

## **Opportunities and Challenges for the Chinese Economy in the 21<sup>st</sup> Century**

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### **I. Major Achievements Scored in the Development and Reform of the Chinese Economy since 1978**

After the Third Plenary Session of the Eleventh Central Committee of the Communist Party of China (CPC) in December 1978 the Chinese socialist cause entered a new historical stage. Over the past twenty and more years great achievements have been scored in China's reform, opening-up and modernization drive, profound changes have taken place in the society and economy and overall national strength has been considerably enhanced. The gross domestic product (GDP) in 2000 was, in parity pricing terms, 6.4 times that of 1978, with an average annual growth rate of 9.52%. By the late 1990s, the output of China's main industrial and agricultural products such as grain, cotton, oilseeds, coal, iron and steel, electricity, chemical yarn and electrical domestic appliances, had reached the forefront of the world. The volume of China's annual imports and exports increased from US\$ 20.64 billion in 1978 to US\$ 474.29 billion in 2000. China reached the strategic goal of "two steps" it had set in the early 1980s, that is, by the year 2000 China would quadruple its 1980 per capita GNP and provide a "fairly comfortable" life for its people. Starting from 2001, China began its march towards the third of the strategic goals: full-fledged modernization and a per capita income at the level of moderately developed countries by the middle of the 21<sup>st</sup> century.

A market-oriented reform was initiated as early as 1979 and, following many years of investigation in theory and practice, it was decided at the Fourteenth National Congress of the CPC in 1992 that the goal was to develop a socialist market economy. After more than twenty years of reform, a socialist market economy has now been basically instituted in China, as shown by the following:

Firstly, the economic system and operating mechanism of the countryside have seen radical change. The rural people's communes set up on the basis of "a larger size and a higher degree of public ownership" and "the integration of government administration and commune management" were disintegrated in the early 1980s. In their place were introduced a two-tier management system based on the household contract system and a combination of unified management with independent operation, which is more compatible with a market economy and gives the peasants more autonomy in production and management, and the right to free migration.

Secondly, the ownership structure has been readjusted and reformed, and the

principle was formulated of keeping public ownership in a dominant position, while developing diversified economic sectors side by side. The proportion of state ownership in the national economy dropped from 78% in 1978 to 40% in 1999 while the proportion of non-state ownership rose from 22% to 60% during the same period. Of the latter, the collectively owned sector was 35% and private economy was 25% (only 0.9% in 1978). The first two sectors constituted 75% of the national economy, which indicates the dominance of public sectors of the economy. The readjustments of ownership structure have facilitated the development of productive forces.

Thirdly, the reform of the state-owned economy has made breakthroughs and the state enterprises have shifted from administrative appendages to agents in the market that are independent and responsible for their own profits and losses. Most of the state-owned enterprises have been transformed into companies with limited liabilities and some have become listed companies, going in for the modern enterprise system as entities with diversified equity. A large number of small state-owned enterprises have been turned into enterprises with multiple property rights through joint stock partnerships, auction and capital-pooling, and some have changes their operating forms through leasing and contract operation.

Fourthly, we have successfully reformed the price system and constructed a mechanism for setting prices mainly through the market. The twisted relationships among the prices of basic industry products, manufactured products, industrial goods and of farm produce deriving from the planned economy have been basically corrected and streamlined. Except for a few vital commodities and services that have a close bearing on the national economy and the well-being of the people, prices of more than 95% of commodities and services are determined by the market. The market determination of prices now serves as the main lever to regulate supply and demand and achieve a rational allocation of resources. Initial success has been made in setting up factors markets, especially a capital market.

Fifthly, we reformed the government functions, and a basic change from direct to indirect control has taken place in governmental regulation and control of the economy. China has pushed the reform in the macroscopic control system in the following five ways:

- Reform of the planning system. The planning departments of the government have shifted their emphasis from issuing production and circulation quotas to formulating long-term plans of national economic development and coordinating relations between various economic sectors.
- Reform of the investment system. The enterprises of all economic sectors are becoming real investment entities and they are encouraged to get their funds directly from the capital market.

- Reform of the financial system. A tax-sharing system was introduced in 1994 whereby the central and local governments split the taxes and each collects its own.
- Reform of the monetary system. An initial system of macro-control and supervision by the central bank has been set up, non-commercial banking has been separated from commercial banking and specialized banks like the Industrial and Commercial Bank, the Agricultural Bank, China Bank and the Construction Bank are being gradually turned into commercial banks.
- Reform of the government's mode of economic management. We have made great effort to separate the functions of the government from those of enterprises and cancelled the specialized departments of economic management. The government no longer directly administers the internal affairs and business operations of the enterprises, but guides them and standardizes their production and operating activities by economic and legal means.

