

# On the Transitional Economies in East Asia

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## **Abstract**

This paper consists of three parts: (1) Introduction (S. Ichimura); (2) The Characteristics of Transition in the Chinese Economy (S. Ito); (3) Contemporary Status and Prospects of Economic Transition in Far Eastern Russia (K. Miyamoto). The introduction points out political factors and highlights the dominant influence of overseas Chinese merchants and foreign direct investment. The second part examines the transition of the Chinese economy focusing on changes in industrial structure, labor relations, and the ownership of enterprises. It also points out some difficulties confronted by the transition in China. The third part deals with the transition in the regions of Far Eastern Russia focusing on changes in the industrial and regional composition economic activities as well as changes in commodity composition of the region's trade with Asian countries in the 1990's.

# On the Transitional Economies in East Asia

Shoichi Ito, Katsuhiko Miyamoto and Shinichi Ichimura<sup>1</sup>

## Introduction

Shinichi Ichimura (International Center for the Study of East Asian Development)

### 1. A Symposium On the Transitional Economies in East Asia

In East Asia there are six transitional economies; namely, China, Vietnam, Lao, Kampuchea, Myanmar, and Russia. The available information is very limited, however, for Lao, Kampuchea and Myanmar. Nevertheless, some efforts have been made to investigate their problems. As for Vietnam, China and Far Eastern Part of Russia, there is enough information available so that it is worth investigating and comparing the findings with similar experiences in other countries, particularly in Eastern Europe. There is a great deal of interest in Japan as well as other Asian countries in the studies of transitional economies. Especially these transitional economies are facing the double or triple problems of developing the national economies from below and transforming the Socialist economies to the market economies as well as building their nation-states. I believe that it is wrong to discuss the problems of Chinese economy just as the problems of developing economies like other economies that have been in the Free World area ever since the end of World War II.

A symposium on this particular problem in East Asia was held by the International Center for Economic Growth, San Francisco and some Japanese organizations in Osaka on October 29 to 31, 1994. The theme was set as Transition Problems To Market Economies in Asia – Challenges and Prospects of Reform and Transformation. Two reports were published as monographs: *Asian Transitional Economies* edited by Seiji Finch Naya and Joseph L. H. Tan, the Institute of Southeast Asia in Singapore, 1995 and *Ajia ni okeru Shijo Keizai heno Iko Mondai (Transition To Market Economies in Asia)* edited by Shinichi Ichimura and Katsuhiko Miyamoto, Institute of International Relations, Osaka International University, 1996. The latter is the summary version of the former and the main points the discussions at the symposium.

The symposium covered even the economies of Lao, Vietnam, Myanmar, Mongolia and also briefly touched upon Poland and Bulgaria. Some of salient points in the transi-

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<sup>1</sup> This note was written in March, 1999. The authors are respectively Professors of Economics at Kwansai Gakuin University, Osaka Prefecture University, and Director, International Center for the Study of East Asian Development, Kitakyushu, Japan.

tional economies are common to East Asia and Eastern Europe, but there are very significant differences in the approach and the underlying conditions. The symposium did not deal with, however, neither China nor the Far Eastern part of Russia. The following two notes by Shoichi Ito and Katsuhiro Miyamoto report on the current issues in the transitional stage in the Chinese and Russian Far East economies. Since the financial crisis in Asia after June, 1997 caused so much troubles all over the world and triggered the further troubles in the Russian economy, it is very urgent to learn the lessons from our experiences in both East Asia and Eastern Europe as soon and as much as we can.

## 2. Politics and Economics of Transition from the Socialist to Market Economies

After the World War II choice was made between capitalism and socialism worldwide only by political enforcement. The nations that chose the Socialist system did so not by their own choice of an optimal social system as the best for the nations but in most cases under the political pressure of the Soviet Union. In the case of the nations that chose Capitalism the political circumstances were more complicated, because there were more varieties of Capitalism or Private Competitive Enterprise System at the time of ending World War II. The socio-economic system in the Free World was in general the mixed economy. Some European countries might have been more properly called the Welfare State rather than the pure Capitalistic Society. The nations occupied by the Allied Forces had to choose, however, under the pressure of the United States and others the economic system closer to the American economic system.

Many countries in East Asia now were the colonies of the US, UK, the Netherlands, France and Japan. Their economic systems were more or less determined by their suzerain states. After independence, they inherited from the colonial empires their national properties as the new State properties. This heritage and anti-colonial or anti-Imperialistic sentiments of the political leaders in the new independent States made the postwar economic system in East Asia closer to the left in the mixed economy. Many of the leading enterprises in East Asian economies are still the State-Owned Enterprises. Pertamina (State-owned petroleum enterprise in Indonesia) or Singapore Airline are examples of many such state-owned enterprises. There was no sentiment against Socialism in immediately postwar period. Lie Kuan Yeu's Social Action Party in Singapore is a Socialist Party. As time passes by, however, it has become abundantly clear that the SOE's are very inefficient even in those mixed economies. Moreover, many of the Socialist economies have repeated the fatal failures in developing their economies under Socialist Control. The Great Leap Forward Movement in China in the late 1950s gave the first precedent for systemic inadequacy of the Controlled economy in modern times. The fatal blow to the dream of the Socialist system was the collapse of the Soviet Union and its social, political and economic

system. As it becomes evident that the national economies in Free World have definitely prospered with more open-door policies toward foreign trade and capital and with dominant private enterprises running production and distribution, everybody has become convinced the supremacy of Private Competitive Enterprise System to Socialist Control Economy.

Associated with this shift of the choice of economic systems the shift of many social and political paradigms: freedom of speech, freedom of association, emphasis of human rights, free voting right for everyone, the rule of law, equal rights under the law and so on. What is involved, therefore, in the Transition from the Socialist to the Market economies is not just the economic transition but much wider varieties of social reforms. One has to limit the argument, nevertheless, to the important economic problems for the time being.

### 3. The Importance of Overseas Chinese and Foreign Direct Investment

One factor especially important in understanding the transition from Socialist to Market economies in East Asia is the role played by Overseas Chinese. There are about 30 million overseas Chinese in the countries and areas of East and Southeast Asia. Singapore is dominantly Chinese city state with 2.5 million population; 35% of 20 millions Malaysian population are Chinese; 5 to 6% of 200 million Indonesians are Chinese; 10% of 40 millions Thai population are Chinese, 5% of 40 million Filipinos are Chinese; a few million Chinese merchants are still in Vietnam; 6 millions population in Hong Kong are almost exclusively Chinese; 25 millions Taiwanese are almost all Chinese. In business they are all cooperating with each other. They make enormous contributions to the development of all the concerned economies, including the transitory economies. They are outstanding merchants and nowadays excellent businessmen in all fields. They are almost like the Jewish businessmen in the West.

Another feature of East Asian development is the importance played by the foreign trade and FDI from Japan and the US. The typical pattern is the export markets are offered by the US, capital goods are imported from Japan. Both countries as well as European countries and Australia have made direct investment throughout the postwar years. The US and Japan always competed with each other in their economic activities in East Asia and China after the Reform and Open Door Policy of Den Xiaoping in 1979. This fundamental shift in national priority from political struggle to economic development has been the turning point in East Asian countries, as I have argued elsewhere.<sup>2</sup>

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<sup>2</sup> See Shinichi Ichimura, *Political Economy of Japanese and Asian Development*, Springer-Verlag, Tokyo-London-New York, 1998

# I. The Characteristics of Transition in the Chinese Economy

Shoichi Ito (Kwansei Gakuin University)

## I. The first stage of economic reform of China (1979-1984)

### 1-1 . The rural reform was the major problem of reform annual in the first stage

In the second half of the 1970's, China faced the slow-down of the growth rates of industrial and agricultural sectors. Especially the growth rate of agricultural sector dropped significantly. As the result, the average of annual growth rates of national income in the second half of 1970's was as low as 0.7%. Thus, the increase of agricultural production and the activities of people's communes became the major issues in China. At the end of 1978, the Chinese Communist Party decided to change the direction of economic policy and gradually shift from the planned economy to the market economy.

The diligent working of farmers was regarded as indispensable for the increase of agricultural production, especially in the areas along and south of the Yangtze River. For in those areas agriculture was mainly done by manual work. In 1978 various policy measures were taken to give incentives to the farmers for the more diligent and positive works and to raise the price of agricultural products to be purchased by the government. In the summer of 1979 the purchase price of the grain crops by the government was raised by 20%, and the price of grain crops above the assigned amount was raised by 50%. This means that the Chinese government takes the risk of "abundant harvest and the poor income" that farmers used to suffer in the past. As a result, we could observe 6.1% growth rate in the primary industry, mainly, agriculture, of GDP in 1979. However, we had to wait until the first half of 1980's to see the overall increase in GDP of the primary industry. About the same time, the rural people's communes were dissolved, and each farming household became responsible for the production of grain crops of a particular land assigned to it. This change meant that each farming household might increase its own income through the increase in the production of any agricultural products. These measures undoubtedly gave the tremendous incentives to the farmers. In fact, Table-1 shows that GDP of the primary industry grew very rapidly from 1982 through 1984. Thus, we may say that the first stage of economic reform of China was very successful.

### 1-2 The rural reform and the regional economic development

The rural reform at the first stage of economic reform gave the significant impacts on the regional development in China. The high growth rate of the primary industry in the first half of 1980's implies that the provinces whose shares in the primary industry are higher are likely to have the higher GDP growth rates. The primary industry's share in Chinese GDP was 28.1 % in 1978. The average annual growth rate of the primary industry in GDP

over the period from 1978 to 1984 was 7.3 %. It explained 36 % of GDP growth of China in that period, while those of the secondary and tertiary industries explained 38.4 % and 25.6 % of GDP growth respectively. The GDP of China increased by 70 % during this period, and its average annual growth rate was 9.2 %.

