.¹⁸

(b) Development of rural industries (the so-called "five-smalls") is to be pursued, including commune industries which are counted on to contribute significantly to total commune income. In line with this (i) the minimum level of nontaxable income from commune-, brigade- and team-run industrial and other enterprises has been raised from 600 yuan to 3,000 yuan, while the tax rate was left unchanged at 20 percent. (ii) All collective agricultural, industrial, animal husbandry, fishery, and sideline enterprises were exempted from all taxes (except for industrial and commercial taxes levied on industrial products) for a period of three years beginning in 1980 provided that urban jobless youths in a single year account for 60 percent or more of the total number of workers and staff, and that the enterprises in question adopt an independent accounting (profit and loss responsibility) system. Where jobless youths represent between 30 and 60 percent of the enterprise labor force, commercial and industrial taxes (except on industrial products) will be reduced by 50 percent for these three years. (iii) In 1979-80 existing and newly established plants and work teams run by rusticated urban educated youths are exempted from all taxes, provided they adopt an independent accounting system.¹⁹ (iv) The tax holiday for newly established commune, brigade, and team enterprises has been extended from the former 1-2 years to 2-3 years. (v) Newly established commune, brigade, and team enterprises located in minority nationality autonomous counties and border counties are exempted from industrial and commercial income taxes for a period of five years.

6. *State purchase quotas.* In fixing the amounts of compulsory and above-quota produce deliveries to the state, the appropriate

17. *Beijing Review*, July 7, 1980, p. 4.

18. Beijing Radio, Xinhua, July 3, 1980, in *FBIS*, July 7, 1980. The agricultural tax in 1979 amounted to roughly 4 billion yuan or 7.4 percent of all tax revenues of the state budget.

19. Shenyang, Liaoning Provincial Broadcasting Service, May 27, 1980, in *FBIS*, June 5, 1980.

authorities have always been instructed to carefully consider the respective interests of the state, the collective, and the individual, in that order and on the theory that in the people's state these interests, if not always identical, are not antagonistic. Both the ranking of interests and the theory underlying the ranking have been modified. "On how to handle the relationship among the state, the collective, and the individual, some leading cadres said: 'In the past we emphasized considering the interest of the state first, the interest of the collective second, and the interest of the individual last.' Comrade Wan Li told them clearly and firmly: 'We should reverse the order. Individual interest comes first, followed by the interests of the state and the collective.'²⁰ How far the rattled cadres will, in fact, follow the new ranking of priorities, is difficult to say. In fixing the teams' quota and above-quota delivery obligations, greater attention than hitherto is to be paid to the individual peasants' basic grain ration (around 140 kilograms of dehusked grain a year on the average — "ration grain") and the teams' assessment of their accumulation fund needs. In order to help make the fixing of the quotas more rational ("seek truth from facts") a nation-wide agricultural and zoning survey has been commissioned and should be completed within the next 2-3 years. Like the agricultural tax, procurement quotas are to be stabilized, which means that arbitrary upward changes in them are to be ruled out.

The poorest production teams and areas (e.g., Tibet) and production teams which suffer from natural calamities and a drop in income are exempted from grain purchase quotas or the quotas are reduced according to the specific circumstances. From April 1979 through March 1980, state purchases of grain under the compulsory and above quota delivery system were reduced by 2.75 million tons. The increase in output for 1978 and 1979 added up to 49 million tons, while state grain purchases in the same period rose by 8 million tons. The remainder was left in the hands of production teams for distribution to members, the accumulation fund, and other uses.²¹ No quota or above-quota purchases shall be made from the produce of newly opened-up land for a five-year period, beginning from the first

20. Lhasa, Xizang Regional Broadcasting Service, June 14, 1980. in *FBIS*, June 17, 1980. Wan Li is Secretary of the Secretariat of the CPC, Central Committee. Since he spoke to cadres in Tibet (a poor, national minority area) the priorities were probably shifted around more dramatically than would have been the case had he spoken elsewhere in China.

21. *Beijing Review*, September 15, 1980, p. 7.

harvest year. The proportion of surplus grains (i.e., grains remaining after fulfillment of the compulsory delivery quota) which must be sold to the state (above-quota sales) has been reduced from 90 percent to 70 percent nationwide.²² The question of the organizational level for which quotas are fixed (whether for the production brigade, the production team, or some lower unit) is discussed later under "Management of the Firm."

7. *State farm profit remittances.* Like other state enterprises, state farms in the past had to remit all their profits to the state treasury. This requirement has been suspended until 1985. The retained profits are to be used by the state farms themselves "for investment and transforming themselves into amalgamated enterprises combining farming, industry, and commerce." The readjustment is less spectacular than appears at first. Many state farms are still operating at a loss: one-third of them are in Jilin Province alone.²³ Some improvement in this sense has been registered in 1979. That year, nation-wide, state farms showed a profit of 300 million yuan as against a loss of 90 million yuan the year before. The significance of profit and loss as indicators of farm efficiency is, however, questionable in the present state of prices.

8. *Other measures.* (a) Although not explicitly spelled out, the rustication movement (*xia xiang*, the sending down of urban-educated youths to the countryside), which was both unpopular with the peasants (not to mention the rusticated youths) and costly to the production brigades and teams that had to pick up part at least of the rustication tab, will be subjected to close critical scrutiny. The burden of the movement on the commune sector will be lessened by trimming the number of youths rusticated and by making *quid pro quo* arrangements between the teams-brigades accepting the youths and the municipalities from which the young people originate. For example, in return for accepting a certain number of urban-educated youths, suburban communes will receive priority treatment from city-run enterprises in the supply of hard-to-get inputs of various kinds.²⁴

22. *FBIS*, January 8, 1979.

23. Changchun, Jilin Provincial Broadcasting Service, March 13, 1980, in *FBIS*, March 31, 1980.

24. In the past, production brigades and other rural collective units which accepted urban youths were given lump sum resettlement grants by the state; so much per youth. Later most *xia xiang* youths were settled on special farms, separate from ordinary production teams.

(b) Detailed administrative intervention by Party and higher-up governmental authorities in the production decisions of basic units (production teams and lower formations) is to be severely restricted. At the same time the respective responsibilities of Party organizations and governmental organs are to be defined with the aim of reducing the Party's involvement in economic detail. "We are correcting the practice of making no distinction between the Party and the government or between the government and the enterprises. . . . Now the Party's work is to be separated from that of the government."²⁵ This is a Herculean and Augean undertaking rolled into one; it runs against the genetic history of the system, but it is to be given a try anyway. "From now on, when we pass on production plans to production teams, we should only concern ourselves with the state purchasing quotas of farm and sideline products. Among the cash crops, only the planned area under cotton is to be set aside according to directives from above. All the minimum areas set down for other crops are only for reference The decision rests with the teams." Looking to the future more boldly: "In [the] future all agricultural production plans should be initiated from the grassroots and submitted to the higher administrative levels. Some coordination and readjustment can then be done down the line."²⁶

(c) Requisitioning by higher-level authorities — governmental, Party, army — of land and buildings belonging to production teams, and the commandeering of team labor without proper compensation is forbidden. Team buildings occupied by such authorities are to be returned to the owners forthwith.

Most of these various readjustments depend for their efficacy on the cooperation of middle echelon and lower level cadres who, as we have noted, exhibit a certain passivity toward the four modernizations and whose minds are, as the saying goes, in an "ossified" or "semi-ossified" state.

The results of the policies aimed at restoring a measure of balance between the performance of agriculture and industry are said to be gratifying if somewhat worrisome. Industrial wage increases-

25. Hua Guofeng, "Report on the Work of the Government," (1980). *op. cit.*, pp. 24, 26. "The power which should belong to the enterprises and production units is improperly concentrated in the government departments, that which should belong to the local authorities in the Central authorities, and that which should belong to the government departments in the Party committees." *Ibid.*, p. 21.

26. Zhao Ziyang, "Principles of All-Round Economic Readjustment," *Eastern Horizon*, Hong Kong, May 1980, p. 8.

cum-subsidy appear to have stimulated urban demand for farm products to the point where it surpassed the sizeable increases in product supply. Although the basic products are still rationed (grains, edible oils, cotton cloth), restrictions on their sale outside state channels have been relaxed. All this has exerted strong pressure on market prices in the cities and has predictably produced calls for strict administrative control over these prices. In the first half of 1980 retail sales increased 18.5 percent over the corresponding period of 1979 (27 percent in the cities, 17.2 percent in rural areas); sales of pork, mutton, beef, poultry, eggs, and aquatic products rose by 40 percent; and sales on village fairs by 36 percent.²⁷ Concurrently, the authorities have revealed that large increases in personal savings (especially in urban areas) had taken place. The rate of saving is not known, but there is a possibility here of some involuntary saving due to goods shortages or improper assortment and quality — what the Russians euphemistically call “otlozhenny spros” (deferred demand).

Imbalance Within Agriculture

Agricultural imbalance concerns the overemphasis given in the past to grain production at the expense of other pursuits (Table 5). It is now admitted that the indiscriminate carrying out of the central command to regard grain as the “key link” caused serious ecological damage.²⁸

Table 5
AGRICULTURAL COMPONENTS, 1978
 (Percentage of total agricultural output value of
 145.9 billion yuan)

Crops	67.8
Forestry	3.0
Animal husbandry	13.2
Sideline occupations	*14.6
Fishery	1.4
Total	100.0

Source: *Beijing Review*, January 28, 1980, p. 20.

* Including 11.7 percent from the output value of brigade-run small industries, but excluding the output value of commune-run industries.

27. *Beijing Review*, August 25, 1980, p. 5.

28. Vaclav Smil, “China’s Environment,” *Current History*, September 1980, pp. 14–18, 42; Jan Prybyla, “Feeding One Billion People: Agricultural Modernization in China,” *ibid.*, pp. 19–23, 40–42

Two sets of measures are envisaged. First, the area under grain crops is to be reduced to less than 80 percent of total cultivable land and the proportion of the gross value of agricultural output accounted for by livestock, fishery, forestry, and sideline production is to be increased relatively to all crops. Second, instead of the former emphasis on "all-round self-contained systems" (self-sufficient communes, counties and provinces) there is to be more specialization based on the comparative advantage of different zones and locations. Thus, parts of Inner Mongolia are to stress livestock breeding, for example, while parts of Heilongjiang are to concentrate on wheat and coarse grains.

Imbalance Between Light and Heavy Industry

From 1952 through 1974 the average annual rate of growth of heavy industrial production was 13 percent (16 percent for machinery) while light industrial output grew at an average annual 8 percent per annum. Between 1966 and 1978, 55 percent of total investment in capital construction was allocated to heavy industry; light industry got 5 percent. The distribution of investment within industry from 1953 through 1980 is shown in Table 6. Note that during periods of leftist hegemony (1958-62, 1966-70, and 1971-75) the share of heavy industry was actually not all that different from that which it got when the right-wing was in charge. The bias appears to be built into the system.

Table 6

RATIOS OF INVESTMENT, LIGHT TO HEAVY INDUSTRY

	Period	Ratio
1953-57	First Five-Year Plan	1: 8.0
1958-62	Second Five-Year Plan	1:10.8
1963-65	Readjustment	1:12.8
1966-70	Third Five-Year Plan	1:14.1
1971-75	Fourth Five-Year Plan	1:10.2
1976-80	First three years of Post-Mao era (1979-80 expected)	1: 8.3

Source: *Beijing Review*, December 21, 1979, p. 11.

