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SOVIET UNION

Adjustment of Soviet Policy Toward Europe Analyzed

40050299 Beijing GUOJI WENTI YANJIU
[INTERNATIONAL STUDIES] in Chinese
No 2, April 88 pp 24-29

[Article by Zhu Yiqing [4376 6654 3237]: "Readjustment of Soviet Policy Toward Europe in Last 30 Years"]

[Text] Three years have elapsed since Gorbachev took office in the Kremlin in March 1985. During these 3 years, the new CPSU leadership headed by Gorbachev and guided by his "new ideas" in domestic and foreign policies after the 27th CPSU Congress, has laid down the basic policy of accelerating its economic and social development with its foreign policy designed and implemented accordingly. In other words, the Soviet Union would continue to proceed from the bipolar pattern, take full advantage of the tendency toward a multipolar world, improve its relations with the United States, and adjust its relationship with the countries on its European and Asian flanks in order to create a favorable international environment for an expeditious implementation of its strategy. What should be pointed out is that in implementing this general strategy at home and abroad, Gorbachev has attached great importance to Europe's role within the framework of Soviet diplomacy, and has accordingly readjusted the Soviet policy toward Europe with great emphasis on building a "European home extending from Atlantic to the Urals" in order to bring about a long-lasting detente, economic and political stability, and security. His action has attracted worldwide attention.

I

If we look at what Gorbachev has actually done to Europe after he took office in the light of what he called the three imperialist "focal forces" which are full of "overt and covert contradictions" and the "antagonism between the centrifugal and the centripetal forces" in his political report to the 27th CPSU Congress, it will not be difficult to find out that the overall strategy of the Soviet Union in treating the United States as its opponent, alienating it from Europe, and focusing its efforts in winning over Europe has remained the same. However, under the new conditions of struggles at home and abroad, the ideology behind the Soviet policy toward Europe has undergone some noteworthy changes. One of the main characteristics of this new ideology is that instead of constantly striving for military superiority in Europe and applying political pressure in its customary way, it has attached greater importance to the use of economic and political means for softening up and stabilizing Europe for a long-term cooperation. Up to now, the readjustment of Soviet policy toward Europe is generally shown in the following aspects:

1. In the military aspect, the Soviet Union began with the security issue—the most perturbing and sensitive issue for Western Europe. It admitted that "the quest for military superiority can bring no political benefit for anybody," and pointed out that since the present nuclear balance between the East and the West is already at too high a level, it is necessary to "bring the military confrontation down to a much lower level." It also proposed that military forces be "restricted within a rational limit" and that "equal security" should be maintained between them. All these gestures were designed to enhance the sense of security among West European countries. It should be pointed out that Gorbachev did make many partial and limited concessions as shown by his repeated disarmament proposals. For example, on such issues as leaving the discussions on British and French nuclear forces out of the U.S.-Soviet INF talks, the dismantling of medium-range and later medium-range and medium- and shorter-range missiles, the reduction of intermediate-range missiles in Europe and later in Europe and Asia simultaneously, the 50 percent cut of strategic weapons by both the United States and the Soviet Union, the reduction of conventional arms which Gorbachev agreed even on the non-system principle, and on-site inspection and supervision, the Soviet Union did consider the security of European countries as well as the actual requirements of its own interests on the disarmament question. The agreement reached by the East and the West in September 1986 in Stockholm within the sphere of the Conference on Security and Cooperation in Europe concerning confidence- and security-building measures; and particularly the US-Soviet agreement—in which both the East and the West made historical progress in disarmament and arms control—signed in December 1987 for the destruction of medium- and shorter-range missiles in Europe and Asia have produced, or are producing considerable effects on the development of East-West relations and the detente in Europe.

2. Politically, Gorbachev, after taking office, has altered the rigid Soviet stand in accepting the U.S. deployment of medium-range missiles in West European countries. He sought common ground with West European countries with "one Europe" as the main theme and launched frequent propaganda and diplomatic offensives. At the same time the Soviet Union took a series of measures to relax its relations with European countries. Since his assumption of office, Gorbachev has repeatedly emphasized the need for the Soviet Union to "firmly adhere to the principle of peace and peaceful coexistence," and the fact that "the Soviet Union has always viewed the world situation not exclusively from the standpoint of Soviet-U.S. relations." He also pointed out that Europe is "one of the basic areas of international activities" for the Soviet Union and that the European question has been "always the central question for Soviet attention." He favored the idea that Europe should "proceed from the elementary stage of detente to the stage of stable and mature detente," and "build a dependable security." His oft-repeated statements were that the Soviet Union is

first of all a European country, that Europe is "our common home," that "we live in the same Europe with you," and so forth. All these efforts were made to show Western Europe that the Soviet Union's foremost concern is with Western Europe's detente and stability and to accommodate European countries in order to win the confidence of West European countries. At the same time, the Soviet Union gradually restored and developed top-level contacts and dialogues with the major West European countries for a relaxation of their relations. After his visit to England in the name of a Supreme Soviet delegation leader at the end of 1984, Gorbachev invited Prime Minister Craxi of Italy to visit the Soviet Union in 1985 and he himself visited France for the first time in the capacity of CPSU General Secretary in the same year. In 1986, President Mitterrand paid a return visit to the Soviet Union, and in 1987, Prime Minister Thatcher of England, Prime Minister Chirac of France, and President Weizsacker of the FRG separately visited the Soviet Union. In the same year, Gorbachev went to Washington to attend the U.S.-Soviet summit meeting and to sign the agreement. On the way, he stopped over in England for an interview with Prime Minister Thatcher. The Soviet Union's action toward the FRG was even more noteworthy after Gorbachev took office. At first, he was cool to Chancellor Kohl because the FRG government had accepted the United States' deployment of intermediate-range missiles and signed an agreement to participate in the SDI plan. In July 1987, when Foreign Minister Gencher visited the Soviet Union, Soviet-FRG relations became relaxed for a time; but at the end of 1986 and the beginning of 1987, because of some ill-considered remarks in Chancellor Kohl's speech and the Soviet Union's consideration of the general election in the FRG, relations between these two countries were again strained. A formal thaw came in July 1987 with President Weizsacker's visit to the Soviet Union. Later, the Soviet Union supported GDR leader Honecker's visit to the FRG, and praised the FRG for taking the ultimately "constructive stand" on the Pershing IA issue. It also invited Strauss, Chairman of Christian Social Union—one of the major parties in power—and Prime Minister of Bavaria, to visit the Soviet Union. In early 1988, Soviet Foreign Minister Shevardnadze visited the FRG. Gorbachev's meeting with Chancellor Kohl was also tentatively scheduled for early 1988. Comments from external sources on what the Soviet Union did to the FRG was to the effect that in view of the FRG's economic and technical strengths and its role and position in NATO and the EEC, Gorbachev has realized that the reform and *glasnost* (openness) in the Soviet Union as well as its readjustment of Europe policy cannot proceed without FRG assistance.

3. The use of economic means to win over and to attract Western Europe has been all along a Soviet tactic. What is more obvious now is that through various channels including dialogues, propositions, and even expounding his views in writing, Gorbachev has tried hard to win understanding and support from various West European countries for its reform and "*glasnost* policy" and for a

long Soviet-Western Europe cooperation. The Soviet Union also took many practical measures for its external economic relations to serve its internal reform and construction. It requested to join the GATT and to establish relations with the International Monetary Fund and the World Bank; recognized the EEC as an economic and political entity; resumed its talks on the establishment of formal relations between EEC and CEMA; reformed its foreign trade system to include legislation concerning joint ventures with Western countries; and recently raised funds by issuing bonds through Western banks. What has attracted even greater attention is its efforts in establishing long-term economic, trade, and scientific and technical cooperation with Western Europe and signing agreements with the West European countries concerned on a century-long basis. Following the signing of a long-term agreement on economic and technical cooperation between the Soviet Union and England during Prime Minister Thatcher's visit in May 1987, Foreign Minister Shevardnadze paid a visit to the FRG during which the two countries decided to extend the 25-year economic and technical cooperation agreement, signed by Brezhnev during his visit to the FRG in 1978, for another 5 years, thus prolonging their economic contact and cooperation up to the 21st Century.

4. Gorbachev's "new ideas" in his Europe policy are also reflected in the readjustment of the Soviet Union's Eastern Europe policy. These ideas were quite evident when he advocated explorations by East European countries for economic and social reforms according to their national conditions. He also proposed that their foreign policies be conducted on an equal and independent basis, provided the "common interest" of the socialist community is preserved; and that while the CEMA is establishing its relations with the EEC, these countries can separately develop their bilateral trade and economic relations with the EEC. These measures were taken to meet the requirements of the Eastern European countries desiring to develop their relations with Western Europe. Along with the Soviet Union's adoption of an apparently relaxed policy toward Eastern Europe, there was a further development of the "small detente" between Eastern and Western Europe. Since 1987, the visits by GDR leader Honecker and Bulgarian leader Zhivkov to the FRG, originally scheduled for the autumn of 1984 but postponed under certain pressure, materialized. Premier Grosz of Hungary also visited Italy, while Honecker for the first time visited France, one of the three major powers responsible for the German Question. The Soviet Union's readjustment of its Eastern Europe policy was certainly necessary for improving the relations with its Eastern European allies. However, this action was taken not without consideration of the need to strengthen its West Europe policy through the development of relations between the East and the West. In supporting the development of political relations between Eastern and Western Europe, the Soviet Union, first of all, attempted to encourage Western Europe to feel at ease with Eastern Europe and to have more confidence in the Soviet Union. Second, it

encouraged Eastern Europe to turn to Western Europe for the technical and financial resources needed for their own economic development, and thus reduce the Soviet burden. Furthermore, through Eastern Europe, the Soviet Union itself could indirectly obtain the patent technologies it needs from the West. Finally, it can step up its work on Western Europe through its Eastern European allies. Honecker visited France soon after the INF agreement was reached, and took pains to explain that this agreement reflected the stand taken by the Warsaw Pact on the issues of disarmament and arms control.

II

There are profound reasons for the initiative taken by CPSU leadership, headed by Gorbachev, to ease and stabilize the European situation on a long-term basis through an adjustment of its Europe policy.

First, improvement of its relations with European countries would enliven its diplomacy in its pattern of diplomatic rivalry. Gorbachev's Europe policy was formulated after comprehensively weighing the pros and cons of the domestic and foreign policies of his predecessors, especially Brezhnev shortly before his tenure of office ended. Taking advantage of the United States's strategic retrenchment and the European detente in the early 1970's, the Soviet Union succeeded in achieving a general balance with the United States in their global and European regional military strategy. Later on, in striving for military superiority, it vigorously stepped up its armament and external expansion. It gained absolute superiority over NATO in land-based medium-range missiles particularly because of its deployment of SS-20 missile launchers in Europe. Its superiority caused grave concern among the West European countries. To meet this threat, Western Europe strongly urged the United States to increase its armament, and their action led to a supplement to NATO armament and the "dual resolution" in the talks. Firmly adhering to its rigid stand, the Soviet Union first rejected, and later suspended the talks. The West European countries, on the other hand, were united as one in their agreement to the United States's deployment of intermediate-range missiles. The actual outcome was that the huge military spending of the Soviet Union in developing SS-20's became a drag to its national economic development; its relations with West European countries deteriorated; a rare unanimity was achieved among the United States and the European countries on military defense; the intermediate-range missiles deployed by the United States in Europe, which could directly hit Soviet territories, had a high accuracy rate; and the Pershing II which could hit Soviet territory in 8-10 minutes increased the effectiveness of NATO's "flexible response." The Soviet Union also decided to counter NATO's supplementary armament by increasing the number of strategic nuclear arsenals in Eastern Europe, and this action led to dissatisfaction and opposition among the East European countries concerned. It was obviously incompatible with its original intention in

the deployment of medium-range missiles, and contrary to its basic strategy of dividing the United States and Europe by taking advantage of their contradictions. Furthermore, it affected its relations with the Western European countries as well as its Eastern European allies. In a recent talk with a *Novoye Vremya* correspondent, Deputy Foreign Minister Bessmyrtnykh said that the Soviet deployment of SS-20's in Europe in the late 1970's did not fit in with the most ideal strategy, because of its inconsistency with the Soviet concept of military strategy in Europe. This side episode revealed the intention of the new Soviet leadership to correct the mistakes in its former Europe policy. That was why Gorbachev decided to blaze a new trail for disarmament beginning with intermediate-range missile issue and for detente. This beginning touched off many contradictions of the West between the United States and Europe and within Europe itself, caused the removal of NATO's land-based intermediate-range missiles which is most effective for its "flexible response" strategy, and marked a breakthrough in disarmament. It also eased the East-West relations and enabled the Soviet Union to promote its relations with West European countries. This is undoubtedly a wise move by Gorbachev in a diplomatic game.

Second, long-term detente and stability in Europe are necessary for the Soviet Union's domestic reform and speedy strategic developments. After coming to office, Gorbachev coolly assessed the economic situation at home and abroad, squarely faced the difficulties in economic development and the "brink of a crisis" since the 1970, recognized the huge gap between Western developed countries and itself, and pointed out that all these troubles occurred precisely at the outbreak of the new technical revolution in the world. To accelerate its economic development and to keep abreast of the new technical revolution so that it could challenge the United States for superior national strengths in the 21st Century, the new Soviet leadership believed in reform as an "urgent need of the moment." In formulating the strategy of development and shifting the focus of domestic work to economic construction, the Soviet Union must solve two major problems.

First, there must be a large-scale disarmament in order to reduce the huge military spending, which then accounted for 14 percent of its GNP, and a fresh allocation of national resources. Europe has always been the strategic focus in a fierce controversy and the main area of military confrontation between the United States and the Soviet Union. In its controversy with the United States, the Soviet Union has spent huge amounts of manpower, money, and materials and borne a heavy burden. Now that the general balance gained by the Soviet Union with the United States in military strategy cannot be easily upset, even a fairly large reduction of its nuclear and conventional weapons cannot jeopardize its position as a strong military power. Thus provided that the existing strategic balance would not be affected, a

reduction in the scale and speed of its arms race will enable the Soviet Union to gain time and save money for modernization and improvement of its people's living conditions.

Second, it is necessary for diplomacy to serve domestic reform and construction. Along with the intensification of its domestic reform, the Soviet Union is making an all-out effort to establish economic relations with the West so that it can take advantage of the sharp contradictions and keen competition between the United States and Europe to gain economic and technical benefits on a large scale and through many channels. There are relatively greater geographical advantages and traditional influences for the Soviet Union in its development of economic and technical cooperation with Western Europe. For their trade development, there are also fairly favorable conditions, namely, Western Europe's need for Soviet raw materials, commodities, and market, and the Soviet need for Western Europe's manufactured products, foodstuffs, daily necessities, and the technologies and funds required for domestic modernization and construction. In technical transfers, Western Europe has a better chance with the Soviet Union, and particularly Eastern Europe, than with either the United States or Japan. The Soviet Union on the other hand attaches great importance to Western Europe in its economic and diplomatic activities and will treat it as an important trade and economic partner and the main channel for importing technology and funds.

Finally, in readjusting its Europe policy, the Soviet Union has spared no effort trying to divide America and Europe by taking advantage of their contradictions. Since the beginning of the 1980's, there have been increasing contradictions between the United States and Europe over economic, trade, scientific and technology, and monetary issues; marked differences in their attitudes toward the development of economic and political relations with the Soviet Union; and growing disharmony in military defense. Furthermore, the readjustment of military strategic thought brought about by the development of the SDI Plan, the growing isolationist tendency in the United States, and the importance attached to the economic and strategic roles of the Asia-Pacific region have combined to encourage the gradual reduction of U.S. commitments in Europe and to compel Western Europe to bear a heavier responsibility for their own security and defense. In the long run, if we do not dismiss the possibility that the U.S. Congress may gradually reduce its economic and political presence in Europe, Europe will play an increasingly active role as one of the poles in a multipolar world. The Soviet Union has accurately discerned this long-term tendency in the development of U.S.-European relations and made full use of their contradictions and differences on the economic, political and military strategic issues as a golden opportunity to readjust its Europe policy. This is the opportunity for it to make its presence more closely felt in Europe under the "we are also Europeans" slogan.

III

Gorbachev's readjustment of the Europe policy has already shown initial success. Now, all West European countries have universally agreed that proceeding from a desire to improve its own position and economy, the Soviet Union is really striving for a fairly long-lasting detente, and that provided its existing strategic balance is not jeopardized, it is prepared to reduce its nuclear and even conventional weapons by a fairly wide margin starting with the INF agreement. They also believe that despite the many obstacles encountered, the reform is not only necessary for its social and economic developments, but also a good opportunity to develop economic, trade, and technical cooperation between Western Europe and the Soviet Union. At present, despite their differences in degrees, the West European countries are facing Gorbachev's principle of *glasnost* with a positive attitude. Foreign Minister Gencher, who adopted this attitude a little earlier than others, recently called for a serious consideration of Gorbachev's "sincere desire for disarmament and cooperation," with the appeal that "we must not miss the opportunity given by Gorbachev's policy." He further pointed out: "This policy means internal and external openness, improvement of economic results, and channeling national resources to peaceful pursuits instead of arms race." Even Prime Minister Thatcher of England and the famous right-wing statesman Strauss of the FRG, who had always viewed the existing policies of the Soviet Union and the statements and actions of Gorbachev with reservation, have become positive in their stands after their meeting with Gorbachev. On his visit to Moscow, Strauss explicitly mentioned the need to "note the sincerity of the Soviet partner in the quest for reform," and advocated a long and extensive cooperation between the FRG and the Soviet Union. Of course, there are still many difficulties to be overcome before Gorbachev can finally succeed in his Europe policy.

1. Since the United States is the chief opponent of the Soviet Union and the Soviet Union's basic strategy, focussed on a struggle for Europe, remains unchanged, the present readjustment of U.S. and Soviet policies toward Europe does not mean their relinquishment of control over their respective allies, and even less their abandonment of Europe. The Soviet Union's readjustment of its Europe policy is still regulated by the basic contradiction, namely, the U.S.-Soviet rivalry.

2. Under the new conditions of a revived relaxation of East-West relations, Western Europe, for its own sake, are on the one hand willing to develop new economic and political relations with the Soviet Union, and, on the other hand, vigilant against possible Soviet threats. Remembering their lessons from the serious problems of West European security as a result of Soviet armament and external expansion during a detente, Western Europe is taking a close and serious view of every step taken by the Soviet Union under the new conditions of disarmament and arms control, and exercising every

precaution against possible tricks or pitfalls. The United States and Europe are now seeking to coordinate the plans of the West for a general policy to meet the next step of disarmament within the scope of the supreme NATO meeting. After the INF agreement, the West European countries are making every effort to strengthen their joint defense and to mend their weak security and defense links. These measures have led to strong Soviet reactions. The important question of any breakthrough in the development of relations between Western Europe and the Soviet Union now depends on whether the latter can truly reduce its threat to European security. It is anticipated that when a certain form of agreement on a 50 percent reduction in strategic nuclear weapons is reached, the next step will be for the East and the West to conduct talks on the reduction of chemical weapons and conventional forces in Europe. These talks, especially those concerning the European-wide conventional forces, will be far more complicated than those about intermediate-range missiles. Although the Soviet Union has admitted the imbalance of conventional forces in Europe, and expressed its willingness to reduce them on an asymmetric basis, and even granted that the Soviet Union may offer certain voluntary concessions at the meeting, there will be acrimonious bargaining by both parties. Therefore, we cannot be over-optimistic about these talks. They may eventually be successive, but the psychological pressure exerted by Soviet Union's geopolitical superiority cannot be basically eliminated. If we will take a medium- and long-range view of the situation, it may happen that after the 50 percent reduction of strategic nuclear weapons, the Soviet Union will still have problems with the independent nuclear forces of England and France.

3. There are still certain unfavorable elements in the development of economic and political relations between Western Europe and the Soviet Union. For the Soviet Union, the main problem is with the weak structure of its commodity exports. What it exports to the West is mainly petroleum and natural gas, which combine to account for 80 percent of its foreign exchange earnings. Because of the drastic drop of oil prices and the devaluation of the dollar 2 years ago, the Soviet Union lost quite a lot of foreign exchange and this loss affected its imports from Western countries. Furthermore, because of the weak competitive power of its processing industry, the proportion of manufactured products in its exports is dropping and its commodities exported for foreign exchange are in short supply. These conditions cannot be basically reversed in the near future. Again, its agriculture has always been a liability to its foreign trade, because a fairly large portion of the foreign exchange obtained through exports had to be used to finance the import of agricultural foodstuffs. To remedy the shortage of funds from the drastic reduction in foreign exchange earnings, it borrowed \$6 billion from Western banks and another \$15.5 billion from government and private banks in 1985 and 1986, and by the end of 1986, the Soviet government was \$38.2 billion in debt. For the development of economic and technical cooperation in a

new form, it proclaimed the joint venture law in early 1987 with a view to improving the supply of certain industrial products, raw materials, and foodstuffs in the country; imported the advanced techniques, technologies, and management expertise it needed; developed the bases for foreign exchange earning exports and reduced the irrational imports; and brought in Western materials and funds. By the beginning of 1988, it has set up more than 20 joint ventures with the West. In Western Europe, the countries are willing to continue and expand their economic and industrial cooperation with the Soviet Union, including the establishment of joint ventures. Up to now, however, Soviet conditions for investment are not quite propitious. Legislation for agreements on the protection of investment is still under deliberations, and a fundamental reform of its rigid system is no easy matter. The Western European countries are still weighing the opportunities for cooperation against the risks involved before making their decisions. Because of the COCOM's embargo list of materials and technologies against the Soviet Union, the economic, trade, and technical contacts between Western Europe and the Soviet Union are still restricted to a certain extent. On his meeting with people in the economic circles of the FRG not long ago, Shevardnadze sternly accused the COCOM for restricting exports to the Soviet Union and the other socialist countries, and blamed these restrictions for Soviet Union's failure to embark on 20 large projects and for affecting the talks then in progress between the Soviet Union and the FRG on cooperation in 30 projects. For the reasons just mentioned, there can hardly be any breakthrough in the development of economic and trade relations between the Soviet Union and Western Europe in the near future, although, in the long run, there is still considerable potential for the development of their economic relations.

4. In readjusting its Europe policy, the Soviet Union is still faced with some other sensitive and complex problems. There is, for example, the worry about Western Europe's attempt to step up their economic, political, and cultural infiltration and to accelerate the peaceful evolution of Eastern Europe by taking advantage of the latter's economic difficulties and the elements of instability of varying degrees brought forth by the reform and the *glasnost*. Another particularly sensitive problem is with the Germany question which may involve the whole of Europe and even the East-West structure. For some time, rumors were rife in Europe, especially in the FRG, that Gorbachev will some day raise the question of Germany's unification, and that he has already ordered a research to be conducted in the choice of Germany's future, including the combination of two Germany's to form a Confederation of Germany and the withdrawal of Warsaw Pact and NATO from East and West Germany respectively. We have heard that some Soviet officials are also privately sounding out the FRG. Following the development of relations between the two Germany's, the historical visit of GDR leader Honecker to the FRG, and the possible development of relations between the

Soviet Union and the FRG, speculations on the direction of policy developments in East and West Germany, and the fear that the Soviet Union may trade the unification of Germany for the neutrality of two Germany's are now daily increasing. The adjoining countries east and west of Germany are closely watching the developments of the Germany question. We can assert that even Gorbachev's "new ideas" about the Europe policy and the "European home extending from Atlantic to the Urals" he conceived will not, and cannot steer him away from this knotty Germany problem.

On the whole, the Soviet Union is still proceeding with the readjustment of its Europe policy. In the past 3 years, Gorbachev has on the one hand pushed his all-out diplomacy, and, on the other hand, shifted the focus of Soviet diplomacy to the United States. Because of the detente from the INF agreement, there is now more maneuvering room for Soviet diplomacy, and the Soviet

Union has obviously stepped up its work on Europe. Since the end of 1987 and the beginning of 1988, the exchanges of high-level visits between the Soviet Union and the West European countries have markedly increased and the former's work on the FRG have been particularly spectacular. In view of the presidential election in the United States this year and the difficulties which the Soviet Union may still encounter in developing its economic and political relations with Japan, its need for technology and funds from Western Europe will be even greater when its domestic reform enters its second stage. Therefore, we cannot dismiss the possibility that after the fourth summit meeting this year, the meeting between Gorbachev and Chancellor Kohl will reach a high tide, and the Soviet Union may shift the focus of its diplomacy to Western Europe.

9411

NATIONAL AFFAIRS, POLICY

Discussion on Deepening Economic Reform in 1988

40060332A Beijing JINGJI RIBAO in Chinese
24 May 88 p 2

[National Committee on Economic Structural Reform, Production System Bureau: "How To Perfect the Contract Management Responsibility System."]

[Text] Not long ago, the State Council ratified the State Commission for Restructuring the Economic System's 1988 plan for deepening the economic structural reform, which points out that the emphasis of this year's economic structural reform is to coordinate, perfect, deepen and develop the enterprise contract management responsibility system, and deepen the reform of the enterprise management mechanism. To solve the problem of separating government and enterprise in enterprises owned by the whole people, and separating ownership and management while not changing ownership rights, we must hand over to the enterprise the right of holding, right of use, and right of allocation of the publicly owned enterprise's assets. This in order to strengthen the management responsibility of the enterprise, to enable the interests and the results of the enterprise and its workers to be linked and fluctuate together. This in order to actually step by step advance enterprises on the road to market competition and assumption of sole responsibility for their own profits or losses.

According to statistics, by the end of 1987, under the national budget, 78% of industries are already practicing some form of the contract management responsibility system, including 80 percent of the large- and medium-sized enterprises. Among these, the large- and medium-sized enterprises of Beijing, Jilin and other provinces and cities have basically all implemented contractual operations. Approximately 65 percent of large- and medium-sized enterprises have long-term contracts.

Experience shows that the contract system is in keeping with the level of economic development of the elementary stage of socialism in China and the state of mind of the masses, and so it has a powerful vitality to it. Implementing the contract system has strongly aroused the enthusiasm of the managers and the workers, and enterprises have achieved definite beneficial results. According to statistics, under last year's budget the output value of industries grew by 11.3 percent of the 1986 level, worker productivity grew by 7.6 percent, receipts from sales grew by 17.1 percent, realized profits and taxes grew by 9.9 percent, and profits and taxes actually turned over to the government grew by 6.7 percent.

At present, what draws one's attention is that each area, in perfecting its contract system, is trying out various kinds of new experiments in reform. For example, there are enterprises contracting other enterprises, transfer of the possession of the property rights of enterprises, etc. This allows superior enterprises to acquire the property rights of inferior enterprises, so that the productive forces can be organized anew, and thus promote a reasonable adjustment of the industrial structure, the enterprise structure, and the product options. This increases the intensity of operations. We can foresee that 1988 will be a year in which the contract system will achieve even greater benefits. To this end we must on the one hand perfect the development of the contract system, and furthermore we must use this as a foundation for conducting new experiments in reform. We should especially carry out the following kinds of work:

1. We must actively bring in the mechanisms of competition. We must use public bidding and other methods of selecting the best managers. From now on, medium-sized enterprises on down in general should all introduce the competitive mechanism, invite tenders to contract for a base amount, and invite applications for jobs from managers. They can select managers from their own enterprise or from other enterprises of the same industry, or they can accept applications from the outside. Large-scale enterprises can generally first bring in the mechanisms of competition by contracting with their branch factories; and step by step, through contracts within the large-scale enterprise, bring in the mechanisms of competition, accumulate experience, and create favorable conditions. Each area, according to their own situation and needs, should set up for enterprises a marketplace for public bidding, for providing both parties in a contract, those proposing and those accepting contracts, with information and conditions for making wide-ranging contacts.

2. The solemn nature of a contract must be upheld, and the rights and interests of the managers of the enterprise must be protected. The signing of any contractual agreements should be notarized, and as soon as a contract is signed it should carry legal weight. Neither party should be able to modify it any way they please. But especially all levels of government should emphasize upholding the solemn nature of contracts. They should protect the interests of managers of enterprises, and not try to interfere as they please through administrative decrees. At present, to carry out the job of making sure that contracts are fulfilled, those who should be rewarded should be rewarded, those who should be penalized should be penalized. At the same time, the work of auditing contracts during their course should be carried out.

3. We must further perfect the mechanisms of enterprise self-restraint. Contracted enterprises should, through making internal reforms, tap their capacities, perfect their management, and increase their economic benefit. At the same time, in making contractual agreements,

they should stipulate that the enterprise must strictly carry out the nation's pricing policy. They must not indiscriminately raise prices or covertly raise prices. In key enterprises we must further carry out the "two guarantees and one link" contract system in order to ensure the technological reform of the enterprise and ensure the prevention of the inflation of their consumption funds. The number of enterprises practicing the linkage of total wages with economic benefits will increase gradually.

4. We must gradually build a system for enterprise risk funds, to strengthen the ability of enterprises to bear losses. Along with the growth of the enterprise's retained profits, those enterprises that can should take out a certain amount of funds from their retained profits to be the enterprise's risk fund. Also they can implement an employee pledge system. The enterprise's cadres and employees will, according to their amount of responsibility and their risk to the enterprise, pay a certain amount as a security deposit.

5. Along with strengthening and developing the contract system, we must carry forward the various internal reforms of enterprises. We must further practice the factory director responsibility system, the term of office target responsibility system, etc. We must popularize "the full load work method" and "the within factory bank." We must form a system for the internal goals of enterprises and an internal network system for the economic responsibility system. We must reform the labor system, extend the range of the contract system, practice the labour composition system and reform the internal distribution system of enterprises.

