

Wei Liu

Research on China's Market Economy Development

Market-Oriented Reform
Process and Economic Growth
with a Structural Evolution

Translated by Chi Wei Su · Yannong Xie

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Preface

From 1978 to 2008, the great cause of China's reform and opening up has been carried out for 30 years. In the past 30 years, profound changes have taken place in the level of economic growth, economic structure and market economic system. So, after 30 years of reform, what significant changes have taken place in China's economic growth level and economic structure? What are the internal relations between these changes and the institutional changes brought about by reform and opening up? What historical value orientation and method should be used to evaluate the effect of market economy reform? What criteria should be used to evaluate the marketization process and economic development mode of China's economy? That is to say, with the great institutional reform of China's reform and opening up, what changes have taken place in the institutional mode of China's social and economic development? What are the characteristics of this institutional change itself? Did the system change promote socioeconomic growth, if so, how? Is this economic growth based on increased efficiency? In other words, has the reform promoted the unprecedented acceleration of economic growth, and does such growth have real development significance and sustainability? Can the historical justice and progress of reform be proved in the sense of liberating and developing China's productive forces? Looking ahead, what are the main drivers of China's long-term sustainable economic growth? In a word, how to understand and evaluate China's socialist marketization process? How is the relationship between the level of economic growth, the change of economic structure and the improvement of economic efficiency in China's socialist marketization process? This is the central theme of this book. In other words, we should understand and analyze the rationality and progress of economic system reform from the perspectives of economic growth and economic development, expansion of economic scale and improvement of economic quality, acceleration of economic speed and improvement of economic efficiency. At the same time, it further reveals the historical requirements for the in-depth reform of the system, which is the basic issue of this book. Around this core proposition, this book is divided into the following three parts to discuss the development of China's market economy.

Part I: Characteristics of China's Socialist Market Economy Reform Process and the Value Judgment Criteria.

Firstly, this part discusses the value judgment of the reform effect. Along with the historical process of reform, profound changes have taken place in China's economy. On the one hand, unprecedented achievements have been made in the progress of modernization and the improvement of people's living standards. On the other hand, the contradictions in the social process are more complex and acute. It is hard to avoid controversy over reform, at least when it comes to consensus: Should we continue to reform? What historical standards should we use to evaluate reforms that have taken place? What historical values should we use to promote reform? All these have become issues that people are generally concerned about and urgently need to be resolved in social development. The research results of the book have been theoretically studied and answered.

Secondly, this part systematically explains the justice and progress of institutional change in theory. From the divergence and opposition between value theory and different market economy philosophies, this part examines the divergence of value orientation in economic theory regarding whether or not market system should be established and how to establish market system.

Thirdly, this part discusses the evaluation of China's marketization process and economic development mode. What historical stage has China's economic development reached and what are the salient features of this stage? It is always a controversial issue to measure the level of a country's social and economic development. According to the two basic indicators of economic quantity and economic quality, this part judges the level of China's economic development and concludes that China's economy is in a period of accelerating industrialization from the longitudinal perspective. Horizontally, China is now slightly higher than the average level of middle-income developing countries in the world. On this basis, the prominent characteristics of this stage after 30 years of reform and opening up, and economic development have been summarized and refined. This part summarizes the transformation characteristics of China's economic development using empirical method from several aspects, including ownership structure adjustment, changes in resource allocation mode, technological innovation and system evolution.

Fourthly, this part analyzes the relationship between the process of factor marketization and economic growth. The prominent feature of China's current marketization process is to accelerate the marketization of factors. Among the two basic growth factors, labor and capital, capital is more scarce in developing countries, so it is more significant to improve the efficiency of capital. So, the marketization of capital factor appears more important. From the perspective of China's reality, not only is the level of factor marketization far behind that of commodity marketization, but in the process of factor marketization the level of capital factor marketization is lower than that of labor factor marketization. This part reveals the reform path of China with banking and financial institutions as the main body in a comprehensive and in-depth way, puts forward a series of targeted reform suggestions and empirically studies the impact of the reform of the capital market and its financing mode on the actual economic growth.