The share of state investment allocated to light industry is to be increased: in 1978 it was 5.4 percent, in 1979 it came to 5.8 percent or some 2.3 billion yuan. In addition, light industry was allocated state

budgetary funds for "tapping potential" and trial-manufacturing new products (1.5 billion yuan in 1979). The proportion of state industrial investment going to light industry as against heavy is also to rise to somewhere around the First Five-Year Plan ratio of 1:8. A larger share of investment in heavy industry is to go to those projects and branches which turn out producer goods for light industry. Heavy industry itself (e.g., some sections of the defense industry) has been directed to manufacture more consumer goods. In addition to altering the product mix of heavy industry, the development of rural consumer goods industries as well as household and cooperative sideline production are encouraged, not least by removing many administrative restrictions on family sideline activities and by providing loans to groups for the start-up of artisan-type workshops and service establishments in urban areas. Cooperative arrangements have been worked out between factories in the cities and suburban communes under which the factories help set up commune light industrial workshops, the factories' main contribution being (often discarded) equipment and technical advice, while the communes supply labor and buildings. Light industry is receiving favored treatment in the supply of raw materials, fuel, and power. The proportion of the output value of light industry to the total output value of industry is to rise from an estimated 44 percent in 1980 to 45 percent in 1981.

As a result of the several steps taken in support of light industry, light industry's gross output value rose by 9.6 percent in 1979 compared with 1978, while the gross output value of heavy industry increased by 7.7 percent. In the first six months of 1980 the gross value of light industrial output rose by 24.2 percent compared with the same period of 1978, while heavy industrial output value increased by 6 percent. The attention given to promoting consumer goods output is, of course, related to the planners' concern about inflation in the setting of increases in state sector money wages and substantial budgetary deficits in 1979, 1980, and (expected) 1981. "Financially we are still operating in the red . . . Growth [of light industrial output] lags behind increases in the people's purchasing power."²⁹

Imbalance Within Light Industry

The problem here may be summed up as disregard of consumer demand ("disproportion between production and marketing"). This is

29. Yao Yilin, *op. cit.*, pp. 35, 37.

a deep-seated systemic problem traceable to the producing enterprises' overwhelming responsibility upward to their ministerial superiors rather than downward toward their customers, the tautness of production targets, the relative ease with which targets may be manipulated by enterprise managements through assortment violations and the lowering of product quality, and the absence of lateral contractual linkages between manufacturer and consumer which punishes the producer in his pocket book for persistent disregard of consumer preferences. That the problem is systemic and should be resolved by "reforms" rather than readjustments seems to be understood by the more theoretically minded members of the economic leadership. Xue Muqiao clearly perceives that an effective solution to the problem of production losing touch with demand involves a movement toward "regulation by the market mechanism" and a reform of the price system. Incidentally, the break between production and user demand is not limited to light industry.

At the planning level with which we are concerned here, the contradiction within light industry has been tackled primarily by readjusting the flow of inputs into light industry, that is, increasing the input volume and thus reducing the degree of plan tautness in the consumer goods sector. A more promising attempt at reform has been the granting to selected light industrial enterprises of broader rights with respect to direct contracting with users for the delivery of specified volumes and assortments of goods. This has been more important in the case of firms producing for foreign markets than it has been for firms working for domestic consumers. The subject will be discussed later under "Management of the Firm."

Imbalance Within Heavy Industry

The first problem has been the overdevelopment of the metallurgy and machine-building industries relative to fuel, power, raw materials (coking coal, iron ore), transportation, and building materials, especially cement. The readjustment is to concentrate on solving the following problems.

(i) The technical content of domestically produced machinery is to be improved, largely through importation of advanced foreign models and processes. Many of the existing domestically produced machines (factory boilers, internal combustion engines, pumps, motors) are wasteful of material inputs and fuel consumption. (ii) In the past a good part of the output was produced on the bespoke tailor principle: there was too little standardization, serialization, inter-

changeability of parts, and coordination or commerce among specialized departments. Some of these problems were no doubt due to the stress put by the left on "all-round self-reliance" of economic units big and small. Some others are due to the nature of the system which makes vertical self-sufficiency (especially as regards input supply) a prudent thing for enterprise managements in an uncertain materials supply world.

A second intra-heavy industry imbalance consists in the disproportionate stress put on heavy industry's supplying its own needs. The product mix, as we have seen, is to be changed, with more emphasis given to the production of machines used by light industry.

The third imbalance has been between the development of basic and auxiliary or complementary processes within sub-branches of the industry and in individual factories. This has caused bottlenecks and erratic output performance in such industries as coal, for example. Balance is to be restored by increasing attention to the technical development of the lagging processes.

Imbalance Between Accumulation (Investment) and Consumption

The key problem here is said to be the disproportionately high rate of investment over the years (Table 7).

Table 7

INVESTMENT AS PERCENTAGE OF NATIONAL INCOME

Period	Percentage
1953-57	24.2
1958-62	30.8
1959-60	"around" 40.0
1970-78	33.0
1978	36.5
1979	33.6
1980 (plan)	"around" 30.0

Sources: Beijing Review, December 21, 1979, p.10; September 22, 1980, p.32.

"This lower rate of accumulation [in 1979-80] is mainly the result of an increase in the consumption fund for the rural and urban population, of limiting the scope of capital construction, and of economizing on the circulation fund."³⁰ In 1979 and 1980 investment

30. Yao Yilin, *op. cit.*, p. 32.

in capital construction within and outside the state budget was held at 50 billion yuan. It was projected at 55 billion yuan for 1981. "Investment in capital construction arranged by the state has been reduced, while construction outlays from extra-budgetary funds raised by the localities and enterprises themselves, as well as various loans earmarked for capital construction, have increased."³¹ In 1979, 295 large and medium-sized investment projects were suspended or deferred. In 1980 a further 238 such projects were to be canceled or halted. In view of the urgent investment needs of certain formerly relatively neglected sectors and areas (e.g., education, housing, minority areas) as well as of defense, and because of some systemic problems (free budgetary allocations of capital to state-owned enterprises and the concurrent tendency for enterprise managers to inflate their capital requirements), trimming the amount and rate of investment is not going to be easy.

Imbalance Within Accumulation

The following have been the subject of recent criticism:

(a) Too much emphasis on investment in "productive" as against "nonproductive" projects, the latter comprising projects such as housing, public utilities, public health, education, trade, and consumer services of all kinds. The rate of investment in nonproductive projects is to be stepped up. Investments in nonproductive construction having direct bearing on the improvement of the people's livelihood increased from 17.4 percent of the total investment in 1978 to 27 percent in 1979, and were expected to reach 29 percent in 1980.³² Housing, in particular, has received priority attention. In the 1950s urban housing received about 9 percent of total investment in capital construction. In the 1960s and early 1970s it was 4-7 percent. During the Cultural Revolution it apparently dwindled to "almost nothing"; it picked up to 6.9 percent in 1977, 7.8 percent in 1978, and about 10 percent in 1979.³³ Extra-budgetary sources of funds for

31. Wang Bingqian, *op. cit.*, p. 17.

32. *Beijing Review*, July 21, 1980, p. 15; Yao Yilin, *op. cit.*, p. 32.

33. *China Reconstructs*, September 1980, p. 11. Total investment in housing in the 7-year period 1979-85 is scheduled to exceed the aggregate invested by the state from 1949 through 1977. During the 1949-77 period 493 million square meters of floor space had been built. Between 1949 and 1978 the population of China's cities (based on data from 192 cities) increased by 83 percent (to reach 76.82 million in 1978, while total urban population in 1978 was 110 million). During the same period urban floor space increased by only 46.7 percent (i.e., net increase, after deducting houses pulled down). In other words, during that period the floor space per urban inhabitant fell by 0.9

residential housing construction in the cities have been increased and former restrictions on house-building and house-owning by individuals and voluntary collective groups have been removed. Two measures in particular merit attention. (i) The financial powers of local government authorities and enterprises have been enlarged: in 1979, for example, the municipal authorities of 49 large and medium-sized cities were permitted to draw 5 percent of their industrial and commercial profits for urban construction, and county authorities were allowed to use a certain portion of the earnings of county-run industries for nonproductive investments. This measure increased the reserve funds of county and city authorities by some 2 billion yuan. (ii) Individual industrial and commercial enterprises (some 4,000 of them in 1979, more in 1980) were granted the right to retain a portion of their profits, and to channel a part of such retained profits into housing construction for their workers. The total sum involved in 1979 was 4 billion yuan or 9.3 percent of total state enterprise profits transferred to the state. The state of housing (both the pace and quality of construction and the maintenance of buildings) remains unsatisfactory. In 1977 a survey of 192 cities showed an average floor space of just 3.6 square meters per person. In 1979, 62.56 million square meters of floor space were added, or some 0.3 square meters per head of urban population.³⁴

(b) The second intra-investment imbalance is between project starts and project completions. Largely because of the tautness of the capital front (too many starts, too large a scale, too few key inputs) and probably absence of proper project balancing within the planning apparatus, the average length of time for an investment project to be put in operation has risen sharply. During the First Five-Year Plan the average time span for the completion of a large industrial project was around 6 years. In the late 1970s it was 12 years. The remedy adopted has been, as we have seen, to cut down the scale and scope of construction and to dismantle unfinishable projects. The ratio of operational fixed assets to total investment increased from 74.3 percent in 1978 to 83.7 percent in 1979. A longer-term remedy consists in the improvement of the planners' investment methodology.

(c) The efficiency of investment has also been at cause and for broadly similar reasons. The impression given is that careful

square meters (not counting kitchen, lavatory, and corridor floor space). *Beijing Review*, November 30, 1979, p. 18. Most rural houses are built by individual peasants and are the property of households.

34. Yao Yilin, *op. cit.*, p. 34.

calculation of investment effectiveness has been the exception rather than the rule and that the tools for estimating such effectiveness have been wanting. "Initial success" has reportedly been achieved in the economic effectiveness of investment in both agriculture and industry, partly through adjusting the relationships between sectors of the economy, partly through enterprise consolidation, and partly through reforms of enterprise management.

Balanced Development Planning: Tentative Evaluation

The imbalances in the development of China's economy, of which so much has been made in recent years, have been attacked so far by *ad hoc*, fairly straightforward, rule-of-thumb measures designed to right the most glaring disproportions. At the same time the central administrative planning apparatus, which had been subjected for years to disruptions ranging from neglect to extreme political instability, is being rebuilt in terms of professional personnel, coverage, and improved methodology. This is, by and large, the centralizing component of the post-Mao readjustment, and despite experiments with broader rights of enterprise decision-making (to be discussed presently), the economy appears to be moving (thus far at least) in a more structured, more centralist, administrative, command direction. The number of materials balanced by the central authorities was 600 in the 1979 plan (60 balanced by the State Planning Commission, 540 by ministries). In the 1980 plan the number of centrally balanced materials was to rise to 800.³⁵ The reaction of policy-makers to the imbalance and other economic ills has been to tighten up organizational lines of command and restore Leninist discipline. It has been overwhelmingly a reaction against what most of the rehabilitated administrators see as the disruptive, "anarchic" cellular, centrifugal leftist influence of 1966-76. There is still much talk about administrative "overcentralization," but it rings less true than do the calls for restoring structured order and authority. Fascination with reform of the market-decentralization kind is most apparent among academic economists. It is less noticeable, more subdued and cautious among policy-makers. The plan comes first; the market, second. And the plan is still envisaged as basically one of centrally determined materials balances and

35. Bruce L. Reynolds, "Recent Economic Reforms in Chinese Industry." Paper presented at the annual meetings of the Eastern Economic Association, Montreal, May 1980, pp. iv-v, 1-14.

pricing, even though the precise level of determination may be subject to debate. I think that when the dust settles and the excitement of blazing new trails after the death of Mao loses its novelty, the Chinese will turn to Soviet experience and the lessons of Soviet "reforms" of the 1960s and 1970s for instruction on how to modernize the old neo-Stalinist engine.

Management of the Firm

The intent of readjustment, it is often repeated, is to increase the regulating role of the market in the economy, but to keep that role subordinated to centralized ("unified") state planning. The enterprises' "rights of self-determination" are to be enlarged but only within limits defined by the central administrative plan. We shall look at this problem first from the perspective of the collective agricultural firm (the commune and its subdivisions), then from the perspective of the industrial firm.