Sixthly, the policy of opening to the outside world has scored considerable achievements and a radical change from a closed to an open economy has taken place in foreign economic relations. In the early 1980s China set up four special economic zones -- Shenzhen, Zhuhai, Shantou and Xiamen. In the middle of the 1980s China opened fourteen coastal cities from Dalian in Northeast China to Beihai in Guangxi Autonomous Region. Later China established the Hainan Special Economic Region and the Pudong New Area in Shanghai. Since the early 1990s China has pursued an omni-directional open policy and now a pattern of multilevel, multifarious, wide-ranging and omni-directional opening up is already in its place. Structural reform in foreign trade has been continuously deepened and the mandatory planning reduced. By the end of 2001 a single exchange rate system was set up and the RMB is now convertible through current accounts. Over the past twenty years the foreign capital actually used reached 395.4 billion US dollars. There are now more than 390,000 enterprises with foreign investment, employing 17 million people. The export value of the products of enterprises with foreign investment accounts for 40 percent of the total value of industrial exports. The policy of opening to the outside world has brought about great changes in China's economy: foreign capital and advanced technology have been introduced into China, accelerating the upgrading and renewing of products and the expansion of imports and exports. Along with these also come the advanced management techniques and the operating mechanisms compatible with the market economy.

The main reason for the great success in China's post-1978 reforms is that the Chinese Communists, after summing up their historical experiences and lessons, corrected their pre-1978 "Leftist" mistakes, and have upheld the

principle of emancipating the mind and seeking truth from facts. During the process of reform and opening up we proceed from the actual conditions in China, respect the initiative of the people, learn and refer to overseas experience and judge everything by the fundamental criteria of the “three favorables,” namely, whether it is favorable for promoting the growth of the productive forces in a socialist society, for increasing the overall strength of the socialist state and for raising the people’s living standards. We have thus blazed a road of building socialism with Chinese characteristics under the guidance of Deng Xiaoping theory.

## II. Challenges to the Development of Chinese Economy in the 21<sup>st</sup> Century

We are confident of the prosperity of Chinese economy in the new century and soberly aware of the challenges posed to us.

First of all, the pressure of resources, ecology and environment on sustainable development. While China is rich in resources, per capita shares in them are rather low, below the average level of the world in many items. For example, the total volume of fresh water in China is 2.8 trillion cubic meters, making it the sixth largest fresh water country in the world. But in terms of per capita shares China takes up the 109<sup>th</sup> place among the countries in the world, with only 2,400 cubic meters per capita or a quarter of the world average. The forest area is 134 million hectares and the forest cover rate is 13.92%, while the per capita volume of wood storage is only 13% of the world average. The total area of land under cultivation is 95 million hectares, with only 0.07 hectare per head, less than a third of the world average. Soil erosion and desertification threaten to further reduce the arable land. Moreover, some important resources like fine quality energy deposits are also in serious shortage. All these impose severe restraints on sustainable development.

Next, the steady growth of total population and the aging of population bring about more difficulties for employment and social pension security. The total population will be still on the increase during the first half of the 21<sup>st</sup> century due to a large population base and a grim situation will loom for employment. Meanwhile, the age structure of Chinese population is undergoing a rapid change and the pace of its aging is accelerating. By 2010 the number of people over 65 years old will reach 113.78 million, making up 8.2% of the total population. With a low level of economic development too large a proportion of the aged will bring about more difficulties for employment and exert unfavorable influence over the economic growth and the improvement of the people’s living standard.

Thirdly, the unreasonable economic structure is an acute problem in China as manifested by the following: The position of agriculture as the foundation of

the economy is not stable, agricultural productivity is low, there is no outlet for surplus labor in rural areas to be channeled to other sectors, and the income of farmers is growing very slowly. In the industrial setup technology and knowledge intensive high-tech industries account for a small percentage while general processing industries with low added value have a relatively surplus capacity and the supply exceeds demand. With regard to the organizational structure of enterprises, diseconomy of scale is a general phenomenon and there are no large enterprises that can compete with big transnational corporations. The output value of tertiary industry constitutes a rather small percentage of the GNP, and the number of employees in these industries is not large enough.

Fourthly, development is unbalanced between urban and rural areas and between different regions; the gap between them is quite considerable. China remains a developing country and has a typical dualistic economy. On the one hand, it has established a huge industrial system and the output of secondary industry makes up 50% of the GDP; on the other hand, urbanization remains at a low level, 70% of its population make a living on traditional agriculture and a wide gap exists between town and country. The average income ratio of urban to rural residents is 3:1. At the same time, the gap finds its expression between eastern China and western China. The eastern coastal regions are more developed economically than the western regions, the per capita GDP ratio being three or four to one.

