

Socialist Alternatives

- A. Theories of the Socialist Economy
- B. Revolution and Central Planning in the Soviet Economy
- C. Labor Management and the Yugoslavian Alternative
- D. China under Chairman Mao

What is Socialism?

- "From each according to his abilities, to each according to his work" – *Soviet Constitution* (1936).
- Marx was a harsh critic of capitalism, but somewhat vague on socialism. In *Critique of the Gotha Program* (1874) and elsewhere, he included:
 - Dictatorship of the Proletariat after the inevitable revolution
 - Capitalism should have already eliminated scarcity
 - Replacing private ownership with state ownership
 - Rational planning replacing anarchy of market
 - Eliminating wasteful competition
 - Re-education to eliminate last vestiges of capitalism
 - Eventual withering of the state
- Socialism paves the way for eventual emergence of Communism:
 - Withering of the state, elimination of cash economy, self-organization.
 - "From each according to his abilities, to each according to his needs."
 - Louis Blanc, *The Organization of Work* (1840), rephrasing Comte Saint-Simon.
 - "All social rules and all relations between individuals are eroded by a cash economy, avarice drags Pluto himself out of the bowels of the earth." – Marx

But can an economy actually be run by the state alone?

- Pareto's conditions for efficiency (1896): relative marginal values = relative prices = relative marginal costs.
- The Socialist Calculation Debate (*see link*):
- Barone's price planning model (1908): theoretically possible, but not really feasible.
 - Lange's trial and error model (1938): the possibility of market socialism, with the state owning resources and setting prices to "clear" markets.
 - Criticisms from von Mises (1920) and Hayek (1937-48): need for markets to determine marginal values, impracticality of socializing incentive, impossibility of centralizing information, market prices convey information.
 - Other versions of "market" socialism by Taylor, Dickenson, Lerner, Yunker, and Nove.

Institutions of the Classical Centrally Planned/Managed Economy

- ❑ State owns firms (SOEs), arranged under production ministries. State chooses managers to fulfill plans.
- ❑ State statistics agency collects data on inputs and outputs.
- ❑ State planning agency sets targets for inputs, outputs, technology; taut planning, ratchet effect.
- ❑ State pricing agency sets prices based on state goals, not market values. Mark-up pricing and the incentive to use more expensive inputs.
- ❑ State owns banks, collects savings, and allocates capital, labor, land, et cetera. Monobank can ensure that plans are followed.
- ❑ State relies on SOE profits for revenue, and pays for both investment and public goods out of state budget, banks.
- ❑ Foreign trade is controlled through state ministry to augment production plan.

Quantity Planning?

- ❑ Leontief's input-output analysis:
 - Linear relationship between quantities of outputs, material inputs, and resources
 - Input coefficients a_{ij} = how much of input i is needed to produce one unit of output j .
 - Production \geq intermediate uses + final demand
- ❑ For example, for $n=3$:

Input-Output:	$X_1 \geq [a_{11} X_1 + a_{12} X_2 + a_{13} X_3] + Y_1$
	$X_2 \geq [a_{21} X_1 + a_{22} X_2 + a_{23} X_3] + Y_2$
	$X_3 \geq [a_{31} X_1 + a_{32} X_2 + a_{33} X_3] + Y_3$
Production	$K \geq [a_{k1} X_1 + a_{k2} X_2 + a_{k3} X_3]$
Possibilities:	$L \geq [a_{l1} X_1 + a_{l2} X_2 + a_{l3} X_3]$
- ❑ As equations (not inequalities), these can be solved using matrix algebra, though number of calculations rises exponentially with the number of equations.
- ❑ Material Balance Planning (MBP) uses input-output analysis to solve for necessary inputs and outputs, given accurate input coefficients, resource constraints, and feasible final demands.

Problems of MBP

- ❑ Final demand combinations determined by preferences of planners, not consumers.
- ❑ MBP has extremely high information needs. This makes it very slow to adapt to technological change, new circumstances.
- ❑ Tendency to aggregate and separate due to calculation problem, data collection problem. Result is autarky, vague targets.
- ❑ Prices only serve accounting role, and MBP does not allow for substitution between inputs (or outputs) due to scarcity.
- ❑ Input shortages or unmet targets propagate into more simultaneous shortages and surpluses.
- ❑ Efficient allocation and distribution not even considered as a goal of the system. No effort to meet Pareto conditions. Little attention paid to managerial, worker incentives.