Agriculture

System of Responsibility (ding bao jiang)

Central control over collective agriculture is exercised through two main channels: physical quotas (for produce delivery and acreage sown to different crops) and procurement prices. Some of the adjustments made in both these channels of control have been discussed earlier; the general intention was to improve the material condition of the farms. Here we concentrate on another aspect of the readjustment which is to enlarge the decision-making scope of the communes' lower organizational units by making changes in the level at which the quota procurement and prices for a given unit are determined, and in quota coverage, sales outside the quotas and income distribution.

Officially, the rural people's commune consists of three so-called "levels of ownership": the commune, production brigades, and production teams (the last consisting on the average of between 30 and 40 households, and very roughly corresponding to the traditional village neighborhood groups). Since the death of Mao and the arrest of the gang of four, two other still lower levels have been officially recognized: the work group consisting of perhaps 3 to 6 households, and the peasant household itself. Until recently it was insisted that while relatively wide powers regarding arrangements for production (e.g., disposition of labor, cropping patterns) within the general

parameters of the state-set purchase quotas and prices could be delegated by production teams to work groups (or even individual households in the economically more backward areas), the property function with respect to farm tools and other assets, and the income distribution function should be retained by the production teams. In fact, in many places the work group has become the basic production and accounting unit with very wide rights of use to assets nominally owned by the team, while in other places production, *de facto* asset ownership, and the income distribution function are now vested in individual households. This devolution of powers downward is known as the system of responsibility. Similar arrangements had been worked out and were widely used for three or four years after the disaster of the Great Leap Forward (1958-60). By mid-1980 it was reported that over 80 percent of rural production teams have adopted variants of the responsibility system.

The system of responsibility (based on an Anhui Province sample typical of some 25 percent of teams in China with responsibility systems) is described in the following terms:³⁶

Under the new system, the production team is divided into several groups, each embracing five or six households with 30-50 people, of whom about a dozen are able-bodied people. The group which cultivates about four hectares of land *signs contracts for fixed quotas with the production team*, that is to say, it assumes full responsibility for carrying out the production plan and, after *handing over to the state a certain amount of grain as agricultural tax, fulfilling its quotas of grain to be sold to the state and contributing its share to various collective reserves*, it may *distribute* what is left among its members according to the principle of more pay for more work and of giving bonuses if the production quota is overfulfilled. The *land, draft animals, and farm tools* are still owned by the production team and divided among the groups for use. As for agricultural machinery and water conservancy facilities, they are still under the unified management of the team.

Note that the work group is "guaranteed" the use and specific allocation of labor, land, tools, and other inputs in ways it thinks proper, so long as it supplies the team with the contracted for volume of produce. This contracted volume covers the agricultural tax,

36. *Beijing Review*, September 15, 1980, p. 8.

compulsory and above-quota state procurements, and an agreed-on share of collective reserve contributions (capital fund, social fund). Anything above that is for the group to distribute as it wishes, on the basis of differentiated work points. In this instance the group is the legitimized accounting unit. But such is not invariably the case.

An important question, of course, is how much decision-making discretion the groups have under the system. This will depend on the quota content of the contracts (including how detailed the contracts are) and the procurement prices set. As regards quotas, the majority top leadership sentiment seems to be that (i) "the leading organs at all levels should not transmit [indicators for] fixed sowing areas to lower levels. Under the premise of guaranteeing the fulfillment of the state procurement tasks, the production teams [and lower groups] have the right to plant crops according to local conditions."³⁷ The same principle is to be extended to sideline products. "The procurement quota and grain and oil prices will be assessed on the basis of the basic accounting unit [team, group, household] regardless of what production responsibility system is used in the rural area."³⁸ This seems to suggest that the contract responsibilities of work groups or households are likely to be more consistent with the groups'/households' physical and financial possibilities than they would be if quotas and prices were fixed in relation to the specific conditions of higher units. The idea is to introduce greater flexibility into the communes' "ownership structure" and the procurement and pricing responsibilities associated with it. But quota and price planning remain determined above the producing unit.

In hilly, less developed, poorer, and border regions the responsibility system has been carried down to the level of the individual household. This has been the case in Tibet, for example, where output quotas have been fixed for households, as well as some work groups and readjusted teams for a period of 2 years. Under the work group/individual household responsibility system, the land assigned to the contractor is known as the *contracted plot*.

There are several variations on the theme of the contracted plot. For example, in some areas (Tibet is again a good example) livestock belonging to production teams is given over to households for raising. After the households have fulfilled the contracted production quota, they may retain for their own use and as their own property the

37. Guangzhou, Guangdong Provincial Broadcasting Service, June 4, 1980, in *FBIS*, June 10, 1980.

38. Beijing Radio, Xinhua, June 2, 1980, in *FBIS*, June 5, 1980.

young livestock and livestock products remaining. In order to help individual households in fulfilling these contractual livestock-raising responsibilities, and also to help them raise pigs and poultry on their household (private) plots, production teams are allowed to transfer to households so-called "fodder plots." In some areas (especially, it would seem, near urban centers) production teams have established "cash plots," or have contracted for such cash plots with work groups or individual households. Cash plots are used for growing high-priced industrial crops that are readily marketable and are not covered by the state procurement plan. Another variant of the contracted plot in the "grain ration plot." It seems to be most common in underdeveloped regions where the authorities assign responsibility for the production of the basic grain and oil ration to individual households, and allow them to keep anything over that. In effect, the responsibility system amounts to partial decollectivization which is most advanced in the poorest, most crisis-ridden areas. The measures appear to be limited and temporary, intended — like their predecessor Liuist arrangements of the early 1960s — to get the countryside over the worst post-Cultural Revolution problems and raise labor productivity in the short run.

Private Plots and Village Fairs (san zi yi bao)

The *de facto* privatization of the communes' farming functions is in addition to the existence and, lately, liberalization of the "private" sector within the commune organization: the household plot, household subsidiary (handicraft) activities, and village fairs (rural "free" markets). The rule (how strictly enforced, it is difficult to say) is that private plots and contracted plots to households should not exceed 15 percent of the production teams' farmland.

Private plots, which were severely restricted by the left in 1966-76, have been re-established and, indeed, granted comparatively wide privileges. No hard and fast restrictions are to be put on the land surrounding peasant houses; the peasants are to be encouraged to grow trees on them and the trees will be owned by the households that plant them. The practice of commune managements' exchanging good household plot land for poorer land is to cease and the better lands taken away from households in the past are to be returned. As usual, "in returning or allocating additional land, orchards, and livestock for personal needs, certain commune and brigade cadres failed to allocate them in full measure; some allocated bad or oddly shaped land to the commune members; and some even delayed or

took no action at all. In some other localities, commune members' sideline production has yet to be developed."³⁹ Local authorities are warned not to make readjustments in the size of private plots according to the current population [i.e., allot so much fixed area per family member] since "this could only lead to blind procreation." There are to be no quantity restrictions on what the peasants decide to grow or raise on their plots so long as they fulfill their work attendance and manure delivery obligations to the collective.⁴⁰

Village fairs are encouraged. There are 36,000 of them, we are told, doing brisk business in eggs, fruit, piglets, and surplus edible oil and food grains (5 million tons of food grains were traded in 1979). Urban free markets for rural produce are also promoted; 2,500 of them have been established to date.

More generally, the top official line now sanctions, indeed encourages and rewards, a "get rich" spirit by everyone, from individual peasant households on up. "Getting rich is nothing to be afraid of. Only when peasants get rich can the state become rich. Policy requirements should be relaxed, relaxed, and relaxed again."⁴¹ In Hotan County, Xinjiang Uygur Autonomous Region, a meeting was held to find out which commune members were getting rich the fastest. "One hundred and fifty commune members of the Uygur nationality who have actively participated in collective production and rapidly built up family fortunes by diligently engaging in household sideline production were commended and given awards by the county Party Committee." Representatives of some of the poor households who attended the meeting were reportedly "inspired and enlightened by the experience of the prosperous commune members. They vowed to free themselves of government relief and the support of others, and to work to achieve their own prosperity by their own hands."⁴² However, despite assurances that on this sensitive issue "there will be no change in the Party's policies," "the fear of becoming

39. Beijing Radio, Xinhua, June 12, 1980, in *FBIS*, June 13, 1980.

40. *Guangming Ribao*, June 5, 1980, p. 1, in *FBIS*, June 20, 1980. This was recommended by a meeting of Beijing economists sponsored by the Economics Institute of the Chinese Academy of Social Sciences. In Tibet, Inner Mongolia, and other places peasant families which previously owned no livestock can now buy such animals from collectives "at low prices." Beijing Radio, Xinhua, June 2, 1980, in *FBIS* June 4, 1980.

41. Beijing Radio, May 30, 1980 reporting on Hu Yaobang's and Wan Li's visit to Tibet (Wan and Hu were respectively general secretary of the CPC Central Committee and vice premier of the State Council), in *FBIS*, June 3, 1980.

42. Beijing Radio, Xinhua, May 29, 1980, in *FBIS*, June 2, 1980.

well-to-do has continued to prevail in certain localities."⁴³ An interesting sideproduct of the renewed economic man approach to the peasantry has been the reluctance of some team cadres to perform their managerial duties which, they claim, take time away from private plots, rural fairs, sideline activities, cash plots, fodder plots, and so on. While the "blood-and-sweat school" of "braving wind and waves" with death-defying spirit (à la Dazhai and Daqing) only to remain modestly poor, is now decried as a leftist deviation, "incorrect" consumption by cadres and masses alike is criticized.⁴⁴

It is said that as a result of these various measures, the material welfare of production teams has been improved and the production enthusiasm of the masses has been stimulated. Average monthly per capita income derived from work for the collective has risen from 6.17 yuan in 1978 to 7 yuan in 1979 (roughly 14 cents a day). Income from private plots and other household subsidiary activities is given as between 2.50 and 3.30 yuan per month for a total monthly per capita income of a little better than 10 yuan (\$6.00). The cooperatively derived income includes the equally shared foodgrain ration, which works out at roughly 12 kilograms a month, plus differentiated work points income. Commune revenues in 1979 rose by 11.4 percent, and the gross value of agricultural output by 8.7 percent.⁴⁵ On the other hand, in the new spirit of seeking truth from facts, the *People's Daily* noted in its editorial of May 14, 1980, that "in some parts of the country containing in all 100 million people, there has never been a good life since the collectivization [1955] and production has not picked up since the three years of economic collapse [1959-61]. In these regions the population has increased but the amount of grain has not increased. . . . The peasants have lost their faith in collectivization."⁴⁶

43. Beijing Radio, Xinhua, June 12, 1980, in *FBIS*, June 13, 1980. In the past, ". . . 'rich' was as fearsome as a tiger. No one dared to become outstanding. Everyone was willing to be backward and proud of being poor." *Renmin Ribao*, May 16, 1980, p. 5, in *FBIS*, May 22, 1980.

44. Some cadres and peasants have begun to spend "lavishly" on astrologers, geomancers, Taoist priests, funerals, and weddings. See Changsha, Hunan Provincial Broadcasting Service, April 6, 1980, in *FBIS*, April 29, 1980 on funerals, and Beijing Radio, Xinhua, April 26, 1980, in *FBIS*, April 29, 1980 on "the growing tendency to overspend on weddings."

45. State Planning Commission, *Beijing Review*, April 21, 1980, p. 17; Beijing Radio, Xinhua, June 16, 1980. *Renmin Ribao*, November 26, 1978 mentions a county in the Ningxia Hui Autonomous Region where the peasants' monthly income from the collective economy came to 2.42 yuan (\$1.45 a month or 5 cents a day).

46. *Renmin Ribao*, May 14, 1980, p. 1, in *CNA*, No. 1182 (1980), p. 7.