Part II: Economic Growth Cycle and Aggregate Regulation in China's Socialist Market-Oriented Reform Process.

Firstly, this part discusses the long-term strategic objectives of China's economic growth and possible problems. Since the reform and opening up, China has maintained long-term high-speed economic growth. In 2002, China set a new long-term economic growth target of quadrupling its GDP in 20 years, and in 2007 it set a target of quadrupling its per capita GDP by 2020. This part analyzes and studies the possibility, trend, growth rate and possible problems of China's long-term economic growth from the aspects of the comparison between China's economy and East Asia's economy, resident disposable income, and the impact of China's future economic growth on China's international economic status. It reveals a series of problems that determine China's long-term development goals, such as urbanization, the contradiction between short-term surplus and long-term shortage of production capacity, energy and environmental constraints, and education and scientific and technological development.

Secondly, this part analyzes the characteristics of the economic periodic fluctuation in the system transition. With the deepening of marketization, the law of the economic cycle has begun to play a role in China. An important task of macro-control is to reduce the negative impact of such an economic cycle on economic growth through counter-cyclical operation. This part studies the performance, quantitative characteristics and formation mechanism of China's economic cycle, and points out how to make macro decisions according to the characteristics of China's economic activities at the present stage. Due to the historical process of China's industrialization and marketization and other development factors and institutional factors, the imbalance in China's current economic growth has a series of new complexities; the subject system reveals the main factors causing economic fluctuations.

Thirdly, this part analyzes and evaluates the macro-economic policy effects in the system transition. The part makes a systematic analysis of the complexity of contradictions in China's macro-economic operation since the reform and opening up, evaluates the effect of the use of macro-policy in stages, and reveals the factors that determine and influence the effect of the use of macro-policy tools. At the present stage of China's economic development and system, under the historical background of reform, a series of new characteristics have emerged in the macro-economic imbalance, and the corresponding macro-economic policies have also produced a series of new characteristics. The limitations of demand management have become increasingly apparent, and the requirements for supply management have become more and more obvious. This part puts forward and demonstrates the judgment of the transition from demand management to supply management in the new stage of development and new argumentation, putting forward the policy proposal that passes argumentation according to the current macroscopical economy situation.

Part III: Structural Changes and Growth Efficiency in China's Socialist Market-Oriented Process.

Firstly, this part analyzes the evolution path of China's economic structure since the reform and opening up from the quantitative and qualitative perspectives. From the perspective of the high level of industrial structure, the process of industrialization entered an accelerated period after 1998. By 2006, China's industrialization process

had gone through a little more than one-third. This part analyzes the main influencing factors of China's industrial structure changes since the reform and opening up. Besides, it also studies the significance of industrial structure change to economic efficiency improvement from three perspectives. These studies show that in the 30 years from 1978 to 2008, although the changes in industrial structure once made a significant contribution to China's economic growth, with the improvement of marketization, the contribution of industrial structure changes to economic growth shows a decreasing trend, gradually giving way to technological progress. Especially after 1998, China's economic growth model has increasingly reflected its own sustainability.

Secondly, this part empirically analyzes the relationship between industrial structure, ownership structure, regional structure and China's economic growth. This part studies the correlation between industrial structure, ownership structure and China's economic growth through empirical analysis. Using the empirical data from China's reform and opening up, this part empirically investigates the role of market institutions as the goal of institutional change in resource allocation. Besides, this part tries to explain what kind of value orientation the market system should embody in order to adjust the reasonable economic structure through the market. Through the empirical analysis of the industrial structure, ownership structure and the interaction between the industrial structure and ownership structure of China's economy, it is found that the economic structure is unilaterally affected by the industrial structure or ownership structure, and also that the value orientation of market system plays a key role in the adjustment of economic structure through market.