**Table-1 The GDP Growth Rates Under Economic Reform & Open Policy (Unit %)**

	GDP Total	Primary Industry	Secondary Industry			Tertiary Industry		
			Total	Manu- facturing Industry	Construc- tion Industry	Total	Transporta- tion, Post & Telecomm.	Wholesale Retail & Catering
1978	11.7	4.1	15	16.4	-0.6	13.8	8.9	23.1
1979	7.6	6.1	8.2	8.7	2	7.8	7.7	8.8
1980	7.9	-1.5	13.6	12.7	26.7	6	5.7	-1.3
1981	4.5	7	1.9	1.7	3.2	6.9	1.9	18.8
1982	8.5	11.5	5.6	5.8	3.4	10.6	11.7	-5.9
1983	10.2	8.3	10.4	9.7	17.1	12.6	10	12.4
1984	14.5	12.9	14.5	14.9	10.9	17.1	15	13.9
1985	12.9	1.8	18.6	18.2	22.2	16.6	13.5	22.7
1986	8.5	3.3	10.2	9.6	15.9	11.1	12.8	6.7
1987	11.1	4.7	13.7	13.2	17.9	12.9	10	10.6
1988	11.3	2.5	14.5	15.3	8	13.6	13.3	12.5
1989	4.1	3.1	3.8	5.1	-8.4	6.7	4.7	-9.1
1990	3.8	7.3	3.2	3.4	1.2	2.1	8.6	-6.7
1991	8	2.4	13.3	13.8	9.6	5.5	8.5	3.5
1992	13.2	4.1	20.9	20.5	23.8	9.6	9.1	7.5
1993	13.5	4.7	19.9	20.1	18	10.7	12.4	6.6
1994	12.6	4	18.4	18.9	13.7	9.6	9.5	8.4
1995	10.5	5	14.1	14.3	12.4	8	9.5	8.7
1996	9.6	5.1	12.1	12.5	8.5	7.8	12	5.4
1997	8.8	3.5	10.8	11.1	7.9	8.2	10.7	8.5

Source: China Statistical Yearbook 1998, p.57.

As for the growth rates of the agriculture sector in different regions, Table-2 shows that the provinces with the primary industry's share above the national average 28.1 % were twenty among twenty-nine provinces, autonomous regions, and municipalities. Only four provinces among these twenty provinces: namely, Hebei, Jiangxi, Hunan, and Shaanxi, lost their shares of the primary industry during the period from 1979 to 1984. On the other hand, only three provinces among the ten provinces with the primary industry's shares below the national average: namely, Beijing, Shanxi, and Jiangsu increased their shares in the same period.

Among those twenty provinces with the primary industry share above the national average, fourteen of them performed better in the growth rate of GDP than the Chinese econ-

omy as a whole. Only two of them: Hebei and Jiangxi lost their shares in the GDP of China.

**Table 2 Rural Reform and GDP Growth Rates by Region (1978-1984) (Unit %)**

	Primary Ind's Share in GDP 1978	Primary Ind's GDP Growth Rate 78-84	GDP Grow.Rate78-84	GDP Share in China 78	GDP Share in China 84
Total	28.1	52.6	70	100	100
Beijing	5.2	177.2	75.5	3	3.02
Tianjin	6.1	40.3	70.8	2.28	2.06
Hebei	28.5	64.1	57.9	5.05	4.63
Shanxi	20.7	73.9	80.8	2.43	2.75
Inner Mongolia	32.7	64.5	86.7	1.6	1.79
Liaoning	14.2	56.3	57.1	6.32	6.11
Jilin	29.3	79	75.2	2.26	2.43
Heilongjiang	23.5	46.6	51.3	4.82	4.44
Shanghai	4	56.6	58.5	7.53	5.45
Jiangsu	27.6	74.1	85.8	6.88	7.24
Zhejiang	38.1	47.5	115.5	3.41	4.49
Anhui	47.2	59	89.3	3.14	3.71
Fujian	36.1	59.7	97.4	1.83	2.19
Jiangxi	41.6	57.7	71.5	2.4	2.36
Shandong	33.3	92.2	88.2	6.22	8.11
Henan	39.6	71.3	92.2	4.5	5.16
Hubei	40.5	54.4	87.9	4.17	4.58
Hunan	40.7	41.2	58.2	4.06	4.01
Guangdong	29.9	64.9	84.8	5.1	6.16
Guangxi	40.7	40.1	53.9	2.09	2.1
Hainan	53.2	83	81.3	0.45	0.52
Sichuan	42.9	35.5	71.6	6.76	6.94
Guizhou	41.7	72.7	92.9	1.29	1.51
Yunnan	42.7	49.2	72.9	1.91	1.95
Tibet	50.7	71.9	89.3	0.18	0.19
Shaanxi	30.5	41	58.8	2.24	2.08
Gansu	20.4	60.8	40.2	1.79	1.44
Qinghai	23.6	35.6	48.3	0.43	0.37
Ningxia	23.5	83.1	67.4	0.36	0.35
Xinjiang	35.8	90.2	85.3	1.08	1.25

Source: The calculation by the author, using the data of *China's Regional Economy under 17 Years Economic Reform & Open Policy* (in Chinese)

This indicates that broadly speaking, the provinces with high share in the primary industry performed also better in term of overall economic growth rates in 1978 to 1984. Thus the government's policies emphasizing the agriculture sector brought about the different impacts on the various regions in China.

### 1-3 The fiscal reform in the first half of the 1980's

The fiscal system at the first stage of the "fiscal reform" of China in 1980 to 1984 is called "Dividing the Fiscal Revenue and Expenditure into Central and Local Govern-



ments.” It divides the responsibility of government administration into central and local governments. It implies:

- 1) We should clearly distinguish the tax revenue and expenditure of the provincial governments from those of the central government.
- 2) We determine the basic figures of the ratios of tax revenue and expenditures of local governments and those of the central government. For example, if the tax revenue of a local government exceeds its expenditure, its local government gives the predetermined share of its fiscal surplus to the central government and keep the remainder for itself. On the other hand, if the tax revenue of a local government is below its expenditure, its local government receives the predetermined share of industrial and commercial tax revenue of the central government. The local governments’ budget balance is adjusted in this manner. If, however, this adjustment is not enough to cover the budget deficit, the central government provides a certain amount of subsidy to such local governments. This fiscal system was applied to 15 provinces. In the special cases, the different fiscal systems were applied.<sup>3</sup>

In the case of Jiangsu province, the average ratio of its total revenue to total expenditure in the past several years was taken to allocate its fiscal revenue between the province itself and the central government. In the case of some minor regions, the central government provides them with certain amounts of subsidy that may annually increase at a certain rate. The central government may also provide some regions with the special subsidies in case of the special situations. In the case of Shanghai, Beijing, and Tianjin, where the local governments have the ample amount of budget surplus, the central government annually determines the budget indicators and the allocation ratios between the central government and those local governments. The change in tax revenue is divided into two parts, and each part is given to the central government and the local governments respectively according to the ratio mentioned above. The central government allows, however, some reservations to those local governments for their flexible expenditures.

To Guangdong and Fujian Provinces, however, the central government adopted the special fiscal policy as Open Door Policy, because four Economic Special Zones were located. Under this fiscal system, the central government gave a certain fixed amount of subsidy to Fujian Province and received a certain fixed amount of tax revenue from Guangdong Province. This implies that those two provinces may freely spend whatever they gained from the tax revenue or by reducing the fiscal expenditures for their own objectives. The above mentioned changes in the fiscal relation between the central government and

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<sup>3</sup> Li Qiang, Wu You, and Zhao Chun-Ping (1994) pp.100-101.

local governments naturally gave impacts on the regional pattern of economic development. Table 3 shows the budget balances of provincial governments in 1980 and 1985.

**Table -3 Provincial fiscal Budget and Economic Development by Region (Unit 100 millions Yuan, %)**

	Provincial Fiscal Rev. 1980	Provincial Fiscal Rev. 1985	Provincial Fiscal Exp. 1980	Provincial Fiscal Exp. 1985	Ratio of Fiscal Exp. to Rev. 1980	Ratio of Fiscal Exp. to Rev. 1985	% in China's Fiscal Revenue 1980	% in China's Fiscal Revenue 1985
Total	872.26	1182.42	564.32	1054.43	0.647	0.892	100	100
Beijing	51.29	52.44	14.87	32.99	0.29	0.629	2.635	3.129
Tianjin	40.94	48.21	14.67	26.97	0.358	0.559	2.6	2.558
Hebei	35.02	45.15	28.36	41.66	0.81	0.923	5.026	3.951
Shanxi	21	25	19.6	35.5	0.933	1.42	3.473	3.367
Inner Mongolia	4.13	13.39	18.37	36.22	0.445	2.705	3.255	3.435
Liaoning	86.9	85.2	34.1	56.9	0.392	0.668	6.043	5.396
Jilin	14.39	21.67	17.32	34.5	1.204	1.592	3.069	3.272
Heilongjiang	17.06	37.42	25.76	44.63	1.51	1.193	4.565	4.233
Shanghai	174.73	184.23	19.18	46.07	0.11	0.25	3.399	4.369
Jiangsu	63.36	89	28.95	50.53	0.457	0.568	5.13	4.792
Zhejiang	31.13	58.25	17.34	37.4	0.557	0.642	3.073	3.547
Anhui	20.28	30.16	16.66	33.88	0.821	1.123	2.952	3.213
Fujian	15.33	25.08	15.05	30.64	0.982	1.222	2.667	2.906
Jiangxi	12.47	21.18	15.99	29.73	1.282	1.404	2.833	2.82
Shandong	48.11	67.53	30.07	51.3	0.625	0.76	5.329	4.865
Henan	31.86	48.93	26.74	49.51	0.839	1.012	4.738	4.695
Hubei	34.01	50.26	26.53	43.6	0.78	0.868	4.701	4.135
Hunan	29.86	39.19	23.71	40.09	0.794	1.023	4.202	3.802
Guangdong	36.1	65.48	24.93	60.84	0.691	0.929	4.418	5.77
Guangxi	12.29	20.18	17.44	29.75	1.419	1.474	3.09	2.821
Hainan	1.19	3.16	2.1	5.9	1.765	1.867	0.372	0.56
Sichuan	34.62	58.76	33.51	64.16	0.968	0.192	5.938	6.085
Guizhou	6.69	15.17	12.66	24.55	1.892	1.618	2.243	2.328
Yunnan	11.64	27.43	17.32	36.7	1.488	1.338	3.069	3.451
Tibet	-0.6	-0.61	4.66	10.29	-7.767	-16.869	0.826	0.976
Shaanxi	15.81	20.3	18.28	27.5	1.156	1.355	3.239	2.608
Gansu	14.93	16.48	12.3	24.08	0.824	1.461	2.18	2.284
Qinghai	1.65	2.4	5.88	10.09	3.564	4.204	1.042	0.957
Ningxia	2.04	2.91	5.75	9.85	2.819	3.385	1.019	0.934
Xinjiang	4.03	8.47	16.22	28.6	4.025	3.377	2.874	2.712

Source: The calculation by the author, using the data of "China's Regional Economy under 17 Years Economic Reform & Open Policy" (in Chinese)

The specific feature of the ratio between fiscal expenditure and revenue was that its ratio increased in 25 out of 30 provinces, autonomous regions, and municipalities from 1980 to 1985. Thus, fiscal balances shifted in favor of provincial governments and against the central government in the first half of 1980's. Furthermore, some provincial governments made their own extra-budgetary expenditures in addition to the budget expenditures. The size of such extra-budget expenditures was sometimes as much as the ordinary fiscal

budget expenditures.<sup>4</sup> It may be expected that the economic development of each province depended very much on the fiscal budget and extra-budgetary expenditures of the provincial government in the first half of the 1980's, when the planned economy was considered still more dominant than the market economy in China.