Commune Corporations

An interesting experiment was initiated by a people's commune in Shandong Province in the spring of 1980. The commune established a corporation for the production of sake and soybean sauce and the operation of a flour mill. It issued 1,250 shares of stock at a par value of 100 yuan. The shares were sold to various groups as well as to commune members. A shareholders' representative meeting — the highest decision-making body in the corporation — is held four times a year to discuss and review management policy and elect the corporation's "director general" and plant supervisors. The meeting also approves or disapproves recommendations on hiring and termination policies of the management. Of the profits, roughly 60 percent are distributed among the stockholders as "income without labor," 20 percent go for current expenses, and the remainder for the accumulation fund. The corporation is a manifestation of the current leadership policy of encouraging private investments in certain deficiency areas as a supplement to investments by the state.⁴⁷

Industry

As in agriculture, industrial readjustment resolves itself into two main components: incentives to firms (more precisely, to firm managements) and incentives to individual employees of the firms (workers and staff).

Incentives to Firms

Incentives to firms are seen primarily as: (a) enlargement of the decision-making powers of enterprise managements; (b) rationalization of the industrial structure; and, (c) introduction of economic legislation.

(a) Enterprise Decision-Making Powers

So far measures taken or actively under consideration with regard to greater enterprise autonomy have been confined to enlarging the managers' discretionary powers outside the state plan, that is, once the main plan indicators set for the enterprise by the planners have been fulfilled; or "market regulation under the guidance of the state plan." There is nothing very reformist about that, and the Chinese — as of now — have not traveled in this area as far as the Soviets had in the 1960s. The impression of startling

47. Tokyo, Kyodo, June 30, 1980, in *FBIS*, June 30, 1980.

change that one gains from reading about the adjustments China's economy since 1976 arises partly because after years of everything having been quiet on the economic theory front (when such concepts as profit could not even be mentioned), there is now a great deal of running about in the trenches. Workers in science and education (including academic economists), unlike workers in factories, have not so far benefited from wage increases. Their major compensation seems to be their present ability to speculate boldly on possible economic reforms. But their reformist schemes are well ahead of actual reform measures. Expanding managerial discretionary powers under the guidance of the state plan means several things that may be listed as follows:

- Profit retention by enterprises and the underlying problem of price determination.
- Depreciation allowances and the general question of enterprise capital investment financing.
- Lateral contracting for purchases and sales, including the hiring and dismissal of labor.
- Direct access to foreign buyers and sellers.

● *Profit retention and pricing.* In the past all profits of state enterprises were transferred to the state treasury (and, at the other end, all the enterprises' capital needs — as defined by the state planners — were met from interest-free state budgetary appropriations). Despite three major administrative decentralizations (1958, 1964, 1970) "enterprises were all along run by administrative means. Enterprises never had the power to act on their own but could only handle their affairs according to the state plan and the directives and rules received from the [imperfectly coordinated and overlapping] administrative organs above."⁴⁸ Much of the present technical backwardness of Chinese enterprises is attributed to this inability of enterprises to engage in "expanded reproduction" on their own and from their own sources.

The Sichuan and other experiments in enterprise readjustment allow state enterprises (some 6,600 of them in 1980) to retain part of their profits. In 1981 all state sector enterprises will be so treated. There are two approaches to profit retention. In some cases a portion of the total actual profit (planned and over-plan) is retained by the

48. "Changes in China's Economic Management," *Beijing Review*, February 4, 1980, p. 22.

firm, i.e., a fixed percentage of the whole lot. In other cases a percentage of above-plan profit is retained, while planned profits are either transferred to the state in their entirety, or only a small percentage of them is kept by the enterprise. In the case of the Daqing oilfield and some other state enterprises, up to 10 percent of above-plan profits may be retained, not a great deal. The retained profits are channeled into a number of enterprise funds in accordance with centrally prescribed formulae. There are three such funds: a bonus fund (the bonus being distributed to managerial, administrative, and production workers), and funds for outside-plan capital construction and for the social welfare of the employees. Allocation of retained profits to these funds varies, as does the pattern of distribution from the funds (both regulated by central guidelines). In Daqing and some other places, about 30 percent of the retained above-plan profits have gone for bonuses, the remainder into the other two funds. Xue Muqiao, whose position on this question has undergone change in recent months, once believed that the system would enable the "advanced" (profitable) enterprises to make rapid progress, while "the backward ones which have less funds [would] make slower progress." (He suggested that the gap could be narrowed by short-term bank loans which the laggards would have to repay out of subsequently earned profits.)⁴⁹ It should be noted that all after-tax profits of collective sector enterprises are retained by the enterprises and are distributed among the firms' accumulation and social funds, and as payment to members.

Three problems have "cropped up" in this connection. First, there is an ongoing wrangle between "the interests of the state, the collective, and the individual": the respective macro and micro interests do not mesh well, if at all. In February 1980 the State Economic Commission felt obliged to issue again a directive reminding all concerned that "under no circumstances should [enterprises] rely merely on increasing profits reserved for themselves." The second problem is more basic and more difficult to settle. It concerns the meaningfulness (opportunity cost accuracy) of the pricing process of which profits are one expression.

Simply stated the problem is this. Prices in China — with the exception of fairly competitive prices on the 36,000 rural and 2,500 urban-suburban fairs — are fixed by the state at various levels. The

49. Xue Muqiao, "On Reforming the Economic Management System (II)," *Beijing Review*, March 24, 1980, pp. 22-23. See also parts I and III of the series in *ibid.*, February 4, 1980, pp. 16-21, and April 7, 1980, pp. 20-26.

state-set prices can only be changed by the appropriate state organs. The prices are based on an average branch cost-plus formula. This covers the average branch cost of materials ((including fuel and power), depreciation of plant and equipment, and direct and indirect labor, plus an average branch profit markup and (commercial or industrial) tax. Missing from the costing process are the costs of capital and land used in production, i.e., rate of capital cost and rent for the use of natural resources. As in the pre-reform 1967 Soviet experience, this pricing procedure tends to understate actual production costs (especially if the planners' cost figures are adjusted to take account of projected — and probably overly optimistic — cost reductions due to centrally planned technological innovation). Product prices (both at the wholesale and retail levels) are not very reliable pointers to relative scarcities and utilities in the system (the "plus" components of profit margin and tax or subsidy being often hit-and-miss affairs). Prices not being reliable guides to optimal allocative action, it follows that the new emphasis on profits as indicators of enterprise progressiveness may be misguided and that profit-sharing by itself is not the whole answer but, in fact, is perhaps an incorrect answer to the ills that beset enterprise performance. On mature reflection, Xue Muqiao describes the dilemma in Marxist terminology:⁵⁰

"Our previous practice of expanding enterprises' self-determination rights was primarily a practice of profit-sharing. It was also intended to use the distribution of profits to stimulate the enterprises' enthusiasm to improve their management . . . But today the prices and values of various kinds of products are vastly different and an enterprise's profits are determined by low or high prices and not by management [i.e., the problem resides more in the system than in the lack of managerial expertise.] The phenomenon of inequality has consequently appeared in the sharing of profits among various enterprises. The fundamental way to resolve this question lies in adjusting prices. Adjusting prices, however, is a very complicated task that cannot be accomplished for the time being. Hence we have adopted the current method of determining the profit-sharing ratio by the amount of profits earned, in order to reduce inequality in distribution. However, the adoption of this method has become a

50. Xue Muqiao, "Some Opinions on Reforming the Economic System," *Renmin Ribao*, June 10, 1980, in *FBIS*, June 25, 1980.

stumbling block to future price adjustments. Any price adjustment is bound to affect the amount of profits shared between the state and the enterprises. If the price is adjusted upward, state revenue will suffer; if the price is adjusted downward, enterprises will suffer. To avoid favoring either side, we have used the old price prior to the adjustment, as a basis for profits-sharing. This method not only involves complicated computations, but also tends to arouse endless controversies. Furthermore, price adjustments will not be able to regulate supply and demand. An upward price adjustment will not make enterprises produce more goods that are in short supply, because enterprises are not going to get a bigger share of the profits. Likewise, a downward price adjustment will not make the enterprises produce fewer of the goods that are in excessive supply, because they are going to get the same share of profits anyway. In short, reforming the economic system by changing the profit distribution methods contradicts our efforts to use the regulatory functions of the market to avoid disruptions between production and demand.

To date there has been neither a general price recalculation on the Soviet model of 1967 (i.e., a nationwide recomputation of industrial wholesale prices that would produce more accurate cost of production figures by including a charge on capital and differential rent), nor has there been any noticeable freeing of prices from central control. There have only been increases in agricultural procurement prices for some products, selective increases in nonstaple food prices at retail, and selective wage adjustments. Spontaneous illegal price (including wage) increases are common and have been dealt with administratively by all sorts of price inspection procedures carried out by governmental and Party organs.⁵¹ The profit-sharing

51. "The salient problem at present is indiscriminate and covert price hikes." Hangzhou, Zhejiang Provincial Broadcasting Service, May 1, 1980, in *FBIS*, May 2, 1980. Beginning April 1, 1980 interest rates on savings deposits were raised as follows:

Deposit	Old Rate	New Rate
	(percent per month)	
1 year	0.33	0.45
3 years	0.375	0.51
5 years	0.42	0.57

Renmin Ribao, March 27, 1980, p. 1. In Heilongjiang Province, in the fall of 1979, 11,000 enterprises and 1.8 million prices were investigated. In Shanghai 20 percent of state-owned food shops had illegally raised prices. *CNA*, No. 1178, April 11, 1980.

readjustment based on understated cost figures and fairly arbitrarily set product prices will nonetheless be expanded in 1981 to cover all state-owned enterprises in industry, communications, commerce, and elsewhere.

The third problem relating to profit retention is a legacy of China's egalitarian exercises during the tenure in power of the leftists. Instances have been cited of the retainable profits of profitable enterprises being pooled and distributed among all enterprises in the given administratively defined area.

There is talk, some of it in high places, of replacing the profit-sharing experiment with taxes. The idea seems to be catching on. In his report on the 1980 and 1981 economic plans, Yao Yilin, minister in charge of the State Planning Commission, noted that "beginning from 1981 . . . we shall extend to more state-owned enterprises the experimental changeover from the transfer of profits to the state to a tax on profits." It is also proposed to "try out collecting fees from state-owned enterprises for the use of fixed funds so as to promote rational use of state assets" (introduction of a capital charge à la the USSR) and to "impose regulatory taxes and taxes on natural resources" (also a current Soviet practice).⁵² It is difficult to say at this time whether all this signals an impending Soviet-type industrial wholesale price readjustment or portends reformist Hungarian-type measures that would give more "spontaneously generated" flexibility to the price system.

- *Depreciation allowance* rates are set by the state planners. There are several proposals on the books at the present time regarding the treatment of depreciation and its link to enterprise investments. Like their Soviet counterparts, Chinese economists by and large agree that the rate of depreciation is too low and that it should be raised if only to make production cost calculations more realistic. As for the remission of the depreciation charge to the state (100 percent remission is the rule outside pilot firms), the outcome of the present debate cannot be readily predicted. There is fairly widespread agreement that at least a portion of the allowance should be retained by the enterprises and used to feed the enterprise capital construction fund. The controversy centers on the question whether such retention should be accompanied by a continuing interest-free government budgetary capital appropriations for the enterprises. Some argue that the state should put a charge on the enterprises' use of capital granted from the state budget but allow the enterprises to

52. Yao Yilin, *op. cit.*, p. 42.

retain a portion of the depreciation reserves. Others urge abolishing the system of free budgetary appropriations and replacing it with interest-bearing bank loans to enterprises. In this case enterprises would be allowed to keep all their depreciation reserves.⁵³ I think the most likely combination in the near future, at least for the majority of state enterprises, is partial depreciation reserve retention plus capital charge. It should be noted that collective sector enterprises retain all of their depreciation reserves, at least according to the rules set down.