An Alternative Approach: “Market Socialism”

What about *price planning*?

- Mathematical equations to solve Pareto conditions are inherently nonlinear, and also require much more knowledge of cost and utility functions. Barone, for example, implicitly assumed known first derivatives.
- Lange’s Trial and Error Model:
 - State owns capital and natural resources, hires managers to run state firms, directs them to set $P=MC$ and minimize AC.
 - Markets allocate labor and intermediate products, and distribute final goods.
 - State CPB sets capital and resource prices by trial and error to ensure stability, efficient use.
 - Enterprise profits are social dividend.

But what are the managerial incentives? Will the CPB have better information? What about competition and profits?

The Classical Socialist Economy Janos Kornai

The Classical Socialist Economy is a coherent system, with its own internal logic. For example, market socialism is not internally consistent, nor is “democratic socialism.”

Five steps:

- 1) Political power
- 2) Ownership
- 3) Coordination
- 4) Incentives
- 5) Characteristic Phenomena

These are similar to the “characteristics” of any economic system, but the argument is more subtle that listing categories of differences.

Kornai’s Five Steps

Step 1) The Classical Socialist Economy begins with an unchallenged monopoly of power by a Marxist-Leninist Communist Party.

- Party is an elite vanguard with an unquestioned, coherent, and self-legitimizing ideology, and a paternalist approach to representation.
- Marxism-Leninism is key because it advocates the elimination of private ownership and markets.
- Party offers a promise to help a poor economy develop faster while meeting basic needs and full employment.
- Party controls economy and society through interpenetration of the state apparatus and an intolerance for independent organizations.

The Second Step

The Power Block then requires the Party to try to eliminate capitalism, which requires:

Step 2) State ownership of the means of production becomes predominant.

- Conversion of capitalist firms (especially in "commanding heights") into SOEs.
- Collectivization of farmers, small producers, petite bourgeoisie.

The Third Step

Each step creates a need for the following steps.

Power + Ownership then requires:

3) Bureaucratic coordination and management

- Central planning (i.e., MBP).
- Very large enterprises, ministerial autarkies, poorly defined objectives.
- Von Neumann's redundancy: too many mothers-in-law.
- Vertical linkages affect information flows.
- SOE provides housing, education, food, other services to workers. Manager also implements and enforces state policy.

These Three Steps in turn cause:

- 4) Peculiar Incentives for firms, workers, consumers.
- Soft budget constraint and plan bargaining.
 - Weak price response, ratchet effect, seller's markets, investment hunger, labor hoarding, import hunger and export aversion.
 - Poorly-defined, often irrational targets.
 - Misallocation of labor, low morale, shortage psychology, risk aversion.

5) Observable and characteristic phenomena of the Classical Socialist Economy.

- Shortage Economy: goods, capital, and labor.
- Tonnenideologie, capital-intensive large-scale projects, poor quality, calendar pulsation.
- Relative equality of nominal incomes, not access to desirable goods.
- Environmental ecocide (tragedy of the commons).
- Separation of science and product innovation, erosion of human capital, obsolete physical capital.

The Fel'dman Model: Forced Savings and Unbalanced Growth

Shortages may not only be an inevitable outcome of planning, they may actually be intentional.

- ❑ Goal is growth through high rates of capital investment in producer goods (i.e., capital goods, heavy industry), and this requires state monopoly over banks and trading.
- ❑ Low state prices for consumer goods lead to chronic shortages, cheaper wages, and forced savings, which are reinvested through monobank into heavy industry.
- ❑ High state prices for producer goods and low wages lead to higher profits, which are reinvested through state budget into heavy industry.
- ❑ Abram Bergson on *tonnenideologie*: "Under capitalism, bread is the final good and steel is the intermediate input; under socialism, steel is the final good and bread is the intermediate input."
- ❑ Long-term effect on worker motivation, black markets.

