

EC2374

Economy of Modern China

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Topic 3 (cont) Rural Economy & Income Inequality

Achievements and challenges:

- Development and structural changes
- Rural organization & urban-rural divide
 - socialist dualism
 - rural to urban migration & urbanization
 - economic consequences
- Income inequality
- Rural industrialization
 - township & village enterprises (TVEs)

Topic 3 (cont) Rural Economy & Income Inequality

Rural industrialization:

- TVEs as a unique development phenomenon
 - related to China's economic tradition:
rural non-agricultural activities in pre-industrialization
 - originated from rural collectives
 - prospered between mid-1980s and mid-1990s
 - as an organizational form largely disappeared since late 1990s
restructured, transformed, or disappeared

Topic 3 (cont) Rural Economy & Income Inequality

Rural industrialization:

- Origins of TVEs
 - rural non-agricultural activities in China's traditional economy
 - 1950s, collectivization led to de-industrialization
 - 1970s state-sponsored rural industrialization
 - “commune and brigade enterprises”
 - “serve agriculture”: producer goods

Topic 3 (cont) Rural Economy & Income Inequality

Rural industrialization:

- Expansion of TVEs during mid-1980s to mid-1990s
 - the most dynamic part of the economy
grew by 30% a year between 1978 & 1996
 - crucial to absorb rural surplus labor
employment: 28 mil in 1978 => 135 mil in 1996
 - important in transforming the economy
raised rural income => reduced urban-rural gap
created competition for SOEs
contributed to trade expansion (labor intensive industries)

Topic 3 (cont) Rural Economy & Income Inequality

Rural industrialization:

- Factors behind TVE's rapid expansion
 - comparative advantage
 - cheap surplus rural labor
 - less access to cheap subsidized credit
 - entry barriers lowered
 - still highly profitable
 - niche markets (buttons, ribbons, building materials)
 - TVEs as collectives are readily acceptable

Topic 3 (cont) Rural Economy & Income Inequality

Rural industrialization:

- Factors behind TVE's rapid expansion
 - favorable institutional framework
 - support from local governments: owners/stakeholders
 - employment creation & government revenue
 - lower taxes
 - local bank capital
 - local credit institutions
 - proximity to key market
 - urban coastal cities
 - markets in Southeast Asia

Topic 3 (cont) Rural Economy & Income Inequality

Rural industrialization:

- TVE's restructuring post mid-1990s
 - background
 - govt's efforts to improve markets and regulatory institutions
 - market integration & more intensive competition
 - macroeconomic policy (banking)
 - recognition of private ownership mid-90s
 - restructuring & privatization
 - drop in TVE's employment share (of collectives): 50% in '95, 10% in '04

Topic 3 (cont) Rural Economy & Income Inequality

Rural industrialization:

- Recent development & its limitations
 - need to adapt to a more open/competitive environment
 - weaker ties to local governments
 - more inter-regional
 - the emergence of ‘industrial clusters’
 - large number of small firms
 - intense competition
 - fine division of labor among different production stage
 - strong export orientation
 - constrained by their rural-ness
 - lacks in physical, institutional and social infrastructure

Topic 3 (cont) Rural Economy & Income Inequality

Concluding remarks:

- Rural urban gap the main source of inequality
 - Acceleration urbanization
Policy relaxation
 - Equalizing public services between rural and urban China
Integrated rural-urban development
 - Reducing rural-urban as well as regional gaps
Restructure central-local fiscal relations

Topic 3 (cont) Urban & Industry

Reforms & development of urban China

- China's industrialization
- urban industrial reform
- corporate governance (not included in mid-term exam)
- future prospects (not included in mid-term exam)

Topic 3 (cont) Urban & Industry

China's industrialization

- a late comer
 - failed early attempts
 - early 19th century to 1949
 - post 1949
 - big push industrialization
 - continued industrialization during reform
 - current state & future prospect
 - has rural to urban migration reached its peak?
 - has China completed industrialization?