#### 1-4 The Regional Pattern of Investment in the First Half of the 1980's

In the early 80's, the role of planned economy was still very important. In particular the investment activities are of special importance in each region. Table-4 shows the amount of investment in each province and its rank in China in 1980 and 1985.

**Table -4 Total Investment by Region and Its Ranking (Unit 100 millions Yuans)**

	1980		1985		1990		1995	
	Total Invest.	Ranking	Total Invest.	Ranking	Total Invest.	Ranking	Total Invest.	Ranking
Beijing	43.69	11	191.43	5	307.29	9	1256.28	7
Tianjin	35.66	15	88.65	15	134.37	19	524.77	18
Hebei	63.84	6	156.9	9	334.66	7	1226.07	9
Shanxi							412.42	23
Inner Mongolia	18.88	24	61.6	20	124.68	22	372.98	24
Liaoning	56.82	8	174.24	7	392.74	4	1046.6	10
Jilin	28.96	18	81.15	16	182.67	15	451.02	21
Heilongjiang	48.01	10	136.2	11	272.84	10	724.5	15
Shanghai	66.52	5	189.13	6	321.89	8	1551.2	5
Jiangsu	97.44	2	271.42	1	588.44	2	2529.3	1
Zhejiang	49.29	9	145.5	10	252.44	12	1786.79	4
Anhui	28.17	19	113.28	13	204.7	13	824.61	13
Fujian	27.08	20	64.54	18	151.46	17	996.17	11
Jiangxi	36.34	14	68.83	17	126.99	21	444.93	22
Shandong	95.27	3	253.68	2	638.78	1	2247.58	3
Henan	69.2	4	173.43	8	364.81	5	1244.31	8
Hubei	40.1	12	135.43	12	261.95	11	987.03	12
Hunan	40.02	13	92.19	14	184.12	14	800.5	14
Guangdong	63.63	7	214.97	3	511.35	3	2381.31	2
Guangxi	29.08	17	61.8	19	107.4	23	632.47	16
Hainan	3.12	27	22.61	25	60.72	26	219.21	27
Sichuan	106.06	1	199.8	4	359.94	6	1346.15	6
Guizhou	20.95	23	43.62	24	80.42	25	233.94	25
Yunnan	30.3	16	56.76	22	132.16	20	492.77	19
Tibet							32.56	30
Shaanxi					169.37	16	480.48	20
Gansu	24.38	21	47.16	23	104.91	24	222.57	26
Qinghai	8.89	25	21.4	26	28.6	28	77.67	29
Ningxia	8.07	26	19.12	27	37.22	27	82.45	28
Xinjiang	23.15	22	58.43	21	141.17	18	560.88	17

Source: "China's Regional Economy under 17 Years Economic Reform & Open Policy," p.176

<sup>4</sup> *China's Regional Economies under Seventeen Years of Economic Reform and Open Policy*, (in Chinese), 1996 contains the fiscal data of additional expenditure and revenue of some provinces but does not contain the data of all the provinces. Thus, the fiscal extra-budgetary revenues and expenditures of all the provinces in China are not clear.

Note: Total investment indicates total investment of domestic total expenditure

Listing top ten provinces in the amount of investment shows that seven of them are located in the coastal region in 1980. All the other eight provinces except Sichuan and Henan provinces with population of 101.88 millions and 78.47 millions respectively are located in the coastal region in 1985. This indicates that the Economic Reform and Open Policy is definitely favorable for the coastal regions in the early 80's.

According to Table-4, from 1980 to 1985 the rank in the amount of investment rose for ten provinces; such as Beijing, Inner Mongolia, Liaoning, Jilin, Jiangsu, Anhui, Fujian, Shandong, Guangdong, and Xinjiang. Among those ten provinces, only Liaoning lost its share in GDP at the first stage of Reform from 1978 to 1984. Furthermore, the shares in the total of the provincial fiscal expenditures in China declined in four among ten provinces: Liaoning, Jiangsu, Shandong, and Xinjiang. In Jiangsu province, its extra-budget expenditure exceeded the budget expenditure in 1985. In Shandong province, its extra-budget expenditure in 1985 is not published. It seems clear that there are positive correlation's in each province among GDP growth rate, the sum of fiscal budget and extra-budget expenditure, and the amount of total investment.

Thus, we may conclude that in the first stage of the Chinese Economic Reform, two important factors caused the difference in growth among the various provinces; namely, the development of primary industry, mainly, agriculture and the amount of total investment. The latter was greatly influenced by the sum of provincial budget and extra-budget expenditures.

## 2 The Second Stage of Economic Reform: 1984-1991

### 2-1 The Urban Reform as the major part of the second stage of economic reform

Emphasis of the economic reform shifted from the rural areas to the urban areas in 1984, and the second stage of economic reform began. In this stage the conservative way of thinking: "the planned economy as the main part and the market economy as the supporting part" faded away. The Chinese government decided to reduce the direct control by administrative order and to expand the indirect control by macro economic policies through the markets.

In the 7th Five Years Plan (1986-1990), the Chinese government emphasized the reform in three areas. The first area was the enterprises, especially large and medium size state-owned enterprises (SOE). The reform in this area meant to make the SOE's more independent as economic units by developing the top managers' skills and sense of responsibility for the profit and loss under their management. The second area was the market. The reform in this area meant to develop the socialistic commodity markets and establish a comprehensive system of the markets in China. The third area was the government's con-

trol over the enterprises and the national economy. The reform in this area was the shift of the primary way of controlling SOE from direct control to indirect control. The objectives were to establish a new socialistic macro economic management system, to devise the various policy measures and the necessary legal system step by step, and thereby to control the economic activities indirectly with the various administrative means.

In the spring of 1984, the shift of emphasis in economic reform caused the expansion of investment and the increase in wages, which expanded the excess demand for production goods and consumption goods. As the result, inflation, the increase in imports and the trade balance deficit followed in the second half of 1984 to the first half of 1985. Then the government began to tighten the money supply and the fiscal expenditure in the second quarter of 1985. These policies continued until the end of 1986. Only in early 1987 the tight monetary and fiscal policies were relaxed.

In 1987, the expansion of the markets co-existed with the old planned economy, which made the Chinese economy the dual system. The dual system caused the various serious problems such as the dual prices of the identical commodities. Under these conditions, inflation took place, and at the same time the prices of public services were raised in August 1988. Inflation accelerated. In the fall of 1988, the government took the overall tight monetary and fiscal policies and reduced the public investment. As the result GDP growth rate dropped to 4.1% in 1989 and 3.8% in 1990. It was under these situations that Tian-An-Men Incident broke out on June 4, 1989.

Thanks to the tight monetary and fiscal policies, however, the inflation rate above 10% in both 1988 and 1989 calmed down to 2.1% in 1990 and 2.9% in 1991. In addition, the GDP growth rate increased up to 9.2% in 1991, far above the normal growth rate of 7 to 8% in China.

## 2-2 The non-agricultural sectors as the major contributors to growth

The nominal GDP in term of Chinese Yuan tripled in the second stage of the economic reform in 1984 to 1991. The increase in the nominal GDP in this period was 1,444.7 billion Yuan, and the increases in the primary, the secondary, and the tertiary industries were 299.3, 599.7, and 545.7 billion Yuan, respectively. The shares of the primary, the secondary, and the tertiary industries in the increase in nominal GDP were 20.7%, 41.5%, and 37.8%, respectively. The share of the primary industry in the increase in GDP in the period between 1978 and 1984 was 36%. Those of the secondary and the tertiary industries were 38.4% and 25.6%, respectively. Thus, the primary industry which was once the main contributor to development of China in the first stage was no longer the main player of growth. Instead, the secondary and the tertiary industries increased their shares in GDP increase in the second half of the 1980's.

The development of the secondary industry consisting of the manufacturing and the construction industries may be seen as a key sector for growth, as the increment of the industry in GDP as much as 529.8 billion Yuan demonstrates. The gross output of the industry was 761.7 billion Yuan in 1984 and 2,824.8 billion Yuan in 1991. The increase was indeed 2,063.1 billion Yuan. This increase consisted of several components; namely, SOE 969.2 billion Yuan (47%), collectively owned enterprises (COE) 782.2 billion Yuan (37.9%), enterprises owned by individuals 159.4 billion Yuan (7.7%), and the other types of enterprises including foreign enterprises, 152.2 billion Yuan (7.4%). Since the share of the SOE in the gross output of the industry in 1984 was 69.1%, it might be said that the enterprises other than the SOE made more important contributions to the increase of industrial development from 1984 to 1991. The COE includes the so-called Township and Village Enterprises (TVE), and the rural enterprises owned by the individuals are, however, included in the enterprises owned by individuals. The share of TVE in the gross output of the COE of the manufacturing industry was 63.8% in 1991. The share of the rural enterprises owned by individuals in the gross output of the enterprises owned by individuals was 92%. These evidences show that the TVE, which had not been important under the planned economy, made the important contribution to the development of the manufacturing industry in China from 1984 to 1991.

The development of TVE may be indicated by the change in their gross output from 1984 to 1991. Their gross output was 171 billion Yuan in 1984 and became 1,161 billion Yuan in 1991, and its average annual growth rate in that period was 31.5%. Especially, the gross output of their manufacturing industry increased from 124.5 billion Yuan in 1984 to 870.9 billion Yuan in 1991 at the average annual growth rate of 32%. The share of the manufacturing industry in the increase in the gross output of TVE was about three fourths. Thus, the development of TVE was mainly in the area of the manufacturing industry.

The GDP of the tertiary industry<sup>5</sup> was 177 billion Yuan in 1984 and became 722.7 billion Yuan in 1991. The increase was 545.7 billion Yuan, of which the increase by the

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<sup>5</sup> Unfortunately, the above-stated figures of the other industries of the tertiary industry are not listed in *Statistical Yearbook of China*. We could obtain the alternative figures through the comparison of the 1987 and 1992 Input-Output Tables of China. According to the thirty sector I-O Table of China, the tertiary industry consists of the following eight industries: freight transportation and communications, commerce, restaurants, passenger transport, public utilities and services to household, cultural education health and scientific research institutions, finance and insurance, public administration. The increase in the nominal value added of the tertiary industry from 1987 to 1992 is 582.7 billion Yuan. Top five industries in term of their shares in that increase are commerce (34.7%), public utilities and services to household (13.5%), freight transportation and communications (11.9%), cultural education health and scientific research institutions (11.6%), public administration (11.5%). These evidences show that the commerce made the biggest contribution to the increase in the GDP growth of the tertiary industry.

commerce industry was 167.5 billion Yuan. Thus, the commerce industry occupied about 30.7% of the development of the tertiary industry. Similarly the GDP of the transportation, storage, post & telecommunications increased by 108.3 billion Yuan in that period, occupying 19.8% of the increase in the tertiary industry. The sum of the shares of these two industries in GDP increase from 1984 to 1991 was about 50%.