● *Lateral contracting* for the purchase of inputs, the sale of a portion of outputs, and — increasingly — labor recruitment is a common practice for collective sector enterprises of all kinds. Only a relatively small proportion of inputs is supplied to such firms by the state at state-fixed prices. The collectives have to fend for themselves in this matter and they are expected to find their materials and other inputs locally in sources not used by the state (i.e., they should not compete with the government sector for inputs). The bulk of collective firms' output of the more important products is sold to the state commercial network; the rest is sold by contract to individual factories or state authorities at negotiated prices, or on the market. Labor is allocated to collective enterprises by the state's labor bureaus, or nowadays may be hired directly from among the unemployed or those who are not assigned jobs by state labor bureaus (e.g., those who are not among the top in the graduating classes of vocational, agricultural, and technical middle schools). Increasingly, assignment of workers by labor bureaus involves competitive professional/vocational examinations. In these three respects (input supply, output marketing, labor recruitment) collective enterprises have, at least on the theoretical surface, more discretionary power than state enterprises which (except for those undergoing readjustment experiments) receive their inputs and labor from, and sell the greater part of their output to, the state at state-fixed prices. However, post-Mao analysis has revealed far-reaching discrimination against nonagricultural collective enterprises (also against production teams in the rural commune sector) under all three headings and some more (like pay scales, social benefits, and working conditions). The state plan comes first, and it all but uses up the available supply of materials,

53. These alternatives are discussed by S. H. Chou in "Some Observations on Managerial Reforms in the PRC." A paper presented at the 1980 Conference of the Mid-Atlantic Region Association for Asian Studies, Drew University, October 25, 1980, pp. 14-16.

and all kinds of persuasive pressures have been put on collectives to sell most of their output to the state at not overly attractive prices. The labor supply of collective firms consists in large part of housewives, retired people, unskilled youth and others who cannot find jobs in the state sector.

What seems to be happening under the pilot readjustment experiments may be described as a "collectivization" of state enterprises. This is brought out by the discussion relating to profit and depreciation reserve retention, bank financing of at least a part of the state enterprises' fixed capital needs, the insistent calls on state firms to operate in the black with concurrent threats of withdrawing state budgetary subsidies for enterprises which persistently make losses, and the permission now given to state enterprises to contract for inputs and outputs with other enterprises once the state plan has been fulfilled. There has also been a good deal of discussion, but so far little action, on how to break the "unbreakable iron rice bowl," that is, how to get around the principle of guaranteed life-time employment in state enterprises. (An offspring of a retired state sector worker is entitled to a job in the same factory.) The number of mandatory targets set by the planners for state enterprises is to be gradually reduced. This in itself would not amount to much, as Soviet experience of the 1960s has shown. However, the intention at least is to accompany the reduction in mandatory targets with increased resort to "economic levers" to give "guidance to the enterprise." It is not clear, perhaps even to the readjusters themselves, what these economic levers will be in the absence of a flexible price system. There is talk about reducing tautness in the economy by making output targets more reasonable relatively to the available inputs: "The argument of fulfilling 100 percent of a task with 70 or 80 percent of the materials needed is nonscientific." This way of proceeding leaves "gaps" in the plan. Although "some hold that gaps constitute an *inpetus*," that is, a taut plan is a surrogate for market competition by keeping managers on their toes (but it also makes them cheat), most people now realize that "the bigger the gaps, the more serious the harm."⁵⁴ As was the case in the Soviet Union, there is a declared intent to increase the distribution of the means of production through "commercial" channels, perhaps to partially dismantle the material-technical supply network. But there is considerable hesitation and uncertainty about taking this step. Xue Muqiao puts it bluntly: "In future reform of the economic system,

54. *Renmin Ribao*, June 16, 1980, p. 1, in *FBIS*, June 20, 1980.

reforming the commodity circulation system to invigorate our economy seems to be more important than reforming the profit distribution system. This point, however, is generally ignored . . . Increase the circulation channels, reduce circulation linkages, and make it possible for producers and consumers to meet directly."⁵⁵

- *Direct access to foreign buyers and sellers* by selected enterprises has been introduced, especially in Guangdong and Fujian Provinces. In a number of instances representatives of individual enterprises have taken part in negotiations with foreign businessmen and foreign governmental negotiators. Some pilot firms have been granted the right to retain and dispose of a part of the foreign exchange income earned through their firms' exports. Such lateral activities by enterprises are, of course, subject to various controls by the Ministry of Foreign Trade, the Ministry of Finance, the Bank of China, and various special foreign exchange commissions. The most spectacular lateral contact between Chinese and foreign enterprises is the joint venture, which can only be mentioned here in passing. There are many legal and administrative problems that must be hammered out before joint ventures with foreign corporations take on substantial proportions. So far the arrangements that have materialized have been, for the most part, joint ventures with overseas Chinese, especially Hong Kong corporations. A number of special economic zones and industrial districts geared to the export trade have been set up in Guangdong and Fujian. These are patterned on the export processing zones which once played a key role in the development of Taiwan's exports.

To sum up, decision-making powers of the 6,600 pilot enterprises have been widened under the four headings discussed above, but there remain strict state-set limitations on the exercise of the newly acquired powers.

(b) Rationalizing the Industrial Structure

The following measures are being taken to "tap the potential" of existing enterprises (mainly reduce the underemployment of labor and capital):

- Consolidation, specialization, and cooperation of firms.
- Interfirm competition.
- Expansion of the collective and family private enterprise sectors.

55. Xue Muqiao, *Renmin Ribao*, June 10, 1980, in *FBIS*, June 25, 1980.

• *Consolidation, specialization, and cooperation of firms* has already been mentioned in connection with our discussion of the reorganization of the machine-building industry. The basic issues are these: The administrative command system resting on the administratively defined branch principle of planning promotes the emergence of independent ministerial empires, a bureaucratic compartmentalization of independent ministerial empires, a bureaucratic compartmentalization of the economy along industrial branches, enterprise, and politically drawn regional lines. In addition, the Maoist insistence on "self-contained systems" — regional and functional — aggravates the system's natural propensity toward duplication, concealment of "reserves" by each and every enterprise and branch, and deficient lateral micro coordination. Another legacy of Maoism is the proliferation of mini-industries, some of which are wasteful and do (in fact, although they are not supposed to) compete with state firms for scarce inputs of all kinds. Consolidation or outright elimination of such firms has been a constant feature of periods during which a politically emergent Party right cleans up the problems left by an outburst of radical left policies (e.g., the cleaning-up operation carried out in the wake of Mao's Great Leap Forward, from 1961 to 1963). The leftists "did not care about the conditions, never worked out the costs, and set up the 'five small' industries. The damage and waste as a result of such impractical ways are gigantic and frightening . . . [We] must break through the old notion that every place should build an independent economic system for itself."⁵⁶ The sentiment is laudable but the theoretical building blocks for its implementation (correct costing procedures, for example) are scarce at this point in time. The need for calculating opportunity costs is understood by the present leaders and more so by their academic advisers. But such calculation is inhibited by the present condition of Chinese economic science and the state of Chinese prices.

The present drive for consolidation of the less viable smaller enterprises, specialization, and cooperation covers all sectors of the economy, industry as well as agriculture. The essence of the effort is to break through administrative barriers and allow the emergence of the economic "inner ties" among enterprises, sectors, and areas.

Consolidation, specialization, and cooperation take three main forms. (1) Establishment of domestic joint ventures based on division of labor and technological levels among the associated enterprises.

56. *Renmin Ribao*, June 10, 1980, in *FBIS*, June 19, 1980.

For example, Shanghai Municipality runs a number of joint light industrial ventures with Zhejiang, Jiangxi, and Hunan Provinces and the Guangxi Autonomous Region. Technology and funds are provided by Shanghai; manpower and raw materials by the partners. (2) There has also been a movement toward the establishment of specialized nationwide companies equipped with independent self-accounting (*khozraschet*) systems. These are in essence subministries, operating on the (Soviet-type) self-accounting system. The system has also been applied to domestic wholesale commerce. A nationwide chemical product sales network has been set up in which 14 cities participate for the exchange of information, resolution of surplus and shortage problems, and the conclusion of contracts. (3) There is a trend toward setting-up multiplant enterprises under single management (roughly the equivalent of the Soviet production associations of the 1970s).

- *Interfirm competition*, as distinct from interfirm socialist emulation, is considered to be deficient. The problem is rooted in the principles of guaranteed employment and the (now discarded) equalitarianism of interfirm income distribution, the policy manifestation of which has been the immortality of socialist enterprises, at least of those owned by the state. "Extensive competition is to be encouraged under the guidance of the state plan." (Note the qualification: "blind," "spontaneous" market-type competition will not be allowed). Xue argues that competition might enlarge the economic differences between people. "Actually these differences constitute a motive force that encourages the advanced and stimulates the backward. Then the question arises as to whether a large number of medium-sized and small enterprises will go bankrupt. I think this can be avoided by encouraging integration."⁵⁷

In short, the new approach to interfirm competition rejects, at least at the rhetorical and academic levels, the old thesis that administratively created plan tautness (asking for more than can be delivered) is a way of competing superior to the anarchic competition of the market. However, given the powerful (and, since 1976, reinforced) concrete structure of the economy's administrative apparatus and the worrisome unemployment problem, the likelihood of interfirm competition being actually practised in the near or not so near future on any significant scale is, I think, exceedingly slim.

- *Expansion of collective and family (private) enterprises* in urban and rural areas is now encouraged as a quick and relatively cheap way of soaking up some of the urban unemployment (especially

57. Xue Muqiao, *Beijing Review*, September 8, 1980, pp. 21-22.

among the young), supplying badly needed services to the population,⁵⁸ and providing additional income to peasant families and nonfarming employment to rusticated urban educated youths. The new collective or family-type private firms are established semi-spontaneously by individuals and groups in response to market needs as perceived by them, and with marginal financial help (or at least absence of harassment) from the state.⁵⁹ Newly established commercial and service trade enterprises run by collectives are exempted from industrial and commercial taxes and income taxes for 3 years from the month they begin operations, except for industrial and commercial taxes levied on industrial products. Beginning in 1980, commercial and service trade enterprise pay their income taxes according to the collective industrial tax rate, which is expected to lighten their tax burden by about one-third. There is probably ambivalence about this policy at the echelon of local state and Party authorities, judging by frequent complaints about runaway "exploitative" and other "unhealthy" tendencies among the masses.

Capital investment in collective enterprises is relatively modest, recoupment periods are short, and labor intensity is high. The average per capita fixed investment in all state sector and other enterprises is shown in Table 8.

Table 8
AVERAGE PER CAPITA FIXED INVESTMENT, MID-1980
(Yuan)

Sector	Yuan
All state sector enterprises	10,000
State light industry	6,200
State heavy industry	12,000
Collective enterprises	less than 2,000

Source: Beijing Radio, Xinhua, June 18, 1980, in *FBIS* June 20, 1980.

58. In 1957 there were 10 retail shops per 1,000 persons; in 1979 there was only 1 retail shop per 10,000 persons. There were about 1 million shops in the country in 1957; in 1979 there were only 190,000 shops. Many of the shops have no storage space, i.e., goods are stored out in the open. *Renmin Ribao*, February 15, 1980, p. 5, in *CNA*, No. 1178, April 11, 1980, p. 6. The number of shops in Beijing dropped from 70,000 in the early 1950s to 10,000 in mid-1980. "Department stores, shops, and grocery stores have merged, some several times, and many small trades and individual services have disappeared," Beijing Radio, Xinhua, May 28, 1980, in *FBIS*, June 2, 1980.

59. Beijing Radio, Xinhua, June 16, 1980, in *FBIS*, June 18, 1980. In 1979 the total turnover value of one-man businesses in China was less than 1 percent of that of all state and collective enterprises.

In 1979 collective firms provided an additional 2.3 million jobs, almost the same as the state sector enterprises but with much more modest capital outlay.

Allocation of labor to collective enterprises (as we have already noted) is less controlled by state labor bureaus than in the past and than allocation of labor to state and higher priority employments. The procedure nowadays, while not constituting an unencumbered market for collective and family enterprise labor, is comparatively liberal. In Beijing retired workers and unemployed young people are permitted to set up service businesses provided they (1) register at the local industry and commerce bureau, (2) produce a letter of recommendation from their neighborhood committee, (3) pass a test of technical competence, (4) do not propose to employ other people, and (5) obtain a municipal permit.