6. We must continue to develop towards economic cooperation, and promote the adjustment of the economic structure. Through enterprises contracting other enterprises, the transfer of the property rights of enterprises and the implementation of a stock system, we can overcome the rule of the "three unchangeables" (the unchanging form of enterprise ownership, subordinate position of enterprises, and channels for turning in money to public finances). It is especially necessary to encourage industries and scientific research units to cooperate together. This is in order to gradually form a lot of powerful enterprise groups, to develop economies of scale, and to actively enter the international market-places and join in international competition.

13418

Coordinated Reforms, Operation Mechanisms in Beijing Industry

40060320 Beijing ZHONGGUO JINGJI TIZHU
GAIGE [CHINA ECONOMIC SYSTEM REFORM] in
Chinese No 4, 23 Apr 88 pp 17-19

[Article by Yin Zhonghua [6892 6850 5478]: "Reforms in Beijing Industry Begin To Pay Off"]

[Text] In 1987, Beijing industry launched the contracted management responsibility system in its many forms across the board, zeroing in on key enterprises. The core

of the contracted management responsibility system is "two guarantees and one link." Of the 435 enterprises under the municipality's 18 industrial corporations, bureaus, and offices, 432 have adopted contracting. Of these, over 90 percent have adopted the "two guarantees and one link" system. The contracts will remain unchanged for 4 years. In addition, 196 small and medium-sized enterprises and collective enterprises are experimenting with bidding and leasing and four enterprises are carrying out pilot projects in share-holding and the asset management responsibility system. As reform becomes more and more thoroughgoing, we have mapped out a development approach suited to the characteristics of Beijing industry. Practice over the last year proves that contracting has prevented a decline in production and powerfully fueled the growth in production efficiency in Beijing industry.

What lies at the heart of reform in 1988 is coordinating, furthering, developing, and perfecting the contracted management responsibility system. We put forward a reform proposal to achieve 10 external and internal coordinations aimed at achieving the goals of contracting and perfecting enterprise operating mechanisms:

The ten internal coordinations refer to the following: formulating a good development strategy; perfecting an internal economic responsibility system; establishing a comprehensive management-by-objective system; promoting technical progress; accelerating technological transformation; introducing competitive mechanisms; recruiting cadres and improving worker caliber; reforming the management system and introducing a simulated market; reforming the distribution system; encouraging exports and the earning of foreign exchange; introducing modern management; and nurturing entrepreneurship.

—Generally speaking, there are three ways to integrate contracting closely with the enterprise development strategy: 1) "Guarantee" means ensuring the realization of the development objectives of the Seventh 5-Year Plan; 2) Use long-term planning to guide short-term arrangements; and 3) After the contract is written up, the enterprise should revise the original development objectives in light of new demands.

We demand that all enterprises which have gone in for contracting work out and perfect a strategic development plan within the first half of the year based on new conditions.

—Perfect the factory director responsibility system. Establish a new framework and map out a new path in accordance with the requirements of a full-fledged factory director responsibility system, the separation of government from party, and the strengthening of democratic management. Over 90 percent of state industrial enterprises in the municipality have adopted the factory director responsibility system. They are required to

implement a director tenure objective responsibility system, a director tenure auditing system, and end-of-tenure auditing system in groups and stages within the first half of the year.

The implementation of the factory director responsibility system across the board, under which the director assumes full responsibility, will inevitably lead to a string of changes in ideological and political work within the enterprise as far as division of responsibility, management system, work organization, contingent construction, and substance are concerned. There is thus a need to gradually establish a suitable political and ideological work system. It will be a great ideological and political work system bringing together the experts and the masses. While administrative cadres will be its core and political cadres its backbone, the system will also embrace the rank-and-file party and league members and active elements.

—Implement the internal economic responsibility system and a comprehensive management-by-objective system in the enterprise, focusing on contracting. We should integrate the enterprise contracting objectives closely with development strategic objectives, promotion objectives, double increases and double economizing, and factory director tenure objectives and, through the economic responsibility system, bring about a network of objectives that go vertically as well as horizontally. At the moment, 92 percent of enterprises have carried out contracting down to the workshop level and 77.3 percent to the level of teams and groups. Beijing Switch-gear Plant has made "five objectives" part of the factory director tenure objectives and laid down the objectives which must be accomplished during the tenure of the present director. In drawing up the factory's annual plan, they take the highest value of the five objectives to be the factory's objective as well as the highest value to ensure the economic responsibility system. After factory objectives are set in accordance with the decision-making process, various economic, technical, and management targets are decided upon through systems engineering methods for implementation by departments, teams, groups, and individuals level after level. They use the general design of the economic responsibility system to define the enterprise's overall objectives, tasks, and goals so that they are coordinated, interrelated, consistent from year to year, structurally coherent, and forward-looking. The result is a factory-wide comprehensive management-by-objectives system. In conjunction with the perfection of an economic responsibility system and the reform of the distribution system, 93 percent of our enterprises have pegged total payroll to economic performance. Thus the enterprise is free to decide distribution while staying within its total payroll. The overall opinion is that the enterprise should be allowed to experiment boldly in distribution methods suited to its actual conditions. As for working out the relationship between the manager's income and that of

the worker, certain enterprises have obtained some tentative ideas. In addition, they should seriously emulate and popularize the "full load work method" and the within-factory banking."

—Speed up technological transformation in a snowballing way. "Two guarantees and one link" encourages enterprises to make technological transformation an objective they must achieve, in contrast to the past when the two ends (profits to be turned over to the state and rewards to be given out to workers) were ensured at the expense of technological transformation. As a result, enterprises lacked staying power.

After contracting came into existence, as the enterprise increasingly became the primary source of investment, it came face to face with an important question: How to tap the enterprise's potential to the full within the time frame of the contract so as to make capital beget capital, add value to its assets, and increase its material and financial resources for self-development to the greatest extent possible? To put it differently, after contracting was introduced, the enterprise must make use of everything it has to increase its capital and assets. This requires that it put its limited funds to good use and keep reinvesting them to achieve a snowball effect. How to evaluate the "two guarantees," an important part of the "two guarantees and one link" principle, is a complex issue. After repeated discussions, we decided not to put the enterprise through a cumbersome process. Nor did we peg the evaluation to the total payroll. This is because the purpose of contracting is to delegate power to enterprises more effectively and give them a free hand. All we asked of the enterprises, therefore, is that they keep to the investment total in the contract and make annual planning for the import of key technology and major technological transformation projects to measure their annual progress and incorporate it into the scope of the factory director tenure auditing and final auditing for evaluation.

—Introduce the competitive mechanism into the personnel area and reform the personnel and labor system. We looked at cases on an individual basis and made it clear that there should be relative stability among the first contractors at the factory leadership level who have already signed contracts. We analyzed each and every one of the leaders at the 100 key enterprises particularly carefully and concluded that over 90 percent are up to their tasks. It was then that we put forward the principle of relative stability. That is, the leaders should not, in principle, be removed during the contract period. If removal is necessary, it must be reported to the higher authorities for approval. When an operator is of a poor quality, when the leading group lacks unity, and in cases of mismanagement affecting the fulfillment of contracted tasks, open bidding and recruitment may be used to select a new operator, provided approval has been obtained from the higher authorities. A small number of enterprises may be chosen to carry out a pilot project in which the first contractor is free to directly recruit

deputy factory-level cadres on his own, reporting to the higher authorities for the record only. First contractors with outstanding performance may be given preference in having their contracts renewed. Age restrictions should be eased as appropriate. Middle-level cadres should be chosen through open bidding and recruitment. Similar methods should be used to pick rank-and-file cadres. On the basis of a clear definition of worker responsibilities, we should introduce an optimal combination system and system to promote the circulation of qualified personnel within an enterprise so that they are deployed rationally.

—Establish a management assurance system in six areas to modernize management. The practice of contracting proves that contracting must be effected through management. "Contracting" should promote, not replace, "management." Last year, we made enterprise upgrading our central goal and reformed specialized management and established six management assurance systems, targeting quality, consumption, and efficiency. The result is that gradually enterprise activities perpetuate themselves in a positive way. The six management assurance systems are as follows: quality management assurance system, whose goal is to raise product quality and adjust the product mix, resulting in continuous product upgrading; materials management assurance system, whose goal is to lower materials consumption and raise the raw materials utilization rate, resulting in continuous improvements in materials circulation within the enterprise; financial management assurance system, whose goal is to lower the percentage of funds used and improve fund circulation rate, resulting in a continuous positive flow of inputs and outputs; equipment management assurance system, whose goal is to make full use of enterprise equipment and raise equipment operating efficiency, resulting in equipment that is continuously functional; personnel and labor management assurance system, whose goal is to utilize qualified personnel soundly and mobilize worker initiative fully, resulting in on-going personnel development; and information management assurance system, whose goal is to strengthen basic work and raise the level of quotas, resulting in a smooth flow of information for the enterprise.

The standards for the establishment of the six management assurance systems are as follows: developing a set of goals for specialized management; setting up specialized management machinery run by managers with bold thinking and qualities; perfecting the basic work for specialized management; adopting the modernization methods of management for the specialty in question; and applying the computer in specialized management. On the basis of these six systems, an overall pattern of activities for the enterprise should be created to form a modern enterprise management system.

—Integrate contracting with exporting and the earning of foreign exchange to enhance the ability of the enterprise to export and earn foreign exchange. In a number

of enterprises with substantial exports, we incorporated exporting and the earning of foreign exchange into the "two guarantees and one link" and pegged the total payroll to export value and foreign exchange earned. We also worked out and implemented policies on exporting and foreign-exchange earning and appropriately corrected those conditions resulting in less profits for enterprises that exported and earned foreign exchange.

We propose the following major external coordinated reforms to further improve the external environment for contracting:

1) Insist that accounts be settled with enterprises and contracts be honored.

When a contract is completed early, the enterprise can plan and make a profit early. With this idea in mind, we began tackling contract fulfillment aggressively last October in accordance with the following principle: adhere to the base figure, ensure that what is due the state is turned over, retain the surplus, and make up for the deficit.

We worked at both the revenue end and the expenditure end. The enterprise pays taxes as required under Phase 2 of the plan to replace profits with taxes. What is in excess of the target is returned by the finance department to the enterprise to be spent mainly on technological transformation. The first problem we ran into was this: Should accounts be settled with the enterprise or the general corporation? This issue was debated for more than 1 year. We insisted that accounts be settled with enterprises as that is the only way to really fulfill a contract. The finance department worried whether this could ensure that money would be turned over to the state. We analyzed each contracting enterprise, projected the results of enterprise account settlement, and concluded that there was enough money to be turned over to the state. This put the concern of the finance department to rest. The contract was honored for those enterprises which over-fulfilled the contract. Enterprises which failed to fulfill the contract and had difficulties making good the deficit in one shot were "given credit" and allowed to do so next year. In addition, problems in contract fulfillment were resolved reasonably. For instance, an enterprise is usually required to absorb the extra costs resulting from increases in raw materials prices. Special cases, however, were worked out equitably.

2) Determine the contracting base figure and growth percentage scientifically and reasonably.

When we wrote contracts in 1987, we usually took the sum turned over in 1986 as the base figure, a Maginot line that must not be crossed in order to ensure income for the state treasury. This necessarily resulted in an unequal distribution of burden. In our opinion, 4-year contracts that have already been signed should remain unchanged in principle, while adjustments may be made

on a case-by-case basis. The Textile Bureau, for instance, has revised base figures that have been excessively low for certain enterprises. In writing new contracts or in inviting bids, we should determine the base figure as scientifically and rationally as possible. Apart from comparing itself to other enterprises, the enterprise should make inter-industry comparisons and consider them in light of industrial structure adjustment and product mix adjustment. The growth percentage should reflect the development policy. It should be appropriately lower in the case of enterprises that have to be developed, and vice versa.

3) Organize a contracting market.

We should introduce additional competitive mechanisms and risk mechanisms into contracting. When a contract remains unfulfilled because the product does not sell well or because of mismanagement, the enterprise must make up the difference out of its own pocket. In addition, a manager should be selected through open recruitment and the enterprise may be leased, merged, transferred, or sold, depending on the situation. We should break down the barriers of departmentalism and bridge occupational differences by encouraging inter-enterprise and inter-industry contracting. Also, we should encourage institutional cadres and intellectuals from scientific research units and institutions of higher education to go into contracting. We propose to organize a contracting market to be made up mainly of the party who offers the contract, the contractor, the notary, and the insurer. In the present situation, the party who contracts a service consists of the commission, four bureaus, and two offices acting as the representative of state assets. The contractor may be an individual, an enterprise, or a contracting corporation. The municipal enterprise association and the municipal society of factory directors (managers) are planning to establish contracting companies in the business of recommending qualified personnel, offering consulting and training services, and providing information. The notary should discharge three sets of functions: first, asset evaluation and the verification of the contract base figure; second, supervision of the implementation of the contract through economic means; and third, auditing. The notary, therefore, should be a notary organization, the auditing department, or the evaluation department. There are plans to consult with social insurance organizations. Right now, the existing social insurance company should enter the new business of contract insurance.

4) Continue to come to grips with pilot projects in share-holding and experiment with new reforms.

Already there are such experimental share-holding enterprises in Beijing as the Liyuan Share-holding Co. Ltd. and the Station Wagon Share-holding Co. Ltd. We

propose to develop another batch of experimental share-holding companies after reviewing the experience of existing experiments. We also plan to select some enterprises as test sites for experimental fund sharing.

12581

Reexamination of Consumption Levels

40060331a Beijing JINGJI RIBAO in Chinese
27 May 88 p 3

[Article by Zuo Chunwen [1563 2504 2429]: "A Deeper Examination of Current Consumption Levels Is What We Need To Judge Consumption Correctly: We Should Not Be Overoptimistic about the Overall Consumption Picture, Even Though Statistics Indicate That, after Adjusting for Inflation, the Real National Wage Bill Rose by 3.3 Percent in 1987 and That Real Per Capita Wages Rose by 0.28 Percent, Which Is Lower Than the 9.3 Percent Posted for National Income and the Growth Rate Registered in Labor Productivity"]

[Text] Economic analysts are accustomed to using wage incomes to measure standards of living and wage raise rates to determine whether or not growth in consumption is appropriate. But when this approach is applied to consumption in 1987, statistical data and real life come into clear conflict.

In 1987, money wages rose by 9.2 percent, 6.6 percentage points less than the rise recorded in 1986; the employee cost of living index stood at 8.8 percent, 1.8 points higher than in 1986; per capita social commodity retail sales volume rose by 15.2 percent, 0.2 points higher than 1986; and urban-rural resident savings deposits rose by 40.5 percent, 1.5 points higher than 1986. These data suggest that money wages were low, that the price index was high, and that social commodity retail sales and savings expanded rapidly. But such conditions are anomalous and, strictly speaking, cannot really be true. Clearly, the data supplied by the traditional indices to evaluate consumption levels is unlikely to yield correct conclusions. Instead, we must take into account the new problems that have been engendered by the shift from the old to the new economic systems. When this is done, our suspicions are borne out.

Problem Number One: Wage income statistics do not include nonwage income.

The current urban-rural resident income index system essentially measures wage income and thus is rooted in highly centralized planned economy. Yet the socialist market economy continues to function, and there have been at least two marked changes in income distribution relationships in the transformation of the old economic system: (1) Resident incomes have shifted from a monolithic channel comprised of wages to a variety of channels; and (2) income distribution is no longer administered solely by the government but has become a dual system in which both the government and the market

mechanism participate. The current index system does not reflect these changes very well at all. And as the socialist market develops and matures, the marketplace is playing a greater role in distribution, which means that employees are receiving more and more income through nonwage channels. Statistics show that nonwage earnings equal more than 40 percent of and are growing at a rate 20 percent faster than that of the total wage bill. At the 40 percent rate alone, nonwage income would have totaled 74.6 billion yuan in 1987. When this amount is factored in, it becomes clear that total per capita income in 1987 definitely rose by much more than the 12.4 percent posted for the total wage bill.

Problem Number Two: Under the market distribution mechanism, a considerable proportion of income is obtained through underground channels, which means that that share escaped statistical and financial detection and that some of that share was obtained illegally—by diverting state profits into private pockets or by using enterprise productive capital for personal consumption. Numerous investigations have indicated that individuals profiteer through the following underground conduits.

A. In the name of their enterprises, individuals siphon off revenues that are supposed to go to the state and then divert these moneys into their own pockets. The principal ways in which this is done are as follows.

1. Enterprises keep second sets of books and thereby cheat the state and fatten individuals. Investigations show that enterprises do not report income arising from outside manufacture, from selling off producer goods and materials and commodities, or from after-sales operations and instead enter these earnings as "petty cash," which they distribute to employees as bonuses or under other guises.

2. Units collude for illicit gain. The main ways this works are (a) state units grant profits to collectives, which return the favor; (2) enterprises trade products back and forth, which are distributed to employees, reported as damaged and entered on the books as costs; (3) units give each other fees under such guises as technical consulting or services; (4) one unit will give another a fraudulent invoice and pocket a percentage of the take as a good-favor fee.

B. Individuals fleece the state or their units in the following three ways.

1. They manipulate the double-track price system. Some people use their personal authority or connections to sell capital goods or scarce commodities, which they obtain at parity prices and peddle at exorbitant rates, profiteering as middlemen.

2. Some government agencies and mass organizations shake enterprises down for funds, goods or assistance without authorization and then use the cash or all of these proceeds to distribute as bonuses or for banqueting.

3. Some people exploit the business ties of their units to extort favors from business partners.

C. Policy loopholes are exploited to skim nonlabor income. The primary loopholes are:

1. The wage-share quota per 100 yuan of output system, which is manipulated in the following ways: (1) Construction costs are overestimated so that the wage share is increased; (2) more raw materials are procured than necessary so that units can use the leftovers to claim bonuses for "economization" on material use; (3) construction work is subcontracted out at lower rates than provided for in original contracts, with the difference being pocketed by the original contractors.

2. The defects in the free medical and expense accounting systems. Last year, the RENMIN RIBAO exposed a medicine-gobbling "specialized household" in Xian that obtained several thousand yuan worth of free drugs, which the household claimed it was taking but was actually selling.

D. Indiscriminate distribution of material rewards and subsidies.

1. Some units are passing out more and more varieties of better and better material rewards, which goods are obtained through the following channels. (1) They are defrayed out of enterprise welfare funds. For example, enterprises allocate money they claim to be using to subsidize canteen losses to purchase such goods. (2) Labor insurance expenditures are overpaid or increased. For example, units substitute high-grade clothing for work uniforms by issuing workers material, which is then used to make the clothes. (3) The cost of the goods is defrayed out of workshop expenses or enterprise administrative outlays, and the resulting increase in employee incomes is transformed into greater social-group purchasing power.

2. In some enterprises, allowances for meals employees are forced to miss as a result of their work have become a regular part of employee incomes.

These conduits of underground income are widely known and have attracted much attention. Thus one can imagine that they add up to a hefty sum. Regrettably, however, it is impossible accurately to determine what that sum might be.

The above analysis indicates that the figures for employee wage income and urban-rural resident incomes are understated. To be complete, resident incomes would have to include recorded incomes + nonwage

incomes + earnings individuals obtain through underground channels. (There is bound to be some double counting in the total.) Thus 1987 consumption can be expressed with the following formula: The true growth in the actual, total incomes of urban and rural residents + 19.5 percent of the purchasing power wielded by social groups + 11.7 percent of the net per capita productive income of peasants = continued excessive growth in consumption demand. This conclusion is corroborated by the facts that the gap between commodity supply and purchasing power continued to worsen in 1987, when it stood at 78 billion yuan, compared to 5.6 billion in 1983, and that the shortfall of supply relative to demand rose from 1.8 to 12.89 percent during the same period. Thus we can conclude that since 1981 consumption has consistently grown too rapidly, which fact has been concealed.

The masking of excessive growth in consumption is even more harmful to economic development than was the obvious excessive growth of the first several years following 1981. For the concealed growth obscures normal economic relationships and creates greater problems for economic decision-making. The discovery of this growth sheds new light on the two problems in 1987 consumption that have been the focus of widespread concern.

1. The problem of excessive growth in consumption by social groups. Some of this growth during 1987 was due to consumption by individuals who obtained underground income. Thus it is essential that, to execute the order issued by the State Council in 1988 to check the consumption of social groups, we commence by reducing the number of commodities such groups control. But even this will not be enough. For we must also strictly limit the amount of funds the groups wield and choke off the conduits through which such funds flow to the groups, so as to curb concealed shifts of consumption.

2. The problem of the decline in the real standards of living among some urban and rural residents. It is certainly true that the high rate of inflation in 1987 caused some people's living standards to decline. But to determine how many people were actually affected, we have to reevaluate the data issued by the State Statistical Bureau, taking into account the problem of calculating actual, total incomes.

Naturally, fuller analysis of these problems will only assist us in correctly understanding and will not resolve them. As to how to deal with concealed growth in consumption, we believe that the top priorities are to establish an index system to measure actual, total resident incomes and to strengthen statistical and financial supervision so as to plug up underground loopholes.

Questions, Answers on Enterprise Law
40060325 Beijing ZHONGGUO JINGJI TIZHI GAIGE
[CHINA ECONOMIC SYSTEM REFORM] in Chinese
No 23 Apr 88 pp 49, 56

[Text]

What is Enterprise Law?

Enterprise law is the general term for the legal standards regulating government-run enterprises, as well as the economic relations which occur in the course of an enterprise's production management activities. The recently issued "Nationally-Owned Industrial Enterprise Law" is the most important basic law among the enterprise law standards. In addition to this, other enterprise-related laws and regulations, such as the "Nationally-Owned Industrial Enterprise Staff and Workers' Representative Assembly Regulations" are also part of the enterprise law standards.

We can see from the above definition that enterprises are the core around which enterprise law developed. The economic relations regulated by enterprise law can be divided into three types. The first type is relations between enterprise and nation, including relations between enterprise and local people's government as well as central government agencies. Another type is relations between enterprises. Still another type is relations within an enterprise.

The "People's Republic of China Nationally-Owned Industrial Enterprise Law" consists of a total of 8 sections and 68 articles. Section 1, "General Rules", discusses the principles of enterprise legislation, while Sections 2-6 stipulate the contents of the above-stated three areas. Section 2 clearly stipulates from a dynamic point of view the conditions for the establishment, alteration, and termination of enterprises, the procedure for examination and approval, and the registration procedure. Section 7, "Legal Responsibility", stipulates the responsibility that should be borne for violations of enterprise law by enterprises, enterprise leaders, and government agencies. Section 8, "Supplementary Articles", stipulates the scope of the applications of enterprise law.

Enterprise law is a product of the widespread development of modern enterprise after the emergence of capitalist society. Enterprise law appeared relatively early in England. Early enterprise law consisted primarily of labor laws and regulations. Enterprise law has grown by leaps and bounds during the twentieth century, particularly since the Second World War. A special characteristic of enterprise legislation is making basic enterprise law the main foundation, while supplementing it with specific regulations, as with Yugoslavia's "Basic Enterprise Law", Hungary's "State-Run Enterprise Law", Japan's "Basic Small- and Medium-Sized Enterprise Law", and the Soviet Union's "State-Run Enterprise Law". China began enterprise legislation in 1980. After exhaustive research, repeated draft revision, and

repeated submission to the National People's Congress for discussion, the present "Nationally-Owned Industrial Enterprise Law" was formed. It is a summation of China's ten years of experience in enterprise reform. It is of major significance in guiding the continued intensification of reform. At the same time, because enterprise law has undergone discussion by the whole people, it is also a product of participatory, or parliamentary, government, and reflects China's democratic government.

Why Must Nationally-Owned Industrial Enterprise Law Be Formulated?

This must be explained from the standpoint of the following factors:

1. Nationally-owned industrial enterprises occupy an important position in the national economy. According to figures issued by the State Statistical Bureau, China has a total of 96,841 nationally-owned industrial enterprises, accounting for 19.4 percent of the total number of China's industrial enterprises, and their total industrial output value is \$620.14 billion, accounting for 68.7 percent of China's total industrial output value. China's enterprise legislation must make nationally-owned industrial enterprises a priority.

2. The results of economic system reform must be protected by law. Since reform began 9 years ago, China has adopted a series of comprehensive reform measures centered around enterprise stimulation, and has increased enterprise vitality. These measures include a series of stipulations concerning the increase of enterprises' right of autonomy, stipulations concerning lateral economic ties, and resolutions concerning implementation of a system of factory director responsibility. These reform measures have undergone several years of practical testing, and have proven to be effective. In addition, each locality has already accumulated a wealth of experience in carrying out test cases involving separation of the two rights, such as contract systems and leasing systems, and should confirm through legislation that it will use state power to guarantee the progress of reform.

3. Utilize the leadership provided by the law to open the way to further reform. The law's reflection of actual economic relations is not passive. Based on the development of actual economic conditions, the state, after careful research, can foresee the prospects and development trend to reform, and, in order to guide the constant intensification of reform, write into enterprise law those principles of reform which can by dint of effort be realized in the not-too-distant future and have enduring vitality.

What Is Legal Responsibility? What Legal Responsibilities Are Stipulated by Enterprise Law?

So-called legal responsibility is the legal consequence arising from an illegal act which must be borne by the offender. Illegal acts are the premise of legal responsibility, and legal sanctions are the result of legal responsibility. The investigating and affixing of legal responsibility and imposing of legal sanctions can be implemented

only by national specialist agencies. Legal responsibility can be divided into criminal responsibility, administrative responsibility, and civil responsibility. Criminal responsibility means the criminal sanctions, or criminal penalties, which the offender receives for violating the stipulations of the criminal code. China has five principal criminal penalties (surveillance, detention, specified prison sentences, life sentences and the death penalty) and three additional penalties (fines, deprivation of political rights and the confiscation of property.) Administrative responsibility is punishment which is borne for an act under administrative law. It is divided into two types. Administrative punishment is punishment imposed by national administrative agencies on organizations and individuals violating administrative laws and regulations; it includes such punishments as confiscation, fines, warnings, suspension of business, and detention. Administrative disciplinary measures are punishments administered by national organizations and institutions, according to their administrative subordination, to personnel guilty of unlawful dereliction of duty which does not constitute a crime. This includes such punishments as warnings, recording of demerits, dismissal and expulsion. "Civil responsibility" refers to responsibility which must be borne by citizens or legal entities for contract violations or non-performance of other obligations. It consists primarily of property responsibility. According to the stipulations of China's general rules of civil law, the methods of bearing civil responsibility include termination of infringement, removal of obstacles, elimination of danger, return of property, reinstatement to the original condition, repair, reimplementation, replacement, compensation for damages, payment of a penalty for contract violation, elimination of harmful effects, restoration of reputation, and apology.

The "People's Republic of China Nationally-Owned Industrial Enterprise Law" devotes one section specifically to legal responsibility. Article 59 of this section stipulates administrative responsibility. Article 60 stipulates civil responsibility. Articles 62, 63, and 64 stipulate both administrative and criminal responsibility.

13387

Clarification of Role of Enterprise Managers

40060326 Beijing ZHONGGUO JINGJI TIZHI GAIGE [CHINA ECONOMIC SYSTEM REFORM] in Chinese No 4, 23 Apr 88 p 46

[Article by Lan Sheng [5695 3932]: "A Few Words About the Discussion of 'Who Is Enterprise Manager'"]

[Text] *Editor's note: Since last fall, our magazine has sponsored a discussion on "who is enterprise manager." Comrades participating in the discussion have spoken their minds freely and published many helpful opinions that have played a prominent role in clarifying issues and promoting enterprise reform. As a conclusion to the*

discussion, we now publish the following article "A Few Words About the Discussion of 'Who Is Enterprise Manager,'" which was written by Comrade Lan Sheng.

Since it began the discussion of "who is enterprise manager" in August 1987, the ZHONGGUO JINGJI TIZHI GAIGE magazine has published many good representative and convincing articles. Under the excellent situation of deepening reforms and enlivening enterprises, discussing who the enterprise manager is is indeed very necessary because it is not only a theoretical issue but also a practical one that needs to be resolved immediately. There were basically four views during the discussion of who is enterprise manager: The first view thinks that employees as a whole constitute the main body of an enterprise manager; the second view thinks that the plant director (manager) is an enterprise manager; the third view thinks that the enterprise contractor is an enterprise manager; and the fourth view thinks that the enterprise manager varies depending on different historical conditions and enterprises, and should not be generalized. There were also other points of views. The above mentioned viewpoints have similarities as well as dissimilarities. What, then, is the final answer to this question? I would like to share my opinions with you.

Before discussing who the enterprise manager is, we should first clarify the definition of enterprise manager. Let us begin with the word "management." Management refers to a series of organized activities that are oriented toward a market, aimed to achieve enterprise goals, and carried out by commodity producers by means of commodity production and exchanges to achieve a dynamic equilibrium between the production, technological, and economic activities of an enterprise and the external environment of this enterprise. Management is the act of managing the whole process of enterprise production and operation, including the formulation of business strategy, the development and manufacturing of products, market development, and the operations of sales and financial affairs. The central link of all this lies in the process of formulating business strategy. It is thus clear that an enterprise manager is someone who, in the course of enterprise production and operations, makes policy decisions on major issues which are of long-term and strategic significance, affect the enterprise as a whole, and have a close bearing on the external environment, in order to achieve projected business goals or solve major problems that have just cropped up.

Based on this definition, an enterprise manager in general should be a plant director (manager), a small group of people headed by the plant director (manager), or an enterprise contractor. This is because:

1. An enterprise management system usually consists of three levels: policy-making, administrative, and executive. Each level has its competence of management and power. Among the three levels, a plant director (manager) belongs to the policy-making level and policy decisions made by a plant director (manager) belong to

strategic decisions at the enterprise level. Cadres in charge of management at the functional departments of an enterprise belong to the administrative level and the broad masses of workers generally belong to the executive level. Therefore, a plant director (manager) is an enterprise manager.

2. Judged by the requirement of separating ownership from management, the one who has the power to manage everything in an enterprise must be the plant director (manager) or the enterprise contractor who can take overall responsibility for leadership and assume risks involved in making policy decisions of an enterprise.