### 3 The Rapid Economic Development After 1992

#### 3-1 The major factors for the rapid economic development

Mr. Deng Xiaoping visited Hubei province, Guangdong Province, and Shanghai in January and February 1992 and made some important speeches. In these speeches he strongly endorsed the policies for Open Door and Reform. They gave tremendous impacts on the subsequent choice of policies and political decisions in China. The fundamental direction of economic reform in China was firmly confirmed. As the result, the FDI began rapidly to flow in. The two digits rate of growth started and continued until 1995. The GDP growth rate is still as high as 7.8% in 1998. Table-1 shows that the secondary industry consisting of manufacturing and construction industries made the biggest contribution to the GDP growth after 1992 on the production side of GDP. On the demand side, it was investment that showed the largest increase in 1993, and that consumption became relatively more important in the growth of GDP after 1994. The share of investment in GDP was 37.2% in 1992 and became 43.4% in 1993. Investment contributed 62.1% to the GDP growth from 1992 to 1993.

Table-5 China's Investment by Ownership (Unit 100 millions Yuan)

	1990	1991	1992	1993	1994	1995	1996	1997
Total Investment	4449.29	5508.8	7854.98	12457.88	16370.33	20019.33	22913.55	24941.11
Inv. By Ownership								
State-Owned Units	2918.64	3628.11	5273.64	7657.97	9322.49	10898.24	12003.21	13091.72
Collective-Owned U.	529.48	697.8	1359.35	2231.34	2664.7	3289.44	3651.5	3850.87
Urban	163.38	203.83	364.49	600.15	676.13	921.74	849.24	795.23
Rural	366.1	493.98	994.86	1631.19	1988.57	2367.7	2802.26	3055.64
Individuals	1001.17	1182.88	1221.99	1476.23	1970.56	2560.24	3211.17	3429.42
Urban	124.7	140.32	216.47	338.5	451.32	552.39	667.14	738.26
Rural	876.47	1042.56	1005.52	1137.73	1519.24	2007.85	2544.03	2691.16
Joint Owned Eco. U.				56.01	100.48	118.48	126.78	123.12
Share Holding E. U.				231.92	569.27	863.99	1034.57	1387.21
Foreign Funded E. U.				556.03	1280.32	1555.25	1876.26	1955.94
E.U. Funded by Enter.				227.74	430.01	673.63	835.27	937.14
From HK, Mac. & Taiwan								
Others				20.62	32.5	59.99	171.8	165.68
Inv. by Souce of Fund								
State Budgetary App.	387.65	372.95	334.2	463.87	529.57	621.05	625.88	696.74
Domestic loans	870.88	1292.19	2152.02	2925.81	3703.11	4198.73	4573.69	4782.55
Foreign Investment	278.26	316.27	457.14	907.29	1768.95	2295.89	2746.59	2683.89

Fundraising	2329.49	2878.49	4024.63	6218.75	8001.48	10647.87	12414.5	13879.65
Others	583.01	648.79	886.99	1942.14	2543.39	2761.39	2997.9	3216.84

Sources: China's Statistical Yearbook 1994, p.139. China's Statistical Yearbook 1995, p.137. China's Statistical Yearbook 1997, p.149. China's Statistical Yearbook 1998, p.185.

Note: The data for 1996 and 1997 is data after adjustment based on the new coverage.

In order to show some aspects of Economic Reform, this rapid increase of investment may be examined from the viewpoints of ownership and fund sources. Table-5 shows the value of investment by the types of ownership in the 1990's. The figures for the investment by share-holding economic units, foreign-funded economic units, economic units funded by enterprises from Hong Kong, Macao and Taiwan and the others. The last item is not shown before 1992. The SOE show the highest share in total investment in fixed assets: 67.1% in 1992 and 61.5% in 1993. In 1992 to 1993, the investment of the SOE increased by 45.2% in the nominal term and by 14.7% in the real term; the investment of the collective-owned units increased by 64.1% in the nominal term and by 29.7% in the real term; and the investment by individuals increased by 20.8% in the nominal term but decreased by 4.6% in the real term. After 1993, however, the share of the state-owned units in the total investment in fixed assets continuously declined, and the rest of units increased their shares. They are the non-traditional sectors in the planned economy such as the economic entities by individuals, foreign-funded units, economic units funded by enterprises from Hong Kong, Macao and Taiwan, share-holding economic units.

As for the sources of funds for investment, Table-5 shows that in 1992 the share of fund-raising in the total investment in fixed assets was 51.2%; that of domestic loans was 27.4%; and the share of foreign investment consisting of FDI, foreign loans, and others was only 5.8%. It is the domestic loans that rapidly increased from 1990 to 1992. Especially, the investment funded by domestic loans increased by 66.5% in the nominal term and 44.4% in the real term in 1992, when the two digits rate of growth started. In 1992, both the investment by SOE and the domestic loans as their funds very rapidly increased. The share of fund-raising in the investment increase from 1992 to 1993 was 54.5%. In the same period, those shares of the others, domestic loans, foreign investment, and state budgetary appropriation were 22.9%, 16.8%, 9.8%, and 2.8%, respectively. The growth rate of investment by fund-raising was 54.5% in the nominal term and 12.2% in the real term in 1993. Its growth rate by domestic loans was 36% in the nominal term and only 7.4% in the real term. On the other hand, its growth rate by foreign investment was 98.5% in the nominal term and 56.8% in the real term, and its growth rate of the others was 119% in the nominal term and 73% in the real term. Although the contents of the others are not clear, the investment by foreign investment and the others clearly increased most rapidly in 1993. Examination of the sources of funds demonstrates that investment expanded in 1993



rapidly in the sectors that the central government cannot easily control. After 1993, the shares of investment due to state budgetary appropriation and domestic loans continued to decline, whereas those of foreign investment, fund-raising, and the others continued to increase.

Consumption became more important in the increase of GDP after 1994. The shares of household consumption and government consumption in the consumption of 1993 were 77.7% and 22.3%. After 1993, the share of household consumption gradually increased. Thus, the part of consumption that the central government cannot easily control has increased in the same manner as the total investment in fixed assets did. The economic activities by the central government became increasingly uncontrollable under the Economic Reform.

### 3-2 The non-traditional sectors as the major contributors to economic development

The two digits rate of economic growth after 1992 was primarily due to the development of the Secondary Industry, consisting of Manufacturing and Construction Industries, especially the former. Examination of the ownership of enterprises that contributed to the expansion of the manufacturing industry reveals again the impact of reform. Table-6 shows that the share of SOE in the value of the total gross industrial output kept on declining. I should be remembered, however, that some of SOE became share-holding economic entities, so that they are classified not as state-owned units but as share-holding economic entities. The share of COE, especially that of rural collectively-owned industry, clearly increased. In addition, those of urban and rural individuals-owned industry and the others also increased. The others consisted of share-holding enterprises, the foreign funded enterprises, enterprises owned by Hong Kong, Macao, and Taiwan enterprises, and others.

**Table 6 Shares in Gross Industrial Output value (Unit %)**

	1992	1993	1994	1995	1995*	1996	1997
Gross Ind Output V	100	100	100	100	100	100	100
State-Owned Enterprise	51.52	46.95	37.34	33.97	32.61	28.48	25.52
Collective-Owned Ent	35.07	34.02	37.72	36.59	35.55	39.39	38.11
Township Enterprise	10.21	11.1	11.55	12.98		11.78	
Village Enterprises	10.5	10.67	13.76	12.89		15.96	15.77
Cooperative Enterprise	2.51	2.73	3.72	2.32		3.4	4.1
Others	11.85	9.51	8.69	8.39		8.25	
Individual-Owned Ent.	5.8	7.98	10.09	12.86	14.55	15.48	17.92
Enterp. of Other Types	7.77	10.69	12.85	16.57	17.29	16.65	18.45

Sources: China's Statistical Yearbook 1997, p.411, p.413. China's Statistical Yearbook 1998, p.431

Note: The gross industrial output value in 1995\*, 1996, and 1997 was calculated in accordance with new stipulations.

Since the composition of the others in the gross industrial output is not clear in Table 6, the detailed information of the gross industrial output by ownership can be derived from the data on the production of the industrial enterprises: including SOE, COE, share-holding

enterprises, foreign-funded enterprises, and the enterprises funded by Hong Kong, Macao & Taiwan enterprises. The share of the share-holding enterprises in the total gross industrial output of these five types of enterprises was 5.6% in 1994 and 5.4% in 1996, showing little change. The share of foreign-funded enterprises was 7.2% in 1994 and 11.6% in 1996. The share of enterprises funded by Hong Kong, Macao and Taiwan enterprises was 6.9% in 1994 and 9.5% in 1996. These two groups show the significant increase rather than the share-holding enterprises.

Thus, it is clear that the manufacturing industry made the greatest contribution to the rapid economic growth of China after 1992 is not the SOE but the village enterprises, the enterprises funded by individuals, foreign-funded enterprises and the enterprises funded by Hong Kong, Macao, and Taiwan enterprises. They were under the self-governing management with their own responsibility. It may be concluded that in the transition to the market economy, the sectors which can flexibly respond to the changes in the market conditions on both demand and supply sides could make the major contributions to the rapid growth of Chinese economy in the 1990's.

### 3-3 The roles of FDI

The total amount of foreign capital consists of foreign loans, direct foreign investment, and other foreign investments. The share of other foreign investments has been very small and negligible. The foreign loans had been the most important in the amount of foreign capital actually in use until 1991. Since 1992, however, the FDI has exceeded the foreign loans. For example, the amount of FDI was 3.3 times as much as that of foreign loans in 1996. Thus, the major capital flow from abroad to China has recently been the FDI. The FDI was not just the source of capital but made other important contributions to the economic development of China, offering the job opportunities, the technological transfer, export marketing, fiscal revenue, and so on.