Topic 3 (cont) Urban & Industry

China's industrialization

- big push industrialization: 1949-1978
 - government-led, investment driven
 - central planning
 - strong focus on heavy industry
 - the development of the state sector
 - limited interaction with world market
 - balanced regional development strategy

Topic 3 (cont) Urban & Industry

China's industrialization

- industrialization during reform
 - key measures
 - marketization & decentralization
 - opening up to foreign investment & trade
 - re-orientation of industrialization
 - developing consumer goods
 - lower entry barriers for non-state firms
 - uneven regional policies
 - SEZs established in Southeast Coastal region
 - more open policies applied to coastal provinces

Topic 3 (cont) Urban & Industry

China's industrialization

- a different dynamic
 - institutional urban-rural division
 - administrative barriers slow rural to urban migration
 - difference between rural and urban in marginal products of labor remain significantly large

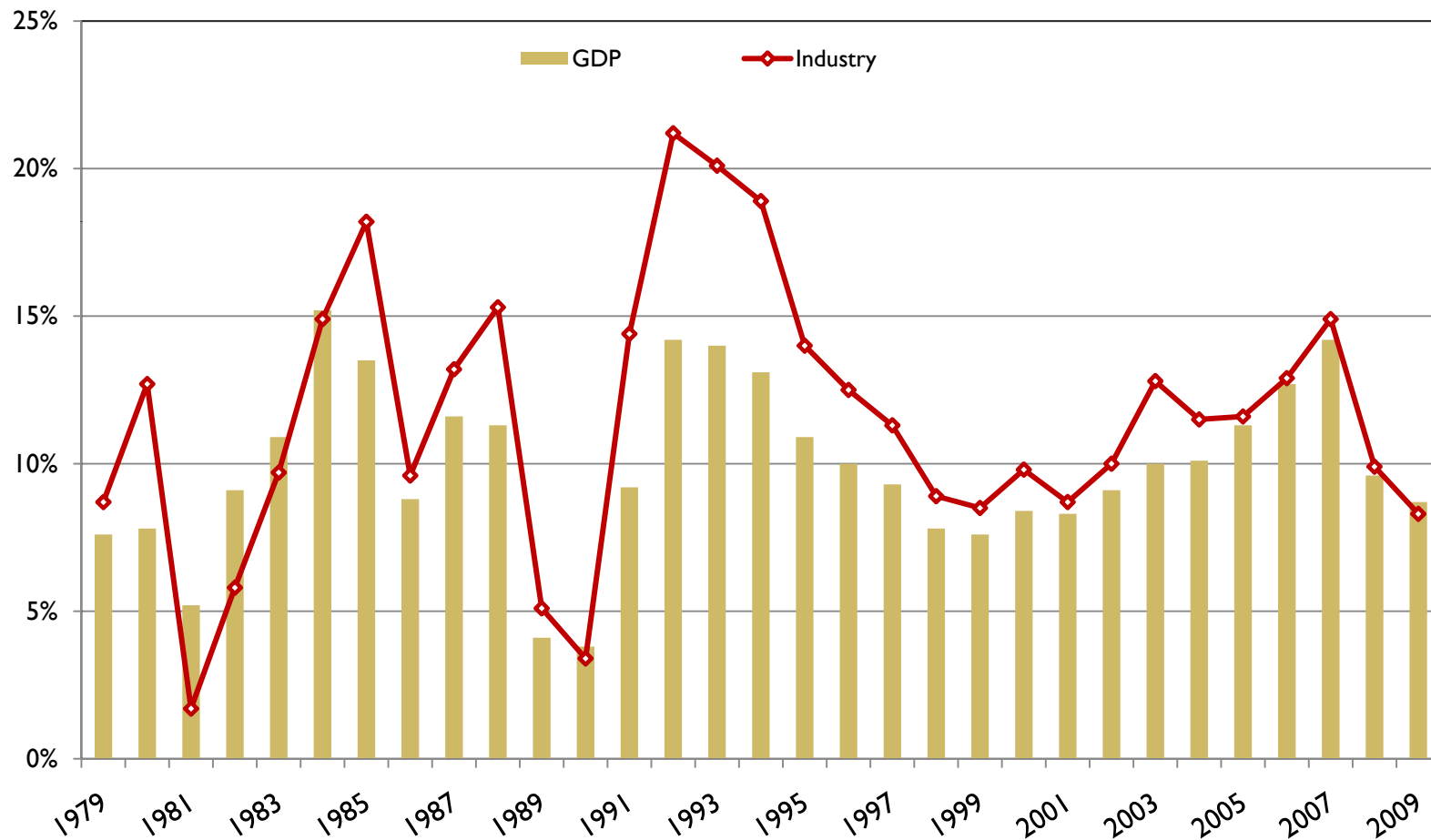
Topic 3 (cont) Urban & Industry

China's industrialization

- post-1978 industrialization & structural change
 - Rapid industrialization:
 - accompanied with ownership diversification
 - TVEs: 1980s-mid-1990s
 - FIEs: since 1990s
 - private, shareholding, etc: since mid-1990s
 - changes in regional structure
 - FDI significant in China's industrialization & structural change
 - expansion of labor-intensive industries
 - FDI related trade expansion in capital intensive goods