3. Judged by the analysis of a contractor's situation, whether an enterprise is contracted to an individual, a collective, a large enterprise, or by the state to the entire staff of an enterprise, the one who assumes the most risk when contracting is the plant director (manager) in charge of making policy decisions for the contract. Even if the enterprise is contracted to the entire staff of an enterprise, the one who assumes main responsibility is still the plant director (manager) who acts as the representative of the contractors while other staff members and workers assume related economic responsibility for the efficiency of enterprise management.

4. While clarifying who is enterprise manager, we must stress workers' role in democratic management and demonstrate their status of master. We should say that we need to make great efforts to bring into better play the workers' role in democratic management. However, it is questionable if we say they are all enterprise managers. Although the master status of workers is closely related to enterprise managers, they are actually two different matters. Enterprise managers and producers are determined by the division of labor in society and is an internal requirement for establishing a planned commodity economy. It is impossible for a production enterprise to have only managers without producers or the other way around. Generally speaking, not all producers can be managers just like Comrade Zhao Ziyang pointed out in his report to the 13th National Party Congress: "State-owned enterprises cannot possibly be run by the whole people and usually are not suitable for direct state management. Forcing them to do so can achieve nothing but stifle the vitality and vigor of enterprises."

Enterprise managers and producers are not set against each other. Instead, they are united. Enterprise managers must have authority in management; otherwise, they cannot possibly guide all workers in exploring and forging ahead. But at the same time, they must fully guarantee workers' master status and give full play to their initiative. In a socialist society, the authority of enterprise leaders is unified with the master status of laborers. The vitality of an enterprise comes from the enthusiasm, wisdom, and creativity of both mental and manual laborers. When the master status of laborers is fully guaranteed in all systems of enterprise and when their

labor is closely linked to their own material interest, their enthusiasm, wisdom, and creativity will be brought into full play. To make correct policy decisions, enterprise managers must rely on the broad masses of workers for collective wisdom and efforts to make management decisions. What is worth mentioning here is that managers who make arbitrary decisions and take preemptory actions do exist, but they are only isolated cases. As the reforms of economic and political structure deepens and workers' role in democratic management increases, the number of such managers is bound to diminish. There always will be isolated negative examples, but they do not affect the reform as a whole.

To clarify who is enterprise manager is to deepen reforms and enliven enterprises, especially state-owned enterprises. Before the reform of economic structure, state-owned enterprises were state-run enterprises under the unified management of responsible government departments, and they had no vitality. Since the reform of the economic structure, enterprise decision-making power has gradually increased, enabling enterprises to gradually resume their vitality. Separating ownership from management makes it possible for enterprises to make their own decisions in management and take sole responsibility for their own profits and losses. Clarifying the definition of enterprise manager under the new situation is of great significance to deepening reforms and enlivening enterprises. First, it can help many intelligent and able entrepreneurs with a pioneering spirit emerge from the storms of market competition. Second, it can help responsible departments and the broad masses of workers choose qualified managers through competition. Third, it enables enterprise managers to boldly assume risks and responsibility under the support of all workers and to make policy decisions on management in accordance with their responsibility and power. Fourth, it can establish a new relation of mutual reliance and close cooperation between managers and producers because managers have to pay attention to developing workers' enthusiasm and creativity to make their enterprises invincible during market competition. Fifth, it can further arouse workers' enthusiasm because the management power entrusted upon managers can facilitate the implementation of supplementary reforms within enterprises, gradually increase enterprises' economic returns, and thereby increase the material interests of managers and all workers.

Implementing the director responsibility system can facilitate the separation of ownership from management and the exercise of power for enterprise managers. Under the director responsibility system, plant directors (managers) are the most powerful managers. When a plant director (manager) is made the head of a plant and the representative of a corporation to assume full responsibility for the leadership of an enterprise, hold a central position, and play a central role, he or she will be able to better exercise their management powers. In addition, the goals of a plant director (manager) during his or her term of office are synonymous with the management

decisions that combine the long-term and short-term policy decisions of the enterprise. Such goals will become common fighting goals for all workers of that plant after they are broken down according to different levels and assigned to functional offices, workshops, work groups, and individual workers. While implementing the director responsibility system, we must perfect the workers congress system and various other democratic management systems, give full play to the rights and functions of union organizations and workers representatives in examining and approving major enterprise policy decisions, supervising administrative leaders, and protecting workers' legal rights and interests, and enable all workers to show off their intelligence and talents and to do their best to enliven enterprises.

In sum, clarifying that plant directors (managers) are enterprise managers not only has not damaged the master status of the broad masses of workers but has further aroused the enthusiasm and creativity of all workers.

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[Article by Liu Chunqin [0491 2504 0530], edited by Lin Daojun [2651 6670 0689]: "Do not overlook the problem of losses on products of profit-making enterprises"]

Editor's Note: Solving the problem of losses on products of profit-making enterprises is an important phase in the current efforts to improve the economic benefits of the industrial enterprises in our country. To draw the attention of the economic management organs at various levels and the enterprises to this important problem, we have specially published this article. [end editor's note]

Not long ago, we conducted a survey on the conditions of the losses incurred by products of over 18,000 industrial enterprises in 18 large and medium-sized cities and towns in the country. The results of the survey showed that the losses on products of profit-making enterprises had been rather serious and had become one of the important causes of the dropping off in their economic benefits.

I. Present Conditions of the Losses on Products of the Enterprises

For comparison purposes, we conducted a survey of the conditions of enterprise losses and losses incurred by products of profit-making enterprises during the years 1984 and 1986. Of the 18,497 industrial enterprises surveyed in 1986, 16,053, or 86.8 percent, had made profits while 2,444 enterprises, or 13.2 percent, had suffered losses. This was more or less similar to the national condition as a whole and possessed a certain representative and comparative character.

The special features of the losses on products of the profit-making enterprises were: large in amount, covering a wide area, centralized in distribution and showing a fast increase rate.

1. Amount of product losses. In 1986, the amount of losses in products of the profit-making enterprises was 796 million yuan while the amount of losses suffered by enterprises operating in the red was 597 million yuan. The former exceeded the latter by 33 percent. In certain cities and towns, the amount of losses on product of the profit-making enterprises actually exceeded the amount of losses suffered by enterprises in the red by several hundred percent. Calculated on the basis of the losses of the enterprises in the whole country in 1986 being 7.24 billion yuan, the losses on products of the profit-making enterprises in the whole country should roughly be above 10 billion yuan.

2. Area covered by losses on products. Of the profit-making enterprises under survey, there were 13,600 categories of products suffering losses, averaging 0.61 category of products suffering losses per each and every enterprise. The machine building industry had 186 large categories of products of which 160 categories were products incurring losses, that is, over 85 percent.

3. Distribution of products suffering losses. Of the profit-making enterprises covered by the survey, 4,459 enterprise were owned by the whole people, occupying only 27.8 percent, but their loss-suffering products amounted to 9,916 kinds, being 73 percent of the total number of 13,583 categories of products suffering losses and their losses totaled 698 million yuan, being 87.7 percent of the gross amount of losses of 796 million yuan. This is to say: Each and every enterprise owned by the whole people had 2.2 categories of loss-suffering products. This was about 600 percent higher than the average of 0.32 category of products in enterprises under other ownership systems. Each and every enterprise suffered on the average a loss of 157,000 yuan, this being 1700 percent higher than the average loss of 8,500 yuan

suffered by enterprises under other ownership systems. It can thus be seen that the problem of losses on products of enterprises owned by the whole people was a much more serious one.

4. Speed in growth of losses on products. In the year 1986 in comparison with 1984 the categories of products suffering losses in profit-making enterprises increased from 9,944 to 13,583, a rise of 36.6 percent. The amount of losses incurred increased from 411 million yuan to 796 million yuan, a rise of 93.7 percent. During the same period, the amount of losses of enterprises running in the red increased from 334 million yuan to 597 million yuan, or a rise of 78.7 percent. In other words, the growth speed of the losses on products of the profit-making enterprises was higher than that of the loss-suffering enterprises.

II. Basic Causes of Losses on Products of Enterprises

To find out the basic causes for the losses on products of profit-making enterprises, we carried out on-the-spot and written surveys on 147 enterprises in two cities. The results of the surveys showed that such causes as the rise in prices of raw materials, fuels, and motive power, stagnant product sales, inability to produce on an economically large-scale basis because of production limits, and defects in management directly contributed to losses on products and were the main sources of the losses.

1. Rise in prices of raw materials and fuels exceeded the digestive capacity of the enterprises. Many of the enterprises in the processing industries and trades lacked the ideological preparations and material preparations for large-scale price-rises of raw materials and fuels and hence have not formed sufficient digestive power. Thus, the products of certain enterprises, particularly those products whose cost of raw materials made up a large portion of their production cost and which could net only a small profit rate in sales, inevitably incurred losses. Losses (including on varieties and in amounts, same below) brought about by the factors of price rises being unable to be absorbed or completely digested by the enterprises roughly made up 52 to 68 percent of the total volume of losses (see accompanying table below).

Table 1: Statistics Showing Causes of Loss on Industrial Products of Enterprises in a Certain City

Causes	Categories of loss-incurring products				Loss amount of loss-incurring products (unit: 10,000 yuan)			
	1986		Jan-Sep 1987		1986		Jan-Sep 1987	
	No.	Percent	No.	Percent	No.	Percent	No.	Percent
1. Price rise in raw materials (including fuels, motive power)	68	59.1	79	68.1	449.5	52.2	466.97	58.6
2. Stagnant sales of products	5	4.3	4	3.4	3.1	0.4	5.50	7
3. Production not large enough	10	8.7	7	6	97.7	11.3	70.6	8.9
4. Drop in price of products	15	13	9	7.8	186.4	21.7	54.9	6.9
5. Wrong policy-making	2	1.7	1	0.8	0.4	—	1.3	0.2
6. Others	15	13	16	13.8	123.7	14.4	197.6	24.8
Total	115	100	116	100	860.8	100	796.8	100

2. Output of products of enterprises of the processing industry exceeded the market's receptive or absorbing

capacity. At present, the production capacity of our country's processing industries is rather large, not only

exceeding the supply capacity of raw materials, fuels, and motive power but also turning out products far in excess of the market's receptive power. This state of "being small at both ends but large in the middle" on the one hand causes an insufficient supply in raw materials, fuels, and motive power, leads to a rise in their prices and brings about losses in the production of certain products. On the other hand, it also makes the output of certain products of the processing industry excessive and exceed the demand for them, resulting in their stockpiling. Under such conditions, on the one hand in certain of the enterprises, because the reduction in the output of their products and thus their production capability cannot be fully displayed, the cost of production will rise while, on the other hand, due to competition being aggravated and the inability to carry out the policy allowed by the state of "buying and selling at high prices" with regard to certain products, the enterprise is compelled, in the case of the products, "to buy at high prices but to sell at low prices," thus literally completing the transaction at a loss. According to statistics, losses caused by supply exceeding demand amount to 16 to 33 percent of the gross volume of losses.

3. The enterprises not having completed yet their "changing of track and altering of pattern" and the operational mechanism being generally not suited to the demands of the environmental changes. Seen from certain of the enterprises under our survey, their concepts and production and operational activities have not shifted to the track of the planned commodity economy and they themselves have not yet truly become producers of, and operators, in, commodities. Products of these enterprises still depend on purchases by the commercial departments. If more purchases are made then they will make profits but if there are fewer or no purchases made then they will be in the red.

They do not want to initiatively grasp market information, nor to study the users' demands, or to actively take steps to push the sale of their products. The ability of the production system of these enterprises to suit environmental changes is very poor. Although the market has provided profit-making opportunities and there are also demands for new products, because of such problems as the production equipment, capital funds and the organizational structure, production on their part still cannot catch up even after 3 to 5 years. Sales of certain of their products in the market may have already become stagnant and losses have already appeared but for various production and organization reasons they still cannot stop producing such products even after 6 months or a year. In addition, the enterprise's management ideas and major points of work have not yet been completely shifted to the track of improving the economic benefits and the problem of losses on the products does not occupy enough of their attention. This too is one of the causes for the losses on the products of profit-making enterprises. Losses on products arising from the enterprise's imperfect operational mechanism and crude management methods account for roughly 15 to 25

percent of the gross volume of losses. It must be pointed out that in the factors causing losses such as rising prices of raw materials, stagnant sales of products and so forth, problems of the imperfect operational mechanism and poor management are also among the composing elements. Hence, the losses caused by internal problems of the enterprise are actually larger than those shown in the statistics.

II. Reasons Why Enterprises Produce Products That Incur Losses

Profit-making enterprises which produce products that incur losses are mostly those enterprises which produce a large variety of products and also products that produce profits, and which have sufficient ground for choice in determining the production of products. This being the case, why should they choose to produce products that incur losses? According to our survey, the main causes of enterprise turning out loss-incurring products are: fulfilling orders from above on planned targets on the quantity and value of products, endeavoring to capture the market, dividing up the fixed production expenses, waiting for market demand to turn for the better, and so forth.

1. Fulfilling planned targets from above. This includes two aspects: 1. For the sake of fulfilling the state's mandatory plan, that is, duty-bound to produce the loss-bearing products; and 2. To fulfill the target on the gross industrial output value fixed for the localities, the enterprises can only produce those products which incur a high production cost but can sell only at low prices. Following the intensified development of the reform of the economic structure, the former will become less but as for the latter, there is still an increase in many localities. For example, from January to September 1987, a portion of the enterprises in a certain city, for the sake of fulfilling the target on the gross industrial output value forwarded downward by the city government, had to produce some 23 categories of loss-incurring products. This made up 27.6 percent of the gross number of loss-incurring products under the survey. The losses incurred amounted to 3.29 million yuan, or 41.3 percent of the total amount of losses incurred by the loss-incurring products under survey. Both in variety and in amount the loss-incurring products exceeded by over 200 percent the portion of the mandatory plan of the state.

2. Capturing the marketing. One of the competitive methods customarily adopted by the enterprises in recent years was to sell the products at prices lower than the production cost so as to open up sales channels, capture the market and replace imported goods. This kind of losses on products generally belongs to losses of a policy nature and is mostly aimed at initially pushing the sale of new products.

3. Dividing up or separately levying the production expenses. Under certain conditions, for an enterprise to produce a small quantity of products that cannot bear

any profit it is possible to even up a portion of the fixed production expenses, lower the production cost of other products, and obtain therefrom a marginal benefit. It is one kind of business method which can be selected when an enterprise has surplus production capacity but can find no profitable product to produce. According to a survey of a portion of the cities, the number of kinds of products produced by the enterprises with this purpose roughly amounted to 22 to 30 percent of the total number of kinds of products incurring losses and the amount of the losses occupied about 10 to 28 percent of the total amount of losses. 4. Waiting for the market demand to turn better. In the market at present, there are a portion of products whose demand varies greatly. The relevant departments would at times reflect that the supply of certain kinds of products were insufficient and therefore demanded that enterprises speed up their production and supply; at other times they would say that the supply of certain kinds of products exceeded demand and accordingly instructed the enterprises to reduce their production. Regarding this category of loss-incurring products, the enterprises could only adopt a no-change policy, that is, temporarily keeping up their production as usual, wait for the supply-demand conditions in the market to turn for the better and hope that new orders would come in or the sales price could be raised and thereby obtain certain profits thereon. The investigation materials showed that this portion of loss-incurring products made up about 14 to 16 percent of the gross volume of loss-incurring products and that their amount of losses occupied 13 to 27 percent of the total amount of losses of the loss-incurring products.

In addition, for the sake of winning honor for themselves, some enterprises would spare no efforts or funds to produce products that were superior products in the province, or department or state, thereby being awarded with gold medals or silver medals or maintaining their products' status as famous brands. This is also one cause for their continuing to turn out loss-incurring products.

IV. An Analysis of the Rationality of the Existence of Loss-Incurring Products

There are three sets of conditions for enterprises' turning out and continuing to turn out loss-incurring products, namely, rational, comparatively rational and wholly irrational.

1. Loss-incurring products that are rational. In our country, during the transitional period from a commodity economy to a planned commodity economy and in the future period of the complete realization of a planned commodity economy, two sets of conditions exist. One is the imbalance in the supply and demand relative to the products (commodities), at times the supply being abundant and at times not. At a time when the supply of a certain kind of products exceeds demand enterprises which have poor production conditions and a low management level will suffer losses in the production of these kinds of products and may eventually be edged out of the

market. The other is that during the life period of the product, its output volume and selling price vary at different stages, sometimes up and sometime down. When the product is located at the entry or initial period and the declining or waning period, losses may occur because of the small output volume and/or the low selling price. Product losses appearing under these two sets of conditions may be caused as a kind of normal phenomenon. At present, among the loss-incurring products, the ratio occupied by this portion is not very large and may be estimated at about 20 percent.

2. Loss-incurring products that appear to be comparatively rational. At present, there are still in existence such loss-incurring products whose production, considered from a certain angle, is still of a definite rational character but viewed from another angle, is irrational. We call this category of loss-suffering products comparatively rational loss-incurring products. They include loss-incurring products produced at the state's mandatory plan and also those loss-incurring products produced for the purpose of apportioning the fixed production cost.

The state may ponder from certain angles (such as aid to agriculture) and endeavor to limit the sales prices of certain products and prohibit them from rising in accompaniment with changes in the production and market conditions. They are the so-called loss-incurring products of a "policy-nature." Viewed from the state's entire economic activities, the existence of such a category of products may possibly be rational and beneficial to improving the socio-economic benefits or stabilizing social order. But if this phenomenon is examined from the angle of the enterprises, then it is irrational. This is because it does not reflect the actual results of the enterprise's production and management activities, is disadvantageous to giving due recognition to the status and position of the producers and entrepreneur of the enterprise's commodities, and is also unable to stir up the initiative and enthusiasm of the enterprise in producing this category of products. That the enterprise produces the loss-incurring products for the sake of apportioning and dividing up the cost of production also has its rational side and its irrational side. When an enterprise has plentiful surplus production power and when after meticulous deliberation is it found that production of certain categories of loss-incurring products can produce certain marginal benefits, then it may be assumed to possess a definite degree of rationality. Even then, its rationality is that it is better than not producing this category or products at all, meaning not having production capacity idle, and this after all is not the most rational or most economical measure. At present, among the loss-incurring products the ratio occupied by this category of products is around 30 percent of the whole. From now on, following the reform of the economic structure being further intensified and the further elevation of the enterprise's technological and management level, production of comparatively rational loss-incurring products should be gradually reduced.

Irrational loss-incurring products. The investigation materials have shown that currently this type of loss-incurring products still exists in the enterprises: although producing them is unlike producing the rational loss-incurring products, this cannot be avoided in the production and operation activities; producing them is also unlike producing the relatively rational loss-incurring products as in the latter case certain benefits can be brought to society or the enterprises. We call such loss-incurring products caused wholly by inappropriate macroeconomic and microeconomic management irrational loss-incurring products. They include: loss-incurring products turned out by the enterprises wholly in fulfillment of industrial gross output value targets forwarded from the upper levels, loss-incurring products caused by the enterprises' errors in policies, loss-incurring products caused by the enterprises' failure to make earnest and adequate accounting in advance, and so on. At present, this category of loss-incurring products makes up about 50 percent of the total amount of loss-incurring products. Taking the measures to turn this category of products from loss-incurring to profit-making products should from now on be the major task in macroeconomic and microeconomic management work.

V. Suggestions To Solve the Problem of Losses Incurred by Products of the Enterprises

The growth of development of loss-incurring products are related to the enterprise's external environment and also to its internal management, being an exceptionally complex problem. To solve this problem, particularly the problem of the irrational loss-incurring products, needs the cooperation between the state and the enterprises to adopt the necessary measures. Hence, we suggest the following:

1. Serious attention must be paid to the problem of losses incurred by products of the enterprises. Despite the considerable seriousness of this matter, up to now people have not given it important or serious attention. This is manifested in the following: First, neither the central government nor the local governments have formed a department to collect statistics analyzing the conditions of losses incurred by products of profit-making enterprises; second, the enterprises themselves have not earnestly attended to the matter of losses incurred by the profits; third, various sides, including the propaganda media, have not yet reflected the problem of losses incurred by products of the enterprises; and fourth, the departments in charge have not made any demand on the enterprises to rectify the situation and nor have the enterprises themselves formulated any definite plan in this connection. In short, losses incurred by products of profit-making enterprises have fallen into a state of basically being nobody's business. It may be said that this is a big loophole in our country's economic management work.

In our opinion, there is only a thin line between profit-making enterprises which have loss-incurring products and enterprises running in the red. In other words, when

the losses incurred by products of profit-making enterprises have reached a certain breadth or depth, the enterprises will become deficit enterprises. At present, this problem is explained by the phenomenon in the course of transforming losses into profits in the deficit enterprises, that is, the phenomenon of after a portion of the enterprise having been transformed from loss incurring to profit making, a portion of profit-making enterprises with loss-incurring products being transformed into enterprises operating in the red (among the loss-incurring enterprises subordinate to the machine building commission, in 1986, 80 percent consisted of deficit units newly added to the list). For this reason, we suggest that the state should expand the scope of work of converting loss-incurring into profit-bearing from the deficit enterprises to the loss-incurring products of the profit-making enterprises. Only by so doing is it possible to further reduce the number of enterprises running in the red and further enhance the economic benefits of the industrial enterprises.

2. Readjusting and consolidating the prices of raw materials. In our opinion, readjusting the prices of products should reach the objectives on three sides: the first is promoting the development of production; the second is readjusting the supply-demand relations; and the third is implementing the principle of exchange at equal value, and proceeding to benefitting the assessment of the enterprise's operation conditions. Among them, promoting the enterprise's production and development is the nucleus. In recent years, readjustment of prices in our country has played a certain active role, promoting the development of production of agricultural products and certain products in short supply. However, at the same time, we cannot overlook the problem on another side of the rising trend in the prices of products in stringent supply brought about by the "double-track" system. From production to circulation, we have endeavored to expand the volume of commodities subjected to negotiated prices or self-determined prices and done our utmost to enhance the extent of the increase in prices of the commodities so that the maximum profits may be derived therefrom. [paragraph continues]

By so doing, in the small portion of benefitted industrial enterprises and materials departments, there is an obvious increase in their realized profits, and through both the legitimate and illegal distribution channels, a portion of the profit-retentions of the enterprises is converted into consumption funds; while the larger portion of processing enterprises, particularly in those products whose cost of production consists of a large proportion of expenses on raw materials, fuels, and motive power, may, because of the scale of the price increases in raw materials exceeding their digestive capacity, suffer a reduction in profits even reaching the extent of an enterprise deficit or losses in products. Once the price increase in raw materials becomes the principal factor for an enterprise's deficit or losses from its products, this will necessarily affect the behavior and management of the enterprise manager. This includes: First, reducing or

stopping the production of the goods urgently needed by the state. At present, the attitude taken by enterprises toward loss-incurring products in mandatory plans is the less the production the better and it would be best not to produce at all. This is one of the important reasons why in the case of certain products the fewer the "orders" the more acute the state of supply lagging behind demand. Second, tending to overlook the enterprise's internal management problems. Too large an increase in the prices of raw materials will first divert the attention of the enterprise manager, make him look outward, and cause him to use the price-increase factor as a tool to bargain for better terms in contracting for, or accepting, tasks from above; and second it will not help in improving the enterprise's management. In addition, the rise in the prices of raw materials makes it difficult to assess the enterprise's economic benefits. Under the conditions of a rise in commodity prices and the "double-track" system, the enterprise's production expenses will fluctuate according to the large or small quantities of raw materials obtained from planned supply and from purchases in the markets and the enterprise's benefits or earnings will likewise vary depending on how much of their products are subjected to planned transfer and how much can be self-marketed by the enterprise. This not only adds to the complexity in the enterprise's cost accounting as well as in planned management but also makes it difficult to correctly assess the enterprise's management conditions since whether the economic benefits are good or poor cannot be entirely determined by the enterprise. At present, the policy on commodity prices has not thoroughly solved the problem of the price of products not being consistent with the products' actual value and nor has it solved the problem of the inequality in joys and sorrows between the enterprises. At a result, it has not promoted the all-round development of production. Hence, we suggest that an all-round refixing be made of the existing prices of raw materials, fuels, and motive power and that a coordinated reform be carried out on the basis of the refixing or readjustment.

3. The growth in the production capacity of processing industry should be limited. After the efforts made in recent years, the production capacity of raw materials, fuels and motive power has developed to a rather larger extent. However, due to the too rapid development in the production capacity of the processing industries, the contradiction of supply lagging behind demand so far as raw materials, fuels, and motive power are concerned has not been basically smoothed out. In our opinion, the too rapid development in the production capacity of the processing industry is the main source of the rise in the prices of raw materials and of the state of the supply of certain products being much larger than demand and having to be stockpiled in the godowns. At the same time the rise in the prices of raw materials and the stagnant sales of certain products are the important factors causing the present losses incurred by the products. Therefore, to rectify the situation of profit-making enterprises

incurring losses on their products, the relevant departments of the state should adopt resolute measures and restrict the continued development in the production capacity of the processing industry and endeavor to convert the enthusiasm of various sides from concentrating on developing the processing industry quantitatively to improving the processing industry qualitatively. For this purpose we should first study the financial policy of "eating from separate kitchens" which has created the conditions for developing the processing industry. According to our investigation, at present "eating from separate kitchens" in finance is being practised on many levels. Not only does central government have a "separate kitchen" apart from the provinces, municipalities and autonomous regions but also the provinces, municipalities and autonomous have their own "separate kitchens" apart from their subordinate governments. This type of level by level "eating from separate kitchens" inevitably leads to level by level wrangling over terms and fighting for profit retentions, level by level investing in processing enterprises which can easily make money, level by level adding to the tasks of the enterprises, level by level embezzling part of the materials that should be issued to the enterprises and level by level imposing levies on the enterprises.

Phenomena of this kind which we have become accustomed to are reflected in the finance of the central government becoming increasingly acute and stringent and in the enterprises finding it difficult to carry on. In short, "eating from separate kitchens" in finance provides conditions for the too rapid expansion of the processing industry while a shortage of the supply of raw materials needed by processing industry in turn brings about a rise in the prices of the raw materials; the price-rise in raw materials and the processing industry's output exceeding market demand lead to the products of certain enterprises incurring losses. Therefore, we suggest an adequate handling of the problem of "eating from separate kitchens" in finance, restricting the continued expansion of the processing industry, and take these as they key measures to open up this "interlocking chain of rings."

4. Strengthening the control over products. Product control, also called product policy, is an important constituent part of enterprise control and management. Its contents specify that the enterprise, based on the life expectancy period, condition of profits, and marking prospects of the various kinds of products, separate them into four categories and adopt corresponding countermeasures so as to achieve better economic benefits. the countermeasures against these four categories of products are: actively developing products of celebrated brands, maintaining or further improving products that yield large profits, handling the problem of risky products with discretion, and eliminating as soon as possible products those sales are on the decline. Celebrated entrepreneurs in the world, in reorganizing enterprises in difficult straits, frequently take the measures of liquidating the products in the production process and stopping

the production of those products which have no future prospects and which also incur losses as the basic steps in rectifying the enterprise's passive state. Seen from the enterprises under our survey, the product control and management work in our country is rather weak. Some of the enterprises basically do not make regular and all-round study and analysis of their products. Some of them even fail to carry out cost accounting on the variety of products. The development of such phenomena is related to the old structure that has been in force in our country for many years and also to the low management level on the part of the enterprises. Following the establishment of a definite status for the producers of commodities and managers in the enterprise and strengthening of the management of industries and trades, such a state of affairs should improved. Hence, we suggest that we should join with the "double-increase double-economy" activities and make the industries, trades, and enterprises mutually cooperate with each other to make an overall survey of the products of the profit-making enterprises, adopt corresponding measures according to the different conditions of those products incurring losses and endeavor to lower to the maximum extent the number of categories and the loss amounts of such loss-incurring products.

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[Excerpts] *Editor's note: Stabilizing money supply and prices, issues about which the entire nation is deeply concerned, are nettlesome problems that we have encountered in our program of economic restructuring and that have become the foci of intense theoretical inquiry and controversy. Some comrades have argued that expansion of the money supply and price rises are unavoidable and that appropriate, moderate inflation is harmless and conducive to economic growth. Is inflation unavoidable? Is it harmful or harmless? These are major issues that affect the smooth implementation of China's economic restructuring and her socialist economic development. To promote further study of and to provide a few useful ideas and measures to restrain inflation, we, in collaboration with the Editorial Department of CHENGBEN JIAGE ZILIAO, invited a number of experts, professors, and scholars residing in Beijing to participate in the first symposium on the issue of inflation and price stability, which convened 19 January and was chaired by Zhang Zhuoyuan [1728 0587 0337]. Following are abstracts of the statements delivered by the participants.*

I. The Current Status of China's Inflation

China's Inflation Is Grave: Xu Xuehan [1776 7185 1383]

In 1987, China's prices soared across the board. Compared to the same period of 1986, which serves as a base of 100, the aggregate social retail-sales price index stood at 107.6 between January and October 1987, and the retail-sales price indices of many large and medium cities rose by double digits.

Another characteristic of price changes is that prices continue to rise and get out of control. In the first spurt of inflation, which occurred in 1980, prices rose by 6 percent. The 1981 readjustment quickly reduced this rate and enabled us to keep the rise within 2 percent over the next 3 years. But the money supply greatly expanded in 1984 and thereafter, so that prices surged once again in 1985, rising by 8.8 percent. At the end of that year, we carried out the policy of "soft landing," so that the rate declined a bit but still raged at 6 percent in 1986. In 1987, prices soared again, indicating that the "soft landing" had failed. If the government does not take major steps and adopt across-the-board, comprehensive, and lasting macroscopic measures, inflation will get out of hand.

We cannot by any means employ inflationary measures as a basic policy or to stimulate the economy. For doing so will severely affect China's economic development and political situation.