(c) Economic Legislation

One of the early tasks undertaken by the post-Mao leadership has been the reinstatement and refurbishing of laws, rules and regulations ("socialist legality") that took a bad beating during the Cultural Revolution.⁶⁰ Economic legislation and economic judicial administrations (including arbitration) are being passed and implemented. Between October 1976 and August 1980, the State Council promulgated more than 40 economic decrees and is currently drafting another two dozen, including a draft planning law and draft laws governing factory work, contracts, and energy. Economic trials have been given wide publicity.

Incentives to Workers and Staff

The stress since 1977 has been on differentiated material incentives to individuals and groups (shifts, workshops, a factory's workers as a whole). Moral incentives have not been abandoned but have lost much of their former position in the system. Punishments (material and moral) for incompetence and violations of labor discipline have been given more prominence than in the past.

60. I agree with Lowell Dittmer ("The Legacy of Mao Zedong," *Asian Survey*, May 1980, pp. 552-573) that the new emphasis in China on "socialist legality" is intended to (a) revive the awesome respect for the Party of pre-Cultural Revolution days, and (b) suppress dissent rather than promote individual rights, or enterprise rights for that matter. See Hungdah Chiu, "China's New Legal System," *Current History*, September 1980, pp. 29-32, 44-45.

Measures taken so far to readjust the incentive system in industry include:

- (a) Wage and salary adjustments.
- (b) Restoration of overtime pay and, in some occupations, piece-work pay.
- (c) Cost of living allowances.
- (d) Payment of bonuses.
- (e) Prizes.
- (f) Restoration of seniority and professional distinctions (including the "directorial principle").
- (g) Restoration of trade unions (aimed, among others, at improving the social wage).
- (h) Measures of codetermination.

These shall be discussed with the utmost brevity.

(a) Wage and Salary Adjustments

Since the fall of the gang of four, three rounds of tariff wage and salary adjustments have been made. (i) On October 1, 1977 tariff wages were raised for 46 percent of state sector industrial workers, employees of state enterprises, and government personnel. This was the first general tariff wage adjustment in twenty years. "Generally" the wage increase was 10 percent. An additional 18 percent of state sector workers and employees were moved up the job grade ladder. (ii) In 1978 wage increases were given to another 2 percent of state workers and employees. (iii) A third round of tariff wage increases for state sector workers and employees, this one benefiting 40 percent of such people, took place in November 1979.

Several criticisms of the wage hikes have been made by the Chinese. First, even after the increases the level of money wages has remained low relatively to the prices of all but rationed staple goods and cotton fabric traded within state commerce. (Some of these articles command high prices on the village and suburban fairs.) The incentive effect of the wage hikes has been eroded since 1979 by substantial rises in most retail prices, both legally sanctioned and illegal. One source estimates the rise in government-set retail prices at 20 to 50 percent between early 1979 and early 1980. Together with disguised price increases, "in real life prices have gone on a rampage."⁶¹ Second, recognizing the material difficulties of their

61. CNA, No. 1178, April 11, 1980, p. 1.

employees, many leading cadres take the "easy way out" and grant wholesale promotions especially "en famille." In other places in deciding on salary adjustments, leading cadres played factional-favoritism and old-score-settling games. Elsewhere, they "avoided contradictions and surrendered their leadership" by resorting to secret ballots or drawing lots in deciding on wage increases and promotions.⁶² Third, large numbers of teachers, scientists and technicians have not had any wage increases so far and have found their real incomes reduced.

(b) Overtime Pay and Piecework Pay

Overtime pay has been restored. Piecework pay has been reintroduced in certain occupations which lend themselves to it (e.g., loading and unloading of ships). Incidentally, piecework pay never played the significant role in China that it did in the Soviet Union in the early stages of industrialization.

(c) Cost of Living Allowances

As noted earlier, the increase in the state retail prices of eight nonstaple foods decreed on November 1, 1979, was accompanied by an across-the-board cost of living allowance of 5 yuan per month granted to all state sector workers and employees.

(d) Bonuses

Bonus payments to managers, workers, and enterprise employees have been restored and a multitude of bonus payment schemes is currently being tried. A preliminary treatment of the subject may be found in the paper by Professor S. H. Chou referred to earlier.⁶³ There is an extensive Western literature on the subject of the effectiveness of bonuses in stimulating efficiency of factor inputs in centrally planned administrative command economies of the Soviet type, some of which is cited by Chou.

Here we limit ourselves to a general description of the current Chinese bonus system and note some problems encountered in the course of its implementation.

In general, Chinese bonus schemes are at the present time regarded by their authors and those who administer them as either a simple subsidy to what some consider to be insufficient, morale-sapping tariff wages, or as a differentiated encouragement to productivity. Some bonuses are, in fact, unabashedly of the subsidy kind: They are paid in equal amounts to each worker of any

62. Xining, Qinghai Provincial Broadcasting Service, May 20, 1980, in *FBIS*, June 3, 1980.

63. S. H. Chou, *op. cit.*

enterprise that has fulfilled its major planned norms, especially those relating to output, assortment, and profit. This practice, which began during the Cultural Revolution, is nowadays criticized in influential quarters. It is understood, however, that given the very modest dimensions of the current tariff wages, not much can be done about this rather widespread manifestation of egalitarianism. (Remember that it is also a form of insurance taken out by cadres against the eventuality of future political retribution from the left.)

Another argument adduced by some in favor of across-the-board bonuses is that the existing enterprise success indicators (centrally mandated norms) are "unscientific" — they are either too "soft" or do not accurately measure the efficiency of relative inputs of work. Under these conditions, the payment of differentiated bonuses would be likely to "impair unity among the workers."

Also "enterprises concoct various pretexts to enlarge the scope of bonuses beyond what is justified by the bonuses' stimulus function. Some enterprises arbitrarily raise the level of bonuses. Some practice fraud and make indiscriminate use of production costs and enterprise funds. . . . In a word they get bonuses by violating financial and economic discipline."⁶⁴ This has a familiar ring for those conversant with Soviet experience.

In his paper, Professor Chou examines five other types of bonuses, not distributed equally among all workers in the firm. He notes that the basic characteristics of all the bonus schemes are the following. (i) The precondition for the payment of any bonus is the fulfillment of centrally planned targets; (ii) the amount of the bonus is calculated according to either the enterprise's wage bill, level of employment, or amount of over-plan profit. The most common basis in Chou's sample is level of employment; the least common is over-plan profit.

As we have seen, Chinese sources are aware of the various weaknesses of the present system, especially of the controversial linkage between bonus and wage fund/employment, which benefits large employers, and those who use labor inputs lavishly. They also have doubts about the economic rationality of the basic targets which condition the bonus.

Individual enterprise bonus formulas are supposed to conform to rules formulated by the central state authorities. At present this is probably observed mainly in the breach. There have been reminders

64. *Nanfang Ribao*, May 20, 1980, in *FBIS*, May 27, 1980.

from the center that only in enterprises that were given experimentally larger powers of decision should the bonus not be limited to 1½-2 months average wage of workers and staff. All other enterprises should stay within the 1½-2 months rule. "If they make big profits and want to increase bonuses beyond that, they must obtain permission from provincial, municipal, and district labor departments if they are local enterprises, or from the State Council departments concerned if they are enterprises directly under the central authorities."⁶⁵

(e) Prizes

Cash prizes on a sliding scale have been introduced for meritorious performance by individuals in invention, innovation, and discovery of mineral deposits (and also in birth control).

(f) Seniority, Professional Distinctions

The old pre-Cultural Revolution principle of no-nonsense prerogatives and responsibilities of the enterprise manager has been rehabilitated and the unruly, faction-ridden Revolutionary Committees have been dissolved. Areas of executive jurisdiction and hierarchical ordering are being defined and encased in rules and regulations. Seniority rights are back in vogue, as is the regard paid to expertise. Many scientists, technicians, and managers who were sent down to the factory floor have been reappointed to their former positions and their back salaries have been paid. Total state outlays under this heading are well in excess of 1 billion yuan. There remains, of course, the problem that those now rehabilitated lost expertise during their long exile on the farm or factory floor.

(g) Trade Unions

Trade unions of the Soviet type are back in business. They were abolished as "elitist" organizations during the Cultural Revolution and replaced at that time by all manner of mass movements dominated by politically alert workers. The main purposes of the reactivated unions are to (i) supervise labor discipline on behalf of the state and (ii) administer portions of the social wage and fringe benefits, especially with regard to work safety and general working conditions (both of which leave much to be desired), pensions and other benefits, and worker housing. Although the Constitution of the PRC guarantees the right to strike, the right seems to be operative only in times of political turmoil and the concurrent weakening of central authority (e.g., 1970-76). Since 1976 attempts by worker

65. *Gongren Ribao*, May 27, 1980, in *FBIS*, May 29, 1980.

groups to stage "collective slow downs" and work stoppages, have been dealt with firmly, "according to law."⁶⁶

(h) Codetermination

In line with the drive to rebuild formal organizational structures and reimpose Leninist discipline, the fluid and fractious "open-door" participatory arrangements of Cultural Revolution days have been abolished, notably the *sida*, or "four-bigs": *daming* (contending in a big way), *dafang* (airing views in a big way), *dabianlun* (arguing things out in a big way), and *dazibao* (big character posters).

The *sida* has been replaced by formalized "enterprise democracy," that is, by (i) elections of lower and middle echelon enterprise cadres (also of enterprise directors in a few pilot enterprises), the electorate consisting of all the enterprise workers or employees concerned, and (ii) the election of enterprise workers' congresses (a system which had first come into being in the 1950s but was suspended for 10 years during the reign of the gang). The congresses are supposed to have far-reaching advisory and supervisory rights vis-à-vis enterprise managements.

There are some problems connected with this version of codetermination. First, the workers do not seem to be convinced that the elections are truly democratic. What happened in a local (people's congress) election in the Shanghai county of Fengxian is probably typical: "All the electors arrived in the hall on time with exception of Hu Yang and two others who stood at the door laughing continually. . . . Asked to be seated, the three tore up their ballot slips, while one of them added his name to the list of candidates and gave himself some votes at the same time. One of their superiors who intervened received a punch in the face, and another official had his arm twisted."⁶⁷ It is reported that "some enterprises have held workers' congresses only for the sake of formality" and that there is opposition to them by "patriarchal" enterprise managements. The system "has not gained the wide attention of the masses of workers."⁶⁸

All in all, the current experiments in codetermination are probably not as effective from the standpoint of incentives to labor as their authors would have wished.

66. See e.g. the incident at the Chinese Steamed Meat Dumpling and Dumpling Soup Department under the Shashi Eating House in Shanghai, Shanghai Radio, June 4, 1980, in *FBIS*, June 5, 1980.

67. Shanghai *Wenhui Bao*, cited by AFP Beijing, May 30, 1980, in *FBIS*, June 2, 1980.

68. *Renmin Ribao*, March 6, 1980, in *FBIS*, March 31, 1980.

Epilogue

My survey of China's economic readjustments does not consider some vital issues — the economic measures taken to limit births, for example. At this stage it is not possible to draw firm conclusions. The system is in flux, the evidence is not all in, and new proposals are being floated all the time. The only clear indication is that so far the bulk of the measures taken (as distinct from proposals for measures to be taken) has been of the readjustment rather than the reform type. The cumulative effect of these readjustments has been to move the Chinese economy closer to its contemporary Soviet counterpart, always allowing for cultural idiosyncracies. An important objective of readjustment is to remedy some basic inter- and intra-sectoral disproportions and to strengthen and improve central control mechanisms. The expansion of enterprise decision-making powers has been, I think, contingent on and circumscribed by this strengthening and improvement of central planning.