First, the job opportunities are examined. According to the *China Labor Statistical Yearbook: 1993 to 1997*, the number of employees by the foreign-funded enterprises was 2,213 thousands in 1992, 2,882 thousands in 1993, 3,997 thousands in 1994, 5,133 thousands in 1995, and 5,400 thousands in 1996. According to *China Foreign Economic Statistics: 1979 to 1991*, however, the number of workers directly employed by foreign-funded enterprises was 483.1 millions in 1991. The ratio of this figure of the workers directly employed by foreign funded enterprises in *China Foreign Economic Statistics* to the one in *China Labor Statistical Yearbook* was as big as 5 in 1989 and 1990. This huge gap is due to the difference in the coverage of the workers. *China Labor Statistical Yearbook* concerns only urban employees, while *China Foreign Economic Statistics* includes also the rural workers employed by the foreign-funded enterprises and their consignment produc-

tion enterprises. Yamamoto (1998) estimates the number of employees of foreign-funded enterprises at the end of 1996 as 18 million.<sup>6</sup> Ito (1998) calculates, by the use of Input-output Table of China, the job opportunities indirectly created by the foreign-funded enterprises is equivalent to 89.6% of those directly employed by the foreign-funded enterprises. Then, the sum of direct and indirect employment created by the foreign-funded enterprises becomes 10.238 millions in 1996, if the data of *China Labor Statistical Yearbook: 1997* was used. If Yamamoto's figure 18 millions is used, the sum becomes 34.128 millions in 1996. Whichever figure may be used, clearly the foreign funded-enterprises created the large number of employment opportunities.<sup>7</sup>

Second, the export marketing is another important area of contributions by the foreign-funded enterprises. With the rapid economic growth since 1992, exports also expanded at the rapid rate: 8% in 1993, 31.9% in 1994, and 23% in 1995. The share of the foreign-funded enterprises in the total exports also increased from 20.4% in 1992 to 31.5% in 1995 and 40.7% in 1996. All the top nine provinces in the value of exports in 1996 are located in the coastal region. The total exports of those nine provinces occupy 85.5% of the total exports of China. Thus, the Chinese exports are almost exclusively done by the provinces in the coastal region. The share of the foreign-funded enterprises in these provinces was very high in the above-mentioned seven coastal provinces, except for Beijing and Zhejiang. For example, those shares of Guangdong, Fujian, and Tianjin were 51.1%, 53.3%, and 63% in 1996. Thus, the foreign-funded enterprises have taken the main exporters in the coastal provinces.

Third, the contributions to the budget revenue in the coastal provinces are examined. The share of tax revenue by foreign-funded enterprises in the total budget revenue of Shanghai was 32.1% in 1996. The same shares in Beijing and Dalian were 23.2% and 27.8% in 1996. It is clear that the Open Door Policy of Reform made the substantial contributions to the Chinese economy in these manners.

#### 4 The Major Current Issues in China

The most important reforms that Chinese economy is facing now are said to be three: the state-owned enterprise reform, the financial system reform, and the government organization reform. In this note, however, our discussion must be limited to the state-owned enterprise reform. This reform causes the serious problems of temporary release from work and unemployment of worker. Those two problems are taken up also in this last section.

##### 4-1 The reform of the SOE

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<sup>6</sup> Tsunehito Yamoto (1998), p.41.

<sup>7</sup> Shoichi Ito (1998), pp.138-148.

The SOE used to have the very large shares in the total investment in fixed assets and urban employment as the major producers in China. For example, the share of the SOE in total investment in fixed assets was 81.9%, and its share in the urban employment was 76.8% in 1980. If, therefore, the SOE utilized their capital and labor force more efficiently, they could make the great contributions to further the economic development in China. For that purpose, the Chinese government naturally put its emphasis on the reform of the SOE in the early 1980's. Their shares in total investment in fixed assets and urban employees remained still as 54.4% and 57.4% as in 1995. Although their shares declined, they are still crucial to the Chinese economy in many ways. Thus, the reform of the SOE is considered to be the most important issue now.

The SOE with the large sizes of capital and labor force are facing the serious "deficit problem." According to the 1995 third Industrial Census, the number of deficit SOE is 29,668 out of 87,905 industrial enterprises with independent accounting system. The share of the deficit enterprises in all the manufacturing SOE was 36.3%. Generally speaking, the percentage of the deficit enterprises is higher among the enterprises producing consumer products than among those producing investment products and also higher among the small and medium size enterprises than among the large size enterprises. The percentage of the deficit enterprises in textile industry was especially as high as 45.3% in 1995. The percentage of the deficit enterprises in the SOE jumped up in 1993, when the foreign-funded enterprises and those funded by Hong Kong, Macao, and Taiwan enterprises rapidly came in, and the TVE dramatically developed.

As the transition from the planned economy to the market economy is promoted, competition among various types of enterprises becomes keener than before, and under the circumstance, a large number of the SOE began to make great loss.<sup>8</sup> According to the *1997 Fiscal Yearbook of China*, the percentage of the deficit state-owned commerce enterprises (43%) far exceeded that of the state-owned industrial enterprises (31.5%) in 1996.

Six major factors may be listed as those causing the financial difficulty to the SOE:

The first is a **decline of the share of SOE in the domestic sales**. This decreased the rate of operation in the SOE which worsened the deficit further.<sup>9</sup>

The second is the **accumulation of inventories**. The size of the inventory investment in China as a flow has been 5~6% of GDP since 1992. The figure is much higher than that of Japan: below 1% of GDP. The inventory investment in 1996 is 353.11 billions Yuan, and the accumulated amount of inventory investment at production enterprises is estimated to be 1,300 billions Yuan at the end of 1996. Half of it is that of the SOE. It is pointed out

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<sup>8</sup> "1995 the Third National Industrial Census Data of the Peoples' Republic of China (The volume of SOE, Subsidiaries of Foreign Enterprises, and TVE)".

<sup>9</sup> Wu Jia-Xiao (1998), p.55 and p.64.

that if the inventory investment in the distribution channels is added to this figure mentioned above, the total amount of accumulated inventory investment becomes 3,000 billions Yuan. It is so much as 43.8% of GDP of China in 1996. This indicates that the huge amount of inventory investment has accumulated in China, and that the SOE occupies its enormous proportion.<sup>10</sup>

The third is the so-called **triangle debt problem of mutual default** of debt repayment among the SOE. The total amount involved is not known as yet. According to the 1996 public announcement by the State Statistical Bureau of China, the credit to be recovered by the Manufacturing Industry's SOE only was 120 billions Yuan at the end of 1996. It is pointed out that the total amount of so-called triangle debt reached as much as 500 billions Yuan at the end of 1996. This was equivalent to 7.3% of GDP of China in the same year.<sup>11</sup>

The fourth is the burdens imposed on the SOE with the employment of **redundant workers and the insurance and welfare costs** for employees. For example, the total expenditure of the SOE for the insurance and welfare costs in 1996 was 227.65 billions Yuan, which was equivalent to 33.5% of the total wage payment including bonus and allowances. The two major items of their total expenditure for the insurance and welfare costs were the pension expenditure for retired employees (55.6%) and the medical & public health expenditure (27.1%) in 1996.<sup>12</sup> The various estimates of the redundant workers at the SOE have been given. According to the sampling survey of the China National Labor Union in 1991, the number of the redundant workers at SOE was about 170 millions in 1991, which is equivalent to 17% of the total employees at the SOE and about 12% of all the wage earners. According to the survey of the Ministry of Labor, the redundant workers of SOE were about 10% of the employees of SOE.<sup>13</sup>

The fifth is the **high debt ratio**. The debt ratio of Chinese enterprises was below 20% at the beginning of the 1980's but became above 50% in 1990. It must be pointed out that this ratio became even above 75% in 1994.

The sixth problem is the **poor managerial capability**. It seems to show up in the quality of products as one of such indexes. According to the sampling inspection of 300 thousands products and commodities at the enterprises in 1996, the acceptance rates of the products and commodities are 70% and 71% on the average, respectively. The rates for the processed food are 85% and 69%; the rates for the electric appliances for households are

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<sup>10</sup> Wu Jia-Xiao (1998), p.55.

<sup>11</sup> Wu Jia-Xiao(1998), p.55.

<sup>12</sup> China Labor Statistical Yearbook 1997, pp.466-467.

<sup>13</sup> Shoichi Ito(1998), p.198.

85% and 69%; and the rates for the machinery and electric appliances are 88% and 58%. These figures indicate the low level of management capacity.<sup>14</sup>

The serious problems mentioned above make the government consider the reform of the SOE as the major target of Economic Reform in China now. In the Report of the Government Activities in 1996, six items are listed as the leading ideas and basic roles of the SOE reform:<sup>15</sup>

- 1) the transformation of management of SOE to establish the modern enterprise system;
- 2) the strategic restructuring of SOE, putting emphasis on the reform of the large size SOE and making the small size SOE free;
- 3) looking for and developing the various types of public-owned enterprises, based on three kinds of advantages;
- 4) linking the reform with restructuring, remodeling, and strengthening management;
- 5) promoting the merger, standardizing bankruptcy, reallocating the temporarily released workers, achieving higher efficiency by reducing redundant workers, and implementing the re-employment activities;
- 6) promoting such related reform as establishing the social welfare system.

Furthermore, the government has tried to facilitate the SOE reform by setting the stage in the following manner:

- 1) selecting the priority industry and supporting the priority enterprises; for example, the textile industry being considered as a gateway of the SOE reform;
- 2) dissolving the loss-making SOE or helping them get away from their difficulties through the reform of the industries;
- 3) considering as the next priority industries such military and machinery industries that got over the difficulties;
- 4) one method for overcoming the difficulties is promoting the share-holding system and share-cooperative system.

#### 4-2 The problem of unemployment and potential unemployment<sup>16</sup>

The Chinese economy achieving two digits growth rates from 1992 to 1995 continuously realized the low level of unemployment. However, the rate rose from 2.3% in 1992 to 3.1% in 1997. According to the data of the Ministry of Labor, it was 2.9% in 1995. On the other hand, according to the one percent population survey in 1995, the unemployment rate for the urban employees was about 4%, and in addition there are about 1% employees

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<sup>14</sup> China Statistical Yearbook 1997, pp.689-690.

<sup>15</sup> Li Pong, "The Government Activities Report 1998", pp.8-9.

<sup>16</sup> Shoichi Ito (1998a), pp.196-202, Shoichi Ito (1998b), p.78, and Li Fu-Dian and Liu Wu (1998), pp.58-60.

waiting recall at home due to cessation of production. Thus, the unemployment problem in China now cannot be taken optimistically as the unemployment rate indicates.

In China, it is often pointed out, there are an enormous number of redundant workers in both rural and urban areas. In 1996, 864.39 millions people are living in the rural areas, and 490.39 millions among them are rural workers in the agriculture sector or at the TVE. The number of workers engaged in farming, forestry, animal husbandry, and fishery was 329.1 millions. It is usually in the agriculture sector that there is a large number of redundant workers. The range of the estimates is somewhere between 50 millions and 200 millions. For example, Zhou (1994) gave 150 millions as an estimated number of redundant workers in the agriculture sector. In estimating that figure, he considered the factors such as the reduction of the area under cultivation, the increase in the number of the workers in the agriculture sector, the increase in the amount of agricultural machinery and the increase in the utilized amount of chemical fertilizer. In the past, the TVE absorbed a large number of redundant workers in the agriculture sector. Recently, however, it is said that about 60 millions rural workers are working in the areas away from their homes, among whom 30 millions rural workers are in other provinces. After 1995, 50 millions rural workers are said to be working in urban areas.