Thirdly, this part analyzes the improvement of efficiency in China's economic growth since the reform and opening up and its impact on economic growth from two perspectives: factor productivity (labor productivity, total factor productivity) and input-output efficiency. Here, technological progress and industrial structure change are decomposed from factor productivity, and the contribution of industrial structure change to China's economic growth is empirically measured and compared with that of technological progress. Empirical research shows that in the 30 years from 1978 to 2008, although the changes of industrial structure once made a significant contribution to China's economic growth, with the improvement of marketization, the contribution of industrial structure changes to economic growth shows a decreasing trend, gradually giving way to technological progress. That is to say, the power of marketization embodied in the change in industrial structure will gradually give way to the power of technological progress. In addition, the study also found that the weakening of the effect of structural change does not mean that the benefits of market-oriented reform will disappear, and some development and institutional factors still hinder the further improvement of the efficiency of resource allocation. From this perspective, China still has a long way to go in improving the market mechanism. In addition, this part analyzes the change trend of China's intermediate consumption level since 1992 by using the input-output data over the years. The effects of technological progress, industrial structure change and price change on the intermediate consumption level of the whole national economy are studied through the direct consumption coefficient matrix and the intermediate demand consumption matrix

time series of the three industrial sectors. The research shows that during this period, technological progress contributed to the reduction of the intermediate consumption level of the national economy and the improvement of economic growth efficiency. However, due to the change of price relationship and the increase of the proportion of sectors with higher intermediate consumption levels, the intermediate consumption rate of the entire national economy reflected by the current price increased instead. In order to change this trend, maintain the sustainable development of China and improve the input-output efficiency of various sectors, we should combine it with the adjustment and upgrading of industrial structure.

In a word, the basic logic of this book is as follows: firstly, it makes an essential analysis of the institutional changes brought about by China's economic reform. At the same time, the prominent historical changes brought about by the reform itself are discussed in particular. From the analysis of the system changes and the characteristics of the reform itself, the historical value orientation of the system changes, namely the development criteria of historical materialism, is clearly understood. Then, according to this historical materialism, we can judge the basic value criteria of the justice and progress of social productive forces development in the change of social production relations, and analyze the economic growth in China's institutional change, including the pace of economic growth and the particularity of the total imbalance in the process of growth. At the same time, it examines the particularity of macro-control on the total imbalance in the process of the reform of China's socialist market economic system, and then recognizes the growth and balance of market-oriented transition. Further, it is to investigate the effectiveness and quality improvement of this growth process in depth. Usually, people have less doubt about the pace and scale of economic growth in China's reform. That is to say, to a large extent, they acknowledge that reform has brought about growth, but there are more doubts about whether effective development has been achieved. Based on China's experience (1978–2008), this book, on the one hand, analyses the evolution of structure resulting from China's economic growth, and at the same time examines the structural benefits of structural changes. On the other hand, it demonstrates the effect of efficiency improvement on China's economic growth from two aspects: factor productivity and input-output efficiency. On the basis of the above investigation, this book makes an analysis of the institutional causes of China's economic growth and development, and puts forward the requirements of institutional changes for the change of China's economic development mode and the realization of sustainable development.

The main contribution of this book, or more prominent innovation, lies in the following aspects. (1) From the perspective of value theory, it reveals the basic motivation of arguing the justice of institutional change in economic theory, and clearly judges the value standard of reform progress from the analysis of the characteristics of China's reform historical process, so as to answer why the process of institutional change is always accompanied by the development of economy. The debate about basic theory, scope, especially value theory? Why does the system change need to support from the aspect of axiology? (2) How to explain the causes of the increasing institutional change? How does China's experience of economic growth explain the