1. Inflationary policy contravenes the general guidelines established by the CPC's 13th National Party Congress, which called for stabilizing the economy and advancing reform. Under inflation, gross output value may be pushed upward temporarily, but the rise will be hard to sustain and ultimately will decline, and the fluctuation engendered by such conditions will severely undermine economic results and strength. First, inflation makes aggregate supply very tight, renders it hard for producers to predict future market conditions, and causes consumers to panic, so that economic conditions cannot be stabilized and it becomes even more difficult for us to seek progress amidst stability. Second, inflation also greatly harms the interests of producers and consumers, dampens enthusiasm for production, exacerbates contradictions between supply and demand, and forces necessary price reform to retreat. Under these grim conditions, it will be hard to get most reforms off the ground, much less to advance them.

2. Inflation pushes domestic prices upward, raises enterprise production costs, increases the central government's burden of subsidizing enterprises and undermines the competitiveness of Chinese goods on international markets. Overly high prices affect sales, but if prices are not increased, the state has to shell out large amounts of price subsidies and subsidies to offset enterprise losses, which practices can easily lead to charges of

dumping and impede our efforts to expand exports. In developing countries, import demand always exceeds export capacity. Under such conditions, inflationary policy increases demand for imports and thus exacerbates trade deficits. China's import dependency rate stood at 6.56 percent in 1983 but leaped to 12.93 percent in 1986, when Japan's rate was 9.1 percent. Inflation makes it impossible for the state to establish a rational foreign exchange rate, without which it is very hard to expand foreign trade and even external economic relations. And if exports do not keep pace, the state's foreign exchange earnings cannot improve, which reduces our ability both to import advanced foreign technology and equipment and to service our debt. And if our foreign debt is not repaid on time or is bungled, we will sink into the quagmire of indebtedness.

3. Under inflation, the state's budget deficit is even harder to eliminate. Inflation exaggerates the magnitude of government revenues, which tends to induce people blindly to emphasize expanding output value and increasing investment, which makes it more difficult to readjust output mix, so that economic results cannot be improved and real fiscal revenues cannot be increased at a steady rate. Inflation also makes it difficult to hold down budgetary expenditures, especially regular outlays, and that makes it impossible to eliminate the state's budget deficit.

4. Inflation prevents markets from growing and developing, for under inflationary conditions enterprises do not enjoy stable environments and equal conditions under which to compete, which makes it impossible to regularize distribution relationships between the state and enterprises. Under inflation, if output value and profits are computed in current prices, contract fulfillment becomes difficult to evaluate, and this undermines contract performance.

5. Under inflation, a few people take advantage of tight supply and excessive demand to engage in speculation and profiteering, whereas a high rate of inflation causes the real living standards of many citizens to decline. This is very detrimental to the interests of the broad masses of people, is engendering growing complaints on street corners and in the alleyways and is becoming a threat to political stability.

Thus resolution of the problem of inflation is a top priority. At present and for a certain period in the future, we must stress this as a major issue. First, the central government must have a clear and comprehensive economic readjustment policy, immediately effect economic readjustment, strive basically to reorder economic relationships within the next 3 years or so, and extinguish inflation (holding price rises to 2 percent or less). Second, we must conduct further studies of the production mix and more effectively integrate macroscopic policy and microscopic invigoration, so as to promote steady improvement in enterprise mix. Third, while fighting inflation, we must cautiously study and

make preparations for reform of the price system and of financial markets. All measures conflicting with our goal of creating a unified market must be eschewed.

II. The Causes of and Measures To Counteract China's Inflation

Inflation and the Future of Reform: Wang Shaofei [3769 4801 7378]

The key to the success or failure of socialist economic restructuring lies in whether or not we can effectively control inflation, which is a fact that has been proven through experience. Confronted with inflation, socialist countries must make a choice: To continue carrying out inflationary policy and thus lead reform to defeat, or abandoning that policy, maintaining socioeconomic stability and exploring scientific routes to reform. We must choose one or the other approach; there is no other. Everyone recognizes that China suffers from inflation, but there are disagreements regarding the causes, degree of threat and ways to deal with the problem. I perceive these issues as follows.

A. The cause of inflation. Academic circles have identified a number of causes of China's inflation—demand-pull, cost-push, irrational production mix, irrational consumption mix, macroscopic factors, microscopic factors, the role of the market, and the like—many phenomena have been enumerated. We cannot deny that these phenomena are related to inflation, but listing more and more factors merely serves to cloud our understanding of the problem. To identify the real cause of inflation, we must clear away the fog created by all these phenomena and get to the root of them. I believe that our inflation occurs largely through a simultaneous expansion of both accumulation and consumption, so that aggregate social demand, which wields purchasing power, exceeds aggregate supply, causing prices to soar. In comparable prices, national income in 1984 grew by 13.5 percent over 1983, national income in 1985 grew by 12.7 percent over 1984, and accumulation funds grew by 24.3 and 38.9 percent and consumption funds rose by 16 and 23.7 percent in 1984 and 1985, respectively, greatly exceeding the real rise in national income during these years. The primary reason why accumulation and consumption rose together, creating excessive demand, is that fixed capital investment was too high during these years. Aggregate social fixed investment rose by 38.8 percent between 1984 and 1985 and by 14.6 percent between 1985 and 1986, exceeding the growth rates for both gross social output value and national income during these years. Aggregate social fixed investment totaled 183.287 billion yuan in 1984, equal to 32.4 percent of national income that year; 254.319 billion yuan in 1985, 36.3 percent of national income; and 291.438 billion yuan in 1986, or 37.4 percent of national income. Such a high ratio of fixed capital investment to national income is rare in other countries of the world. And approximately 40 yuan

of every 100 yuan in fixed capital investment is transformed into consumption funds, so expansion of investment invariably leads to increased consumption. The rise in fixed capital investment is caused, in turn, by a simultaneous increase in budgeted and bank loans, which increase is itself the result of an overly large expansion of the money supply. Thus it is clear that it is the desire to spur high growth rates by increasing the money supply that is the real root of our inflation. Specifically, the process works as follows: Desire for high growth rates leads to expansion of budgeted and bank loans, which then ignites an expansion in the volume of money issued, which sets off increased fixed capital investment, which sparks a rise in aggregate demand (i.e., a simultaneous expansion of accumulation and consumption), which causes prices to soar.

B. Measures by which to curb inflation. In 1988, central authorities decided that we must implement a "double tight" policy to bring the money supply under control and to strive to stabilize prices. This was a correct decision. But executing this tightening will require great effort.

1. We must resolve to lower growth rates and restrain the desire for high growth rates. Given actual conditions in China, our industrial growth rate must not exceed 10 percent and ideally ought to be maintained between 7 and 8 percent.

2. We must carefully formulate proper sequences for all reform, strive to coordinate development and maintain stability. For example, housing system reform and the program to implement fiscal contract systems and should not be handled as mad campaigns but rather require careful study and planning, lest such efforts create even greater obstacles to reform of the entire economy; create tremendous difficulties for other reforms, such as the separation of administration and enterprise, improving market systems, and establishing a regulatory system based primarily on indirect control; and cause the "double tight" policy to come to naught.

3. We must eradicate as quickly as possible the destructive effects on the economy of double-track pricing, which effort will play an important role in curbing inflation. Double-track pricing is a poison that spawns speculation and profiteering, blocks circulation, undermines party discipline, corrupts the body politic and severely hinders economic development.

4. In macroeconomic decision-making, we must ensure that fiscal and banking policy serve as checks upon each other. Specifically, this entails (a) readjusting the budgetary allocation mix, reforming budgetary disbursement procedures, using taxation and other forms of state revenue to restrain investment, and preventing investment levels from determining budgetary allocations; (b) raising the status of the central bank, making the issuing of banknotes independent, severing the direct ties between banknote issuing and bank loans and between

government treasuries and banknote issuing, and prohibiting governments from making overdrafts on banks; (c) having the supreme organs of state power set limits on the amount of currency that is to be issued each year, and implementing a banknote-issue responsibility system.

5. While reforming the tax system, we must make enterprises the principal investors in our economy, ensure that investment is dependent on income and create investment control mechanisms.

We Must Resolutely Reform the Investment System and Establish a Budgetary-Financial Account System: Yang Peixin [2799 1014 2450]

To curb inflation, we must resolutely reform the investment, budgetary and credit systems.

The expansion in investment is a major factor behind the increase in the budget deficit, the rise in banknote issuing and the shortage of producer goods and materials. Reform of the investment system must above all stress reform of the entities that engage in investment and change the notion that the central government should monopolize all key energy, transport and raw-material industry development projects. In reforming the investment system, we first must clearly stipulate that enterprises are to play the principal role in expanding reproduction and use the contract responsibility system to enable enterprises to retain 40-50 percent of their net incomes so that firms have the ability and the authority to undertake accumulation and to expand reproduction on their own and to transform and upgrade themselves. Raw-material and processing industries should be improved mainly through expansion, refurbishing or rebuilding existing enterprises. Second, we must clearly specify that energy, transport, infrastructural facilities and public facilities are to be handled primarily by local governments, which are to use these projects to soak up local liquidity. Investment in such key projects as electric power plant or transport construction should be transferred to localities. Third, central agencies should assume responsibility for interprovincial-municipal projects, but the scope of these is to be curtailed. Meanwhile, we must also change the forms in which investment is made. We should establish a system for funding development projects so as to effect thorough reform. When fiscal agencies allocate energy, transport and capital-construction investment funds, they should restrict investment authority to those agencies that are empowered to decide investment policy. Authority and responsibility must be linked, and results must be evaluated. Once investment reform is completed, most projects will be decided very carefully, because investors will have to bear the economic responsibility for their decisions. This will enable us to cut down on investment in key construction projects, reduce budget deficits and curb inflation.

Establishing and improving the budgetary system is another key to curbing inflation. The sharp rise in administrative costs is a major contributor to budget deficits. We should establish a budgetary-final account system, require that all government budgets and final accounts be examined and approved by the budget committees of respective Peoples Congresses, and use economic democracy to restrain the aberrant swelling of administrative agencies and other forms of waste.

We must smash the "big pot" system in bank credit and reduce demand for loans, the gap between revenues and expenditures in credit operations, and inflationary pressure. We should institute bank contract responsibility systems, have the state allocate a certain amount of credit funds to branch banks, meet demand for loans by letting banking agencies attract deposits, and change banks' traditional habit of always looking to and demanding credit funds from their superiors. Banks should contract to remit a certain share of their profits to their superiors but be allowed to keep whatever amounts they earn in excess of these quotas so as to expand their operations. Once banks assume contracts, we should use banks to soak up liquidity in society, have them carefully plan and budget their loans, and enliven fund flows among banks, so as to meet local demand for capital and to check the sharp rise in the money supply. The over-issuance of fixed capital investment is also a major contributor to the expansion in investment, the overextension of the capital-construction front, the gap between revenues and expenditures in credit operations and the expansion of the money supply. We must stop the aberrant growth in loans for fixed-capital investment and abolish the practice by superior agencies of issuing loan targets to lower levels.

If we resolutely reform the investment system, establish a budgetary-final account system and institute contract responsibility systems in banks, we will be able effectively to control investment demand and the purchasing power of social groups, and this will enable us within 2-3 years to eliminate budget deficits, curb inflation, and stabilize prices and the economy.

We Must Carry Out the "Double Tight" Policy and Restrain Aggregate Social Demand: Liu Guangdi [0491 0342 4574]

In our strategic decision-making, we must recognize the danger posed by currency inflation, resolutely overcome the outmoded concept of seeking high growth rates, and strictly hold economic growth to a sustainable level. We should also reexamine the "three guarantees and three restrictions" policy, for not only should nonkey and non-plan construction projects be restricted, certain key and in-plan projects also require appropriate restraint. We must also guarantee expanded inputs in agriculture so as to ensure increased output in that sector. Thus we must make strategic shifts in sectoral and investment policies and reexamine everything. In addition, we must resolutely slash the state's administrative costs, restrain

consumption by social groups and, from the central government down to the localities, but especially leading central agencies and cadres, we must struggle to build up our nation through thrift and hard work. Central leaders, in particular, should take the lead in belt tightening.

Specific measures are as follows:

- (1) We must implement the "double tight" policy and restrain aggregate social demand; cut aggregate loans granted by the central bank to specialized banks and reduce bank loans for fixed capital investment; yet also provide for dynamism amidst retrenchment and by letting specialized banks lend more money if they take in more deposits, improve capital-use results, and accelerate fund turnover. To meet the needs associated with the enterprise contract responsibility system, banks should also carry out such systems. They should be permitted to create bank president funds from a certain share of their operating earnings and to collect commissions and service fees, and we should abolish the practice of regulating bank expenses per person costs. Meanwhile, we should implement fiscal contract responsibility systems, have central and local governments sign contracts providing for progressive increases in upward revenue remittances, set reasonable base figures for and average annual increases in contract-period revenue remittances, ensure that localities remit revenues as required, let localities retain additional receipts but require that they make up any shortfalls themselves, and maintain this system for several years. Or we can retain the current system, under which there are base figures for central and local governments and a certain ratio of revenue sharing, while appropriately readjusting these figures and ratios.
- (2) We must strive to increase commodity supply. The most important thing that we need to do at present is, while separating ownership and management, to implement a variety of contract responsibility systems.
- (3) We must strengthen control of markets and prices, ensure reasonable price competition, crack down on illegal activities, and maintain basic stability in market prices.
- (4) We must strengthen review of responsibility costing and prevent costs from being passed on. Encouraging enterprises nobly to absorb price increases for raw materials is a positive approach that will help stabilize prices. To this end, while carrying out enterprise contract responsibility systems, we should conduct reviews of responsibility costing. Enterprises that nobly absorb increased prices for raw materials should be accorded preferential treatment in terms of profit retention policy, for this will alleviate enterprise apprehensions concerning price changes for the means of production. Firms that pass on costs and raise prices should be restrained from doing so.

For the Time Being, We Should Adopt a Relaxed Monetary Policy and a Balanced Fiscal Policy: Wang Songqi [3769 2646 1142]

A. China's current inflation stems from the interaction of a variety of factors and thus is a mixed form of inflation. In the sustained price rises of the past few years, the pent-up demand caused by previous supply shortages; recent transitional demand; cost-push inflation, which stems from increases in wages and in the prices of raw materials; supply mix contradictions, which result from the underdevelopment of certain sectors; enterprise profiteering and price gouging and the increase in the range of goods sold at negotiated prices, both of which phenomena result from the current dual-economic and double-track price systems; and the like are important contributing factors that cannot be overlooked. To blame China's inflation entirely on lax controls of the money supply or on monetary policy errors is not convincing.

If we recognize that inflation is defined as sustained price increases, we will discover that, although policy errors contribute to inflation, even more profound systemic factors are involved and therefore also merit careful attention. For example, (1) the controlled prices that were consistently maintained under the traditional system for 30 years distorted the relationship between commodity utility and cost. Thus many price rises that have occurred since reform was initiated involve a certain amount of self-readjustment. (2) It was not until our economy was opened up to the outside world that the prices of our old autarkic system gradually began to catch up with international levels. (3) When the competitive mechanism is weak, enterprises are under little or no pressure to reduce prices to sell their products, and monopolistic prices are hard to avoid in the absence of true capital markets. (4) The dovetailing of the double-track price system and the dual economic system reflect a repudiation of monolithic planned pricing and thus represent progress. Nevertheless, these systems do not promote balance, and the greater emphasis enterprises place on profits naturally provides more fertile soil for inflation. (5) The predominance of state ownership in China's enterprise system, its cadre system, its wage system and the like are not conducive to the development of consumption-fund self-regulatory mechanisms.

Since China's inflation is a mixed variety that is caused by the interaction of a variety of factors, we will have to adopt a comprehensive approach to curb our inflation.

B. Preliminary ideas on how to control China's inflation. In accordance with the principle that the remedy must suit the malady, inflation caused by systemic factors ultimately can only be resolved by advancing economic restructuring, and price rises that stem from policy errors must be handled through policy readjustment. If China's economic restructuring continues to advance in a healthy direction, improvements in productivity ultimately will pave the way for ameliorating the prolonged

contradiction between supply and demand and will eliminate some of the systemic factors contributing to inflation. This said and given our short- and medium-term aims, the question on which we should focus our discussion is how we can curb inflation by readjusting policy.

Thus we can conclude that, until the many systemic factors are eradicated and productivity is substantially improved, China's inflation definitely cannot be eliminated through the simplistic expedient of readjusting macroeconomic policy. The basic objective of our economic stabilization policy is not to "eradicate" or "eliminate" but to control inflation, which means that we should strive to avoid severe or galloping double-digit inflation. In view of the fact that inflation ultimately is conditioned by the relationship between supply and demand, we should adopt policies that best reduce the contradiction between supply and demand and eschew those measures noisily advocated by a few people in the past and even now—simplistic efforts to improve the relationship between supply and demand by strictly clamping down on demand. The "double tight" policy China unveiled in 1988 did not transcend this simplistic approach, will surely threaten economic growth, will not promote expansion of effective supply, and ultimately will cause the relationship between supply and demand to continue to deteriorate.

I suggest that China, for the present and in the short run, adopt a relaxed monetary policy; strive basically to balance its budget; adopt a deflationary tax policy; formulate measures to guide consumption; maintain, within resource supply limits, a fairly high rate of economic growth; restrain expansion of consumption funds; and strive to limit premature or advanced consumption. Meanwhile, while working to develop an externally oriented economy, we should, within our capacity, make appropriate use of foreign capital, avoid subjecting ourselves to a heavy foreign debt burden and, while stimulating economic growth and striving to achieve economic takeoff, maintain relative economic stability under conditions of moderate, not high, inflation.

Strictly Control Inflation and Promote Economic Growth: Hu Naiwu [5170 0035 2976]

Some comrades believe that an appropriate level of currency inflation helps accelerate economic development. This view is not tenable either in theory or practice. The Keynesian theory that inflationary policy stimulates economic growth assumes a number of preconditions. China, however, is at the preliminary stage of socialism and is resource poor, her commodity economy is underdeveloped, her market system is poor, and her returns on investment are very inelastic. Thus an inflationary policy will not accelerate China's economic development but rather will impair her reform environment and create difficulties for both her development and her reform. Because Western countries employed inflationary policies for a long time after World War II,

they began to suffer from stagflation in the late 1970s, which development signaled the bankruptcy of Keynesianism. In fact, developed capitalist countries did not really stimulate economic growth with inflationary policies but rather achieved their growth precisely by strictly controlling inflation. For example, the FRG experienced 1.1 and 2.3 percent rises in her consumer price index and economic growth rates of 11.3 and 5.9 percent during the 1950s and 1960s, respectively. And between 1953 and 1972, Japan's gross national product climbed at an average annual rate of 9.46 percent, while her consumer price index rose by only 4.38 percent a year. It is precisely because inflation is not conducive to stable economic growth that Western nations have made strict control of inflation rates one of the strategic objectives in their economic development.

China has certainly experienced inflation during the last 3 years. Can we achieve growth and yet avoid inflation during the shift from the old to the new economic systems? It seems that this will be hard to do. For our inflation stems largely from demand-pull factors and from structural imbalances. Faced with the reality of inflation, we have no choice but to adopt a variety of countermeasures and strive to hold the inflation rate to the lowest level possible. Given the limitations of our fiscal resources and the tolerance levels of our enterprises and citizens, the inflation rate preferably should be held to under 3 percent and not be allowed to exceed 6 percent.

We can approach control of inflation through both macroeconomic and microeconomic measures. Macroscopically, we can do the following. First, we must maintain an appropriate rate of economic growth. China is still at the preliminary stage of socialism, her per capita income is only 800 yuan, her savings and consumption rates are 30 and 70 percent respectively, so she has per capita savings of only 240 yuan and per capita consumption of only 560 yuan. In view of these limitations, we should not be overambitious in our efforts to develop the nation and improve the people's standard of living. Failure to take our nation's capacities into account and setting overly ambitious growth rates and investment levels are bound to create huge budget deficits and excessively high inflation rates. Thus maintaining a proper level of economic growth is a prerequisite for ensuring sustained, stable economic growth and preventing inflation. Second, total social consumption funds should grow at a rate slightly below that of national income, per capita urban-rural household incomes should rise more slowly than social labor productivity, and total social consumer-good purchasing power should be in line with market-supply capacity for such goods. Third, we must carry out a correct sectoral-mix policy so as to improve supply mix, improve macroeconomic results, increase effective supply and reduce the impact of structural inflation. Fourth, money supply should expand by a rate that is less than the combined total of the economic growth rate, the price rise engendered by structural price readjustment, and the price rise required

for economic monetization. In view of current conditions, our economic growth rate should be about 7 percent, structural price readjustment should cause prices to rise by 2 percent, and the price rise required for economic monetization should be about 2 percent. This means that we should hold growth in the money supply to below 12 percent. Fifth, we should not allow governments to cover their deficits through bank overdrafts but rather have governments sell development bonds to banks. This approach would not entail increasing the amount of money in circulation, would ensure that bank funds are used to support key projects and would improve supply mix. Microscopically, the main thing is to use contracts, leasing, joint stock systems and other approaches to separating ownership and management so as to strengthen enterprise operational autonomy and budgetary controls and to improve the incentive and self-restraint systems within enterprises. Only when these things are accomplished can macroscopic controls be successful.

Stabilizing Prices Requires Comprehensive Control Measures: Qiao Rongzhang [0829 2837 4545]

Stabilizing inflation and prices has become the key to whether or not economic restructuring can advance. And to stabilize prices, we must effect comprehensive control measures.

1. We must unify our understanding of these issues. Using inflationary policies to accumulate capital and accelerate development is not desirable. History proves that inflation reduces markets to chaos and impedes economic development. China must not go this route.
2. We must maintain a basic balance in the state's budget. Allowing budgetary expenditures to exceed receipts and issuing money to cover the resulting deficit are sure to bring about currency depreciation and price rises. Experience over many years has shown that maintaining a basic balance or slight surpluses in budgets ensures the material basis needed to stabilize the money supply and prices.
3. We must establish a system of compensating workers for price rises. The goal of our reform is to unleash productive forces, enhance economic results and improve standards of living. Thus we can by no means accept reductions in most people's real living standards as a price for economic reform. Because currency depreciates and prices rise during reform, workers' cost of living increases, so we should take appropriate steps and compensate workers for these cost rises. The best approach would be to coordinate wage raises with price hikes.
4. We must reduce the range of commodities subject to state fixed prices. Under current conditions, the prices of major agricultural produce should be fixed by the state, ceilings and floors should be established for important produce, and normal produce can be decontrolled and

left to market regulation. The prices of extractive industrial products should continue to be fixed by the state, flexible price limits should be established for important processed goods, and the prices of normal, minor commodities should be decontrolled and left to market regulation. The retail prices of major consumer goods should not be decontrolled; high prices may be set for a number of high-grade tobacco products, alcoholic beverages and luxury goods; and flexible price limits can be established for nonstaple foods that have already been decontrolled. Housing rents, medical costs, and fees for municipal transport, water, electricity and gas should continue to be fixed by the state and not decontrolled.

5. We must establish market price readjustment funds. The switch by enterprises to contract responsibility systems will have a major impact on markets. Under the old system, state enterprises primarily served the interests of society, but once enterprises assume contracts, they will mainly look after their own interests, not society's. This will transform enterprises from currency and price stabilizers into factors driving prices upward. Thus to ensure price stability and contain inflation, we must establish price readjustment funds and use these funds whenever necessary to induce enterprises to absorb cost increases and keep their own prices reasonable, and thereby hold prices down and stabilize currency value.

III. Issues Relating to Theoretical Interpretations of Inflation

We Must Correctly Understand the Meaning of Inflation: Liu Guangdi [0491 0342 4574]

In the past few years, China's prices and money supply have risen too rapidly, sparking "currency inflation." Well, what is "currency inflation"? Westerners generally define it as "a sustained rise in the prices of goods generally." The index that is generally used to measure and monitor inflation is the "rate of increase in prices." And China's theorists have established the following equation: "currency inflation = rising prices." But actually, this interpretation of the intrinsic relationship between price rises and inflation is one-sided and, in the case of China, inaccurate.

Inflation, which is defined as "a situation in which the actual volume of money in circulation exceeds objective demand for it," is manifested in different ways under different economic systems. In open market economies, inflation occurs as a rise in the level of prices and a depreciation in the value of currency, and in centralized, planned economies, it appears as "controlled inflation," under which major prices are artificially kept stable, while rationing, coercive replacement effect and other measures are employed. Thus inflation is not necessarily, or at least not completely, manifested as price rises or, if prices do rise, their rate of increase does not accurately reflect the true level of inflation.

Actual demand should always be "effective demand." Social reproduction occurs in the form of the continuous interaction between and development of the contradictions between commodity supply (demand for money) and commodity demand (supply of money), which if the process works properly, engenders a dynamic balance between commodity supply and demand and thus between money demand and supply. If the money supply exceeds objective demand for money, currency inflation occurs, which is precisely the same thing as commodity demand exceeding commodity supply, where demand inflation arises. Thus currency inflation is demand inflation, and to restrain the former we must curb the latter.

From the viewpoint of price rises, although expansion in the supply of money creates an "inflationary gap" and is the principal cause of price rises, it is not the only factor involved and sometimes even is not the major one. So we cannot simplistically use the rate of price rises to gauge the level of inflation. For example, liberating the many prices that have been subjected to artificially low ceilings over the years (such as minerals, major raw materials, agricultural produce and other goods) is essentially different from currency inflation, for the price rises such a decontrol engenders exceed the potential decline among other products, and the difference will be reflected as a rise in the prices of final products. Although the latter rise requires corresponding expansion of the money supply, the rise is not caused by currency inflation. Another example is increases in commodity costs, which although prompting cost-push price rises, do not stem from excessive demand and therefore basically cannot be classified as currency inflation. On the contrary, these price increases cause a nominal increase in aggregate social supply and appear as excessive supply, which creates a "deflationary gap." And if goods and services are priced at current, higher, cost-pushed prices, the money supply and aggregate demand will have to rise if aggregate social supply and demand are to be balanced in value terms. If, on the other hand, we reduce, not increase the money supply, we will have to cut output or sales, which actions will lead to recession and higher unemployment. Distortions in sectoral and output mixes can also lead to price increases. For example, after 1983 distortions occurred among comparative returns within China's agriculture, agricultural produce prices were irrational, and grain prices nosedived so that peasants were unwilling to grow grain. And once grain supply became tight, meat, poultry, and egg prices rose as a result of feed shortages. In addition, poorly developed markets and unhealthy microscopic behavior can also drive prices upward, and there are also price expectations, import-led price rises and the like. Clearly, besides money, many other factors contribute to price rises. And, in addition to prices, a variety of other complex factors affect money supply. Thus the price rise = inflation equation is too simplistic and does not adequately describe complex reality.

China's experience in the last few years demonstrates that price rises are certainly linked to some extent to price reform and do not stem entirely from currency

inflation. Before 1985, about one-half of the rise in our price levels stemmed from planned price readjustments, and only half occurred spontaneously in the marketplace. But while no new price reforms have been unveiled in the past several years, prices continue to surge at increasingly higher rates each year. Thus it appears that current inflation is basically due to currency depreciation, which is caused by an excessive supply of money, and not by decontrol of artificially repressed prices.

The Relationship between Price Reform and Price Increases: Lu Nan [6424 0589]

If we are going to effect price reform, price rises will be unavoidable, and this is something for which everyone must adequately prepare himself. We cannot expect to keep prices from moving or to hold rises to only 1 or 2 percent while carrying out reform. Naturally, the rise must not be too sharp; otherwise reform will be hard to implement. There are several reasons why price reform sparks inflation.

1. One of the important tasks of price reform is to readjust the inordinately low prices for basic products, particularly of agricultural produce. To change the irrational price parity between industrial and agricultural goods, we have to increase agricultural prices. For while an alternative might be to reduce industrial prices, thereby holding agricultural prices down, this approach is unfeasible in real economic life. Thus we have no choice but to increase agricultural prices, which move is bound to set off increases in general price levels.

2. Another important aspect of inordinately low prices for basic products is that price parities within industry are irrational, with those of extractive and raw-material industries being too low. To change this state of affairs, we have to increase the prices of minerals and raw materials. As in the above case, we could reduce the prices of high-priced goods and thereby maintain basic stability in general price levels, but in actuality this approach is hard to effect. Thus we have no choice but to increase prices for minerals and raw materials, which move will drive general price levels higher.

3. Although the prices of basic products were hiked during the reform of the past several years, we failed to raise the sales prices of related goods. Thus as reform progressed, we had to provide more and more state subsidies, which increased the state's financial burden. In the long run, this problem must be resolved. Yet in so doing, we must not allow the prices of basic products to slip back to their original levels. Thus we have no choice but to raise the prices of related goods, and this inevitably will cause general price levels to rise.

4. We must also properly handle the relationship between price and wage reform. In theory, wages should rise at the same rate as labor productivity, and an important component of price reform is that price and

wage reform must be coordinated so as to facilitate reordering of the relationship between wages and prices. Thus the steady rise in wages in the absence of productivity improvement means that appropriate price increases are unavoidable.

In sum, price reform will inevitably lead to price increases but in the long run will prove beneficial to the functioning and development of the entire economy. Nevertheless, we cannot turn around and assert that price increases stem solely from price reform, for experience over the last several years shows that many factors that are not necessarily related to price reform contribute to price increases and to a certain extent work against price reform. Clarifying this point is of great importance to our ability correctly to understand the relationship between price reform and price rises.

The Relationship Between Inflation and Economic Growth: Zhao Haikuan [6932 3189 1401], Zhu Suzhen [2612 4479 5271]

In academic circles, definitions and conceptualizations of inflation greatly differ, and thus conclusions naturally differ. Since this paper addresses the issue of how to resolve the problem of inflation, we define inflation as price increases above the rate of 4 percent. We adopt this definition because we would like to exclude those price increases that result from price stickiness during economic growth and to focus our analysis on the effects of human, political factors on price rises.