In the urban sectors, the number of redundant workers of both SOE and COE is said to be between 20 millions and 30 millions. One important method to reform SOE with large numbers of redundant workers mentioned above is "lay-off" (temporary release from work). The estimated number of unemployed urban workers at the end of 1997 is 5.7 millions, and the unemployment rate is 3.1%. The number of laid-off workers is said to be 11 millions at the end of 1997, and they occupy 6% of urban employees. The government expected that the increase in the laid-off workers in 1998 would be 4 millions. Thus, the number of laid-off workers is expected to reach 15 millions at the end of 1998. The laid-off workers are distinguished from the unemployed workers. The former still belong to particular enterprises but are not expected to go back to work at the enterprises. They are given a minimum amount of allowances for their living costs and receiving the training for reemployment, while they look for the reemployment opportunities. On the other hand, the unemployed workers do not belong to any enterprise. The laid-off workers are expected to be re-employed within three years; otherwise, they will become unemployed later. If the laid-off workers are regarded as the potentially unemployed, the sum of the genuinely unemployed and the potentially unemployed workers exceeds 11% of the urban employees at the end of 1998.

Into the urban labor markets a large number of rural workers are coming, and the workers of SOE and COE are laid off. This worsening situation of unemployment may

cause the very serious excess supply of labor in the urban labor markets, and is considered to be the most critical problem facing the Chinese economy under Economic Reform now.

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## II. Contemporary Status and Prospect of Economic Transition in Far Eastern Russia

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### 1. The Economy of the Russian Federation and Russian Far East

Russian Far East (RFE) occupies the eastern part of the Russian territory and is situated in the northern part of Far East. The RFE has a total area of more than 6.22 million sq. km (36.4% of entire Russia) and is composed of the Republic of SAHA (Yakutia), Jewish Autonomous Region, Chukot Autonomous Territory, Primorski Region, Khabarovsk Region, Amur Territory, Kamchatka Territory, Magadan Territory, and Sakhalin Territory. The population of the RFE reached its highest level of 8.06 million in 1991 and then dropped to 7.42 million estimated as of January, 1997. This is approximately only 5% of the total population of the Russian Federation, 147.5 million. The population density is about 1.2 persons per sq. km, compared with 8.6 in entire Russia. This implies the serious shortage of labor force needed for regional economic development. The high rate of wages in the RFE was inherited from the Soviet period and has significantly raised the cost of production. It made the industries in this area less competitive domestically and internationally.

**Table 1 Growth Rate of Population in Russian Far East (%)**

	1981~1985	1986~1990	1991	1992	1993	1994	1995	1996
Russian Federation	0.7	0.7	0.1	-0.1	-0.2	-0.1	-0.2	-0.3
Russian Far East	1.6	1.2	-0.3	-1.7	-1.4	-2.1	-1.6	-1.1

Source: Russian Statistical State Committee, Russian Regions, No.2, 1997

After the Russian Revolution the RFE part became independent of European Russia and began to pursue its own economic development. Around that time approximately 30% of the gross production of the region was dependent on the foreign trade within the Asian area, and the main items were timber, gold, and fishery goods. In the 1930's the State government actively adopted the policies to develop industries, mainly military industry, and high economic growth followed in RFE. Then, more than 75% of the industrial output in the RFE was consumed within the Soviet Union, while only 5% was exported. The rela-

tionships of RFE with the rest of the Soviet Union were strong but those with other Asian regions were weak.

After 1992, however, the economy of RFE changed once again in the other direction; that is, the relations with the European Russia weakened, and those with Asia-Pacific regions were strengthened. The domestic factors for this change are the following:

- 1) 'Moscow centralism' and disregard of the regional economies,
- 2) High wage rates in the RFE, compared to the rest of Russia. For example, in 1997 wages in the RFE were 169% of the average rate in Russia,
- 3) High electric power energy costs. During 1992-97 production price increased up to 8,500 times in Russia, and the increase of energy price in RFE was raised 15,000 times during the same period,
- 4) Price liberalization raised transportation costs. Railroad between RFE and European Russia exceeds 5,000 km., so that delivery costs of the raw materials brought from Siberia are almost equal to the prices of products, and petroleum in Siberia would be cheaper if imported from Japan,
- 5) Special subsidies from the central government were provided earlier to control price distortions, were terminated in 1992.

In addition, the following external circumstances made the economic cooperation of the RFE with the Asia-Pacific countries more preferable to the trade with European Russia:

- 1) Economic development of Asia-Pacific countries,
- 2) The end of the Cold War,
- 3) Attractiveness of the RFE natural resources to Asian countries.

In the recent years, approximately 73% of the RFE industrial output has been consumed within the RFE area, 13% exported to European Russia, and the remaining 14% exported to Asia-Pacific countries.

## 2 The Economic Status of the Far East.

In the same way as the entire Russian economy, the RFE economy experienced a sharp decline since 1992. Although the rate of decline decreased somewhat in entire Russia, it remained large in the RFE, as Table-2 shows.

**Table 2 Growth Rate of Industrial Production of Russian Federation and Russian Far East (%)**

	1990	1991	1992	1993	1994	1995	1996	1997
Russian Federation	-0.1	-0.8	-18.0	-14.1	-20.9	-3.0	-4.0	1.9
Russian Far East	-2.0	-2.7	-15.2	-12.3	-22.8	-18.0	-13.0	-8.1
SAHA (Yakutia) Rep.	1.0	-2.4	-20.2	-3.9	0.4	-0.4	1.0	-4.2
Jewish Autonomous Region	4.0	-5.0	-24.0	-33.3	-29.0	-39.0	-24.0	-7.3
Primorski Region	-1.8	-3.7	-6.9	-11.8	-29.3	-0.7	-9.0	-5.6

Khabarovsk Region	-2.1	-1.2	-13.6	-18.2	-41.5	-19.0	-14.0	-6.5
Amur Region	0.5	-6.4	-17.3	-7.4	-22.9	-15.0	-23.0	-5.5
Kamchatka Region	0.3	-7.9	-26.9	-6.5	-30.8	8.0	0.2	-6.9
Magadan Region	-4.9	-3.1	-8.1	-10.6	-11.6	-14.0	-13.0	-13.0
Sakhalin Region	-7.2	3.1	-21.8	-26.9	-10.0	9.0	-16.0	-11.8

Source: Russian Statistical State Committee: *Russian Industries*, 1996,1997

In 1997 industrial production index turned positive in the Russian Federation, while the RFE still showed a negative growth of 8.1%. Table 3 shows that the industrial production in the RFE declined sharply in many industries.

**Table 3 Equipment Manufacturing in the Russian Far East Regions**

	1991	1992	1993	1994	1995	1996	1997
Cranetools in Khabarovsk	-	538	243	97	71	62	36
Lumber Machines Primorski Region	2702	2780	656	61	147	13	-
Power Press in Amur	744	559	419	60	24	2	-
Washing Machines in Primorski	133500	83800	64000	16400	2700	1000	40

Source: Japan Association for Trade with Russia & Central-Eastern Europe, Russian Far East Data Book, 1992-98

Table 4 displays industrial production by the types of output. The primary industrial products in the RFE are non-ferrous metals and processed food. This is different from the rest of Russia.

**Table 4 Types of Industries in the Russian Federation and the Russian Far East (1995, %)**

	Electric Power	Fuel	Steel	Non-ferrous Metals	Petroleum products
Russian Federation	13.5	16.4	9.1	6.5	7.5
Russian Far East	19.3	10.5	0.5	20.7	0.7

	Machinery	Wooden Products	Construction Products	Light industry	Food
Russian Federation	17.9	5.1	4.8	2.5	12.1
Russian Far East	8.5	5.4	4.0	0.6	25.3

Source: Russian Statistical State Committee, Russian Statistical Year Book, 1994,95

Some causes for the economic slump in the RFE were the same as those for the slump in entire Russia, but the main factors were considered unique to the RFE as follows:

- 1) Decline in defense expenditure due to the end of the Cold War. Munitions industry was important in the RFE so that the total output dropped.
- 2) Transformation of munitions production into non-military use was not successful. Special governmental subsidies for the transformation program covered only 10% of requirements. Companies failed to obtain resources to satisfy the needed restructuring of the industry without external help.

- 3) As it was pointed out earlier, products of the RFE were not competitive due to the high costs in the domestic market as well as in the international market.
- 4) Imports of consumption goods from China, the Republic of Korea, Japan, USA and Australia were more attractive and competitive.
- 5) Economic environments for foreign investment are very poor, especially in infrastructure and business laws and regulations, even in comparison with Central Russia.
- 6) Returns to foreign investment are higher in neighboring countries in East and South-East Asia than in the RFE.
- 7) Import items are confined primarily to consumption goods instead of capital equipment that could be used for industrial development and potentially for accumulating foreign assets.
- 8) Policy measures to advance the technological level of industrial structure has not received high priority. Once the Central Government's subsidies were cut off, foreign trade of RFE was oriented to export primary products and import consumption goods for many years.
- 9) Collisions between the Central and Local Governments.
- 10) Decline of population.

### 3 Outline of the Russian Far East Foreign Trade.

**Table 5 Russian Far East major foreign trade partners (US\$ million)**

	Export		Import	
	Total	%	Total	%
Japan	1,037	36.6	160	9.2
China	707	25.0	219	12.6
Rep of Korea	329	11.6	307	17.7
USA	128	4.5	413	23.8
Vietnam	38	1.4	19	1.1
Hong Kong	35	1.2	2	0.1
Taiwan	30	1.0	2	0.1
Germany	21	0.7	58	3.3
Singapore	21	0.7	54	3.1
Canada	6	0.2	21	1.2
Australia	1	0.0	21	1.2

Source: Statistical Data of the Russian Far East Local Governments, 1997

Main destinations of the RFE exports are Japan, China, Rep. of Korea, USA. The RFE import mostly from USA, the Republic of Korea, China and Japan. Major export items are:

raw materials, fish, timber and wood products. There are also occasional export of armaments and combat equipments. The basic imports are consumption goods such as foot-wears, used cars and fuels.

Due to lack of reliable statistics on the economy of the entire RFE, the pattern of foreign trade for the Primorski Region will be examined as an example. It will be compared with the Russian Federation and China. China has successful experiences in developing the transitional economy.

First, there is a significant difference in the shares of export and import in GDP among the Primorski Region, Russia, and China. **Fig. 1** shows that Chinese export has leveled off around 20% of GDP. In the case of Russia and the Primorski Region the same ratios have fluctuated very much. In 1993 export/GDP ratio for the Primorski Region was lower than in China and Russia. The same situation can be seen for imports from **Fig. 2**. It shows the ratio of import/GDP in which China maintains a stable level, and Russia and the RFE change from year to year. Except for 1995, the RFE has a ratio lower than both China and Russia. This indicates that the Region's foreign trade is underdeveloped. Since the Primorski Region is the closest to Asia-Pacific countries, it may be presumed that the rest of the RFE has also the underdeveloped foreign trade sector.