Fifthly, China has initially set up a socialist market economy, but the task of economic restructuring is far from being accomplished and, in particular, the reform in the state-owned enterprises is confronted with many difficulties. It is still to be solved how the state as owner will effectively encourage and restrain the management of the state-owned enterprises after these enterprises become the independently operating entities. A modern enterprise system according both with market principles and with the actual conditions in China has yet to be formulated. The high rate of debts and high proportion of redundant personnel in the state-owned enterprises hinders their competitiveness. Monetary institutional reform must be further deepened and how to solve and prevent financial risks waits for a better answer. There are also problems to be solved in the markets for factors such as capital and labor, not to mention the investment and social security systems.

Sixthly, corruption is a historical phenomenon prevalent in all countries. During the period of transition towards the socialist economy the traditional highly concentrated administrative restraints have gradually been weakened while new systems, mechanisms and legal institutions have yet to be perfected, giving rise to many loopholes. As a result, corruption cases of trading power for money and abusing power for personal gain are rather numerous, doing great harm to the relations between the Party and the government and the broad masses of the people and negatively impacting on the reform, opening up and economic construction.

Seventhly, following the return of Hong Kong and Macao the complete reunification of the motherland is an important historical task confronting the Chinese people. The CPC and the Chinese government have reiterated once and again their adherence to the principle of “peaceful reunification and one country, two systems.” However, with the connivance of and support from international anti-China forces the Taiwanese authorities have deliberately avoided and refused to acknowledge the principle of “one China” and continue to stick to the stance of an independent Taiwan. They have been engaging in arms expansion in a vain attempt to obstruct the reunification of Taiwan and the mainland. How to accomplish the great cause of the peaceful reunification is another major problem faced by us.

In international terms, China also faces rigorous tests with the approach of the new century. First, the process of globalization will hasten its pace, the Chinese economy will be more closely related to the world market; transnational corporations will appear on the market in China as fierce competitors, thus making the domestic economy an arena of international competition. The entry of China into the WTO will drive forward the reform, opening up and economic development of China, but it will also place pressure on the economy, especially on agriculture, technology intensive industries and the banking and insurance industries, in which China lags behind the developed countries.

Second, China will face competition from the developed countries in science and technology. In the 21<sup>st</sup> century, scientific and technological advance will be the primary force driving human society forward. The outcome of economic competition between nations hinges on scientific and technological innovation and the capability to transform science and technology into productive forces. Whoever has the highest technical level and the most powerful transforming capability will occupy the dominant position in the increasingly fierce international competition. For historical and institutional reasons, although China has greatly improved its capacity for innovation since the reform and opening up, it is still weak in this field. Achievements in scientific research cannot smoothly be turned into real productive forces; scientific and technological advances make far less contribution to economic growth in China than in developed countries. China still has a long way to go to catch up with the advanced countries in science and technology.

On top of that, China must face up to hegemony and power politics. The mainstream will remain unchanged in the 21<sup>st</sup> century, but, in the wake of the cold war, a few superpowers continue to pursue hegemony and power politics and continue to keep to cold war thinking. They invent every excuse to interfere in the internal affairs of other countries, using force or the threat of it against other states and violating their sovereignty. They hate to see a powerful and prosperous China and therefore try every means to contain China and check its advance.

### III. Tasks and Opportunities for the Development of Chinese Economy

Looking ahead, China will face severe challenges in its economic development, but it also has many favorable factors. China began to implement the tenth Five-year Plan in 2001. The goal is for the average annual growth rate of GDP to be 7% in the next ten years, and the present GDP to be doubled by the end of 2010. The present relatively comfortable life of the people will be further improved, the economic structure will be optimized and the national aggregate economic strength will be greatly enhanced.

After the cold war, the world is still full of contradictions and local conflicts have broken out here and there. However, peace, development, social progress and a prosperous economy are what the people all over the world want: they are the main themes of the 21<sup>st</sup> century and striving for their realization is an unstoppable trend of history. China will continue to pursue an independent and peaceful foreign policy and strive for a relatively long period of peace in the international environment so that it can concentrate its efforts on economic construction.

China is still in the throes of industrialization and far from completing this task. The per capita GDP falls short of 1,000 US dollars, belonging to the lower-middle category. China's advantages as a newcomer to modernization have not been given full play. Meanwhile, as a big developing country with the largest population in the world, China has great market potential and a broad space for development from infrastructure, manufacture to services, in either urban or rural areas, in either the east or the west regions. Tapping these potentials will contribute to the achievement of the third-phase strategic goal of socioeconomic development, industrialization and modernization of national economy.