Revolution and Central Planning in the Soviet Economy

- ❑ Early Russian history:
 - Eastern orthodox, European periphery;
 - The Kievan Rus, Duchy of Moscow, Mongol invasion (1237-1452);
 - Ivan the Terrible (1547-84), first Tsar (Czar) of all Russia.
- ❑ The Romanov dynasty (1613-1917): 19 Tsars, including:
 - Peter I, the Great (1682-1725): Europeanization of aristocracy, building St. Petersburg, centralizing government, modernizing military, expanding empire, and increasing the subjugation of serfs.
 - Nicholas I (1825-1855): Creation of Secret Police, repressive state.
 - Alexander II (1855-1881): Crimean war, emancipation of serfs (1861) through redemption payments and village ownership; started industrialization (i.e., limited liability companies), massive railroad construction; murdered by revolutionaries.

Nicholas II (1896-1917):

- In the late Imperial Period, Russia was a contradiction of characteristics: dual economy, with wealthy and modern elites and traditional agriculture; collectives (Mir) for peasants after Emancipation; rising military and industrial power; naive Czar determined to hold on to "God-given" powers.
- Revolution of 1905 after Japanese War (Bloody Sunday).
- New Duma given consultative powers - Czar still an autocrat.
- Stolypin Reforms by decree: peasants given freedom to elect *zemstvo* councils, opportunity for land ownership, anti-terrorist laws, compulsory education, factory worker councils (*soviets*); Premier Stolypin lost support of Tsar, assassinated in 1911.
- First World War: Czar supported Balkan independence, initially resisted general mobilization. Assumed control of military in spite of inexperience, left rule of Russia to Empress and Rasputin.
- March 1917 Revolution started by Food Riots in Petrograd.
- Nicholas abdicated, successor refused crown. Prince Lvov led provisional government.

The Bolshevik Revolution

- ❑ After Tsar's abdication, Alexander Kerensky of the SDP (Menshevik) party became premier.
- ❑ Provisional government was hesitant to stop fighting the war.
- ❑ Germans returned Vladimir Ulyanov (Lenin) by secret train.
- ❑ Before elections could be held, Lenin's Bolshevik Party stormed Winter Palace (November 1917).
- ❑ Civil War (1918-1920): Reds vs. Whites, murder of royal family in 1918.
- ❑ Founding of Union of Soviet Socialist Republics (1922). 12+3 Republics.
- ❑ Soviet sphere included Mongolia (1921), eventually six CEE states under Warsaw Pact.



War Communism (1918-1921):

Civil War not the only problem:

- ❑ Treaty of Brest-Litovsk with Germany.
- ❑ Invasion by Allies in 1918.
- ❑ Invasion of Ukraine by Poland under Pilsudski.

A Jump to Communism?

- ❑ Military-style economy: labor armies with no mobility, forced extraction of agricultural surplus, nationalization of land, livestock.
- ❑ Nationalization of industry: 37,000 enterprises under Vesenhka (BCHX), the Supreme Council of the National Economy.
- ❑ Private trade outlawed, little use of money, rationing.

Results?

- ❑ Drought, famine (1920-21), death of estimated 5 million.

New Economic Policy (1921-28):

- Lenin: "We are not civilized enough for socialism." Russia still primarily an agrarian nation, with small urban population and weak industrial base. "In order to take two steps forward, we shall have to take one step backward."
- Restored some private ownership to farming, Bukharin's slogan of "Get rich!"
- Leased small enterprises to private entrepreneurs. Soviets retained "commanding heights" which employed 80% of industrial labor.
- Legalization of trade, private markets, money.
- Labor laws (1922): 8 hour day, 2 week holiday, benefits, collective bargaining, mobility.
- Foreign peace treaties, commercial recognition, international trade and recognition.

Russian Growth Estimates

According to Maddison's estimates for Russian Empire/Early USSR:

Population:

- 1820-1870: 1.0% growth (annual average).
- 1870-1900: 1.1% growth.
- 1900-1913: 1.8% growth (1.6x U.S. pop., 2.4x Germany).
- 1913-1922: -0.3% growth (net loss of 4 million lives; gross loss of 30 million if population growth had continued at 1.8%).
- 1922-1928: 1.8% growth.

Per-capita income:

- 1820-1870: 0.6% growth (annual average).
- 1870-1900: 0.9% growth.
- 1900-1913: 1.4% growth (30% of US/UK).
- 1913-1928: -0.5% growth (net decline of 8% after recovery, no income estimates for 1922 but they probably weren't pretty).