relationship between institutions and growth? What are the particularities of the total imbalance in the system transformation? In view of these particularities, what is the particularity of the aggregate demand and supply management, what is the significance of the aggregate supply management to the transitional society, and what are the system requirements? The answers to these questions not only deepen the understanding of China's reform and development experience, but also, more importantly, make distinctive discussions on macro-economic theories based on China's experience. (3) The most important is whether China's growth is the growth based on efficiency gains and therefore sustainable. This book not only makes an empirical analysis of the efficiency characteristics of China's economic growth from the aspects of the evolution of industrial structure, factor efficiency, input-output efficiency, etc. but also examines the motivation of the institutional reform behind the efficiency improvement, and then makes a more profound demonstration of the necessity and rationality of the reform. It is this emphasis on structural efficiency and total factor efficiency of economic growth. In the macro-analysis, besides considering the aggregate demand, the supply analysis is emphasized, and the macro-economic regulation and control mode, policy orientation and the corresponding micro-based market mechanism and order are further explained based on the demand of aggregate demand and aggregate supply and structural equilibrium.

This book is the final result of *Research on China's Market Economy Development*, one of the major research projects in the philosophy and social science research of Ministry of Education of the People's Republic of China. Liu Wei is the chief expert on this subject. The members are Xu Xiachun, Sun Qixiang, Huang Guitian, Lin Shuanglin, Wang Yuesheng, Liu Yi, Li Shaorong, Cai Zhizhou, Su Jian, Zhang Hui, et al. As a phased research results, around this basic theme "China's market economy development", four monographs were published in recent years; in addition, 34 academic papers were published in *Economic Research Journal*, *Social Sciences in China*, *China Industrial Economics*, *Journal of Financial Research*, *Journal of Peking University (Philosophy and Social Sciences)*, *Journal of Management World*, *Economic Perspectives*, *Economic Science* and so on. Among them, Prof. Liu Wei, the chief expert on the subject, has published 11 papers and one monograph.

This book is mainly based on the research results independently completed by Prof. Liu Wei from 2002 to 2008 and the research results completed in cooperation with Huang Guitian, Cai Zhizhou, Li Shaorong, Su Jian, Zhang Hui, et al. It is also the systematization and deepening of the research results of these 7 years.

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Part I

Characteristics of China's Socialist Market Economy Reform Process and the Value Judgment Criteria

This part consists of three chapters. Firstly, it discusses the progress and characteristics of the historical practice of China's economic reform, the historical evolution of the reform itself which brought about institutional changes, and value orientation and divergence of the reform from the analysis of the process of institutional change and reform evolution (Chap. 1). Then, it discusses the debate of economic theory on institutional change, especially on institutional reform and value orientation aiming at market economy (Chap. 2). Furthermore, on the basis of the analysis of the value orientation of the reform in practice and theory, this chapter examines the profound changes brought by the reform in China's economic development mode, and points out the internal relationship between the change of this economic development mode and China's economic growth and development. Or in other words, it analyses the reasons for the growth of China's economy from the changes of development mode, in order to clearly demonstrate the fundamental basis of the justice of reform in methodology (Chap. 3).

Chapter 1

What Historical Value Orientation Should We Take to Understand and Promote the Reform



With the historical progress of reform, China's economy has undergone extremely profound changes: on the one hand, the development of modernization and the improvement of people's living standards have achieved unprecedented achievements; on the other hand, the contradictions in the social progress are sharper and more complex. Therefore, it is inevitable that there will be controversy about the reform, at least, there will be serious difficulties in the consensus on the reform: Should we continue the reform? What kind of historical value orientation should be used to evaluate the reforms that have taken place? What historical values should we use to promote reform? All of these have become some issues of general concern. At the same time, they are also the problems that need to be solved urgently in the social development.