Over the twenty and more years since the reform and opening up we have maintained sustained and rapid development of the national economy. The overall national capacity of the country has been considerably strengthened. The bottlenecks in infrastructure industries that long held back national economic development have now been loosened. In the field of science and technology, a complete research and development system consisting of basic, applied and development research is shaping up, which will lay a good foundation for China's economic development in the 21<sup>st</sup> century.

China has initially established a socialist market economy, an ownership structure with public and state ownership in the dominant position and diverse forms of ownership developing side by side is coming into being, the market is beginning to play a fundamental role in resources allocation under the macro control by the state. All these changes will constitute institutional guarantees for the development of Chinese economy.

A worldwide scientific and technological revolution is in the making, with information technology as the forerunner and with microelectronics, biological engineering, new energy resources, new materials, aviation and aeronautics, and ocean engineering technologies as the main contents. And achievements in the revolution are gradually being commercialized and industrialized. New high-tech sectors are emerging and traditional industries are being transformed with high technologies. All these provide new opportunities for China to make use of the achievements of technical revolution in other countries and give full play to its staying advantages in order to bring about a leap in the development.

Since the 1990s economic globalization has gathered momentum. There have been more and closer contacts between countries and regions through commodity trade, capital flow, technical diffusion and information transmission, exerting extensive and profound influence over the politics, economy and culture of all countries. As a big developing country, China will take an active part in the international division of labor, exchange and competition, take up the gauntlet of economic globalization, and at the same time make every effort for the establishment of a fair and rational new international economic order.

As the ninth biggest export country, China will, with its entry into the WTO, have more opportunities to participate in international cooperation and division of labor, promote the marketing of Chinese commodities all over the world and make export further stimulate the growth of domestic economy. The comparative advantage of cheaper labor will still be present for China in international competition as the country is very rich in human resources.

In order to seize the opportunities, face up to challenges and attain the goal of socioeconomic development in the new century, China will continue to take Deng Xiaoping theory as the guidance and march forward along the road of building socialism with Chinese characteristics.

First, we shall continue to make economic construction our central task and balance reform development and stability in order to create a favorable social and political environment for economic development.

Second, we shall further deepen economic restructuring, make strategic readjustments to the state-owned economy, effectuate strategic reorganization of state-owned enterprises and strive to seek various forms of for materializing public ownership. Further, we will establish and improve the modern enterprise and social security systems, actively standardize and develop production factor markets, and improve the macroeconomic control system, including reform and improvement of tax, monetary and investment institutions.



Third, we shall continue to readjust and optimize the economic structure with the main aim being to strengthen the competitiveness of industries and enterprises. The main tasks are as follows: Readjust the rural economic structure, promote agricultural industrialization and urbanization and hasten the steps of agricultural modernization, with a focus on increasing farmers' incomes; Accelerate development of high-tech industries with the information industry as the leading edge, base the national economy on information and networks and link informationization with industrialization; Transform traditional industries with advanced technologies and equipment, speed up the technical upgrading of traditional industries and the renewal of products; Encourage and guide the tertiary industry so that it will develop at an accelerated pace. Open up new areas of service and raise service quality.

Fourth, we shall implement the strategy of developing the country by relying on science and technology, enhance the scientific and technological innovation capacity and improve the quality of the whole population. The main measures are: With economic development, gradually increase input in scientific research, technical development and education; With reform as a driving force and through institutional innovations, reintegrate science, technology and education with economic development, and encourage enterprises to undertake technical innovation; Closely follow world developments in science and technology and the knowledge economy, and concentrating on selected areas to speed up the high-tech development and its industrialization.

Fifth, we shall promote rational distribution and coordinated development of regional economies and gradually narrow the gap between regions. Taking advantage of its favorable conditions, the eastern part of the country will continue to play its role in leading the reform and opening up. It will actively develop technology and knowledge intensive industries, raise its ability to take part in international competition and accelerate the process of modernization. The central zone will, on the basis of consolidating the position of agriculture, promote industrialization, vigorously transform traditional industries, raise productivity and operating efficiency of industry. China will actively and steadily carry out the strategy of developing the western region, focusing on rational tapping and utilization of natural resources, protection and improvement of biological environment and construction of infrastructure.

Sixth, we shall further expand in opening to the outside world and strive to do better in this regard. Taking advantage of its entry into the WTO, conforming to the trend of economic globalization and in accordance with the rules of international economic operation, China will extensively take part in international economic cooperation and competition, strive to raise the level and quality in the use of foreign capital, and channel foreign capital into the development of the middle and western parts of China, into the technical transformation of existing enterprises and into new and high-tech industries.