In China, comrades who advocate expansion of demand believe that inflation can stimulate economic growth in two ways: (1) through resource mobilization, under which it is alleged that inflation promotes full utilization of idle resources in the community, and (2) through concentration of capital, under which it is believed that inflation enables the state to focus more funds on key development projects. It must be admitted that, under certain conditions, these processes do work (even though they entail exorbitant opportunity costs). For example, after World War II, a number of countries managed to promote economic growth by stimulating demand, and this is what happened with China's recent expansionary fiscal and monetary policies and economic hypergrowth. Yet to stimulate production with inflationary policy, two preconditions must be present. (1) There must be idle resources and insufficient effective demand, and (2) the public must suffer delusions about money. Where these two conditions coexist, inflationary policy may be used to increase effective demand either by fully exploiting idle resources or by taking advantage of the public's money delusions to enable governments to wield more funds. However, in China, where investment has swelled for a long time, there are clearly no idle resources or lack of effective demand. Thus if we are going to stimulate economic growth with inflation, we will have to focus on the public's ignorance about money.

Money delusion, a concept that is frequently mentioned in studies of the interrelationship between inflation and economic growth, refers to people's tendency to "place psychological value on but ignore the purchasing power of money." Of the three Western schools of thought concerning the role of inflation in promoting economic growth—the supporters of the stimulative-effect thesis, the proponents of the negative-impact thesis, and the neutralists—even the positivist claim in effect boils down to an emphasis on the role of money delusion, arguing that governments take advantage of people's failure to anticipate inflation to increase investment, savings and profit rates and thereby stimulate economic growth. Yet as a psychological response, money delusion does not last long. For when delusions about money are shattered, people begin to expect corresponding readjustments in prices and nominal wages. Thus while in the short term this factor can influence real output and prices, over the long run it leads only to price increases.

After having experienced 30 years of low wages and prices, our people seem to have been very pleased to accept wage and price hikes. And widespread delusion about money afforded economic decision-makers a good opportunity to use expansion of the money supply to increase demand and thereby spur production and economic growth. But after several rounds of inflation-retrenchment-inflation, people's money delusions were basically supplanted by expectations of and revulsion toward price increases. A survey by China's social-survey system showed that in 1987 79.9 percent of the population was dissatisfied with inflation. And a sample survey conducted by the State Statistical Bureau discovered that the share of urban and rural residents whose real incomes had been eroded by inflation rose sharply from 20 percent in 1986 to 40 percent in 1987.

Some comrades have exaggerated the community's receptiveness toward inflation, arguing that inflation should give no cause for concern so long as society remains basically stable and peaceful. But let us ask, if inflationary growth policy dissatisfies 80 percent of the population and causes the real incomes of 40 percent of the population to decline, of what use is it to belabor the positive effects of such a policy?

In Western nations, powerful labor unions and income indexing have enhanced the role of the public's expectations of inflation in government decision-making and the economy. But in China, there is no formal requirement that people's money incomes have to be raised when prices climb, so we have not yet placed much importance on the study of inflationary expectations. And some comrades even argue that social groups do not understand the internal workings of the economy and merely "pick up their rice bowls to eat meat and scold their wives when they set the bowls down," so their inflationary expectations need not overly concern us. But, in fact, as money delusions are shattered and as people increasingly come to expect price increases, the negative effects of inflation are becoming increasingly

salient. The growing tendency to favor, in the realm of production, breeding over cultivation, industry over agriculture and sideline industry, construction over industry, transportation over construction, service industry over commerce, and transport of goods for sale over service industry, and, in the area of distribution, bonuses over wages, material rewards over cash bonuses, and other such distortions should not be overlooked in the study of economic theory and policy. Continued attempts to use inflationary policy to stimulate economic growth will only increase the community's expectations that prices will rise, and this will lead to malignant, galloping inflation.

The Issue of the Economic Effects of Inflation: Yang Shengming [2799 5110 2494]

Some comrades believe that China's current inflation is all bad and produces only negative effects, whereas others emphasize the positive effects of inflation, believing that it stimulates China's economic growth. Given this divergence of opinion, we must carefully analyze the issue of the economic effects of inflation so as to determine which view is correct.

1. The Effects of Inflation on Income Distribution

Inflation has a strong distribution effect on incomes. People whose incomes rise at a rate higher than that of price rises benefit from inflation, whereas those whose incomes fail to keep pace with prices are harmed. In China, the people who are hurt by inflation are fixed-wage earners employed in public institutions and their dependents, retirees, people on leaves of absence, and a very small number of people who live off interests and rents. The people who gain are those who share in enterprise profits. This redistribution effect of inflation intensifies contradictions among social strata and undermines existing distribution policy and relationships. If distribution policy and relationships are correct, they will be distorted by the redistribution effects of inflation, and if the current distribution system is defective, we should reform or readjust it. Why resort to inflation to correct the problem? Using inflation to redistribute citizens' incomes will either undermine the principle of distribution according to work or work against correct distribution policy.

2. The Effects of Inflation on the Distribution of Wealth

There are two kinds of wealth—material and money. Money wealth, which is also known as variably priced property, includes cash on hand, bank savings deposits, and various types of bonds. The real value of this type of wealth varies inversely to the inflation rate. During inflation, money wealth inevitably depreciates, giving rise to a transfer of value, which reduces the wealth of some groups and enriches others. As of the end of 1987, China's populace had more than 300 billion yuan in savings, 100 billion yuan in cash on hand, and, including treasury and other types of bonds, held a total money

wealth estimated at approximately 450 billion yuan. Under these conditions, even if inflation rates exceed interest rates by only 1 percent, citizens will lose as much as 4.5 billion yuan in money wealth, which is tantamount to a transfer of 4.5 billion yuan from the people to the state via banks. Inflation clearly amounts to uncompensated expropriation and represents a powerful "communist wind."

One view maintains that, no matter how much prices rise, people will be able to put up with inflation so long as their money incomes outpace price rises. But experience proves that this view is simplistic and that it ignores the unequal impact inflation has on incomes and the way it erodes everybody's money wealth. And even the people who can cope with inflation have been screaming bloody murder about the depreciation of their money wealth, which is a major reason behind the loud protests that inflation has sparked. The effects of inflation on the redistribution of wealth have made many people very uneasy.

3. The Stimulative Effects of Inflation on Economic Growth

People who praise inflation assert that it stimulates economic growth and even believe that it is a precondition for economic takeoff. The major argument such people advance is that, during inflation, wages rise at a slower pace than prices, and wage raises generally lag behind price hikes, so governments can exploit these factors to transfer consumption funds into savings and thereby accelerate economic growth. This was one of the "secret formulas" employed by Western countries to develop their economies during the 18th and 19th centuries, but it no longer works in the Western world today. Powerful unions resist letting wages fall behind prices, even though they have failed to prevent this from happening. Thus since the 1970s, Western inflation has not only failed to accelerate growth but rather has combined with economic stagnation to form what is commonly known as "stagflation." Yet some comrades still insist on applying the old Western "secret formula" to China. What are we ever to make of that? While we certainly must master the good things of the West, the refuse of Western history must be abandoned and by all means must not be introduced into China. Ours is a socialist country in which the people are the masters, so there is absolutely no need to resort to inflation to "pick the people's pockets." If there is a shortage of funds, we must carefully explain the problem to the people and get them to pitch in, tighten their belts and support national development. Aren't treasury bonds and savings good enough ways to raise large amounts of funds? Why must we resort to the unsavory approach of using inflation to "pick pockets"?

On the basis of this analysis of the principal economic effects of inflation, we conclude that China must firmly oppose inflation. Of course, opposition is not going to

make inflation go away just like that. Rather, since inflation is caused by economic conditions, it can be eradicated only by improving the economic environment.

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JINGJI YANJIU on Price, Inflation

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[Text]

I. General Level of Prices and Inflation

1. Inflation Analysis

People have frequently taken the rise in the general level of prices and monetary inflation as possessing the same meaning or significance. Over the past several years the general level of prices in our country has maintained a sustained rise and inflation and the economy tending to be conventionally heated have seemed to be facts without question. People have analyzed their causes frequently from the angle of the system. The period of China's inflation in demand in the years 1984 to 1985 happened to precisely coincide with the period of the introduction of the theory of shortage economy and use of the shortage theory to explain their inflation in demand quite naturally has obtained the conclusion that shortages in the traditional structure are inevitably shown in demand being overly large and the economy being excessively heated. The computation results showing the existence yearly of a large gap between gross supply and gross demand have also given positive support to this theoretical analysis and seem to have given added force to the above-mentioned logic.

Nevertheless, such an analytical angle not only leads people away from making a concrete analysis of the special characteristics of the rise in the price level but also can lead to errors in judging the effects of the macroeconomic policy and the selection of policies. At the same time, to understand the rise in the general level of prices from the angle of the structure and to attempt to use the measure of levelling down the general level of prices by means of exercising overall control have in themselves logical contradictions. Generally speaking, monetary inflation is a general quantitative problem in the short-term operation of the economy and measures countering monetary inflation are not related to changes or reform of the economic structure. If a rise in the general level of prices is treated in a sweeping manner as the inevitable result of structural shortages, then before the completion of the reform of the economic structure, the rise in the general level of prices and monetary

inflation in short-term operation are not related and use of counter monetary-inflation measures cannot depress the price level. If general quantitative regulation can effectively change the macroeconomic stature and make it approach a certain point of equilibrium, then it will be possible to check and keep under control monetary inflation. Nevertheless, even though the macroeconomy approaches a state of equilibrium, the general level of prices can still rise. The problem lies in to what extent changes in the general level of prices are related to the evolutions or changes in the stature of the short-term economic operations and in after all the functions general volume regulation can play in levelling and suppressing the general level of prices.

Obvious, in studying the general level of prices and monetary inflation, we should start by analyzing the operations of the economy. Analysis of the operations is different from analysis of the system. In the case of the latter, the changes in the stature of short-term operations may not be taken into consideration but in analyzing the short-term operations, a relative stability of the economic structure is assumed. In the long-term process of the slow evolutions of the economic structure, such problems as "expansion motivation," "hunger and thirst for consumption," and "insufficient effective supply" are existent and constitute the basic (normal) state of the economic operations while surrounding this stature, the economy continuously expands or shrinks or contracts and these short-term undulations usually comprise the temporary tightening and easing of the relative changes in demand and the contradictions in the market's supply and demand structure. The object of general volume regulation consists of the short-term undulations and not of the basic stature. Relative to an ideal market economy, this basic state is imbalanced but in the economic operations under the existing structure the balanced state of the short-term undulations is this basic stature. In the short-term undulations, a part of the general level of prices correspondingly develops changes and if the economy is relative to the basic state tending to be heated, the responding price changes constitute monetary inflation. Under the conditions of double-track prices, planned prices and market prices possess a different degree of sensitivity toward the short-term undulations of the economy, and in such a juncture to discuss in a sweeping way the general level of prices cannot grasp the characteristics of price changes in the short-term undulations.

2. Comparison of the Dissimilarities and Similarities in the Rise of List and Market Prices Under the Conditions of Double-Track Prices

Double-track prices means that in the price system the price of a commodity can either be a list price or a market price. For the sake of simplicity, we shall call all non-market prices list prices, including planned prices, guidance prices, and so forth. Market prices not only refer to prices in the means of production markets and in country fair trade but also include the computed prices

concealed in the exchange of resources. Double-track prices have been in vogue in China for a long time. Before the reform of the economic structure, the state purchase prices and the country fair trade prices as well as the purchase prices of industrial products by state-run enterprises and those by town and township enterprises had all along been double-track prices. However, at the time, the relative weight of market prices had been small and both in theory and in policy little consideration had been given to the role of market prices. In recent years, following the reform in the purchasing structure of agricultural products, structure of the resources commercial trade and the price structure, double-track prices have become daily more common and the study of economic operations cannot but take the existence of double-track prices as the fundamental background.

The price determining mechanisms of market prices and list prices are different. Market prices are determined by supply and demand and can sensitively reflect changes in supply and demand. Only a few months after the beginning of the retrenchment in 1985, the market prices of means of production in short supply fell every month. The market prices also reacted sensitively to the changes in the supply and demand relations of grain determined by the changing volumes in grain production, foreign trade, mouth grain and feed grain, and grain for use in wine-making. Regarding the changes in list prices, in principle they are determined by the price control departments. Seen from the long run, readjustment of list prices must abide by the law of value but in the short term, the price control departments usually react very slowly to the changes at times in supply and demand and, besides, readjustment of list prices must have regard to the various sides of society and to the ability to bear on the part of finance. There are thus many hindrances. Naturally there are disparities in the price control capability of the price control departments regarding the list prices of different commodities. In the case of commodities of a single standard or variety, such as cement, coal, grain, eggs and so forth, their list prices can easily be subjected to unified control and supervision. Their ordinary changes are rare and once price readjustment is made the scale is usually a large one. In the case of commodities of a complex standard and different varieties, such as non-standardized electrical machinery and equipment, fruits, vegetables, and so forth, the price control departments are unable to strictly control their list prices, resulting in relatively frequent changes in the list prices. Thus while they are slightly sensitive to changes in supply and demand, they are still subjected to administrative intervention.

Between the list prices and market prices of the same commodity, there does not exist any rule that they will inevitably change toward the same direction. In 1979, the state purchase price of grain was adjusted upward but its market price dropped. In 1986, the price of cement in unified distribution was raised by 60 percent, but its market price, though generally stable, registered a slight

fall. At a time of falling market prices, list prices obviously will not suffer any changes and when market prices rise, whether or not list prices follow will frequently be determined by the degree of laxity or strictness of the current price policy.

In the entire price structure, while the chained changes or reactions of the market prices of various kinds of commodities are subjected to the restriction of supply and demand, chained changes or reactions between list prices show an obvious characteristic of the cost of production being serially or progressively affected. In fact the control regulations of list prices recognize the stiff character of the enterprises' interests. Hence when the rise in the list prices of products in the initial process leads to, and is followed by, similar rises in the subsequent production stages, the price control departments frequently give the matter support and secret approval, and such a procedure has no great connection with the supply and demand conditions of the commodities at various stages. Rises in the market prices of initial-stage products will affect the marginal cost of production of products in the following-up or subsequent processes and form a chained reaction in the list prices of products in the subsequent or following-up processes. On the other hand, a rise in the list prices of products at the initial stage does not necessarily lead to a chain reaction in market prices of products in the subsequent or following-up processes. For example, in 1987 there was a rise in the list prices of raw materials and motive power in the production of steel products but a similar reaction in the market prices of different varieties of steel products was wanting. Thus, there was a strong demand for steel materials for production use and their list prices and market prices rose simultaneously. On the other hand, the demand for steel materials for building use was stable and steady. However, while their list prices rose, their market prices stood still.

Hence, in economic analysis a differentiation must be made between rise in list prices and rise in market prices. Only in there being changes in market prices can corresponding changes in supply and demand be reflected. Rise in list prices and short-term supply and demand relations have no necessary liaison with each other. The state's unified readjustment of prices undoubtedly has no relation with short-term supply and demand and this is also true when the enterprise itself raises the list prices. This may happen when the economy is in a state of equilibrium or tends to be in a tightening state and may also happen when the economy tends to become heated. Naturally, if the economy expands and market prices rise, generally the enterprises may be stimulated to raise the list prices. At such moments, the control exercised by the price control department can frequently be rather weak and as a result a situation may appear in which the list prices follow the step of market prices in going up. Only at such a moment is there a similarity in the nature of the signals given by the list and market prices vis-a-vis the economic stature. Since the general level of list prices will in specially fixed conditions change or move in the

same direction with the general level of market prices, then obviously relying solely on the general level of list prices to judge macroeconomic conditions easily leads to errors in judgement. Only the general level of market prices is the signal lantern correctly reflecting the macroeconomic condition.

3. What is monetary inflation?

In recent years, the general level of prices in our country has maintained a sustained rise. According to the definition of western economics, it seems that this is inflation. However, the meaning of the general level of prices is not the same in China and in countries of the market economy. In the those countries, the general level of prices is tantamount to the general level of market prices and a rise in the general level of market prices indicates an over-heated economy and thus monetary inflation and the macroeconomic condition are in direct liaison with each other and the anti-monetary inflation measure is gross volume control. On the other hand, in China under the conditions of double-track prices, the general level of prices is a mixed general level of list prices and market prices. A problem would arise if we were to adopt in full the western concept of monetary inflation.

In China the economic significance of changes in list prices and in market prices is clearly different. But in the index of mixed average prices this distinction is obliterated. Logically speaking, rise in the index of mixed average prices envisages four possibilities: First, no change or rise in list prices but rise in market prices; second, no change or fall in market prices, but rise in list prices; third, both list prices and market prices remain unchanged, but transaction volume in list prices is reduced; and fourth, fall in market prices, but drop in transaction volume in list prices falls even more heavily. Of these four possibilities, only the first manifests that the economy has tended to be heated. It is almost absolutely certain that after China has taken the road of reform, generally speaking there is little possibility of the index figure of mixed average prices being lower than 100. Rise in the general level of mixed average prices does not necessarily imply an over-heated economy. If a rise in the general level of mixed average prices is defined as "inflation," then this concept of "inflation" is out of joint with the macroeconomic stature and even resorting to gross volume regulation cannot effectively check this "inflation." A definition of this kind basically goes against to the macroeconomic theory. With the definition not being appropriate, if in policy guidance the macroeconomic theories continue in use then this very easily can lead to errors in the selection of policies: when the rise in the general level of mixed average prices has no connection with the economy tending to being heated, if a decision is made on the basis of the above-mentioned definition to enforce the policy of anti-inflation, quite possibly not only the effects of checking and depressing price levels cannot be attained but also economic depression may result.

Hence, we are of the opinion that inflation which is in liaison with the macroeconomic stature and the gross volume policy refers to the sustained increase in the general level of market prices (here the general level of market prices should be computed on the basis of the total transaction volume of commodities and not on a weighted transaction volume at market prices). The general level of market prices sensitively denotes the macroeconomic condition and provides guidance to gross volume regulation. This interpretation of inflation is determined by the economic short-term undulations and is not directly related to shortages in the structure. The prolonged ossified and twisted list price structure under the traditional structure is the associate of structural shortage. It necessarily produces pressure on the depressed prices to rise. Readjusting the list prices and price reform are for the purposes of letting the twisted list prices return to being balanced prices. This procedure can entirely be gradually realized under the conditions of the general supply and demand being basically normal and the general level of market prices being relatively stable. Although readjusting list prices can also lead to a rise in the general level of list prices and depreciation in the value of money, this is obviously different from inflation (rise in the general level of market prices). Rises in list prices is caused by the use of money to replace the coupons, credentials and targets for purchasing list price commodities and the money used in purchasing market price commodities will not, because of this, be depreciated in value. Therefore, readjusting the list prices may bring about a rise in the general level of list price but this rise in list price logically has no necessary liaison with inflation in demand, or a heated economy, or monetary inflation (rise in market prices). Naturally, we may call a rise in the general level of list prices as another kind of "inflation" (such as nominal inflation) but decidedly we cannot mix it with real inflation (rise in market prices) and thus lead to confusion in understanding.

Theoretically deviating the rise in the level of list prices from inflation does not imply a proposition to leave aside the readjustment of list prices. Readjustment of list prices is a procedure of readjusting interests. The inclination of the enterprises and people to protect their acquired interests determines that changes in the interest pattern cannot be too fast, or too severe and therefore the speed of readjusting list prices should be kept under control. This cannot be achieved, however, by relying on gross volume regulation. At the same time, in the course of list price readjustment, changes in income may lead to transfers and movements in demand and produce causes attracting inflation (the constituent causes of inflation are multiple and complex; what is meant here is the possibility and not the inevitability) and controlling the speed of list price readjustment is at times beneficial to stabilizing the macroeconomic stature. However, as a whole, control of the process of list price readjustment is a problem of the planned management of list prices and cannot be confused or mixed up with gross volume regulation. Outside of the purchase prices of agricultural

products, the great proportion of list prices are determined by the sellers and using gross volume regulation to change the volume of money or the buyers imposes little restriction on the sellers' actions in adjusting prices.

Nevertheless, onesidedly emphasizing the stability of list prices still produces the after-effects of leading to coming or future monetary inflation. The sustained stability in list prices may lead to shortages in the commodities of list prices, and to raising the cost of transactions (such as falling in line, searching for, sellers' poor services, and so forth) and at the same time cause a rise in the market price of the commodity. If the market price is again kept under control, supply will be depressed, shortage will be aggravated and in the end concealed monetary inflation will take the place of open monetary inflation.

4. Gross Volume Policy and Price Control

In economic operations, periodic or cyclical changes frequently occur in the macroeconomic stature and this needs the prompt application of gross volume regulation. The purpose of gross volume regulation is to shorten the gap between actual production level and potential or concealed production level and seek for a relatively stable general level of market prices. Stabilizing the general level of list prices is not the target of gross volume regulation, because the object in gross volume regulation is demand but changes in the general level of list prices have no necessary liaison with the size of demand. At the time of demand inflation, list prices naturally will rise rather rapidly but when demand tightens (shrinks) market prices will fall but list prices may possibly still rise. Since stabilizing the general level of list prices is not the objective of gross volume regulation while the general level of list prices has great effects on the general level of mixed and average prices, then in studying the effects of gross volume regulation we should not turn to the changes in the general level of mixed average prices. One of the important measures in gross volume regulation is the monetary policy. Between monetary supply and the price level two kinds of relationship exist: A lax money market will lead to rise in market prices and regulating money supply can influence the general level of market prices. The relations between changes in list prices and money supply are different. Tightening the money market cannot restrict the rise in list prices. In the event list prices have risen, the value of coupons and credentials has depreciated, and the monetarized degree of the economy has risen, then money supply should be correspondingly increased, otherwise the scale of reproduction will shrink; at such a juncture the rise in list prices takes the initiative while money supply is passive. Therefore, it is incorrect to talk about tightening the money market and checking the rise in commodity prices in general terms. At a time of a rise in the general level of market prices, definitely we should tighten the money market; even though the general level of market prices is stable, the general level of list prices each year may also rise. This is not over-heating of the

economy or monetary inflations; a monetary policy of increasing money supply in accompaniment with a rise in list prices is not one of "stimulating inflation."

The task on the side of macroeconomic control on the part of the price control department is to relatively stabilize the general level of list prices. So long as list prices exist, there must be a special control department to handle the administrative control and this department's main measures of control should be administrative ones. It is a natural process for list prices to gradually rise but if in the short-run the rise is too rapid and compensation is not sufficient then this would cause violent changes in the interest pattern. Price control departments should suitably control the speed of the rise in the general level of list prices and this and gross volume control are two different things. Price control departments lack the measures to carry out gross volume regulation and hence cannot control the general level of market prices through regulating supply and demand. If the price control department is requested to stabilize the general level of market prices what it can do is to apply administrative measures to control market prices. The functions of market prices are to reflect the instant changes in supply and demand, guide production and consumption, and adjust the distribution of resources. Once market prices come under regular administrative restrictions, their functions will be shattered to pieces and they may from then on assume the status of an additional type of ossified and twisted list prices. This not only will produce the results of restricting supply and encouraging consumption but also may give added hindrances to future price reform.

Due to the imperfection in fostering and developing the markets, under certain conditions sellers have resorted to improper means such as substituting second-rate goods for 1st-grade goods and cheating in various ways and thus have contributed to a rise in the market prices. This is an important reason and argument for putting market prices under control and restriction. In reality, the sources of such problems are the imperfection in the market structure and laxity in commercial and government control. Restricting the market prices does not solve the problem.

In the course of macroeconomic control, we should differentiate between the different tasks, different objects and different task-bearers between gross volume control and price control. This is a prerequisite to the enforcement of effective macroeconomic control.

II. Value of Money, Coupons and Credentials and Residents' Real Income

Here, we shall principally dwell on the problems of commodity prices and income of the consumers. In recent years, the problem of commodity prices has become the central theme in talks among social circles. In 1987, commodity prices became all the more the hot point and attracted concern from all sides. However, in

the social concept of commodity prices, there is much confused understanding which can hardly find any elucidation in theoretical research. For example, such questions as: do the staff members and workers feel the same about the drop in their purchasing power and the actual changes in the value of money? What benefits do the residents receive from the coupons and credentials? How can we protect interests already gained by the residents? Should the residents' demand for subsidiary food products be regulated by the law of value? Let us begin from the starting point of China's actual economic conditions—the double-track price system, and follow a new angle to probe into these problems.

1. Two Categories of Buyers and Two Kinds of Money Value Under Conditions of Double-Track Prices

On the topic of how in theory to treat the real changes in money value, we should begin with talking about the two categories of buyers under the conditions of double-track prices. Under the conditions of double-track prices, for a long time consumers have been divided into two categories. One category consists of buyers of list price commodities. They are represented by urban permanent residents. Another category consists of buyers of market price commodities and we may take peasants entering on cities to represent them. When they buy the same kind of commodities such as grain, oils) these two categories of buyers differ greatly in their form of transaction. First, buyers who have the qualification to buy list price commodities and those buyers who can buy only market price commodities have a different status in conducting their transactions. The former can freely choose the form of purchase. They can buy list price commodities and can also buy market price commodities. The latter will find it very difficult to enter the "territory" where in list price commodities are transacted. Second, the transaction measures of the two categories of buyers are different. Buyers of market price commodities use money as the only means of exchange whereas in their transactions buyers of list price commodities, aside from paying out money, must make an outlay of a stated amount of certificates (below various kinds of coupons, evidences, and vouchers will all be termed certificates).

In transactions on list price commodities, the mere exchange of commodities and money cannot complete the exchange process. Actually the exchange process consists of the mutual exchange activities of commodities and (money plus certificates).¹ When buying the same quantity of commodities, the buyers of list price commodities will pay less than what the buyers of market price commodities pay and the difference (equivalent to the differences between the list price and the market price) is in effect the price of the certificates. If the holders of the certificates do not buy the commodities but transfer them to another holder (without taking into account the exchange cost in the transfer activities of the certificates), the receipts from the transfer of the certificates are equivalent to the price of the certificates and the interests represented by the certificates are thus

converted into monetary form. Distribution of the purchase certificates is determined by the pattern of interests already gained and is formed under the traditional economic structure and the prices of certificates are determined by the differences between list prices and market prices in different localities, each according to the different conditions in the localities. Certificates are a necessary constituent part of the purchasing power in transactions involving list price commodities. The buyer's actual purchasing power is equivalent to purchasing power in money and purchasing power in certificates.

Thus, so far as the two different categories of buyers are concerned, their money value is different. If the two categories of buyers purchase the same quantity of certain commodities, the amount of money they have to pay is different. The money value of the buyers of list price commodities is higher than the money value of buyers of market price commodities and this is due to the existence of the prices of certificates. In the case of the former, if the list prices are increased and the certificates depreciate in value, then their money value falls but such conditions do not affect the money value of the latter. The existence of double money value under double-track price conditions causes economic analysis much more complex. Western economists can simply take the changes in money value as reflecting changes in the buyer's purchasing power. In our case, we must concretely differentiate between whose money value has suffered changes. At the same time, the economic meaning of these two categories of money value is different. Theoretically speaking, the higher estimation of the money value of buyers of list price commodities is preconditioned on the existence of the prices of certificates. Their money value is a so-called conditioned one and its being high or low is not determined by changes in general supply and demand but by the list price policy. The money value of buyers of market price commodities manifests the real purchasing power of money and only due to the appearance of monetary inflation will the money in the possession of this category of buyers depreciate in value.

Hence, the real value of money is the money value of buyers of market price commodities whereas against this money value the money value of buyers of list price commodities is nominal money value. Before reform of the economic structure, for a long time nominal money had been highly estimated and to the urban residents the feeling had been that the purchasing power of their money was exceptionally strong. This was of course propped up by the high prices of certificates. Now in comparison with 1978, real money value has not fallen much but nominal money value has continuously fallen and is approaching real money value. Regardless of whether we are speaking from the angle of putting the price system in order or the angle of social justice, the fall in nominal money value is normal. The worth of certificates is seen from the real money value and fall in nominal money value merely shows that certificates do not worth as much money as before. Naturally, in the

course of the fall, in nominal money value what the living standard of the staff members and workers is cannot be seen from the nominal money value itself.

2. Residents' income and real benefits

Before the reform, the income of staff members and workers constituted principally of their basic salaries and wages and this formed the traditional concept of looking at the basic salaries and wages in order to find the level of income. At present, the structure of the monetary income of staff members and workers has basically changed. This concept of income is no longer worth accepting and is actually harmful. However, definitely many people and even comrades of certain propaganda departments have still used the basic salaries and wages to measure the income level and come to the inappropriate conclusion of a fall in the standard of living. In reality, measuring the monetary income of the staff members and workers must not be based only on the basic salaries and wages but must also on the large amounts of bonuses, subsidies and income from spare-time work (among the intellectual elements the rapid increase in their spare-time income is rather universal to a certain extent). A large portion of the income outside of the basic salaries and wages is income of a normal nature and determines the high or low level of consumption. In addition, in recent years in enterprise units the current practice of wages in kind (units after buying subsidiary foods and industrial consumer goods sell them at cheap prices, or distribute them without compensation, to the staff members and workers) is occupying a considerably large proportion of the entire income of the staff members and workers.

Despite that in recent years commodity prices have risen to a large extent, the government in the once-over readjustment of list prices has usually given monetary subsidies and made direct compensation. At the same time the yearly increase in monetary income has performed a compensatory function against the rise in commodity prices. Seen only from the monetary income, the actual income of the staff members and workers has already increased considerably, adding income in kind to it the entire real income is thus much higher.