1.1 Social Economic Changes Brought by the Reform and the Historical Changes of the Reform Itself

1.1.1 *The Social and Economic Changes Brought by the Reform Are Mainly Embodied in the Institutional Change and Economic Development in China*

As far as institutional change is concerned, after 30 years of the reform and opening up, market mechanism has basically replaced planned system as the main mechanism of resource allocation in China, and price signal has replaced quantity signal as the main signal to guide resource allocation. Although there are still serious problems

The content of this chapter was published in the 5th issue of *Economic Perspectives* in 2006, as a stage achievement of the subject. Later, it was reprinted in the 16th issue of *Xinhua Digest* in 2006.

such as disorder and unfair competition while at the same time people still have different opinions on the quantitative judgment of the specific degree of China's marketization process, there is a general consensus that the market mechanism has fundamentally replaced the status of the planning system.¹ Besides, it is generally acknowledged that the speed of China's marketization is faster than that of all countries in transition, especially in comparison with Russia's economic transformation. China's marketization index or economic liberalization index is generally considered higher than Russia's; in international trade practice, more than 70 countries have recognized China as a market economy country.²

In terms of economic development, China's economic reforms have contributed unprecedentedly to China's economic development, whether in terms of quantitative indicators of economic growth or qualitative indicators of structural changes in the economy, the degree of economic development or the level of social development, the progress of absolute indicators or the improvement of relative indicators, the social and economic progress of China since the reform and opening up has been unprecedented. The level of GDP, whether in total or per capita, has increased more than 10 times compared with the level before the reform and opening up, with an average annual growth rate of more than 9.8% in comparable terms. The proportion of agricultural employment has dropped from 80% at the beginning of the reform and opening up to about 43% at present. The proportion of food expenditure (Engel coefficient) in the household consumption structure of urban and rural residents has entered a well-off society (over 40%) after subsistence-level (over 50%) from the poverty state at the beginning of the reform and opening up (over 60%). These profound changes are indeed unprecedented in the history of China's economic development. In terms of the pace of development, it is rare even in the comparison of the history of world economic development.

In fact, in order to achieve a social consensus on reform, we must first answer the following questions: Do we acknowledge that reform has promoted China's social

¹ Scholars in China have made abundant achievements on the progress of China's marketization, such as Lu Zhongyuan, et al., "The Impact of Marketization on China's Economy", *Economic Research Journal*, No. 12, 1993. Jiang Xiaowei, et al., "Exploration of China's Market Economy", *Journal of Management World*, No.6, 1995. Former State Development Planning Commission Research Group, "Judgment of China's Economic Marketization", *Macroeconomic Management*, No.3, 1996. Gu Haibing, "The Latest Estimation and Judgment of China's Marketization Degree", *Journal of Management Science*, No. 2, 1997. Chang Xiuze, et al., "The Marketization Degree and Development Thought of China's National Economy", *Economic Research Journal*, No. 11, 1998. Fan Gang, et al., "The 2000 Report on the Marketization Process of China's Regions", *Journal of Chinese Academy of Governance*, No. 3, 2001. Chen Zongsheng, et al., *The Study of Chinese Economic System Towards Market Economy*, Shanghai: Shanghai People's Publishing House, 1999. Li Xiaoxi, et al., *Report on the Development of China's Market Economy in 2003*, Beijing: China Commerce and Trade Press, 2003.

² In the reports of the Heritage Foundation and the Frazer Institute, the speed of marketization and the degree of economic liberalization of China ranked before Russia. In the analysis carried out by the World Bank, the speed of marketization in China was also among the top countries in transition. In the *Economic Freedom of the World: 2000 Annual Report* proposed by the Frazer Institute, China ranked 101, while Russia ranked 116. In the *2003 Index of Economic Freedom* published by the American Heritage Foundation, China ranked 121 and Russia ranked 131.

and economic development unprecedentedly? Does China's social and economic progress have a profound internal historical logical connection with the reform and opening up? Is social and economic development the most important or fundamental proof of the historical progress of the reform and opening up? Can contradictions and problems arising from the reform and opening up fundamentally negate its historical progress? Are the contradictions and problems in reform and development mainly caused by marketization itself, or are they mainly caused by insufficient depth of marketization and imperfect market mechanism? Is the objective existence of the contradictions and problems facing China's social and economic development a reason to negate the previous reforms or a new requirement for the further deepening of future reforms? In principle, the answers to these questions should be found and explained from the historical facts of the social changes brought by the reform and opening up in accordance with the basic methods of historical materialism.