The Great Debate (1924-1928)

Left Deviation: Teleologists

(Trotsky, Preobrazhensky)

- Fear of capitalist encirclement, need for rapid industrialization and militarization.
- Concern over re-emergence of new capitalist class.
- Advocated return of state monopoly over trade, agriculture.
- Rapid shift towards centrally planned socialism.

Right Deviation: Geneticists

(Bukharin)

- Need to consider current conditions.
- Smychka – alliance between workers and farmers.
- "Get rich!" incentive for farmers.
- Continuation of NEP.
- Gradual movement towards planned socialism.

Stalinism



- Josef Dzugashvili, CPSU General Secretary when Lenin died (1924).
- Ruthless rise to power. Bukharin called him a "New Genghis Khan."
- Originally supported Right Deviation, switched to Left. Purged Trotsky, Bukharin, and virtually all "Old Bolsheviks."
- Political purges, show trials in 1930s, Cheka/OGPU/KGB, Gulag Archipelago (see Solzhenitsyn), Reign of Terror. Perhaps 5-20 million people died.
- First Five-Year Plan (FYP) in 1928-33, focus on rapid growth in producer goods, state monopoly over trade, banking. Forced collectivization to get state control over surplus, exterminate Kulaks. Perhaps 7 million died in Ukraine alone during first winter.
- World War II: secret Ribbentrop-Molotov agreement (1939), German invasion (1940), estimated 17 million Soviet deaths.
- Stalin's total control over military, society until his death (1953).

Institutions in the Soviet Union

- Party (CPSU) run by Central Committee, Politburo, General Secretary. Party cells at every level, including enterprises.
- Administration: Council of Ministers, Premier.
- Legislature: Supreme Soviet a rubberstamp, Chairman of Presidium was "President".
- Nomenklatura: 200,000 jobs controlled by CPSU.
- Gosplan: state planning agency used approximately 4000 I-O tables, FYPs passed into law by Supreme Soviet.
- Gosbank: Control by Ruble, cash used by consumers, no independent monetary/fiscal policy.
- State-owned enterprises: managers appointed by ministries; large, capital-intensive, self-sufficient; use of *tolkachy*; labor shortages, layoffs difficult, rationing, housing; MBP targets; cost-plus pricing.
- Foreign trade: CMEA, state-administered, price equalization, soft overvalued Ruble, accumulation of hard currencies (Eurodollars).
- Unions: not independent of CPSU, no strikes or disruption allowed.

Agriculture in the Soviet Union

- Prior to WWI, Russia was the world's largest exporter of grain.
- After Forced Collectivization, agriculture organized into Sovkhoz (large state farms, preferential treatment), Kolkhoz (collectives). Small private plots allowed. In 1985, one study found:
 - Sovkhoz: 53% of land, 37% of output.
 - Kolkhoz: 44% of land, 34% of output.
- Poor coordination, infrastructure, transportation: estimated that half of potato harvest rotted in fields, trains.
- Central planning not adaptable to change, poorly suited for agriculture.
- Lack of motivation, low state prices, poor assessment of worker performance.
- Soviet Union became world's largest importer of grain.

Soviet Expansion

- USSR (1922): originally 12 Republics.
- Mongolia (1921): first satellite.
- Stalin headed Comintern: training of revolutionary cadres.
- Baltic States (1939): Latvia, Lithuania, Estonia in USSR.
- In 1944-45, Soviet Red Army occupied all of Central and Eastern Europe (CEE) except Yugoslavia and Albania.
 - Eastern European governments in Czechoslovakia, Hungary, Poland, Bulgaria, Romania, Yugoslavia and Albania all formed socialist governments. Most became Soviet allies.
 - Joint Allied Occupation in Germany and Austria: East German Soviet Zone became DDR, Berlin Blockade and Airlift, building of Berlin Wall.
 - North Korea also occupied by Soviets. Communists took power in China (1949 Revolution), North Vietnam (after liberation from French), Cuba (1959 Revolution), and in other small countries.
- Churchill's "iron curtain": U.S. Policy of Containment, Cold War, Marshall Plan, and NATO.
- Soviet Union established Warsaw Pact and CMEA (Comecon).