In analyzing the income of urban residents, the role of certificates should be taken into consideration. Income from certificates is the product of the number of certificates and the prices of the certificates. The actual benefits of the residents should include actual income and income from certificates. Income from benefits is the residents' actual benefits. Although in surveys of family planning such benefits is the residents' actual benefits. Although in surveys of family planning such benefits cannot be correctly reflected and the governments also prohibits the transform of certificates at a price, yet in the existing transfer activities in certificates anybody can easily see their value and in the exchange of goods in kind with certificates both parties calculate according to the prices of the certificates. With the

volume of certificates remaining unchanged and the list prices remaining stable, a rise in market prices implies an increase in the income from certificates. If market prices remain stable, a rise in list prices indicates a reduction in income from certificates; if prices remain unchanged, reduction in certificates indicates a fall in income from certificates whereas an increase in certificates indicates a rise in income from certificates.

For the sake of briefly and simply illustrating the effects of price changes on the residents' real benefits, certain abstractions will be made in the following analysis, namely, the assumption of there being no changes in the monetary income of salaries, wages and bonuses and the income of the residents' families. This can show that there are three possibilities for the fall in the residents' actual benefits.

(1) Rise in market prices type. No changes in list prices or in the number or volume of certificates, if market prices rise, money value falls when residents purchase market price commodities; at this juncture prices of certificates rise, if the residents' market price purchase volume is larger than the list price purchase volume and the increase in income from certificates is smaller than the increase in monetary outlay, the actual benefits are reduced. Such a condition may be caused by the short-term changes in the supply and demand relative to market price commodities and may also be the result of the list prices being low too long and shortages in list price commodities.

(2) Non-compensatory price adjustment type. No changes in market price or in the volume of certificates, if list price is raised, but amount of monetary compensation to residents is smaller than the price readjustment amount of list prices and the purchasable volume of list price commodities, or if the residents do not have any monetary compensation, then the residents have to increase their monetary outlay, there is a reduction in income from certificates, hence actual benefits drop.

(3) Change of structure type. No price changes, in the event of a reduction in amount or volume of certificates or of insufficient supply volume of list price commodities procurable by certificates and residents' income from certificates being reduced while to maintain the original purchasing volume will have to purchase market price commodities, then this will cause a drop in actual benefits. But such a condition is not necessarily reflected in the commodity price index. Similarly, the price index may not be able to reflect any increase in actual benefits resulting from an increase in the amount or volume of the certificates.

In actual fact, only when the three above-mentioned conditions appear and the increases in salaries, wages, bonuses and income in kind are not sufficient in compensation, then the residents' actual benefits are really reduced. Adoption of this method of analysis helps in

rectifying the traditional concept of income and in correctly and fully understanding the extent of the effects on people's actual living caused by a rise in prices.

3. Policy on Commodity Prices and Policy on Consumption

"Stabilizing the vegetable basket" is a central work of the current city governments. However, experiences from the past several years have shown that we should not take a short-term view of stabilizing commodity prices and ensuring or protecting consumption but that we should prevent causing a long-term instability by bringing about a short-term stability. Hence, how to stabilize and what to protect or ensure constitute a problem that is worth studying.

Policy on commodity prices has all along been closely related to policy on consumption. The purpose of stabilizing the prices of consumer goods is to protect the public's interests. However, if control of commodity prices brings about the results of depressing supply and stimulating consumption, then in the end we shall be confronted with the difficult situation of damaging both commodity prices and consumption.

Looking back on the reform of the prices of subsidiary food products in the cities in 1985, it can be discovered that the results appearing at that time of list prices being raised but going out of control, of consumption being expanded but refusing to be depressed, and the financial burden tending to be enlarged were due to an important cause of the cyclical fluctuations in agriculture while the non-coordinate between the policy on commodity prices and the policy on consumption also taught us a lesson. Take pork for example: Reform of the prices of subsidiary food products in 1985 started at a time when after the peak period in agricultural production market prices were at the lowest ebb. The subsidies made at that time on the basis of the consumption base figure were changed from being secret to out in the open and in fact price subsidies were used to ensure and protect the food consumption base figure of the masses. Following the sharp increase in the income of the staff members and workers, the ability to spend on food consumption ascended to a new stage and the continuous increase in consumption pushed the rise in commodity prices. After more than a year's time it was necessary to revert anew to controlling the prices of state-run commerce. Nevertheless, while in the first half year of 1987 pork was once again subjected to double-track prices, the supply volume of pork at list price was not under control. As the demand for pork at list price not subjected to quantitative restriction nor to price regulation, naturally it was greatly expanded. Moreover at the time pig production was at a low ebb, financial subsidy was rapidly expanded and the ability to subsidize ultimately reached a critical point when it could no longer be sustained. As a result, only in the second half of the year was supply restricted in a passive way with simultaneously raising the list price. Thus in three years' time the sequence of events

was: liberating price and liberating quantity to restricting price and liberating quantity and back to restricting price and restricting quantity. All this illustrated one point, that enforcement of double-track prices was needed by objective circumstances.

Looking at the situation now, it seems that the increased outlay on our country's residents is being increasingly spent on food and that the demand for food can very easily exceed the conditions of our country's agricultural resources. Under such conditions, we should no longer protect by the use of list prices the newly increased food consumption on the part of the consumers. The method of allowing the boat to rise higher with the rising tide such as opening up the supply of list price food or yearly and progressively increasing the supply volume at list prices tends to stimulate consumption and to aggravate the contradiction between supply and demand in food.

Speaking from another side, due to the market prices of agricultural products tending to steadily rise, consumers will demand stabilizing the list price and expanding the supply volume at list prices. This in reality is demanding the continuous increase in their income or receipts from certificates. Adding to this the increases in salaries, wages and bonuses, they will receive double benefits. This is tantamount to bringing pressure to bear on the country's finance from two sides,—making secret subsidies (additional financial outlay) and increasing salaries and wages (reducing financial receipts). To continue in this way is not only abnormal but also impossible.

At present, we should carry out the guideline of "protecting one section and opening up another section" and coordinate the policy on commodity prices and policy on consumption toward that end, that is recognizing and protecting the already acquired benefits of the consumers to buy list price food products according a basic fixed quantity but subjecting their additional consumption to regulation by the law of value and to conforming with the condition of supply. In the policy on commodity prices we should stabilize the list prices and should not stabilize the mixed average prices and should open up market prices to guide consumption. In the case of certain subsidiary food products of a single or unitary variety and specification, we should insist on the principle of supplying a basic fixed quantity at list prices and by the use of certificates with the requirement that any purchase in excess of the fixed norm should be subjected to transactions at market prices. Only by so doing will it be possible to achieve the stability of commodity prices in unison displaying the functions of prices as economic levers.

In the event of list price being raised then monetary subsidies should be increased based on the basic fixed norm and the price-adjusted amount to ensure that the acquired interests will not be subjected to any loss or we can resort to the linking of subsidy with the list price index. But subsidy should not be linked with the index of

mixed average prices, otherwise this would mean subsidizing the rise of market prices and also would be tantamount to acknowledging and accepting that excessive demand is reasonable and should be encouraged. Subsidizing the rise in market prices will increase the volume of money for purchasing market price commodities and this will revert to pushing further the rise in market prices and will form the vicious cycle of "rising more subsidizing more" and "subsidizing more rising more." Since subsidies are computed on the basis of the basic fixed quantity they should be given on a person to person basis. The method of linking salaries and wages with the list price index will make the per capita subsidy in low-income families tend to the low side and is not just enough.

Footnotes

1. Here the theory of "joint exchange" created by Song Guiqing [1345 0948 7230] is employed. A systematic analysis and conclusion of this theory are seen in the book "Macroeconomy in the Reform," published by the Sichuan People's Publishing House, 1988 edition

Article Advocates Scientific Approach to Use of Law of Value

40060330 Beijing JINGJI RIBAO in Chinese
20 May 88 p 3

[Article by Yang Shengming [2799 5110 2494]: "Adopt a Scientific Approach to Understanding and Employing the Law of Value"]

[Text] How can we properly use the law of value? This is a major issue in the development of a socialist market economy. I believe there are a number of issues we must fully grasp if we are to understand and use the law of value properly.

First, we must correctly understand the law of value. There are two extreme interpretations of law—ossification and mythicization. The ossified approach used to be displayed as an abhorrence of the law, in the belief that the law is alien to socialism but is now manifested in the tendency to treat the law and planning as antithetical and in the preference for rooting the law in planning and contracts instead of the reverse. The mythicization approach is displayed as a blind faith in the workings of the law, as if the law could readily solve all problems, as in the era of the "invisible hand."

These two extreme views are readily apparent in agricultural price policy. Contracts for procurement of fixed amounts of grain are not based on the law of value but rather are set quite arbitrarily and subjectively. Prices that ought to be increased are instead kept low, the law is used as a pretext to "further readjust" decontrolled prices of cash crops and aquatic products, problems are ignored, and necessary supplementary measures go unapplied. This is the basic reason why grain prices have been too low and that the prices of some cash crops and

aquatic products have been too high in recent years. Experience shows that we will never be able correctly to employ the law if we do not do away with ossified and mythicized interpretations.

The law of value is the basic law governing commodity production and exchange. Given this status, once the law is understood, it immediately becomes the basis for scientific planning and for procurement contracts, any plan or contract that deviates from it loses its scientificity. Nevertheless, fully affirming by no means implies blind worship of the law. The era of the "invisible hand" is long gone and will never return. So we must master the use of the law under new conditions.

Second, the operational levels and forms of the law of value should be in line with the levels of development of the commodity economy and domestic markets. The law is related to the commodity economy and domestic markets as fish are to water. It might seem that its levels and forms could be manipulated at will, but that in fact is not the case. Generally speaking, the law operates more fully and in more varied form the more advanced the commodity economy and domestic markets are. And when the latter are less advanced, the law operates less fully and in less variety.

How developed, then, are China's commodity economy and domestic market? On the whole, they are underdeveloped or very underdeveloped, which condition is reflected in the large share of our total economy comprised by the natural and seminatural economies, which are antithetical to commodity economy and domestic markets; by the existence alongside commodity economy and domestic markets of a fairly powerful planned economy, which is signified by traditional command planning; by the fact that our commodity economy is a seller's market of scarcity, is comprised of a variety of conflicting systems of ownership, and thus is subject to considerable state interference; and in the great disparity among the levels and components of commodity economy and domestic markets, which have yet to form organic systems.

The current state of China's commodity economy and domestic market dictates that the law of value will have to function within a small area of the economy, within a small range and in a limited number of forms. Given these conditions, we should not blindly copy the practices employed by nations whose commodity economies and domestic markets are highly developed in employing the law of value. Because of the great diversity between regions, sectors and economic components in China, the law must accordingly operate in different directions and at different levels. Thus in employing the law we cannot "use one knife for everything" but must analyze specific conditions and come up with concrete approaches.

Third, we must emphasize study and determination of the magnitude of value. Serious disagreement still persists in theoretical circles about what value consists of. I

believe that value includes at least the following components: (1) The substance of value, namely the abstract human labor embodied in commodities; (2) the essence of value, namely relationships among commodity producers; (3) the magnitude of value, or the amount of socially necessary labor expended in the production of commodities; (4) the form of value, namely the form in which the magnitude of value is expressed. These components are interdependent and check and balance each other, and none is dispensable.

While trying to understand the concept of value, we should emphasize the different components of it at different times. Prior to the seizure of power by the proletariat, we addressed the issue from the viewpoint of our revolutionary tasks and generally stressed the essence of value. That is to say, we analyzed things through the essence of value, thereby revealed the nature of human and class relationships and thus laid the foundation for our revolutionary strategy and tactics. Once the proletariat seizes power, and especially during the period in which economic development becomes the central task, we should place particular emphasis on the study and determination of the magnitude of value. This work remains crucial to our current price reform and to all of our economic work, because the magnitude of value is the criterion by which we must judge price levels. If we do not master this criterion, we will never be able to decide how much each price varies from value and thus will find it difficult to make prices accurate and to achieve our aims in price reform.

We recently made a number of attempts to determine the magnitude of value and thus were able to devise some useful theoretical and policy prices. Regrettably, however, work in this area has progressed slowly, even wavered and not gone far enough in addressing the needs associated with price rationalization. To use the law of value properly, we must strengthen research on and determination of the magnitude of value.

Fourth, we must properly handle the relationship between price stability and movement. The relationship between value and price is one between content and form and between essence and appearance. Price movement is determined by many factors, the most important of which are worker skills, the level of scientific development, the degree to which science is applied to the production process, the linkage of production to society, the scale and efficiency of the means of production, and natural conditions. Since these factors frequently change, value naturally changes along with them. But the factors change slowly, which means that value changes slowly, too. Thus in dealing with the issue of prices, we must oppose ossified, static views that fail to respond to change, and enable prices to change as value varies, oppose the practice of willfully manipulating prices so that they fluctuate sharply, and instead seek to coordinate the range and frequency of price movements with

changes in value. Only by avoiding or overcoming these two one-sided extremes can we establish a correct perspective on price movements and accurately employ the law of value.

Nevertheless, the ossified, static view dominated China's pricing for a long time, interpreted price stability to mean price freezes, and kept prices the same for 10-20 years, which is why prices, especially those of agricultural produce, have become so severely divorced from value. In the last 9 years, on the other hand, prices have changed rapidly. These two extremes are abnormal. As argued above, these extremes can be avoided if we maintain a constant effort to keep prices in line with value. If fact, except in times of severe natural disasters or of war, supply-demand relations and state price policy generally should not change radically, so prices should not change too fast, either.

Fifth, the government should effect necessary, appropriate administrative intervention. As stated above, the "invisible hand" is passe, so we cannot allow the law of value to operate completely spontaneously. Instead, we need to adopt appropriate administrative measures to supplement the law and to enable it to function better. Such measures include the following.

1. The government must wield a certain amount of authority to set prices. Given the fact that the production of some goods and services—for example, running water, cooking gas, posts and telecommunications, and train transport—is absolutely monopolistic in nature and does not engender competitive markets, the prices of such goods should be set by the state in a unified fashion and not be left to enterprises or be subject to the double-track system. Naturally, in setting such prices, the state must provide, as required by the law of value, for profit margins that are in line with average rates.

2. The government must retain a certain amount of regulatory power over prices. When necessary, the state should be able to freeze all prices, establish price ceilings for goods and services in short supply, and provide protective floor prices for commodities affecting the national economy and the people's livelihoods whenever oversupply occurs.

3. We must ensure that the law of value regulates production in a positive way, not a negative one. Governments at all levels must gather and disseminate accurate price information so as to guide production.

4. We must conscientiously enforce the Law on Prices, maintain strict investigation and supervision of prices, and promptly check law breaking, disorderly conduct, and price gouging.

Greater Citizen Involvement in Capital Accumulation

40060331b Beijing JINGJI RIBAO in Chinese
20 May 88 p 3

[Article by Feng Yuzhong [7458 3768 1813]: "Increase Citizens' Concern for Capital"]

[Text] Too little concern for capital on the part of China's citizens is a big impediment to our economic reform and a major issue that must be solved as we seek to eliminate the potential threats to our economy and to advance reform.

By "concern for capital," I mean the amount of interest people display toward assets and capital reproduction, which interest is a fundamental mark of and a motive force propelling national social, economic and cultural development.

The lack of concern for capital in China has adversely affected our society, economy and political life. This problem has many causes, but the major roots are two.

First, the property right relationships between producers and enterprises are blurred, and the money incomes of China's workers can be spent in only one direction. Who is the real owner of enterprises that are supposed to belong to all the people? Economically and legally, only one group is so anointed—various types of government departments at various levels. Enterprise employees are "masters" only politically or morally, and citizens employed by nonstate enterprises are even more "estranged" from the property relationships of enterprises "of all the people." Under these conditions, hundreds of millions of employees can spend their money incomes in but one way—on consumption, and this prevents them from investing in expanded reproduction. Furthermore, egalitarian and free-supply welfare benefits cannot but strengthen citizens' "you can't buy land, you can't buy a house, so if you've got the money, spend it on color TVs and refrigerators" mentality. Thus citizens lack sufficient enthusiasm for capital reproduction. This is the inevitable result of the "state owned, government operated, bureaucrat run" model we pursued for so long and is a historical lesson from which we should learn.

Second, citizen's private property and inheritance rights lack proper theoretical support and legal protection.

The basic way to arouse the enthusiasm of hundreds of millions of employees for investment and to strengthen all of our people's concern for capital is to reform existing property-right relationships and to deepen reform of the system of ownership.

First, we must establish a model of mixed community ownership and transform state enterprises into socialized and pluralized entities that operate under this model. This system of ownership can be organized

through sale of stock, and its advantages are that (1) It infuses more vitality into state owned entities and assets and into reproduction of capital. (2) It promotes change in the function of government and facilitates administrative streamlining. (3) It directly "couples" the interests of individual, enterprise and collective producers, hundreds of millions of employees and the state. Especially important is the fact the system allows employees to buy shares of their companies, which is bound to give citizens much more enthusiasm for investment and to transform tens of billions of yuan in consumption funds into productive capital, thereby eliminating aberrant consumption, imbalance between supply and demand and other economic anomalies. (4) The system directly links producers and the means of production, thus giving producers incentive to work.

Second, is to provide legal protection for private property, private capital and inheritance rights. Once the system of mixed community ownership is established, the number of stock owners will rise, total stock equity will increase, and inheritance of stock shares and of other forms of private property will become widespread. Thus we must provide legal protection and moral support for the right to inherit private property and capital. This will give citizens incentive to invest and is an important way by which to enhance the concern of all the people for capital.

Strengthening concern for capital and providing incentive for investment are important not only economically but also politically, for the establishment of socialist democracy. For this approach will closely link citizens' personal interests with the future of the nation, with social order, and with economic prosperity and thus will enhance people's confidence in and sense of responsibility toward the socialist cause.

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FOREIGN TRADE, INVESTMENT

Tianjin's Li Ruihuan on Foreign Trade Reform

SK1607020488 Tianjin TIANJIN RIBAO in Chinese 17 May 88 p 1

[Text] Li Ruihuan called for great efforts to facilitate reform in foreign trade in the third part of his government work report, which dwelt on deepening the economic structural reform. It is necessary to reform the foreign trade administrative system in an active and stable manner in line with the principle of "sole responsibility for profit and loss, open management, coordination between industry and foreign trade, and wide application of the system whereby foreign trade corporations act as agents for other enterprises in the export of their commodities."

First, we should popularize universal contracted managerial responsibility system in foreign trade and ensure that contracted targets are fulfilled at every level. We

should assign export plans to foreign trade enterprises and commodity supply plans to export-oriented production enterprises, allow those which surpass the contracted quotas to gain benefits, and reduce the amount of self-retained foreign exchange of those which fail to fulfill the contracted quotas. Second, we should permit a large number of production enterprises to export on their own or to serve as foreign trade agents and should implement various preferential policies encouraging exports so that production enterprises will be able to participate directly in international exchanges and competition. Third, we should improve the foreign trade operational mechanisms. Foreign trade enterprises should use the information on the supply and demand of the world markets to guide production enterprises in developing readily marketable products. Meanwhile, we should organize a number of import-export corporations combining industrial or agricultural enterprises with foreign trade enterprises, which actively carry out multi-formed joint operation and marketing so as to take risks and share profits together. Fourth, we should exert great efforts to develop foreign trade intermediary organizations, establish service and consulting institutes, establish export associations on a trial basis which are composed of enterprises of the same trades, and open reimbursed brokerage organizations to serve as the bridges for enterprises' exports and to render various services. Fifth, with regard to production enterprises whose export commodities account for a larger proportion and which earn a great amount of foreign exchange, we should assess their performance based on their export volume, volume of foreign exchange earnings, contract fulfillment rate, product quality, cost of earning foreign exchange through export, and date of goods delivery. Sixth, we should extensively introduce the experiences of Chinese-foreign joint ventures and cooperative enterprises and enterprises that are run exclusively with foreign funds and should conduct reforms of the labor and distribution systems first at enterprises having high labor efficiency, ability to create a great amount of profits and taxes, and good export prospects in order to raise their labor efficiency. We should also invite foreign businessmen to come to Tianjin to contract or lease our municipality's enterprises and directly bring in foreign advanced managerial methods to increase the enterprises' export competitive edges. In short, we should make the best use of the good reputation that our municipality has established over the past years to further rationalize the foreign trade system, and even the entire economic managerial system dealing with foreigners, and implement the strategy for the economic development of coastal areas more quickly.

ECONOMIC ZONES

Haikou Customs Director on Hainan Tax Privileges

40060293a Guangzhou NANFANG RIBAO in Chinese 11 May 88 p 1

[Report on interview with Haikou Customs Director Wang Gaotang [3769 7559 1016] by correspondent Wang Hongru [3769 1347 0320]; place and occasion not given: "Hainan Has Greater Customs Tax Privileges Than Other SEZs; Enterprise Taxes on State-Restricted Imports Have Been Cut in Half; Traders Can Take

Duty-Free or Tax-Reduced Imports for Private Use Out of Hainan"]

[Text] Haikou Customs Director Wang Gaotang answered this reporter's questions on 9 May 1988 on issues such as how state policy on Hainan customs tax privileges is being put into effect.

This reporter asked what was the main effect on customs of the state's more flexible, open economic policy that is being carried out in the Hainan SEZ? Wang Gaotang answered that the main effect is greater customs tax privileges. For instance, the machinery and equipment, raw and processed materials, spare parts, means of communications and transportation, and other material, as well as office supplies, that are imported by enterprises in the Hainan SEZ to supply their building and production needs are all exempt from customs, product, or value-added taxes. Customs, product, or value-added taxes have been cut in half for merchandise that Hainan enterprises import to sell on Hainan markets. In particular, taxes on state-restricted imports have been cut in half. These are greater tax privileges than the other SEZs enjoy.

In response to the question of whether merchandise imported to Hainan from ports outside of Guangdong Province will enjoy Hainan's privileged policy, Wang Gaotang answered that merchandise imported to Hainan from ports outside of Guangdong which has undergone customs formalities in ports outside of Guangdong will not enjoy Hainan's duty-free or tax-reduction privileges. Imported merchandise under customs supervision that is transshipped to Hainan to undergo customs formalities will enjoy Hainan's duty-free and tax-reduction privileges.

This reporter asked if customs will allow Hainan traders to take duty-free or tax-reduced imports out of Hainan. To which, Wang Gaotang answered that duty-free or tax-reduced imports to the Hainan SEZ, such as goods that are assembled with imported duty-free or tax-reduced components, can only be used and sold in the Hainan SEZ. Individuals can only take reasonable amounts of these goods for private use out of Hainan.

In responding to whether customs will allow Hainan enterprises to ship imported duty-free or tax-reduced raw and processed materials out of Hainan for processing, Wang Gaotang said it is permitted, but only based on the instruments of ratification of the responsible Hainan SEZ departments, after registering processing contracts with customs, and according to the approved customs "Registration Manual." All processed products must be shipped back to Hainan by the contract-stipulated deadlines. Duty-free (unprocessed) goods that are imported by Hainan enterprises can be used only in enterprise construction or production and can only be marketed in other areas in Hainan subject to the approval of the responsible State Council departments.

This reporter asked if people from outside of Hainan who buy homes in Hainan or live in Hainan for a long time will be allowed to bring in household goods, such as electrical appliances and other state-restricted imports. Wang Gaotang replied that they must apply to customs for certificates issued by the relevant, responsible Hainan SEZ departments. Upon ratification, reasonable amounts of these goods for private use can be cleared duty-free after examination by customs, but they are only for private use and cannot be transferred or sold.

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TRANSPORTATION

Construction Begins on Second Bridge Over Qiantang River

40060333a Hangzhou ZHEJIANG RIBAO in Chinese
22 Apr 88 p 1

[Excerpt] Full-scale work on the second bridge across the Qiantang River, a focus of national attention, commenced yesterday. Relevant leaders and more than 1,000 bridge builders participated in a grand ceremony marking the beginning of construction at the site, at Sibao, Hangzhou.

This new bridge, which will cost a total of 240 million yuan, will span the Qiantang River 13 km downstream from the older bridge and have on a single deck a four-lane roadway and a double-track railway, and the bridge proper will consist of a 1,340 m, 18-span continuous concrete deck. Since commencing work on the northern and southern banks in August of last year, the Bridge Engineering Bureau of the Ministry of Railways, which is responsible for the construction of this massive, modern bridge, completed in a short 8-plus months preparatory work which usually takes 15 months, doing a top-notch job in the process. Eight work sites have already been set up for the approach on the southern bank, where construction can begin on 16 pier footings, and 5 sites have been readied on the northern bank, where 10 piers will be built. From the river bank, one espies a forest of hoist derricks, drilling rigs and drilling rods soaring against the sky on both sides. And the surface of the river bustles with an unusual amount of activity. Within 300 m of the northern bank lies an assemblage of large floating cranes, tug boats, and barges that will be used in positioning the spans. In a single array, four floating platforms that will construct the midstream piers tower above the waves, carrying one soaring drill rig after another. And the eight steel-fender cofferdams that will be used to construct the piers, which will support the highway side of the bridge downstream and the railway side upstream, have already been driven into the river bed. On the southern bank, two access trestles extend out over the water like a pair of dragons sprawled side by side, and on top of them two traveling

platforms are already in place, so that the four mid-stream piers can be constructed simultaneously. On both banks, 2,000 bridge builders and regular construction workers struggle day and night in an effort to complete the bridge by 1991.

Railway Minister Li Senmao [2621 2773 5399], who made a special journey here to participate in the ceremonies, expressed his satisfaction with the preparatory work and thanked Zhejiang province and the city of Hangzhou for the interest and support they have displayed for the construction of the bridge.

Governor Shen Zulun [3088 4371 0243] described the commencement of full-scale work as "a joyous occasion for our province"; extended cordial greetings to the 1,000 builders who have worked so hard at the site; and asked representatives of all levels of government, all departments and all units in Zhejiang attending the ceremonies to continue to show concern for and to support railway construction and to unite, cooperate and work together to ensure that the bridge is completed on schedule.

Mao Yisheng [5403 0110 0581], who directed construction of the first Qiantang River bridge a half a century ago, cabled his congratulations from Beijing and relayed the solicitude of old bridge-building experts for the construction of the new span.

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PRC MEDIA ON FOREIGN ECONOMIES

Zhou Chuan on Applying NICs' Experience To Develop Coastal Economy
40060305 Beijing JINGJI GUANLI [ECONOMIC MANAGEMENT] in Chinese No 4, 1988 pp 11-15

[Article by Zhou Chuan [6650 1557]: "What the Economic Take-off of the 'Four Small Dragons' Has Taught Us"]

[Text] This article is a comprehensive analysis of the economic evolution of Taiwan, South Korea, Hong Kong, and Singapore, all in Asia, to analyze the dynamics of their rapid growth and the tactics and measures adopted by them and to explore for experiences that we can use as reference to speed up the economic development of our open coastal areas.

Basic Characteristics

Everything goes through a process of development and change. To study the economic conditions of the "four small dragons," we must analyze them from a historical viewpoint not only to understand their present but to know their past. This will help us make up our own

minds to catch up with them and make China prosperous and strong. The basic national (regional) conditions and characteristics of the "four small dragons" are similar in many ways but mainly in the following:

First, they are small in territory. Among the "four small dragons," Singapore is the smallest with only 588 sq km of land and 2.6 million people. Hong Kong has an area of 1,069 sq km and a population of 5.53 million. Taiwan has an area of 36,000 sq km and a population of 19.29 million. South Korea is a little larger with 98,000 sq km and 43.61 million people. They are smaller than any of China's coastal provinces. Guangdong, with 210,000 sq km and more than 63 million people, is equivalent to several Taiwan Provinces.

Second, they are poor in natural resources. South Korea not only lacks such resources as timber, cotton, and sugar, but is particularly deficient in coal, iron, and other mineral resources. Taiwan has fairly good agricultural resources, but lacks energy and basic materials. Hong Kong and Singapore are both very deficient in natural resources. Hong Kong was once a small barren island inhabited mainly by fishermen, without even enough fresh water. Their major resource is manpower, that is, cheap labor.

Third, their economic foundation is weak. During World War II, the "four small dragons" were all occupied by Japanese imperialist forces, and to varying degrees all suffered from the ravages of war, particularly South Korea, which was devastated in the Korean War. In the 1950's, they were still beset with difficulties. Per capita income in South Korea was just over \$60. Hong Kong at that time was a place where "tens of thousands of people slept in the streets." Singapore was rather hard up then, with declining production and rising unemployment.

Fourth, their geographical locations are good. Hong Kong and Singapore are both free ports with exceptional geographical advantages for entrepot trade. South Korea and Taiwan are both on the Pacific coast with good seaports, which provide favorable conditions for them to expand foreign trade and speed up their economic growth. Objective geographical advantages and favorable international environment provided important conditions for the rapid economic development of the "four small dragons."

Economic Evolution

As shown by their past conditions, the "four small dragons" have two common advantages: 1. They have good harbors and are strategically situated on important lines of communications. 2. They are rich in labor resources. They also have two common disadvantages: 1. They are poor in natural resources and do not have the fuels and raw and semifinished materials needed for industrial development. 2. Their domestic (local) markets are small, and prospects for developing a commodity economy and exchange markets are extremely limited. How could they get out of their economic backwardness? Knowing how to develop their strong points and work around their shortcomings, they have all chosen

an export-oriented strategy and actively developed an export-oriented economy. In other words, they have turned their attention to the international market, set up step by step an economic operations mechanism geared to market demands abroad, and adopted an economic cycle of the import (primary and intermediate products)—production (including processing and assembling)—export model. Each of the "four small dragons" has its own ways and has gone through different stages of economic changes, but they have all made export and trade the goals of their economic evolution.