After 30 years of reform from 1978 to 2008, we may be able to summarize the outstanding characteristics of the reform in China. In that case, the following characteristics are very prominent. (1) Basic purpose and institutional objectives of China's reform are to seek the unification of the basic system for the co-development of various ownership systems on the basis of socialist public ownership and the resource allocation mode in which the market is the basic force for allocating resources, that is, the socialist market economy with Chinese characteristics. It can be said that the real difficulty of China's reform, or its fundamental feature, lies in the unification of the public ownership of means of production and market mechanism, which is not only a breakthrough in the traditional dogma of Western economics, but also a development of traditional Marxist economics that negate the mutual integration of public ownership and market; it is not only a critique of the fundamental value of the so-called "Washington Consensus" regulated by Western value standard, but also the real difficulty of socialist economic reform. (2) The basic way and process of China's reform is to follow the principle of gradual progress, rather than the "shock therapy" advocated by Western scholars. This "gradual" reform is not only the price reform or some other specific reform that has taken a gradual approach, but also a gradual progress in an all-round way: under the conditions of significant urban-rural differences characterised by a dual economy, we should adopt the comprehensive reform of gradually transferring from rural to urban areas; under the condition that enterprises and governments are facing important institutional defects at the same time, we should first take enterprise reform as the core and then gradually transfer the reform core to reforms of government and social security system; in the process of enterprise reform, we should shift the reform core from state-owned enterprise reform to non-state-owned enterprise system innovation and reform; in the two inter-related but differentiated aspects of enterprise reform and price reform, the focus is gradually shifted from price reform to enterprise reform, especially the reform of enterprise property rights, and further to promote the transformation of reform in both aspects at the same time; in the major adjustment of economic relations dealt by the reform, the reform of distribution relations has gradually deepened into the essential field of production relations, especially the property rights relations; in the process of the reform and opening up, it has been gradually deepened from coastal

areas to the mainland; especially in the price reform, it has been pushed forward from the “double-track system” to the comprehensive market pricing. Generally speaking, in the way of reform, we should start from the most urgent aspects, start from the local aspects, and start from the areas where consensus is relatively easy to achieve, and gradually deepen and fully develop. On the whole, in the way of reform, we should start from the aspects of the most urgent need for reform, start from the partial parts, and start from the areas where consensus is relatively easy to achieve, and gradually deepen and fully develop the reform. (3) The basic logic and fundamental goal of China’s reform is that basing on the requirements of development and promoting development. If reform as a system change belongs to the transformation of production relations, then, according to the basic principles of historical materialism, the nature and movement of production relations fundamentally depend on the nature of social productive forces and the requirements of development. From the very beginning, China’s reform has clearly taken liberation and development of social productive forces as its fundamental purpose, and made it clear that “development is the absolute principle” and “development is the first priority”. That is to say, all reforms should radically obey the requirements of development. The objectives and processes of reform should be done according to the requirements of development, and the results of reform should be tested by development.

1.1.2 The Historical Progress of Reform Gives New Features to Reform

Reform is historical, so, after 30 years of reform progress from 1978 to 2008, what historical changes have taken place in the reform itself? Or rather what new features have been given to the reform by the historical progress?

1.1.2.1 Whether the Core of Reform or the Key to the Successful Reform Lies in Enterprise Reform? In Particular the State-Owned Enterprise Reform should be Transformed to Government Reform, Especially to the Transition of the Function of the Central Government

At the beginning of the reform and opening up, we clearly pointed out that the core of the reform and opening up in the new era is to invigorate enterprises, especially the reform of state-owned enterprises. The clarity of this reform core is fundamentally different from the core issues dealt by the previous system adjustment in China. However, after the reform progress since 1978, can we still say that the key or core proposition of China’s reform is enterprise reform, especially the reform of