SUPPLEMENT AND UPDATE

The paper was completed in October 1980. Since that time the process of readjustment and reform (much readjustment, some reform) has proceeded space with, however, more finely tuned discrimination and less haste than in the euphoric early post-Mao years. The costs and problems involved in absorbing and paying for the originally (1978) proposed massive technology and capital goods imports are now better understood, as is the difficulty of grafting market-type institutions onto a centralized, administrative, command economy which to this day has trouble overcoming its lingering Maoist aversion to individual, unequal, material incentives. To lift the economy out of the doldrums and move it away from extensive toward intensive (factor-innovative) growth, the system of incentives must include more pay for productive workers and less pay for laggards, the willingness and ability to fire loafers and incompetents, shut down factories that run only by the grace of government subsidies, and allow the profitable firms to keep the bulk of their profits and to spend them as and when and where they wish in a market that is not emptied of resources by the actions of the State Supply Bureau and its component bureaus and corporations that still today reach into every nook and cranny of the economy. However, as was noted earlier, readjustment without structural reform may prove to be a cure worse than the disease. In the present state of most Chinese prices the profitability of a firm is not even distantly an

indication of the firm's cost effectiveness or social utility, and wage levels and spreads are still too low and too narrow to elicit satisfactory individual effort and commitment. In the longer run (but not too long, or else reform will be seriously compromised by bureaucratic forces of special privilege and status quo) the whole central planning network with its baroque ministerial empires and administrative modes of thought may have to be pruned out of existence if marketization is to be more than word-deep. The present leaders want the country to reap the benefits of a freely operating "law of value" but they still recoil from the idea of dumping a system of central planning with which they are familiar and which in 1979 put 20 million tons of newly-produced steel (out of a total production that year of 34.4 million tons) straight into the warehouse.

In the setting of inflation, urban unemployment, low real income levels, budgetary deficits, and balance of payments disequilibria, it takes guts made of Japanese steel to keep talking about structural reform which many "responsible persons" (and not only unreconstructed Maoists) blame for the economy's present malaise. On top of technical difficulties inherent in the process of early development and the even more elusive and politically awesome problem of institutional reform, there is the old factionalism within the Party (not improved by the show trial of the gang of four), and there is the need to raise public morale. Despite a widespread sense of relief that the Maoist nightmare is over for the time being, there is much fear of future political score-settling and renewed "historical transitions." While devotion to China is strong, a distinction is increasingly made — and not only in intellectual circles — between China and China's communist leaders. The Party's credibility has been eroded by too many 180 degree turns and dialectical twistings of an already tortuous and reason-offending line. Public goodwill and the citizens' willingness to make personal sacrifices on the promise of a brighter future, have been largely squandered and are not likely to be brought to life quickly by corrupt, arrogant, and self-serving cadres who flourish and multiply in direct ratio to the number of *People's Daily* editorials deploring their behavior.

This SUPPLEMENT AND UPDATE follows — albeit roughly and with some poetic license — the conceptual guideposts of the original paper.

(March 1981)

Balanced Development Planning

1. The possibility of constructing a coherent long-term (five-or-ten-year) plan has been officially ruled out for the time being until, that is, 1985 at the earliest.⁶⁹ Earlier plans of this nature have been scrapped. After 1981 and until 1985 planning will be done on a yearly basis, "step by step," and the whole question of planning — including comprehensiveness and methodology — is being reexamined.

2. While homage is paid to the principle of plan decentralization, increased de facto privatization of property relations, and greater resort to market-type policy instruments ("law of value"), there has been so far no perceptible dismantling of the ministerial-special commission-administrative-command edifice: the sprawling and immensely powerful conglomerate of bureaucratic self-interest. The core of the central administrative command economy (the economic equivalent of the Communist Party in politics) is the material-technical supply network headed by the State Bureau of Supplies, which physically apportions key producer goods, including most raw materials and fuels. The network appears to be thriving. It employs an unhealthy half a million people at the county level and above, and its Beijing headquarters have a head count of 1,300. The Bureau's actions remain based on administrative criteria far removed from the inner logic of the law of value. There had been growth in the number of central ministries as well as some organizational consolidation and occasional administrative decentralization (mainly to the provincial level). For instance, a State Machine Building Commission was established under the State Council to coordinate the work of the various machine-building ministries. This represents a growing bureaucratization of the economy: additional coordinating, "guiding," and "assisting" organs of administration are being added to an already huge state and Party bureaucracy for the avowed purpose of bringing about a transition to more markets and less administration. It is a typically "Soviet" reaction to the challenge of economic reform. In answer to a question put to him by Western journalists as to whether the industrial ministries would one day be replaced by business corporations, vice-premier Bo Yibo (chairman of the State Machine Building Industry Commission) replied evasively that "this was not finally decided and it may take a certain amount of

69. Zhao Zhiyan, briefing visiting Roumanian premier Illie Verdet, *The Asian Wall Street Journal*, December 30, 1980, p. 1.

time."⁷⁰ But time in China is a scarce commodity these days, what with the opposition waiting eagerly around the corner and the people's expectations raised to a pitch.

3. The number of material balances (disaggregated input-output tables) prepared by the State Bureau of Supplies was 256 in 1980. The centrally balanced "important, commonly-used" products covered two major categories of producer goods: (a) fuels, raw materials, and other materials (e.g., coal, steel products, nonferrous metals, wood, cement, sulfuric acid, nitric acid, soda ash, rubber, tires), comprising 101 items in all, and (b) machinery and electrical equipment (155 items), including machine tools, motors, industrial boilers, automobiles, and bearings. Another 581 categories of goods known as "important means of production with specialized uses" (power plant equipment, for example) were balanced by central industrial and transportation ministries. Over 10,000 "ordinary means of production" were balanced by the planning organs of provinces, municipalities, and autonomous regions. As in the Soviet Union this is both not enough (for comprehensive central physical planning) and too much (for flexibility of adjustment — material-ordering conferences which deal with 70 percent of the balanced products are held once a year, and ordering meetings, which deal with the remaining 30 percent, are held biannually). "It is difficult," in the words of Li Kaixing (director of the State Bureau of Supplies), "to adapt to changes in production and needs, and this causes some units to be short of materials, while other units are overstocked."⁷¹ Thus, as of 1980, the central materials balancing process (central in the sense of being carried out above the province level) covered 837 commodities, up 237 from the year before. Interestingly, the number of goods balanced by the State Bureau of Supplies rose the sharpest: from 60 in 1979 to 256 in 1980 (assuming that the 1979 figures given to Bruce Reynolds are accurate). There is talk of *reducing* the Bureau-balanced goods to 68 or "even less," but the evidence so far points in a contrary direction. Even a simple description of the supply and distribution system for key producer goods in China sounds incredibly complex and bureaucratic. It will take more than well-intentioned talk to dismantle it. The centrally balanced goods (in fact, they are categories of goods comprising many subitems) are taken out of the commercial network (that is, they are unaffected by the "law of value") and the procedures used in determining the

70. *The China Business Review (CBR)*, November/December 1980, p. 12.

71. *CBR*, November/December 1980, p. 15.

input-output balances and the distribution of inputs and outputs have little if anything to do with notions of market equilibria and optimality. In the future, according to Li, greater consideration will be given to market forces in determining commodity circulation. But this, on present evidence, amounts to mere speculation.

4. To reduce future imbalances between what is produced and what is wanted in the economy, the Ministries of Light Industry and Commerce have conducted market surveys and, for the first time in more than thirty years, have come up with market forecasts. This is a step forward provided the underlying work is analytically sound and acted upon by the planners.

5. Since 1978 another imbalance has been added to the list of imbalances discussed in the paper. The first budgetary deficit appeared in 1978. By 1979 the government appears to have lost control over expenditures, thus joining the family of nations in this respect. In 1979 the budgetary deficit came to 17.06 billion yuan (\$11 billion), or roughly 7 percent of all budgetary revenues and expenditures. In 1980 the deficit was expected to be 8 billion yuan (\$5.3 billion), but it could turn out to be higher when the final figures are in. For 1981 a deficit of \$3.5 billion is envisaged. The imbalance has been caused by lower-than-planned revenues (due in part to enterprise profit retentions and reductions in, or exemptions from, the agricultural tax — the latter will be even more significant in 1981 because of the natural hardships visited by floods and drought on many communes), and by much larger expenditures than those planned, linked to wage increases, payment of higher agricultural procurement prices, outlays on imported capital goods, relief payments to communes, and expenditures on renovation of existing industrial and transportation enterprises. The deficits were fueled by an unaccustomed absence of fiscal restraint by the Ministry of Finance and lavish spending on capital projects by some provincial authorities that since 1978 had been granted relatively broad autonomy in this matter.

Budgetary deficits have helped spur inflation, open and unabashed this time. The officially conceded inflation rate (retail prices of consumer goods) was 5.9 percent in 1979 and 6.5 percent in 1980.⁷² These figures probably understate the actual inflation rate in the cities, which is likely to be two to three times the official rate. In addition to open inflation, there is significant and widespread

72. Beijing, Xinhua, February 8, 1981.

suppressed inflation in the form of goods shortages, lines of customers outside stores, and "disguised" price increases ("putting fewer meat balls in a bowl of soup"). The authorities have reacted to all this in two main ways: through (a) general fiscal measures, and (b) specific administrative controls.

(a) The most important general measure is the long discussed but now apparently imminent implemented reduction in the government's capital expenditures, especially outlays on new industrial projects (particularly in metallurgy and machine building). Many of these projects are wasteful because the required complementary goods and infrastructural services are missing (e.g., electric power, transportation). Such cuts were to have been made gradually in 1979 and 1980, but they were not made largely because the system as presently set up favors additions to capacity rather than more efficient use of existing capacity and improved product mix. Thus, while "left leaping" is criticized, the policy-makers find themselves forced in 1981 to command another leap-like retrenchment: an investment slash of 40 percent in one year, the cut being directed primarily at new plant and equipment in metallurgy, machine building, and similar heavy industry subsectors. Henceforth, investment is to be concentrated on renovation, that is, on upgrading the performance of existing establishments, and resources are to be shifted into bottleneck producer industries and services, light industries producing consumer goods, and residential housing.

Some of the investment in consumer services is to be accomplished outside the state plan through the encouragement of private initiative. The same is true of housing. In the first ten months of 1980, privately built housing in 111 cities and towns came to about 5 percent of the total new floor space added during that period. Sichuan-type experimental state enterprises are also expected to use some of their newly retained profits to build workers' housing.

However, the 40 percent reduction in basic capital construction by the state is bound to encounter stiff resistance. A good part of such investment indirectly benefits the military, who are already chafing at what they consider to be the scandalously low priority assigned to defense in the four modernizations. Direct (identifiable) military spending is believed to have been cut by 13 percent in 1980 compared with the year before. Further cutbacks in metallurgy and machine building, statistically classified as civilian industries but in fact of direct relevance to national defense, are bound to be resisted by the powerful military lobby. In short, pressure for raising the absolute amount, share, and rate of investment in basic capital construction is

likely to be strong in the years to come. Given the objective internal laws of the administrative command system and the subjective neo-Stalinist experience of the system's directors, the bias in favor of more and faster investment in the "classical" subsectors of heavy industry (steel, machine building) will not be easily displaced.

The problem of inflation is compounded by two developments. First, industrial output (including the output of consumer goods) was not remarkable in 1980: about 8 percent better than in 1979. The goods needed to soak-up the pent-up consumer demand are not coming onto the market at the required pace and in the correct qualities and assortments. Second, agricultural production in 1980 was afflicted by bad weather in at least two major producing provinces. Grain output fell 5 percent compared with 1979 (316 million tons in 1980 against 332.1 million tons the year before), while the number of grain consumers rose by at least 1.2 percent (about 12 million extra mouths to feed). Given the low per capita grain consumption levels in 1979, the 1980 production figures are distressing. In the early months of 1981 China reportedly applied for international disaster relief to the United Nations (another first). Crop losses of 30-50% caused by floods — the worst in 26 years — and the worst drought in 37 years, "seriously affected more than 20 million people" in Hubei and Hebei Provinces (combined population: 95 million).⁷³

(b) Specific anti-inflation controls in China, as elsewhere, tend to be of the administrative-decree kind. Thus, maximum prices have been imposed on rural free market transactions, a measure which runs counter to the government's new incentives policy and does not square with the announced intent to let the "law of value" do more work in the economy. Citizens have been encouraged to inform the authorities of cases in which they believe themselves to have been short-changed by government sellers. Punishment for "disguised" price-raising is severe.