Next, the ratios of net primary goods import to net value-added goods export may be examined. They are shown in **Fig. 3**. The higher the ratio is, the more the country exports primary goods. The Chinese ratio is always less than 1, while Russian and Primorski's ratios are high but not stable. Especially in 1994-95 the export of primary goods from the Primorski Region was very high. **Fig. 4** displays primary goods / value-added goods ratio in the import. China has significantly low values less than 0.23, and the ratio of Primorski Region is slowly decreasing. Compared with China, clearly it is still importing and exporting a lot of primary goods.

Last, the weight of machinery, equipment, and transport equipment in the total exports and imports may be examined. The proportions for export are shown in **Fig.5**. China has incredibly a high ratio, whereas both Russian and Primorski's values for import of machinery and equipment are low. In 1996 and 1997, the ratio for Primorski Region has grown. This can be explained by armament exports to China and other countries. **Fig. 6** displays the weight of machinery, equipment, and transport equipment in the imports. Chinese ratio is relatively high; that is to say, it imports a lot of equipment necessary for its industrial modernization. The Primorski Region's ratio is lower than Chinese and Russian ratios. It is worth pointing out that a large part of Primorski's imports is composed of used cars. This does not help the industrial development. Thus, there does not seem to be any sign of improving the industrial structure in the Primorski Region. Its foreign trade pattern remains as

primary goods exporter and consumption goods importer. Unless this character fundamentally changes, industrial modernization will hardly take place.

#### 4 Foreign Investment in the Russian Far East.

Foreign investment in the RFE is only 2% of the total in Russia. Considering the RFE weight in Russian GDP that is 5%, it is too low. It is as small as 0.05% of foreign investment in China that is about US\$45.4 billions in 1997. Major destinations of foreign investment in the RFE are natural resource development, banking and finance, foreign trade, and restaurant business.

Table 6 Foreign Investments in Russian Far East 1997 (US\$ 1000)

	Total	Direct Investments	Others
Russian Federation	10,498,000	3,897,300	6,600,700
Russian Far East	215,121	140,195	74,926
SAHA (Yakutia) Rep	14,046	9,789	4,257
Jewish Autonom. Region	439	439	-
Primorski Region	43,133	9,953	33,180
Khabarovsk Region	10,796	10,469	327
Amur Region	419	239	180
Kamchatka Region	32,925	832	32,093
Magadan Region	62,802	61,610	1,192
Sakhalin Region	50,561	46,864	3,697

Source: Russian Statistical State Committee, *Russian Society and Economy in January 1998*, 1998

#### 4 Conclusion

These considerations seem to indicate the following conclusions.

- (1) Liberalization weakened the cooperation between the RFE and the Central Russia, but it was not replaced by the necessary cooperation with the Asia-Pacific countries.
- (2) The current pattern of foreign trade does not stimulate industrial modernization.
- (3) The current level of foreign investment is too low and cannot be expected to help economic development.
- (4) In order to stimulate industrial modernization, what is required is the change in foreign trade pattern from primary goods export/value-added goods import to primary goods export/machinery and equipment import.
- (5) More in-flow of investment from the Central Government and abroad is essential to the development of the RFE. But it does not seem to be expected in the near future.