Rapid industrialization key to China's rapid growth

Increased by 11.5% a year: 1978-2009 (vs. 9.9% for GDP)



Topic 3 (cont) Urban & Industry

- **Development: growth and structural changes**
 - ✓ Industry contribute to around 40% of GDP
 - ✓ Heavy industry gained relative significant since early 2000s
 - ✓ leading industries shifted from labor intensive to capital- & technology-intensive industries
- Smelting & pressing of ferrous metals
- Manufacturing of communication equipment, computers & other electronic equipment
- Manufacturing of raw chemical materials & chemical products
- Manufacturing of transport equipment
- Manufacturing of electrical machinery & equipment

Topic 3 (cont) Urban & Industry

- **Development: ownership diversification**
 - ✓ The starting point: SOEs dominate the industries
 - ✓ 1980s to early 1990s: TVEs and export-oriented FIEs
 - ✓ Since mid-1990s: reforming SOEs & attract large MNCs
 - ✓ Since early 2000s:
 - encourage domestic non-SOEs (SMEs)
 - restructure monopolistic industries
 - ✓ **Current (2008):**
 - State: 5% of firms, 28% of output, and 44% of assets

Topic 3 (cont) Urban & Industry

- Trade & FDI essential

- ✓ Became sizable 1990s
- ✓ Mostly in manufacturing
- ✓ FIEs Significant especially for export and certain industries

Contribute to 70% of industrial export, 30% of output & employment

Manufacture of communication equipment, computers and other electronic equipment (92% EX, 77% Emp, & 81% output)

Manufacturing of raw chemical materials & chemical products (49% EX, 15% Emp, & 27% output)

Manufacturing of transport equipment (51% EX, 28% Emp, & 45% output)

Manufacturing of electrical machinery & equipment (68% EX, 40% Emp, & 45% output)

remain important in labor-intensive export-oriented industries

Topic 3 (cont) Urban & Industry

urban industrial reforms

- pre-reform system

- state-owned and urban

- 1978: SOEs accounted for 78% of industrial output & 76% industrial employments

- the rest by rural and urban collectives, owned by local govts

- resources were allocated by administrative means

- prices set by govt

- profits remitted to govt as revenue dual track pricing

- the govt's control over resources was less central than USSR

- fragmentation across regions

- limited trade across administrative regions

- vertical integration

Topic 3 (cont) Urban & Industry

urban industrial reforms

- 1978 to mid-1990s
 - existing hierarchical relationships remain
 - introduce market incentives
 - “profit retention” => “contract profit-loss responsibility
 - dual track pricing
 - introduced “tax for profit”
 - more reliance on market and less price distortion
 - encourage new forms of firms
 - rural collectives
 - private and household
 - foreign invested enterprises

Topic 3 (cont) Urban & Industry

urban industrial reforms

- 1978 to mid-1990s: incentive and autonomy
 - rapid increase in output
 - especially in non-state sector
 - export expanded rapidly: FIEs and TVEs
 - some improvement in productivity
 - modest improvement among SOEs
 - more market-oriented business environment
 - growing competition
 - declining subsidy
 - hardening of budget constraints

Topic 3 (cont) Urban & Industry

urban industrial reforms

- post-1996: real restructuring
 - forced by increasing financial difficulties
 - restructuring SOEs to improve profitability
 - lay off large number of workers
 - “grasping the large, and letting the small go”
 - central government vs. local governments
 - maintain control of resource related, capital intensive industries & public utility
 - various ways to restructure
 - corporatization, privatization, bankruptcy, and mergers and acquisition
 - provide a uniform legal framework
 - Company Law (1994)

Topic 3 (cont) Urban & Industry

urban industrial reforms

- post-1996: real restructuring
 - rapid growth continued, except in employment
output, export, labor productivity, and product quality
 - increase in market-oriented business behavior
rapid expansion of foreign-invested enterprises
accelerated growth of domestic private manufacturing
Increasingly commercial orientation of state-controlled corporate groups
 - FIEs become significant in many industries
garments, instruments & meters, electronics & telecommunications, textiles, etc.
Integrating Chinese industry with the global business community
more standard practices observed