6. For the first time in years, in the wake of the 1978 foreign shopping spree (now criticized as a "left" mistake of the leaping genius) China's balance of trade began to exhibit sizeable deficits (another imbalance to be added to the list). On the export side there had been excessive optimism about oil export potential. In a very few years oil output was expected to reach 1.5 billion barrels annually. Now it is thought that oil production will probably stagnate over the next several years, until offshore fields are tapped and technological-

73. *Japan Times*, February 8, 1981, p. 5.

ly more efficient recovery methods are applied to existing onshore fields. The crude oil target for 1980 (774 million barrels) was the same as for 1978 and 1979, and it was expected to decline by almost 40 million barrels in 1981, and by 70 million barrels in 1982. Coal production is also sluggish; it has been maintained with great expenditure of manpower at about 600 million tons a year but is likely to decline in 1981. To combat the payments deficit, imports of plant and equipment are being sharply curtailed, a measure which fits into the overall retrenchment of basic capital construction. The cutbacks have affected Japanese suppliers the most: the postponed Baoshan steel project alone involves contracts worth more than \$1 billion. The Chinese government has promised to compensate foreign firms for the losses incurred through these delays and cancellations.

In the latter part of 1980 the government moved discreetly to deter imports and promote exports by introducing a separate foreign exchange rate for trade purposes. Beginning January 1, 1981, the exchange rate for foreign trade purposes was to be \$1 = 2.8 yuan, whereas the official rate for other transactions (including tourism) is \$1 = 1.5 yuan. The trading rate will apply to all of China's foreign trade corporations and other (mainly provincial) bodies doing business abroad. The two-tier exchange rate amounts to a selective devaluation of the yuan; it is another example of the sort of things that have been practiced by the Soviets for years and tolerated by the industrialized countries of the West. One problem is that the new rate will raise the cost of China's grain and cotton imports. If this increase — or some of it — is passed on to the domestic consumers of food and clothing, it will strengthen inflationary pressures directly. If — as appears more likely — it is not passed on, the government's grain and cotton subsidies will have to be raised, and the fight against the budgetary deficit will become that much more onerous. In this case inflationary pressures would be strengthened indirectly.

7. Not much progress has been made so far in getting the Party out of economics, or at least out of economic minutiae. The respective areas of primary responsibility of the government and the Party remain blurred, with the Party butting-in at every turn and level of decisions. Recent articles insist that, whatever may have happened in the past, the division of labor between government and Party will be implemented from now on. However, the proposed implementation raises legitimate doubts about the outcome. It is promised that "with the introduction of division of work between the Party and the government, Party leadership will be *strengthened*."⁷⁴

74. *Beijing Review*, January 12, 1981, pp. 5-6.

Management of the Firm

1. Pricing. As noted before, in the absence of fairly competitive, flexible, and largely self-regulating prices (not limited to baskets, toys, bamboo whistles, and home-made soup) the so-called "Sichuan model" of profit orientation, profit retention, and self-accountability by state sector enterprises cannot indicate to either managers or planners the efficiency of enterprise operations, nor can it put an end to the divergence between the interests of the firm and the interest of the community as perceived by the planners. So far there has been no detectible drift toward free prices, with the exception of prices on rural fairs, which merely amounts to a restoration (and even these prices, as we have seen, are monitored and being interfered with by government authorities), prices of some consumer services in urban areas (food served in privately run restaurants, clothing and shoe repairs, tailoring, haircuts), and prices of home-made handicraft products. In a few cases the prices of above-quota traded commodities have been allowed to float between centrally approved limits (e.g., steel products sold directly by a few experimental mills). While such limited price liberalization no doubt adds to the material welfare of the consumers of dumplings and basketry, it can hardly be described as of historic significance.

There is talk in highly placed circles about moving one day toward a Hungarian-type three-tiered price system. Under this arrangement the prices of key inputs and outputs would be regulated by the planners in accordance with improved production cost computations (the planners would also determine what is key and what is not). Some prices of "less important" products would be designated as "limit" prices, that is, they would be allowed to fluctuate within a certain range in response to changes in cost and demand conditions. The remaining prices would be free to move without any restrictions whatsoever. The reform would be accompanied by a reduction in the number of goods allocated outside the commercial network through the material-technical supply empire and introduction of at least some contractual commercial relations between the Supply Bureau and individual enterprises. It is difficult to say at this point how seriously such steps are being considered. If implemented, they would represent a shift in the direction of economic, as distinct from administrative, decentralization; i.e., they would amount to changing the system quite a bit, as they did in Hungary. However, it is unlikely that a dismantling of the material-technical supply network and of its parent planning apparatus is seriously contemplated at this time. The Hungarian reforms have

shown that partial remedies do not get rid of the misallocations, rigidities, and delays that beset the central administrative planning model. In fact, the very patchiness of the remedies invites invidious comparisons by those opposed to any and all reform and produces an almost certain recentralization and a return to the old administrative monster. When strategic materials are bureaucratically controlled and priced, the sphere of market operations is restricted and distorted, and the market principle is compromised.

2. Enterprise Autonomy. Experimentation with marketization (within an overall environment of state monopoly and state-dominated prices) continues and is being enlarged. It includes, as we have noted earlier, experiments with broader enterprise decision-making rights, profit retention by enterprises, lateral enterprise purchase and sale contracts, and bank financing. One gets the impression, however, that, so far at least, the major result of economic readjustment (for that is what these experiments amount to) has been the discarding of Maoist accretions and a return to the underlying administrative command structure adapted from the Soviets in the early 1950s and Sinicized by Deng's men in the early 1960s. "Probably one of the most important aspects of the transition from Maoist to Dengist economic planning, with the latter typified by Zhao [Zhiyang's] Sichuan experiment, is the exclusion from the planning process of concepts rooted in war, encirclement, and sheer survival."⁷⁵ The more important question is still where to go on from here, since the Soviet model, however much modified to fit Chinese conditions, will not do the job of modernization.

Pilot enterprises are nowadays allowed to market directly part of their state-set quota output and all above-quota output. The exact proportions are subject to negotiation with superior planning authorities. For example, the Chongqing, Taiyuan, and Anshan iron and steel complexes have been permitted to market directly (i.e., not via the material supplies network) respectively 19, 15, and 5 percent of their 1980 output or a total of 400,000 tons of steel products. In fact, no two cases of direct marketing are the same. Pilot enterprises may also start new production lines not specifically endorsed by their supervisory ministries. They can merge with other firms or set up joint ventures. However, and this is important, they can do all this when and only when they have fulfilled the state plans for output, delivery, sales, productivity, innovation, and so on. The plan comes

75. David Bonavia, "In Economy, Learn from Sichuan," *Far Eastern Economic Review (FEER)*, November 21, 1980, p. 31.

first; relative freedom of enterprise action comes second. The Soviet reforms of the late 1950s and early 1960s were similar. In Russia the plan took most of the available inputs. The managers' complaint (like the complaint of Soviet consumers) was that they had the money, but that there was nothing they could buy with it once the state planners were through with their output commands and input allocations. Depending on the tautness of the state plan, this could prove to be true of China too.

Direct marketing (lateral contracting by some firms) is said to have declogged some of the supply bottlenecks and improved the quality of products (i.e., producers produce for consumers and not for planners; they produce goods that are saleable instead of just volume). On the other hand, in addition to the problems mentioned earlier in the paper, other difficulties have cropped up. One is simply an extension of the problem already encountered in compulsory delivery versus free sale of farm produce. Better quality steel and other products are sold directly at semi-free, floating, "limit" prices, which as a rule are higher (i.e., yield more profit) than state-fixed prices for compulsory quota deliveries. The result is that better quality steel will be sold directly, while poorer quality steel will go to the government. This simple and natural propensity of human nature to maximize its satisfactions is made all the easier by the reported prevalence of "unscientific" (meaning "soft" or easily fulfillable) output quotas introduced during the years of cultural muscle flexing. It is encouraged by the policy of allowing the experimental enterprises to keep a portion of their profits and to spend that portion as enterprise managements see fit — outside the plan. Profit retention rates are subject to negotiation. There are at present many combinations of profit retention, depreciation allowance retention, and profit taxation. Overall, three basic experimental schemes exist: (1) retention by the enterprise of 5 percent of planned profit and 20 percent of above-planned profit (this is bound to lead enterprises to seek a soft planned profit plan); (2) retention by the enterprise of 20-30 percent of total (planned and above plan) profit; (3) full self-management, under which the enterprise is responsible for its own profits and losses, is taxed on its profits, and pays a capital charge on its fixed assets. In general, the movement of the experiment is supposed to be from (1) to (3).

The search for profit is not restricted to producing enterprises. For example, the Institute of Physics of the Chinese Academy of Sciences had by the end of 1980 contracted some 20 new technologies to 20 factories on terms that included the transfer to the Institute of

enterprise profits derived from the technology on a sliding scale (20 percent in the first year, 10 percent in the second, 5 percent in the third, and so on, or alternatively royalty payments based on sales and also on a sliding scale.)⁷⁶

Increased self-management has been accompanied by expansion of the role of banks in enterprise capital financing. Medium-term lending in Sichuan Province rose 21 per cent in 1980. In the country as a whole, large and medium power and textile industry projects entirely financed by bank loans amounted to 2.8 billion yuan (end 1980). This should be kept in perspective. In 1980 planned state expenditures on capital construction were roughly 30 billion yuan, plus 5 billion yuan for enterprise renovation.

3. Worker Participation. As noted, worker participation in management is on the agenda. It is seen as a component part of the incentive system. In fact, it is the main nonmaterial incentive of the post-Mao era. Participation is to be structured in two ways: (1) through the resuscitated trade unions, and (2) through direct elections (by "secret ballot") of workshop supervisors and even plant directors.

The state-controlled trade unions are apparently not doing the job expected of them because the job cannot be done. If they are truly to speak up for the workers' interests they will have to be liberated from their feudal status vis-à-vis the state. Moreover, trade union leaders know on which side their bread is buttered: they are in awe of senior officials of all stripes, including enterprise managers. Like other bureaucrats they worry about possible future retribution and present legal or extra-legal action against them if they argue the workers' case too eloquently.⁷⁷

"Workers' self-management" also appears to be faltering. Here the problem is twofold: (a) the workers doubt that workers' congresses and elections of factory officials will in reality change anything very much, and (b) they are not convinced that the election procedures are above-board. In any event, "the strongest motivation for working harder and more efficiently now. . . is money and not the right of workers to elect their own officials."⁷⁸ More money without more consumer goods is not going to do the trick either.

* * * *

76. *CBR*, November/December 1980, p. 3.

77. *FEER*, October 31, 1980, p. 9.

78. Harry Bernstein, "Major Shifts in China Put Labor in Control," *Los Angeles Times*, December 26, 1980, p. 24.

The tentative conclusions reached in the original paper remain. China's economic problems are not all that different from those experienced by other similarly placed developing countries. There, as in China, systemic defects compound the objective difficulties inherent in the developmental process. It is to the credit of the post-Mao leaders that they do not shirk from admitting the existence of institutional obstacles to development and modernization and that they are taking steps to reduce them. The experimental phase is now at a crucial point. The reform movement could easily fizzle out, as it did in the Soviet Union, in which case China will be left with a cumbersome Soviet-type system, a very imperfect vehicle in which to travel along the long and tortuous road to modernization.

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