Taiwan was a mainly agricultural province with few industries. To promote economic development, the Taiwan authorities in the 1950's called for "agriculture to nurture industry." Making full use of its abundant labor resources, Taiwan first developed its traditional agriculture, then moved on to agricultural modernization, and quickly increased production of export goods, laying the foundation for industrial development. In the 1960's, with the onset of the new technological revolution, the world's developed industrial countries began a major overhaul of their production structure and moved labor-intensive industries to foreign countries. Taiwan seized the opportunity to bring in large amounts of capital and technology, actively developed an export-oriented economy, and pushed its products into the international market. In the 1970's, the petroleum crisis shocked the developed industrial countries into new structural readjustments, this time moving energy- and material-consuming industries abroad. Taiwan again seized the opportunity to make use of foreign capital and, while developing heavy and chemical industries, quickly developed technology-intensive, export-oriented light industries. Taiwan's industrial evolution has gone through roughly four phases.

First phase (1950-1960): Emphasis was on labor-intensive agricultural and sideline products processing industries and light and textile industries, producing mainly sugar, flour, edible oil, canned food, textile, and plywood.

Second phase (1960-1970): Emphasis was on labor-intensive and technology-intensive light and textile industries, producing mainly semiconductors, black-and-white television sets, household electrical appliances, plastic products, and garments.

Third phase (1970-1980): Emphasis was on the development of capital-intensive heavy and chemical industries, including petrochemical, iron and steel, machine-making, shipbuilding, and automobile industries.

Fourth phase (beginning in 1980): Emphasis is on the development of technology-intensive industries, such as the manufacture of computer monitors, keyboards, terminals, data units, and other electronic products and other high-tech industries.

Through the above phases of development, Taiwan has become a newly industrialized region with export processing industries playing a dominating role. Foreign

trade is growing at a super high speed. Between 1960 and 1980, Taiwan's exports increased at an annual rate of 24-29 percent. In 1986, Taiwan's exports totaled \$39.7 billion, and its GNP was \$72.3 billion. Its per capita GNP increased from \$207 in 1964, when the economy began to take off, to \$3,448 in 1986.

South Korea has followed the road toward industrialization from producing substitutes for imports to producing mainly for exports. It has gone through the following process of economic evolution.

1. During the period 1962 through 1966, as the United States, Japan, and other developed countries readjusted their production structure from one of light and textile industries to one of heavy and chemical industries, South Korea took the opportunity to implement a policy of "developing first light and then heavy industries with the former supporting the latter" and set up a series of export industrial and agricultural manufacturing and processing bases.

2. During the period 1967 through 1971, it continued to put the emphasis on "export promotion," adopted effective measures to bring in advanced technology from abroad, and enhanced the competitiveness of its export goods. During this period, its GNP grew at an average annual rate of 9.6 percent.

3. During the period 1972 through 1976, relying on progress in science and technology and aimed at speeding up the development of heavy and chemical industries and achieving self-sufficiency in food production, the emphasis was placed on the development of petrochemical, electronic equipment, iron and steel, shipbuilding, automobile, and other export industries, which added momentum to the country's economic growth.

In the past 10 years, South Korea has actively imported most advanced technologies for the development of technology-intensive industries and has, in the fields of heavy and chemical industries, turned out a series of hot-selling export products. In 1986, its exports totaled \$34.7 billion, and its GNP reached \$99.1 billion. Its per capita GNP increased from \$87 in 1962, when the economy began to take off, to \$2,272 in 1986.

Singapore has gone through the following phases in its economic evolution.

First phase (1961-1965): Emphasis was on labor-intensive industries, including metal-fabricating, shoemaking, tailoring, papermaking, and printing industries, aimed at creating more jobs. At the same time, a number of industrial processing zones and free trade zones were established.

Second phase (1966-1970): The transition was made from producing substitutes for imports to producing mainly for export. The emphasis was on the development of oil-refining, ship-repairing, machine-making, and electronics industries.

Third phase (1971-1980): Emphasis was on developing an export-oriented economy. The authorities raised \$920 million to speed up industrial modernization, increase exports to the developed countries, and develop entrepot trade. Industrialization made a big stride forward during this period.

Fourth phase (beginning in 1980): The production structure is being readjusted. In view of the fact that wages rose too much for a time and of the soaring oil prices, the authorities are encouraging the development of capital-intensive and technology-intensive industries to gradually eliminate the labor-intensive industries. They are also giving support to export industries with sophisticated technologies and high additional values and helping the traditional export industries to carry out technological transformation and expand their markets with new products.

Singapore's economy has developed rapidly in the past 20 years and more. In 1986, its exports totaled \$15 billion, and its GNP was \$18.7 billion. Its per capita GNP rose from \$531 in 1966, when the economy began to take off, to \$7,200 in 1986.

Hong Kong's economic development has gone through roughly three phases.

1. Transition from entrepot trade to processing industries. Before 1950, the British Hong Kong authorities had taken advantage of Hong Kong's free port status to vigorously develop entrepot trade, which played an important role in Hong Kong's quick economic recovery. In the early 1950's, the United States launched a war of aggression against Korea and subsequently imposed an economic blockade against China. As a result, Hong Kong's entrepot trade was dealt a serious blow. Imports and exports were on the decline for 3 years on end, forcing Hong Kong to turn to the development of export-oriented processing industries. Thus began the development of light industry, mainly cotton mills. In 1959, locally made products accounted for 69.6 percent of Hong Kong's total exports. In 1960, the proportion was 72.8 percent. It was an indication that processing industry had taken the place of entrepot trade as the dominating factor in Hong Kong's economy, a very important step in Hong Kong's economic development.

2. Development of an export-oriented economy. In the 1960's, the Hong Kong authorities set up a number of semi-official organizations, including the Hong Kong Federation of Industries, Association for Scientific Management, Trade Development Bureau, and Productivity Promotion Bureau, to provide greater support and guidance to industrial and commercial enterprises in funding, technology, designing, quality control, and marketing abroad, which gave a strong impetus to the development of export-oriented industries. From 1960 to 1969, the number of factories increased from 4,784 to 14,078, and the number of workers increased from 220,000 to 1.52 million. Major trades such as the textile and garment industries grew rapidly, and the output of

cotton yarn and cloth doubled. Electronics, clock, watch, toy, and other new industries also grew considerably. An increasingly large proportion of Hong Kong's total output value was contributed by the manufacturing industries, which boosted both exports and imports, created new jobs, and gave an impetus to the development of banking, building, real estate, shipping, and other trades.

3. Diversified economic development. Toward the end of the 1960's, making full use of funds, technology, and business management experience provided by the United States, Japan, and Western European countries, Hong Kong leaped forward in the development of banking, commerce, transport, real estate, information, communications, and other trades, while accelerating the growth of the processing industries, thus entering a period of diversified economic development. Since 1970, Hong Kong's economic look has taken on great changes. First, the production structure has undergone major readjustments. The contribution to GNP of primary industry dropped from 2.2 percent in 1970 to 0.6 percent in 1985; that of secondary industry dropped from 37.1 percent to 29.3 percent; and that of tertiary industry rose from 60.7 percent to 70.1 percent. Second, export goods have been constantly updated. For example, the timely move from traditional textiles and clothes to high-grade apparel has made Hong Kong one of the world's major clothing exporters, and clothing now accounts for 34 percent of Hong Kong's total export earnings. Traditional plastic flowers and toys have been replaced by silk flowers, filament flowers, and electronic toys, and Hong Kong is now the world's largest exporter of these items. Third, banking, shipping, real estate and building, and tourism have become the four main economic pillars of Hong Kong. Hong Kong is today the world's third largest financial center, after New York and London. In 1985, Hong Kong handled 58.35 million tons of cargo and became the world's second largest container docking and shipping center, after only Rotterdam. Fourth, trade and markets have become highly diversified. At present, Hong Kong has trade relations with more than 170 countries and areas, forming a very extensive international trade network. At the same time, many countries have set up consulates general and headquarters of well-known conglomerates in Hong Kong, turning Hong Kong into the Far East command center of western countries and transnational corporations. In 1986, Hong Kong ranked 13th in the world in imports and exports.

In Hong Kong's economic evolution, because its processing industry was export-oriented from the very beginning, and because it skipped the heavy and chemical industries and proceeded directly to develop technology-intensive industries, it has quickened the process of industrial modernization and followed its own unique way of economic development. In 1986, its imports and exports totaled \$70.8 billion, and its GNP was \$37.4 billion. Its per capita GNP increased from \$360 in 1966, when the economy began to take off, to \$6,769 in 1986.

Dynamics of Take-off

Many factors have contributed to the rapid economic growth of the "four small dragons." The following have provided the main driving forces.

First, adoption of the "export orientation" to set the economic cycle in motion. This is the common strategy used by all the "four small dragons." Facts show that the strategy has produced important results. By moving into the world market, they are no longer restricted by their small domestic or local markets and lack of natural resources, but are able to develop a commodity economy beyond national borders. Through the cycle of import-production-export, they have not only expanded exports and earned more foreign exchange, but effectively used international capital and resources, brought in advanced technology and scientific management, and increased their own economic strength. The pressing need for enterprises to bring their technological and managerial standards up to the international level has quickened the countries' (area's) overall industrial modernization.

Second, taking advantage of opportunities provided by the international environment. During the 1950's and 1960's, the world economic trend provided many good opportunities. International trade was growing rapidly, and the economically developed countries generally adopted free import and export policies. The rising tide of the technological revolution and the radical readjustment of production structures in the industrialized countries led to the rapid development of capital-intensive and technology-intensive industries in the underdeveloped countries and areas. The Korean War and the Vietnamese War provided markets for export goods. These and other opportunities were recognized by Taiwan, South Korea, Singapore, and Hong Kong, and became favorable conditions for them to speed up their economic reorientation.

Third, implementation of preferential economic policies. Hong Kong has a low-tax policy, which limits the income tax rate to 18 percent for foreign- and locally-owned companies of limited liability, and 17.5 percent for enterprises of unlimited liability. The policy has proven very effective in attracting foreign investors to build new factories in Hong Kong. As free ports, Hong Kong and Singapore not only allow free entry and exit of goods, but impose no customs duties on ordinary commodities. The Taiwan authorities help exporters with low-interest loans, export subsidies, and other measures. As a result, the number of export-oriented enterprises and total exports have increased sharply. In 1986, Taiwan drew worldwide attention when it became the largest exporter among the "four small dragons."

Fourth, full decision-making power for enterprises. They all pay attention to stimulating enterprise initiative by enacting favorable rules and regulations. In Singapore, the board of directors of an enterprise has a great deal of power. It has the power to make its own decisions on management and investment policies, hire competent people, and deal directly with foreign firms in commodity buying and selling. The Hong Kong authorities follow a noninterference policy. The government provides overall industrial development directions, financial support, technical assistance, and export guidance, but does not interfere in the enterprises'

operations and management, nor assume economic responsibility for them. The enterprises are on their own to compete internationally for survival and growth.

Fifth, construction of infrastructure. To create a good investment climate, the "four small dragons" have paid much attention to improving the infrastructure. In the 1960's, more than 60 percent of South Korea's investment funds were used on railways, highways, harbors, airports, postal and telecommunications services, and other construction projects. Since 1974, Taiwan has launched its "10 major construction projects" and "12 major construction projects," which include funds for expressways, international airports, and harbors. Since the 1970's, Hong Kong has stepped up construction of tunnels, subways, airports, and docks to turn itself into a modern city. All this has provided a suitable investment climate for foreign investors and the important material conditions for the economy to take off.

Sixth, development of intellectual resources. South Korea invests 4.1 percent of its GNP in public education. In 1980, the people's literacy rate reached 95 percent, and the enrollment rate of primary schools was 100 percent. The authorities also ordered higher education to move from the "stage of elite education" to the "stage of popular education." At the same time, vigorous efforts were made to develop technical and vocational education, training large numbers of skilled workers. To guarantee funds for education, the Taiwan authorities set specific proportions aside for education in budgets at different levels: not less than 15 percent at the "central" level; not less than 25 percent at the provincial level; and not less than 35 percent at the city and county levels. The willingness of the "four small dragons" to spend huge amounts of money on education to raise the cultural and technical quality of workers to a fairly high level is closely related to their success in developing an export-oriented economy.

What Can Be Used for Reference

In order to use some of the feasible ways and experiences of the "four small dragons" in the light of China's conditions to more effectively speed up the economic development of our open coastal areas, we need to properly handle the following relationships.

—The relationship between overall regulation and control and supporting reforms. In capitalist countries, the general form and means of economic control is a market regulatory mechanism suited to the commodity economy. What we should have is a perfect market regulatory mechanism guided by the state's macroeconomic policies, by which "the state regulates the market, and the market guides enterprises" to speed up the development of the socialist commodity economy. To establish this new economic mechanism, the government should give full play to the role of the law of value and use such economic levers as prices, taxes, interest rates, exchange rates, and wages as means of macroeconomic control to regulate and guide the supply and demand in the commodity, financial, technology, real

estate, and labor markets based on the needs for developing an export-oriented economy. Therefore, it is necessary to speed up the supporting reforms in the planning, investment, material supply, finance, banking, and foreign trade systems to change the functions of the relevant economic control departments.

—The relationship between developing labor-intensive industries and emphasizing application of science and technology. The strategy for the economic take-off of the Zhujiang delta and Changjiang delta is to vigorously develop labor-intensive industries oriented to the international market. The question is how to enhance the competitiveness of our products in the international market to earn more foreign exchange. Judging by the experience of the "four small dragons," sheer "quantity" is no substitute for value. To increase the foreign-exchange earning power of export goods, we must reduce production cost and upgrade product quality. Thus, in developing labor-intensive industries, we must pay attention to new information on demands for different commodities in the international market, introduce relevant new technology, and strengthen lateral economic cooperation. Labor-intensive production should be integrated with technology-intensive production.

—The relationship between macroeconomic control and invigorating enterprises. In developing a planned commodity economy, it is necessary not only to strengthen macroeconomic control, but to enhance microeconomic vigor and vitality. Neither should be overemphasized at the expense of the other. From an overall viewpoint, it is necessary to use various economic and legal means and necessary administrative intervention to adjust the production structure, lay down the course of development, rationally distribute the productive forces, and effectively strengthen control and guidance in project construction, capital investment, technological applications, marketing, economic efficiency, and other areas according to objective economic laws. It is also necessary to really delegate powers to the lower levels and straighten out the external economic relations of enterprises according to the principle of separation of ownership from management, so that enterprises can really make their own decisions, operate independently, and assume full responsibility for their own profits and losses. Enterprise which are able to compete should be allowed to deal directly with foreign enterprises and enhance their ability to meet challenges through competition in the international market.

—The relationship between opening wider to the outside world and improving the investment climate. Experience of the "four small dragons" shows that a good investment climate is essential for attracting foreign firms to make investment in factories, bring in advanced technologies, and expand economic cooperation. In the past few years, the investment climate has improved a great deal in the open coastal areas. It can be said that a fairly good foundation of

tangible conditions has been laid. To take full advantage of the opportunities provided by the changing international economic situation and further expand economic cooperation with foreign countries, we should also pay attention to improving the intangible conditions. One of these conditions is the exchange of currencies. The problem is to readjust the exchange rates. This problem involves a lot of people in the country, and their tolerance must be fully appraised. As the scout for the entire country, Guangdong can make a full appraisal of the people's tolerance in the province. Experiments can be made step by step first in the SEZs. Another intangible condition is the legislation and improvement of economic laws so that there will be laws to follow to protect the legitimate rights and interests of business people.

—The relationship between economic take-off and training of competent people. Before and after their economic take-off, the "four small dragons" all attached great importance to the development of intellectual resources and training of competent people, regarding it of great strategic significance for modernizing production. In the last 30 years, many good opportunities have been presented by the changing international economic situation. Most of the developing countries have cheap labor, but only a few countries and areas have succeeded in developing an export-oriented economy. Why? The answer is: Competent people are the decisive factor. These few countries and areas all have three levels of training. The first is the leadership and policy-making level. Included are specialists, whose studied opinions are the basis for consulting organizations to give counsel and formulate policies. The second level is for the training of large numbers of entrepreneurs who are competent administrators and managers. The third level is for the training of a vast number of workers with culture and a fairly high technical standard.

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AGRICULTURE

National Tea Output

40060396a Chengdu SICHUAN RIBAO in Chinese
18 Jun 88 p 2

[Excerpt] Estimated gross output of tea in 1988 is 530,000 tons; state-run and supply and marketing cooperatives will procure 340,000 tons, and domestic sales are estimated at 190,000 tons.

Jilin Beet Prices Increase

40060396b Shenyang DONGBEI JINGJIBAO in Chinese
14 May 88 p 1

[Excerpt] Jilin Province has raised the negotiated price of sugar beets from 108 yuan to 120 yuan per ton.

Document on Taxation of Cultivated Land
40060329a Beijing ZHONGHUA RENMIN
GONGHEGUO GUOWUYUAN GONGBAO [STATE
COUNCIL BULLETIN] in Chinese
No 4, 1 Mar 88 pp 122-123

[State Council Circular on a Summary of the Minutes of the Conference on the Collection, Administration and Use of the Land-use Tax on Cultivated Land (1 February 1988)]

[Text] The following document, which was approved by leading comrades of the CPC Central Committee and the State Council, is transmitted to you for study and implementation.

Summary of the Minutes of the Conference on the Collection, Administration and Use of the Land-Use Tax on Cultivated Land (Excerpts)

The conference was convened 4 January, was chaired by Comrade Tian Jiyun [3944 4764 0061], studied the issues of how to collect, administer and use the land-use tax on cultivated land, and was attended by Du Runsheng [2626 3387 3932], member of the CPC Central Committee Finance and Economics Leading Group; Chen Junsheng [7115 0193 3932], secretary general of the State Council; Bai Meiqing [4101 5019 3237] and Li Chang'an [2621 2490 1344], deputy secretaries general of the State Council; Liu Zhongyi [0491 0022 0001], of the State Planning Commission; Chi Haibin [6688 3189 3453], of the Ministry of Finance; Chen Yaobang [7115 5069 6721], of the Ministry of Agriculture, Animal Husbandry and Fishery; Gao Dezhan [7559 1795 0594], of the Ministry of Forestry; Qian Zhengying [6929 2973 5391] and Yang Zhenhuai [27992182 2037], of the Ministry of Water Resources and Electric Power; Liu Kan [0491 1030], of the CPC Central Committee's Rural Policy Research Office; and other comrades.

The conference expressed the view that conditions in agriculture are good due to the facts that all areas of the country strengthened leadership in agriculture, adopted a variety of measures, and thereby managed to increase output of grain, cotton, oil-bearing crops and other major agricultural produce, but that to enable China's agricultural production, especially grain, to increase at a steady rate and to achieve new levels, we must deepen agricultural reform, perfect relevant policies, adopt forceful measures to increase agricultural inputs, and strengthen agricultural development work, so as to enhance the developmental reserves of this sector. Increasing agricultural inputs will require the efforts of many quarters and the use of many channels. The State Council has decided to employ all of the land-use tax that has been levied on cultivated land to support agricultural production. These taxes produce considerable revenue which, if properly used, can enhance the developmental reserves of agriculture and play an important role in achieving the targets of the Seventh 5-Year Plan and the struggle objectives that have been

established for the end of this century. To this end, the conference discussed and passed the following resolutions on the collection, administration and use of the land-use tax on cultivated land.

1. Financial agencies must assiduously strengthen collection of the land-use tax, bolster basic-level collection forces, appropriately increase the number of tax collectors, stress completion of the collection of this tax as an important task, conduct their work in accordance with tax laws, collect taxes at the proper rates as prescribed in tax regulations, refrain from unauthorized grants of tax reductions or exemptions, establish and improve collection systems and measures, prevent evasion and fraud, properly supervise and inspect collection work, and ensure that the revenues that are due are in fact collected. Land management agencies should actively cooperate with financial departments in this work.

2. Half of the land-use tax shall be remitted to central authorities, and half shall be retained for local use. But the tax must be handled in accordance with the principle of "take from the soil, apply to the soil" and be used to develop agriculture and may not be diverted to other purposes. The Ministry of Finance shall keep separate accounts for the revenues remitted to central authorities and list receipts of and disbursements from these funds separately.

3. Establish a State Land Development Fund to improve land development. And to coordinate the work of the various departments and the administration and use of this fund, so as to obtain better economic results, we propose creating a management leading group for the fund, which group would be responsible for drawing up national agricultural development plans, reviewing and approving development plans for key regions, and managing and planning, in a unified way, use of the fund. The fund will be derived from the land-use taxes remitted to central authorities as well as a portion of the concessional loans obtained from abroad. To strengthen leadership of this work, we suggest that Comrade Chen Junsheng serve as the head of the management leading group; Comrade Du Runsheng serve as adviser to the group; Comrades He Kang [0149 1660] and Liu Zhongyi serve as deputy heads; and Comrades Qian Zhengying, Gao Dezhan, Li Chang'an, Xiang Huaicheng [7309 2037 6134] (of the State Land Bureau), Ma Yongwei [7456 3057 0251] (Agricultural Bank), Li Zhensheng [2621 2182 5116] (Chinese Academy of Sciences), and Wang Lianzheng [3769 6647 6927] (Chinese Academy of Agricultural Sciences) serve as members of the group. A small, skeletal office shall be established under the group, over which office Comrade Liu Zhongyi shall serve concurrently as director and Comrade Xiang Huaicheng shall serve as deputy director. The office shall have a Finance Section, whose staff shall be comprised primarily of personnel from the Agricultural Finance Department of the Ministry of Finance. No other staff or organs shall be created. If more staff is required, it can be assigned from relevant departments.

4. The Land Development Fund must be used in a planned way and be concentrated on land development projects in key regions and on the development of commodity bases. National land development must be effected in a planned, step-by-step way. In view of the nation's actual capacity, [the government] plans to develop the Sanjiang Plain of the Northeast and the combined drainage areas of the Yellow, the Huai and the Hai rivers. In these two zones, full development of agriculture, forestry, animal husbandry, sideline industry and fisheries and comprehensive control of land, water, fields, forests and highways should be carried out, and effort should be made to create efficient agricultural commodity bases that have stable, high outputs.

5. The Land Development Fund shall be used on an operational and compensated basis. From the outset, a turnover mechanism shall be created so that the fund can truly get rolling and create a large amount of investment, and the fund shall be used for investment on a project-by-project basis. Large projects shall require appraisal by experts, be awarded through bidding and require the signing of contracts and acceptance of economic responsibility. The land-use taxes and other investment received by the regional governments in the two development zones must be coordinated with state plans and used in a unified way so that these two large commodity grain bases can properly develop.

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Circular on Strengthening Planned Control of Cotton Marketing

40060329b Beijing ZHONGGUO RENMIN GONGHEGUO GUOWUYUAN GONGBAO [STATE COUNCIL BULLETIN] in Chinese No 4, 1 Mar 88 pp 125-126

[State Council Circular Promulgated by the Ministry of Commerce, the State Planning Commission and the State Economic Commission on Strengthening Planned Control of Cotton and Short-staple Cotton (20 January 1988)]

[Text] Leading comrades of the State Council have ordered that different procurement and marketing procedures be drawn up for different types of agricultural and sideline industrial products having different degrees of effect on the national economy and the people's standards of living and that the procurement-marketing system be improved. Cotton and short-staple cotton are important raw materials used to produce textiles, special types of paper, and chemical fibers and therefore are subject to state planning and require enhanced macroscopic and planned control. In recent years, unplanned or out-of-plan supply of these commodities has occurred in some regions; some areas have engaged in blind, out-of-plan development of textile mills and exceeded cotton supply capacity; other areas and enterprises have wantonly pilfered state cotton stores; and the resulting drain off of short-staple cotton has adversely affected

planned allocations, for production purposes, to key state industries and enterprises. To ensure market supply of cotton goods and military, special and export needs, and to maintain market price stability, we issue the following special directive.

1. Cotton and short-staple cotton are subject to state command planning, and all surcharged and award-sales procurement of cotton (including improved varieties and substandard) shall be controlled and handled by the state in a unified, planned fashion.

2. Supply and marketing cooperatives at all levels shall draw up plans for cotton and short-staple cotton trading. Enterprises using cotton must report their expected needs for the product to local supply and marketing cooperatives, which shall then draw up annual draft plans to be submitted to respective people's governments (or planning commissions) for approval, whereupon the plans shall be submitted upward for approval at each higher level. The Ministry of Commerce shall then draw up plans balancing aggregate supply and demand and for each province (autonomous region and municipality), which plans shall be submitted to the State Planning Commission for review to ensure overall balance, whereupon they shall be sent to the State Council for approval and transmission to lower levels for implementation.

3. Plan implementation shall be organized and effected by the Ministry of Commerce, period by period, in accordance with annual state plans. Supply and marketing cooperatives shall not reduce, exceed or provide unplanned supply of cotton and short-staple cotton. And provinces (autonomous regions and municipalities) having no cotton export quotas shall not provide unauthorized supply of cotton to foreign-trade departments for export or use establishment of horizontal ties as a pretext to pilfer state cotton reserves.

4. Priority in supply of short-staple cotton shall be accorded to production of No. 103 type paper, special military supplies, important chemical fibers and special paper products. The contracts that have already been signed by the State Planning Commission with short-staple cotton using regions or units that are included in state planning should be incorporated into state plans.

Short-staple cotton exports must be included in state planning and handled in a unified way based on available supply. Given current shortages, supply and marketing cooperatives, cotton-flax companies and ginning mills should not be allowed to engage in out-of-plan export supply.

5. The Ministry of Commerce and the State Council shall bear responsibility for the state's stores of cotton, which they shall entrust to provincial (autonomous region and municipality) supply and marketing cooperatives to manage on their behalf. These stores may not be touched by any department, unit or individual without approval

of the State Council. Cotton reserves approved in annual state plans shall be employed only to facilitate turnover and may not wantonly be used to fulfill supply or use targets.

6. Out-of-plan spinning mills shall be controlled. Spinning capacity exceeds raw cotton supply, and thus out-of-plan spinning mills must be subject to strict control. So long as state-planned out-transfers of cotton are ensured, the cotton needed by out-of-plan mills in major cotton producing regions that went into production prior to the end of 1987 at the approval of provincial (autonomous region) planning commissions shall be included in state plans. The state will not provide cotton to out-of-plan mills run by villages, individuals, non-cotton producing regions, or cotton producing provinces (autonomous regions or municipalities) that, lacking self-sufficiency in the product, require allocations from other regions.

Cotton used for state-planned spinning constitutes the standard for spinning and includes mills run by the textile, light industrial, military, township and town

enterprise, supply and marketing cooperative and other systems. Supply and marketing cooperatives at all levels, together with respective planning commissions, must plan and rationally distribute cotton yarn.

7. Planning agencies and supply and marketing cooperatives at all levels must strengthen planned control of cotton and short-staple cotton, urge trading units conscientiously to implement the plans, carry out inspections of progress in plan fulfillment at regular intervals, and resolve problems in plan implementation. Provincial (municipal and autonomous region) supply and marketing cooperatives shall be responsible for applying for the trucks, ships and other conveyances needed to transport state-mandated allocations of cotton and short-staple cotton. We request that railroad and other transport agencies render vigorous assistance in this work so as to insure smooth execution of allocated-supply and industrial-production plans.

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Reflections on Probability of Nuclear Conflict
40050260 Beijing GUOFANG DAXUE XUEBAO
[NATIONAL DEFENSE UNIVERSITY JOURNAL] in
Chinese No 11, 1 Nov 87 pp 67-68, 54

[Article by Wang Zhidong [3769 1807 2639], graduate student Class One: "Some Reflections on the Probability of Using Nuclear Weapons in Actual Combat"]

[Text] Studying and forecasting the prospects for the use of nuclear weapons in actual combat in a future war has become a central issue for government and military figures in various countries as well as a given in major political, military and economic policy-making of many countries. "A nuclear war cannot be fought" is a common aspiration of people who desire peace and development. "Nuclear war will not be fought" is an important topic which concerned figures actively expound upon. Yet, the objective existence of nuclear weapons is itself a great threat which cannot be denied. I think that this reality should be looked in the face and the possibility of the use of nuclear weapons in actual combat should be analyzed objectively.

I. The Development of Nuclear Weapons Itself Provides the Possibility for Their Use in Combat

The enormous destructive power of strategic nuclear weapons and the supersaturation of the quantity of nuclear bombs makes the technologically developed countries pay more attention to increasing the actual combat usability of nuclear weapons. In the past 20 years, the quality of nuclear weapons has improved very quickly as is evident primarily in the following areas: 1) warheads have been miniaturized so that the smallest nuclear weapon now is equivalent only to 10 tons of TNT; 2) the types of missiles have increased so that large numbers of various types of nuclear guided missiles, cruise missiles, nuclear shells, nuclear land mines, nuclear sea mines, and nuclear torpedoes are produced and equipped in great quantity; 3) power has been divided into categories so that as warheads have become smaller, strategic, campaign, and tactical nuclear weapons systems for a variety of distances have appeared; 4) guidance has become more accurate so that a warhead will hit the target precisely but the significance is clearly not only in that it improves its power, but that it creates the conditions for exercising more effective control.

At the same time, third generation nuclear weapons are at the stage of intensified research and development and partial production, primarily neutron bombs, induced radioactive bombs, strong shock wave bombs, and electromagnetic pulse bombs. The common characteristic of this generation of nuclear weapons is that they effectively attack selected targets while not causing greater damage to non-attacked targets and do not hinder subsequent combat action. Although they produce the same lethal and destructive elements as shock waves, light radiation, penetrating radiation, radioactive contamination, and electromagnetic pulses as nuclear explosions,

the usefulness cannot be compared with those of current nuclear weapons. In particular, is the vast superiority of selecting weapons with different effects for different targets. A neutron bomb can be selected for massed tanks; the effects of a strong shock wave bomb are optimal for destroying solid fortifications; and the electromagnetic pulse bomb's direct destruction of electronic components will make its use in electronic warfare clearly impressive.