Fig 1 The Ratio of Total Export to GDP

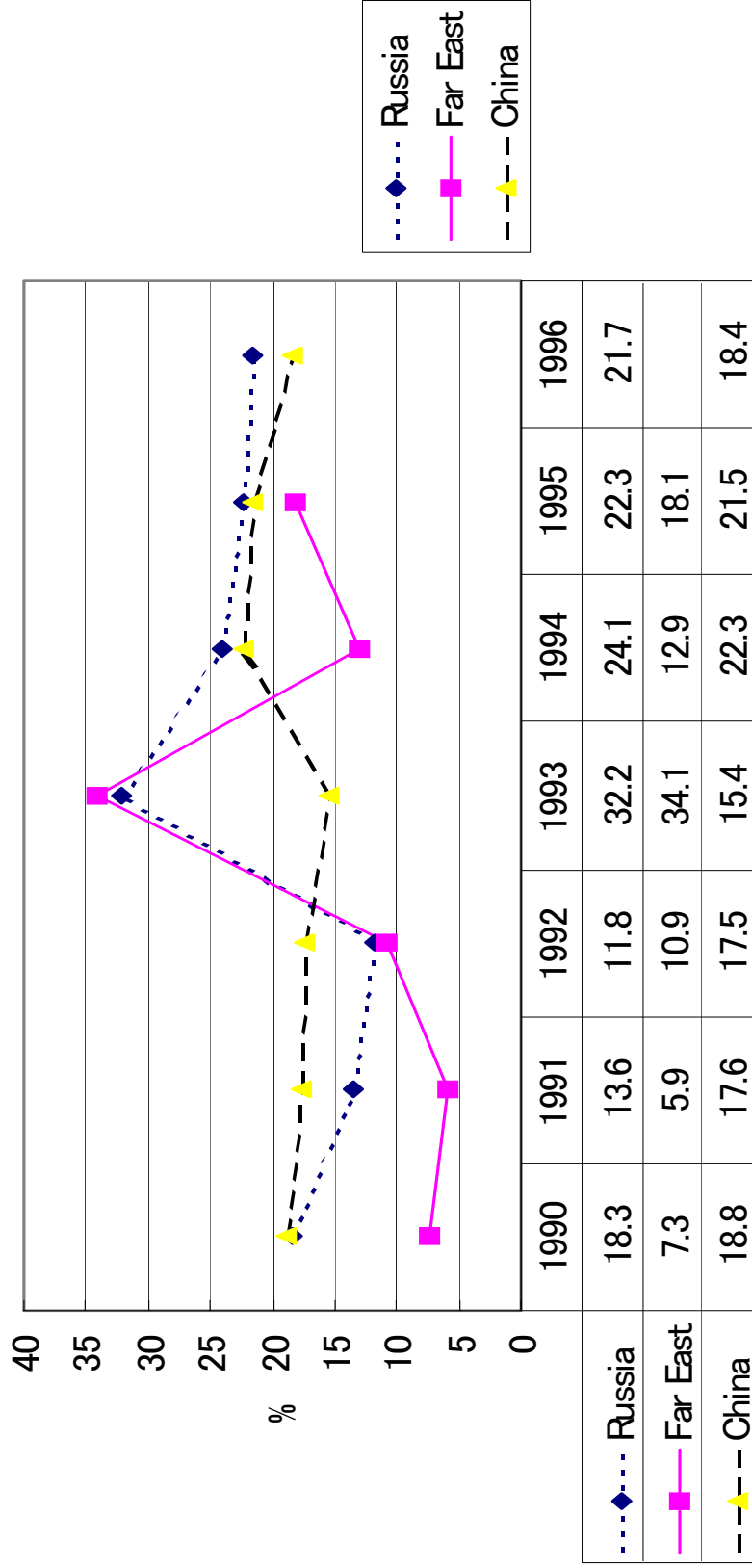


Fig. 2 The Ratio of Total Import to GDP

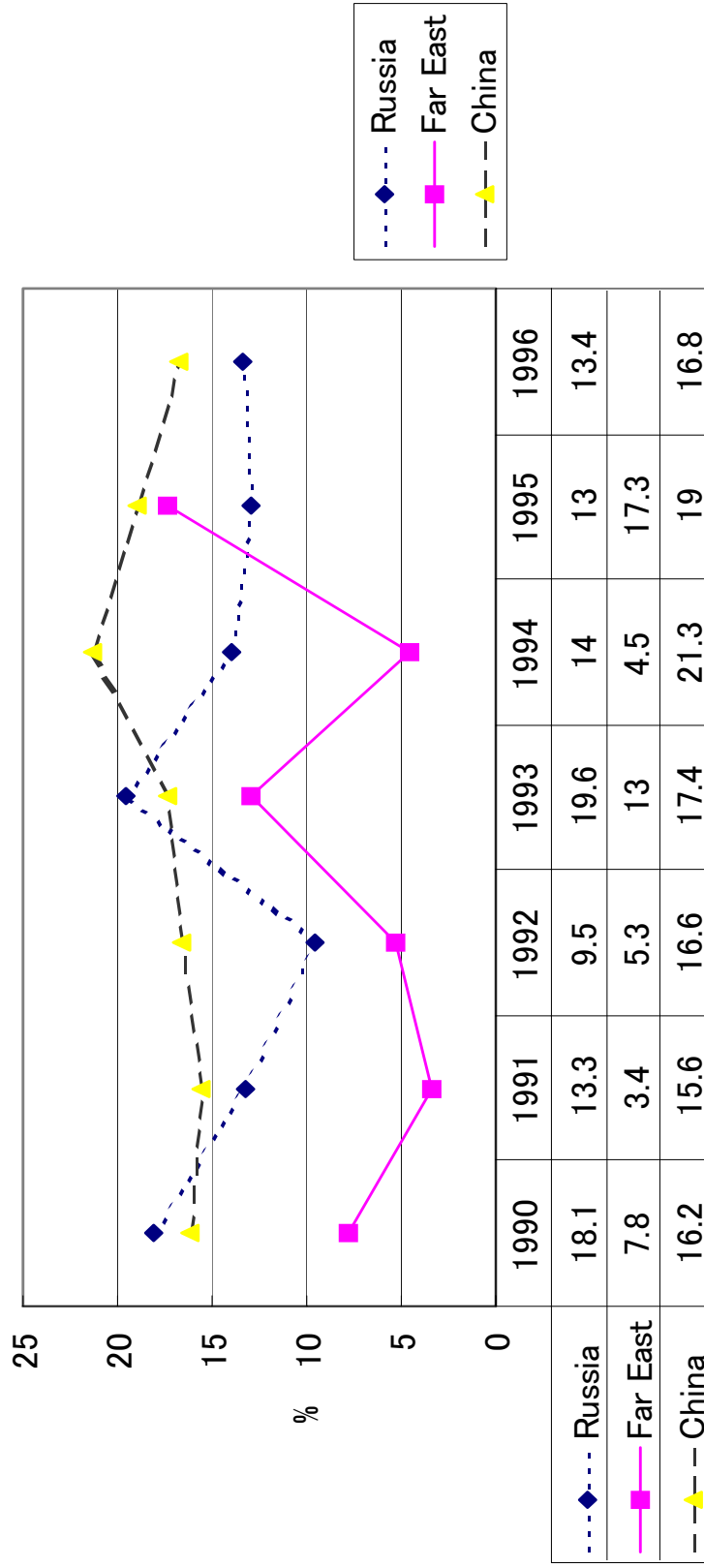




Fig.3 The Export Ratio of Primary Products to Secondary Products

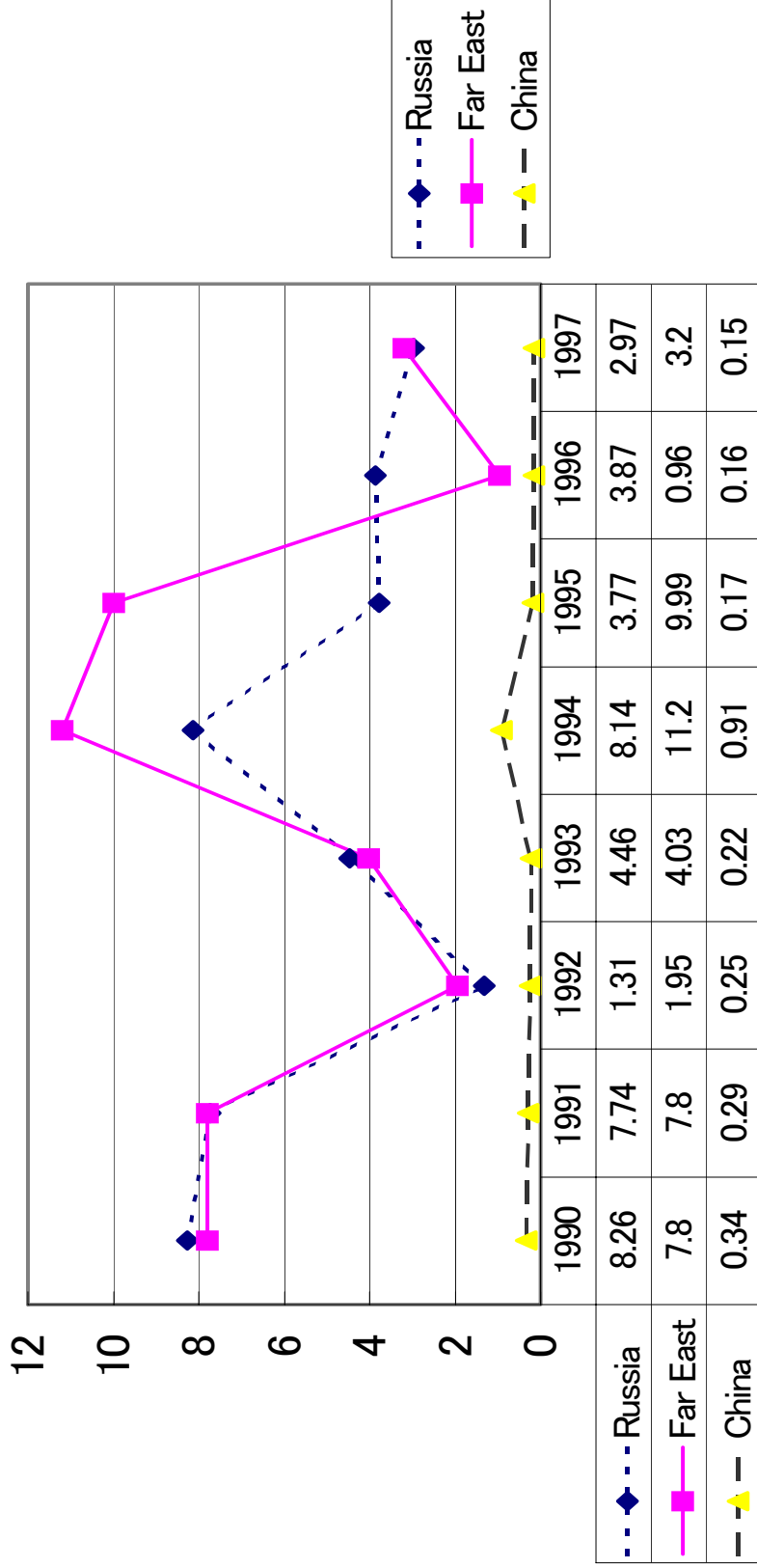


Fig.4 The Import Ratio of Primary Products to Secondary Products

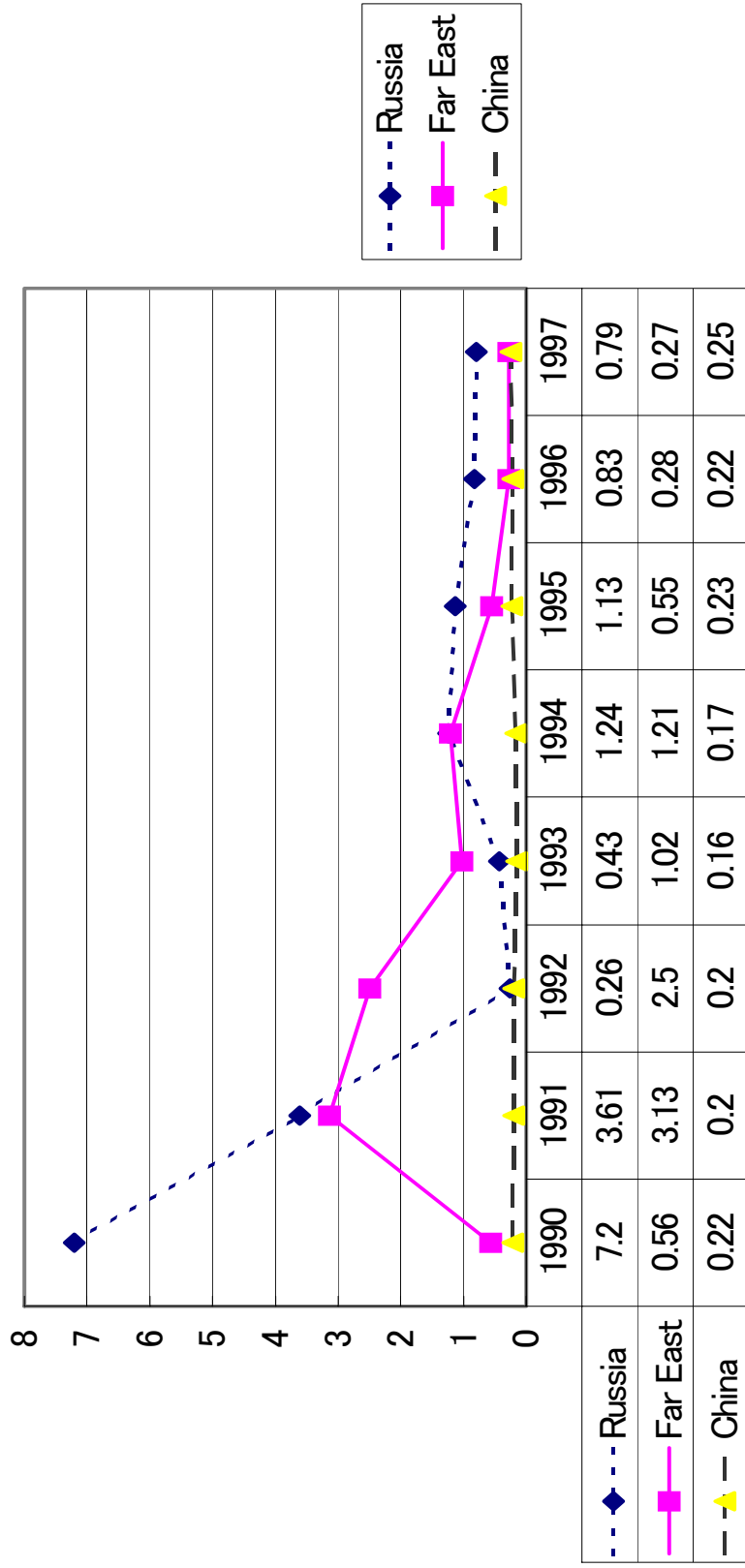


Fig.5 The Ratio of Export of Machines, Equipment and Transport  
Machines to Total Export

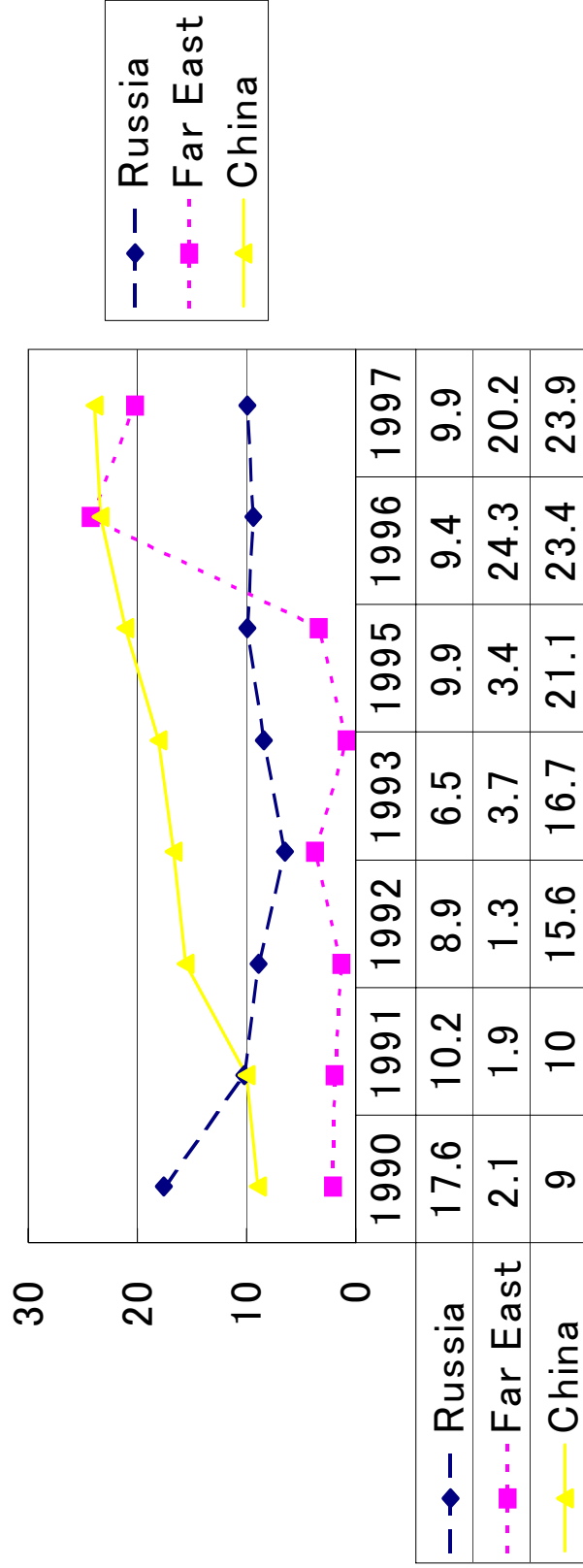


Fig.6 The Ratio of Export of Machines, Equipment and Transport  
Machines to Total Import