The rapid growth in the quality of nuclear weapons undoubtedly creates the daily improving conditions for their use in wars of various scales and levels. In terms of war decision-making, the improvement of the usefulness of nuclear weapons in actual combat gives them more means in deciding the use of combat forces and the avoidance of unfavorable situations, increases greatly the latitude for selection and the increase in methods of use and levels of control and the fact that in terms of public opinion it does not cause such violent opposition as nuclear war furnished the possibility of actual use of nuclear weapons.

II. The Power of New Conventional Weapons Approaches That of Small Nuclear Weapons Lowering the "Nuclear Threshold"

Because of the adoption of precision control and guidance and the use of new materials and technologies in the design and production of explosives, the lethal and destructive power of conventional weapons has been raised to unprecedentedly high levels. The actual lethal and destructive power of some conventional weapons is tending closer to strategic nuclear weapons. Some people feel that by using only new conventional weapons they can both achieve the goals which previously could only be achieved by nuclear weapons as well as not encountering violent opposition from international public opinion and thus avoid the need to use nuclear weapons. While the destructive ability of new conventional weapons is fairly close to that of small nuclear weapons, when war decision-makers select weapons, it is generally the weapon's performance with regard to the effect on the target that is given more consideration and not cautiously controlling the level of combat that is in first place. In addition, people's fear of, and resistance to nuclear weapons is because of their large scale lethal and destructive ability, but since the power of new conventional weapons is close to that of nuclear weapons, this may dissipate and weaken people's prior violent opposition to nuclear weapons. All of this will lead to a lowering of the "nuclear threshold." Large-scale conventional warfare may include the use of a large number of tactical nuclear weapons, but this is not an issue of technological escalation.

III. Runaway Conventional Warfare May Lead to Nuclear Conflict

Under conditions of nuclear parity, all-out war of the superpowers will lead to suffering on both sides, and there is a fundamental contradiction here with their

political and economic goals of world hegemony. At the same time, the anti-nuclear movement is running higher daily throughout the world and the outbreak of nuclear war is more and more restricted. Many people thus predict that future nuclear war will be a conventional war under nuclear deterrence. Although this is a very practical low level type of war with a rather small risk, in a conventional war under this type of nuclear deterrence, nuclear weapons are both a deterrent force, as well as an actual means of combat, thus it cannot be viewed as equivalent to a conventional war in the original sense. Besides, in warfare, the opposing sides can only ascertain the attempts of the opposition through various indications and thus there is a very large measure of unreliability. In addition to that, the antagonistic behavior of the combatants is both mutually restricted and mutually influenced, but if one side is willing, under certain conditions there is no way to prevent the war from escalating and when this becomes the pivotal choice which must be made concerning the existence of the country the war may become more violent as it expands and lead to a rapid escalation of the range and force of combat or even to loss of control. Actually, the essence of military strategy of all nuclear countries includes the dual importance of both being ready to fight a conventional war as well as being ready to fight a nuclear war. Americans who feel that the possibility of the outbreak of nuclear war is becoming smaller and thus are taking the lead in promoting the theory of conventional warfare under nuclear deterrence also have not abandoned the readiness to win a nuclear war. This reflects their misgivings concerning whether or not war can be controlled within the scope of conventional conditions. Generally speaking, in conventional warfare under nuclear deterrence, when one is reduced to absolute inferiority, conventional forces are powerless to rescue a defeat; when both sides reach a stalemate and continuing this way is more disadvantageous; when the superior side must conclude the war quickly; or when some signs indicate that both sides may use large scale nuclear or chemical lethal weapons all are situations in which the warring forces may lose control.

IV. Proliferation of Nuclear Technology Is the Ultimate Cause of the Use of Nuclear Weapons in Actual Combat

Since the sixties, only five countries in the world—the United States, the Soviet Union, France, England and China—have made it known that they had nuclear weapons and the means to deliver them. Although calls for a “nuclear-free zone” have been repeated and the anti-nuclear movement is just now in the ascendant, the rapid proliferation of nuclear technology is an undeniable reality. On the one hand, the enormous usefulness of nuclear weapons militarily makes them both a deterrent as well as a means of actual combat and they are ranked as a development key by the great military powers; on

the other hand, the widespread use of nuclear technology under peaceful conditions also gives it very promising prospects and makes it extremely attractive. The dual usefulness of the peaceful and combat uses and the compatibility of both the military and the civilian in a turbulent world situation is something which all countries which strive for security and development seek in common. Only if science and technology and economic forces permit does the mastery of nuclear technology and the development of nuclear weapons become an urgent strategic mission. This is a basic reason why the proliferation of nuclear technology cannot be contained. At the same time, the rapid growth of nuclear science and technology causes more and more countries to master the technology for manufacturing nuclear weapons and even some medium and small developing countries have also mastered the technology for developing nuclear weapons. According to Western estimates, by the end of this century over 30 countries may have nuclear weapons.

At the same time that nuclear technology is proliferating, the world has been unable to break free of the shadow of war. Some of the countries which have already, or are about to, get control of nuclear weapons technology have directly or indirectly been in a state of war and under such conditions, the proliferation of nuclear technology has some dangers which cannot be overlooked. There are primarily three reasons for this: first, in a war, the possibility that the military forces, especially nuclear forces of both sides will be in a situation of imbalance increases greatly; second, in a war, medium and small countries may very quickly face a critical moment with regard to the existence of the nation; third, the inclinations of some war policy makers makes it clearly hard for them to accept responsibility for the history of all mankind. Everyone knows that the use of chemical weapons is prohibited by international treaties and is violently opposed by public opinion. But in the Iran-Iraq War this type of toxic bomb called “the poor country’s atomic bomb” has been used many times. It’s no wonder people say that if one side in the Iran-Iraq War had nuclear weapons, who could guarantee that they would not be used in actual combat.

Through the above analysis, this writer feels that the possibility exists that nuclear weapons would be used in actual combat in future wars. In terms of preparations for war to victoriously carry out various types of combat missions, being prepared only for conventional war will not be enough to respond to the complex situations which may appear in actual combat. Researching combat theory under nuclear conditions should be an important aspect of China’s military construction which cannot be overlooked.

Commentary on Agricultural Subsidy Policies
40060299 Taipei CHUNG-YANG JIH-PAO in Chinese
18 May 88 p 14

[Article in "Freedom Forum" column by Zhuo Wuxiong [0587 2976 7160] of Zhanghua, Assistant Professor of Business Education at the National Taiwan Education College: "A Multi-criteria Assessment of the Agricultural Subsidy Policies"]

[Text] In addressing the legislative assembly on 17 April, a certain government official stated that there are few examples of success among all the agricultural subsidy policies implemented by the governments throughout the world. The official went on to emphasize that economic problems should be solved by economic means. I personally feel that this is debatable. This writer is prepared to make a multi-criteria analysis, from economic, social, and political points of view, and from the perspective of national security, of why the government should implement a proper subsidy policy as long as the country is not self-sufficient in agriculture.

On the surface, it appears that there is "perfect competition" in the market for agricultural products, because there are many buyers and sellers, and the producers are free to get in or out of any business and market they choose. Because of free market competition, we naturally have attained efficient allocation, selection, and utilization of all the resources, and the consumers enjoy agricultural products at a low price. Therefore, it seems that the government should not intervene. But in fact, this is not entirely true. The major capital investment in agriculture is the cultivated land itself. Most farmers either inherit their land or lease it from others on a short-term basis. In the former case, the farmers often neglect to include the opportunity cost of the land into the cost of their capital investments, that is, they only include the direct labor cost and the cost of raw materials as "production cost." When agricultural product prices are low, and the revenue from sales is lower than the "production cost," the land may lie fallow in the next season, and consequently supply will drop, and the prices will rise. Higher profit may entice the farmers to resume production in the season that follows. Therefore, the market for agricultural products tends to fluctuate more severely than the market for industrial products. Furthermore, often in agriculture, the investor is also the operator. After the government started the policy of giving land to the tiller, and encouraged leasing cultivated land, the farms have become noticeably smaller, and most farmers are no longer entirely dependent on agriculture for their livelihood. Moreover, with increased mechanization and automation in agriculture, less human labor is needed, and the farmers can spend their spare time working in factories or on construction jobs to supplement their income. (In fact, agriculture is their side-line occupation.) Therefore, when the market for agricultural products is in a slump, they simply quit and let the land lie fallow while they concentrate on their other business.

These facts point out that people who invest in agriculture can get in or out of that line of business much easier than those in industry, and therefore market prices tend to fluctuate more for agricultural products than for industrial goods.

Because the price of agricultural products is cyclical and fluctuates with the production cycles, the relationship between prices and supply-demand conditions is often depicted as a spider web. Under this condition, the producers often cannot ascertain the market price or the supply-demand condition, and therefore their profit is low. The consumers' demand for agricultural products is relatively inelastic (limited fixed demand), and agricultural products are not very durable. Although the consumers can enjoy low prices this season, they might have to pay a very high price in the next season. Therefore, the government must step in to guide the production and sales. For example, the government should formulate policies to adjust agricultural product prices or implement price support and purchase a certain amount of the agricultural product to stabilize market prices, as well as guide the farmers to ensure that the supply is regular and stable, so that the country can be self-sufficient in agriculture. Beyond this, we hope to slow the outflow of the rural population and, at the same time, stabilize the overall price level. This will also help the country's leaders fulfill their social and political goals. On the other hand, it will also preserve the system of moral principles of the traditional rural families, and prevent industrialization from spoiling the natural environment and the pristine scenery of the countryside.

Furthermore, as a special interest group, the farmers have sufficient voting power to tip the balance in an election. (For example, in Japan 26 percent of the votes for the Democratic Party came from the farmers.) In the process of democratization, the farmers have become more demanding of the government. If the head of state fails to consider the privileges of the farmers, many representatives from the rural areas who are in the ruling party will probably lose the election, and this will enhance the power of the opposition party in congress. If the ruling party does not have majority control in congress, it could prevent the government officials from carrying out their administrative duties. More seriously, they may not be able to form a cabinet. Therefore, increasing the benefits of the farmers has long been the slogan of those seeking public office.

The author feels that the major agricultural products which are essential to the livelihood of the people are just as important as petroleum and energy, and weapons for national defense. When one nation is at war with another, there can be a sudden economic blockade. For example, in 1979 when the Soviet Union attacked Afghanistan, the U.S. immediately declared a Soviet grain embargo which lasted for several years. Today, hostility on both sides of the Strait of Formosa lingers, and without warning, the Strait can be closed. When that time comes, even if there is ample supply of defense

weapons, if we do not have sufficient food supply, it can be very dangerous. Therefore, it is essential that the government guides the production and sales of agricultural products, and helps the agricultural sector maintain steady growth.

Scanning the economic development of the major western nations, none would not hope for self-sufficiency in agriculture, and all programs of guidelines and subsidies are policies to achieve this goal. On 1 April, the CHUNG-YANG JIH-PAO published a detailed report by this writer on the agricultural subsidy policies of the major countries in the world, and I will not repeat the details here.

I only want to demonstrate that economic problems are not necessarily solved by economic measures alone. When the government formulates a certain policy, it must consider the "national interest." I also feel that it is in the interest of the nation that the government maintain a proper and selective agricultural subsidy policy as long as we are not yet self-sufficient in agriculture. It is not necessary for the government to subsidize exports or restrict imports, but proper subsidies to keep the farmers in production will pay off in the long-run.

12986

Discussion of Foreign Trade Surplus
40060298 Taipei CHUNG-YANG JIH-PAO in Chinese
16 May 88 p 3

[Article in "Guide to Foreign Trade" Column by Chen Sixian [7115 1835 6343], Assistant Professor at the Mingzhuang Business College: "The Moderating Trade Surplus Is of No Serious Concern"]

[Text] In the past 3 years, we have seen significant growth in Taiwan's foreign trade, especially in its export trade, and as a result we have a huge trade surplus. In 1985, the trade surplus was \$10.6 billion, and it has grown to \$15.6 billion in 1986, and \$19 billion by 1987. We have accumulated a substantial surplus in the balance of international payments as a result of the trade surplus, and there has been a sharp increase in our foreign exchange reserve. We have become an economic force to be reckoned with internationally. Both the developing and the well-developed nations envy our spectacular success. However, this has brought pressure on us to raise the value of the NT dollar, and domestically, product prices are poised to rise. Nations with trade deficits are constantly demanding that we ease the import restrictions, and incessantly urging us to stimulate domestic demands, expand the domestic market, and reduce exports.

Four Reasons for the Export Reduction During the First Quarter

While our economy is forging ahead, and in order to placate the international economic community and increase the bilateral trade benefits, we have taken the initiative and adopted many policies, such as lowering the tariffs, abolishing trade regulations (restrictions), lifting import restrictions, increasing domestic demands, and encouraging imports, and we are hoping for good results. Since the fourth quarter of last year, we have increased our imports significantly, and this increase has become even more evident during the first quarter of this year. For example, during the first quarter of this year, export only increased 21.9 percent, but import increased 63 percent over the same period last year. In terms of the NT dollar value, exports have actually fallen by 0.8 percent, and imports have risen by 32.8 percent over the same period last year. As a result, some people are worried that our export trade will not be able to fulfill the goals for this year as anticipated, and many wonder if the trade surplus will be reduced so drastically that it will necessitate some changes in our strategy. This is indeed a puzzle.

The Reduction in Trade Surplus Does Not Represent a Recession

The reduction in exports during the first quarter of this year can be attributed to the following factors:

1. In the past, to avoid losses on exchange, most manufacturers would take orders early, and get ready for shipments quickly, but they would delay imports as much as possible, and therefore, there were some unusual rushes and delays. Since the end of last year the exchange rate for the NT dollar has stabilized, and the manufacturers no longer expect the NT dollar to continue to appreciate, and therefore they no longer have the need to speed up exports or delay imports.

2. After the central bank announced in November that, once again, it would halt the purchase of surplus exchange bought on forward exchange transactions by the foreign exchange banks, the manufacturers could no longer use forward exchange transactions to reduce exchange rate risks, and many hesitated to accept large export orders without careful considerations.

3. Based on the United States' Morgan Bank's calculation of the index of the effective exchange rates of the various nations, comparing March of this year with the base period of 1980-82, the NT dollar has been overpriced by 3.2 percent relative to the U.S. dollar, while the Hong Kong dollar has been undervalued by 5.6 percent, and the Korean won and the Singapore dollar have been undervalued by as much as 15.4 percent and 21.6 percent, respectively. It is clear that in terms of prices, Taiwan's products have lost their competitive edge, and a reduction in exports is the inevitable consequence.

4. During the second quarter of 1987 the labor cost of the manufacturing units fell by 7.7 percent compared to the same period in 1986, but by the fourth quarter, labor cost was on the rise again, indicating that the increase in labor productivity has lagged behind the increase in wages, and this has an adverse effect on those manufacturers who are mostly export-oriented. The shortage of skilled workers in particular has also affected exports.

Furthermore, the political upheaval in the Philippines last year, and the political, labor, and student unrests in Korea during the third quarter, prompted many countries to switch their purchase orders to Taiwan. In addition, the year before last, the export capacity in the mainland fell sharply. Today, these factors which had helped our export trade in the past have vanished.

The reduction in exports does not represent an economic recession. It only indicates that we are in a process of restructuring our industries. What kind of changes and adjustments should be made to cope with the internal and external pressure? At least, we should try to mitigate the adverse effects of the following conditions:

1. We should stop the continuous increase in foreign exchange reserve for the time being to ease the pressure on us to appreciate the NT dollar, so that those who invest abroad and those engaged in the export trade can accurately calculate the cost and profit of exports, and avoid the risks associated with exchange rate fluctuations. Furthermore, this will enable us to ease the friction among nations because of the trade situation, and avoid the retaliatory measures of the nations which have trade deficits.

2. After the exchange rates have stabilized, international idle funds (hot money) will stop flowing in to stir up our financial and stock markets, and the central bank will no longer have to issue more treasury bonds to prop up the NT dollar, or purchase large quantities of gold to reduce our foreign exchange reserve in order to maintain their face value.

3. If the trade surplus is reduced, the pressure to appreciate the NT dollar will diminish, and manufacturers and others, who in the past have waited for the NT dollar to appreciate more before importing goods, and thus have delayed the country's domestic investment plans, will no longer maintain this wait-and-see attitude. Instead, they will have to seize the opportunity and import in large quantities.

Respond to the Internal and External Changes Firmly and Steadily

Our national economy has flourished in recent years, and the people's income have increased. Those in the garment industry which used to export most of their goods have turned to the domestic market, and fast food businesses have sprung up everywhere. Demand for luxury cars far exceeds supply, and the department stores

are vigorously competing with each other. This is real prosperity, not just a facade. In modifying the industrial and trade structures, and adjusting domestic and foreign sales, we should respond to both the internal and external conditions, and deal with the situations firmly and steadily, and we must get rid of archaic strategies.

12986

Forum on Trade With Mainland China

40060289 Taipei CHING-CHI JIH-PAO in Chinese
16 May 88 p 3

[By staff reporter Liao Ching-chou [1675 1987 3166]:
"From Permitting Import of More Raw Materials From
the Mainland to Developing Economic and Trade Con-
tacts Across the Strait"]

[Text] Minutes of the 363d Discussion Meeting

Host: Hou Chia-chu [0186 1367 7467], professor, Soochow University

Guests: Hsu Feng-ho [1776 7364 0735], standing committee member, board of directors, Industrial Association

Chang Jung-feng [1728 2837 6265], associate research fellow, Chung Hua Economics Research Institute

Observer: Liu Lang [0491 2597], deputy editor in chief, CHING-CHI JIH-PAO

Note-taker: Liao Ching-chou [1675 1987 3166], staff reporter, CHING-CHI JIH-PAO

Photographer: Chang I-kung [1728 5030 1362], staff reporter, CHING-CHI JIH-PAO

Hou Chia-chu: The government announced recently that the ban will be lifted further on agricultural and industrial raw materials imported from the mainland. Though the items that can be imported are still limited, the move has raised expectations in the industrial and commercial circles. This will be the subject of our discussion today.

Hsu Feng-ho: Since ancient times, trade has helped people supply each other's needs. It is also the best way to promote peace and prosperity. Therefore, as early as during the time of the Council for Economic Reform, I called for lifting the ban on trade contacts with the mainland. Take coal, the ban on which is now lifted, for example. The price of coal from the mainland is \$28, or NT\$800, per ton; the international coal price is \$38, or NT\$1,100, per ton; and the price of coal produced in Taiwan is as high as NT\$3,000 per ton. Again, take the cement industry for example. A rather significant proportion of its production cost, about 20 percent, is spent on coal as fuel. If the ban on mainland coal is lifted, it

will help the cement industry greatly in reducing costs. In fact, South Korea has long been importing coal and other raw materials from mainland China. We cannot ignore these developments.

Chang Jung-feng: For all the talk about lifting the ban on imports from the mainland, the fact remains that trade with the mainland is still indirect. The only change is in the way the so-called contraband goods from the communist bandits are handled. Offenders are no longer turned over to the Taiwan Garrison Command. In the present stage, maybe everyone is in favor of lifting the ban on imports, but it is still necessary to maintain some control so that progress can be made in an orderly way.

Hou Chia-chu: The greatest worry about lifting the ban on imports from the mainland is that we may become too dependent on the mainland and allow ourselves to be manipulated. Take petroleum imports for example. Despite our very good relations with Saudi Arabia, we import oil from different sources. This same principle should be followed in importing raw materials from the mainland.

Don't Put All the Eggs in One Basket

Hsu Feng-ho: I think that businessmen should know the principle of diversification, that is, "not to put all the eggs in one basket." If they do not know how to overcome risks by diversification, they shouldn't be in business.

Hou Chia-chu: The risks to an individual firm are different from those to the nation as a whole. The question is, shouldn't the risks to the nation be considered, and isn't some control necessary?

Chang Jung-feng: From South Korea's experience in trading with the mainland, it seems that South Korea has sustained a trade deficit most of the time, which relatively reduces the chance of communist China starting a trade war. South Korea is also more relaxed than we are in controlling trade activities.

More worrisome is the question of how to help the small- and medium-sized enterprises from becoming too dependent on imports from the mainland. The small- and medium-sized enterprises use a lot of raw materials, but they do not have the kind of information sources and sales network large enterprises have. Therefore, they have the greatest need for government guidance. For example, the textile industry eagerly hopes to import cotton from the mainland. However, data show that owing to crop failure, there is a serious cotton shortage on the mainland, where the cotton crop is estimated to be less than 1.5 million tons this year. Under the circumstances, how can we hope to import cotton from the mainland?

If Control Is Needed, It Must Be Effective

Hou Chia-chu: Basically no one is opposed to importing raw materials from the mainland. However, should we take a laissez faire attitude, or is control still necessary? If control is needed, it must be effective. Otherwise, it can only hurt the government's prestige.

Hsu Feng-ho: We can import more items from the mainland on a trial basis for 6 months or a year, and then a decision can be made on the next move according to the actual situation.

Chang Jung-feng: As is often the case, policies can be revised and made better while being implemented.

Liu Lang: Basically I don't think we need to worry about being manipulated because of some imported raw materials. After all, we have economic and trade relations with more than 100 countries, and raw materials from the mainland are far from playing a dominating role. In any case, if the situation changes, we can always import from other sources.

Hsu Feng-ho: Judging by the present situation, we know for sure that the mainland needs far more from us than we need from them. Foreign exchange is a most obvious example of what the mainland can get from us.

Liu Lang: Technology is another.

Chang Jung-feng: Through trade we can also make counterdemands on the Chinese communists. The communists' economic and trade policy toward Taiwan is obviously based on the theme of "reunifying the motherland before the end of the century," and one of their tactics is to deal blows to Taiwan in the international arena. For example, they asked the European Common Market, in a memorandum 1 or 2 years ago, not to give Taiwan most-favored-nation treatment. Then again, in July last year, the authority to trade with Taiwan, which had earlier been delegated to the lower levels, was taken back by their central government and placed under the Ministry of Foreign Economic Relations and Trade, and foreign business is excluded from participating in economic and trade activities involving Taiwan. All these are unfriendly acts.

Chang Jung-feng: At present, our exports through entrepot to the mainland amount to \$1.2 billion each year, about 2.7 percent of our total exports, and our imports from the mainland are less than \$300 million, about 0.75 percent of our total imports. However, it is easy to open the door, but difficult to close it again. When we sense danger and want to close the door, it may be too late. A point that is overlooked is that although the mainland accounts for only 2 to 3 percent of our exports now, the proportion will rise to 15 to 20 percent by 1997, when

Hong Kong is returned to mainland China and our exports to Hong Kong are added to the total. We do not see any serious problem now, but we must guard against increasing dependence.

Hsu Feng-ho: I went to Hong Kong recently. New buildings are under construction, and the place is a picture of prosperity. Banks are handling instalment plans with payments stretched into the 2000's. Some influential people there told me that the mainland needs far more from Hong Kong than Hong Kong needs from the mainland.

Allow Free Imports, But Maintain Vigilance

Hou Chia-chu: The emphasis should be placed on setting up entrepot trade stations. On the development of entrepot trade, what worries us most is policy change. That's why we should be cautious in further lifting the ban at present. The best policy may be free imports with a warning system. Either the Foreign Trade Association or the Import and Export Association should maintain statistics on raw materials imported through Hong Kong. As soon as imports reach the danger level or upper limit, say, 30 percent, a warning should be issued to prevent over-dependence.

Chang Jung-feng: The upper limit should be flexible and may differ from trade to trade. In the past, the Chung Hua Economics Research Institute did some statistics and analysis on exports. Exports to the mainland made up as much as 90 percent of some companies' total export volume. For example, an average of 50-90 percent of some companies' chemical fiber products, including more than 10 items, were exported to the mainland. Comparable ratios may be applied on imports. However, our information is obtained entirely from Hong Kong at present, and we should develop cooperation with relevant organizations in Singapore, Japan, and other countries.

Liu Lang: Will there be problems in operating a warning system? Should the statistics and studies be focused on items or quantities imported?

Chang Jung-feng: Both items and quantities should be studied. In practice, a common understanding should be established between government and business. Based on security considerations, the government may intervene when companies become seriously dependent on imports. The first step will be to notify the companies, and the next will be to clamp down on imports.

Hsu Feng-ho: This is the way Japan's Ministry of International Trade and Industry usually works. It is called guidelines. Basically control should not be too rigid.

Getting Information Is the Greatest Problem

Chang Jung-feng: The best way to set upper limits for different items is through consultation with the traders. But for the traders, the greatest problem is how to get the information they need. As a personal experience, nowadays I often hear from the other end of the telephone: "The goods have gotten into the mainland, but we have not received the money yet. What should we do?" For this reason, information on the trend of the communists' economic and trade policies toward Taiwan, their ability to pay in foreign exchange, recent developments in producing substitutes for imports, changes in foreign trade administration, etc., should all be made known to the public. However, there are 20 to 30 newspapers and more than 300 periodicals on the mainland, and it is hard to decide where to start. That's why relevant organizations should be instructed to do it in an effective way.

Hou Chia-ju: Companies should also spend some money on investigation and study so that they can make their own assessment.

Hsu Feng-ho: Except for products like coal and cotton which do not make much difference transhipped or not, it is better to import bulky goods directly in the long run. The permission for people to visit relatives on the mainland is a sound policy and meant well, but it still requires people to travel by way of Hong Kong, which is causing inconvenience. In the words of an ancient sage, "love what the people love." Government actions should still follow the will of the people.

Chang Jung-feng: Direct trade is the trend. At present, we are in the process leading to it.

Hou Chia-chu: Should customs duties be imposed on imports from the mainland? If not, we must guard against dumping on the one hand, and face objections by other trading partners on the other.

Chang Jung-feng: The Chinese communists levy regulatory taxes. From a long-range viewpoint, the precondition for direct trade is the establishment of remittance, postal, and air and shipping services.

Hou Chia-chu: These are also bargaining counters to ease the tension between the two sides in the future. Basically the two sides of the strait are still in a state of hostilities. Therefore, I think trade can be started by individual businessmen and gradually developed into joint efforts. Then, under government guidance, our industrial and commercial organizations can negotiate with individual entrepreneurs and establishments on the mainland on questions of postal links, remittance, air and shipping services, investment protection, and so forth. In the final stage, a "breakthrough in the center" can be achieved, and everyone can help make it possible. The ruling party

has revealed the watchword for its 13th congress: "Taiwan's future is on the mainland; the mainland's hope is in Taiwan." It should have struck a sympathetic chord in all of us.

Chang Jung-feng: Development of trade with the mainland depends on economic and organizational conditions there. As Professor Hou has pointed out, the growing number of individual entrepreneurs and town and township enterprises on the mainland means increasing potential trading partners for us.

Hou Chia-chu: The pace of our opening up depends, of course, on the other side's reactions. The important thing is that free enterprise and the free economic system, once they are accepted by the Chinese communists, will begin to take the communist ideology apart and become a force for change.

Sell Our System While Doing Business

Hsu Feng-ho: There is more to trade than the exchange of goods for money to the satisfaction of both sides. More important, when we trade, we also sell our system. Taiwan's products are good and inexpensive. They are products of the free enterprise system, and they are also more affordable to our compatriots on the mainland. European, American, and Japanese goods are too expensive. This is why South Korea is so eager to expand its market on the Chinese mainland.

Hou Chia-chu: We must not continue the past practice of confiscation and prohibition. That practice hurts only ourselves while helping our competitors like South Korea, and has no effect at all on our political adversaries. It has no chance of success, but will make our own lives much more difficult. We shouldn't benefit others at our own expense. In trade or investment, even though we may sustain losses, we still will create job opportunities for our mainland compatriots. Blood is thicker than water. Any improvement in their living standard will help strengthen the forces for change.

Liu Lang: A system cannot be changed in a short period of time, but hostile feelings can. Perhaps direct trade between the two sides of the strait can begin as soon as the hostile feelings are gone without waiting for the system to change. It will be the same as our trade with Eastern European countries. Our systems may be different, but there is no hostility, and trade is growing smoothly.

Hou Chia-chu: Whether hostilities can be put to rest depends on the communists. But whether trade can be developed step by step as suggested previously depends on us.

Chang Jung-feng: A person who spent more than 2 months on the mainland told me that it is unlikely that the system can be changed in the present stage. We often talk about counterattack by economic means, but the communists do not think we can succeed. However, the intellectuals on the mainland can influence communist policies. We might let them come and take a look for themselves. If they find something better than what the communists are doing, they certainly can give it some publicity. We should have confidence that they will find our system better.

Liu Lang: I met with some Chinese communists in the United States in the past. The way they openly criticized their own system, of its problems and the extent to which it has opened up to the outside world, went beyond our imagination. Now we have gradually lifted the bans on travel to visit relatives and on trade, which I believe will have an immeasurably profound impact.

Hsu Feng-ho: After attending the inaugural ceremony of Panama's President 3 years ago, I met with the president of the Industrial Bank of Japan. I asked his opinion on the difference between the Soviet Union and Communist China. He said: There are no overseas Soviet communities like the overseas Chinese population. In addition, there is the "big hole" of Hong Kong, through which information from the free market can find its way into China. If Taiwan gets into the picture, it will have an even stronger impact on the mainland, and the forces for change will grow more powerful. Therefore, we should take on the mission as "economic crusaders."

Liu Lang: Traditionally we are phobic of the communists, regarding them as terrible and vicious. However, we are now in a new period. Even if we are anticommunist, we have to use new methods.

Flexibility and Assimilation

Hsu Feng-ho: It is important to make use of opportunities with flexibility and follow the trend toward assimilation. I suggest that the Action Group allow participation by representatives of the industrial and commercial circles and make more practical trade policies.

Hou Chia-chu: In short, lifting the ban on raw materials from the mainland and formulation of economic and trade policies have to proceed in an orderly way and step by step. It is impractical to ask the government to lift all the bans at once. On the other hand, with the rising consciousness of labor and the need for environmental protection, industrial development in Taiwan is entering a new period. Changes are needed, and economic and trade contacts with the mainland are inevitable.

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