Economic Reform After Stalin

- Reform under Stalin was nonexistent:
 - Brutal repression of economic science
 - Two major attempts at reform (1933, 1947) led to execution of reformers.
- Khrushchev Decade (1953-64):
 - Denunciation of Stalin's personality cult and purges.
 - Emphasis on agricultural investment, decentralization. Not successful.
 - Resurgence of economics, mathematics, and planning.
- Brezhnev Era (1964-1983):
 - Premier Kosygin's Reforms in 1960s – recentralization, Shekino method to reduce labor hoarding, managerial incentives, etc.
 - Slowing growth, stasis afterwards.
 - Brezhnev Doctrine.
- Andropov (1983-84)
- Chernenko (1984-1985)



Perestroika – Restructuring

- Gorbachev selected as General Secretary, 1985
 - Margaret Thatcher: "Here is a man we can work with."
- China's initial reforms a successful example, but the USSR began in industry.
- New attitude of *Glasnost* led to improved international relations.
- *Uskorenye* (Acceleration) during 12th FYP:
 1. Retooling rather than expansion
 2. New independent quality control agency
 3. Anti-alcohol campaign
 4. Attack on underground economy
 5. "Human Factor" – *Glasnost* (Openness)
- Problems and "cavalier inconsistency": bottleneck in machine-building, conflicts with quality control, falling revenues (vodka, oil), Chernobyl).
- Growth fell to 0%, budget deficits > 8% by 1987, financed by Gosbank credits → repressed inflation.



Osnovanye Polizhenya – Basic Theses

After failure of *Uskorenye*, Gorbachev realized the need for more radical reforms (*Perestroika*) – but with the objective of saving Socialism, not transforming to Capitalism.

- Law on Private Activity, 1986 → small entrepreneurs
 - Law on State Enterprises, 1987 → contracts
 - Law on Cooperatives, 1988
 - Political Reform → led to elections in Republics, new Union Treaty
 - Renunciation of Brezhnev Doctrine for Eastern Europe
- Economy began to shrink by 1990: high deficits, rising inflation, disarray.
- Gorbachev turned away from reform, Shevardnaze resigned, Shatalin's "500 Days" Program killed by hesitation.
 - Coup in August 1991 failed: republics seceded, CPSU outlawed in Russian Federation, USSR dissolved.

Russian Growth Estimates (Part 2)

Again, according to Maddison's estimates:

Population:

- 1928-1940: 1.2% growth (annual average).
- 1940-1946: -2.0% growth (net loss of 12 million lives; gross loss of 37 million if population growth had continued at 1.2%).
- 1946-1990: 1.2% growth.
- 1990-2003: 0.03% growth.

Per-capita income:

- 1928-1939: 4.6% growth (annual average).
- 1939-1946: -2.2% average (net decline of 15%).
- 1946-1960: 5.3% growth.
- 1960-1970: 3.5% growth (37% of U.S.).
- 1970-1980: 1.4% growth.
- 1980-1990: 0.7% growth.
- 1990-1996: -9.2% average for successor states (net decline of 44%).

Growth Performance

- We would expect that central planning would be good at marshalling resources in a backwards economy, but not good at using them efficiently.
- By 1990, official data estimated Soviet per-capita output equal to almost half of U.S. level. Services, black market.
- Growth rapid in 1930s, postwar recovery, 1950s. Krushchev (1956): "We will bury you."
- Growth failed to meet FYP targets after 1960s, and targets continued to fall. By end of 1980s, economy was stagnant.
- Prices hard to measure: no markets, repressed inflation (shortages), so real growth overstated.
- Extensive growth, not intensive: priority on heavy industry, high savings, high labor force participation, use of easily available resources, ecocide. Educated workforce, but severe problems with motivation, product quality, innovation, chronic shortages. Labor shortages in Russia, surplus elsewhere.
- After collapse of the Soviet Union, economy fell by over half. Some economists estimated that Soviet GDP was significantly overstated due to distorted prices.

Labor Management and the Yugoslavian Alternative

- Historical context:
 - Battleground of three empires (Austro-Hungarian, Ottoman, and Russian)
 - WWI and Treaty of Versailles
 - Factions in conflict with long history of grievances – including Croatian Catholics, Bosnian Muslims, Orthodox Serbs, Albanians, Slovenians, Macedonians.
 - Civil War 1921-41, followed by Nazi Occupation, Croatian puppet government, and indigenous partisan resistance by communists.

Marshall Tito

- Josip Broz (Tito) ruled 1945-1980:
 - Sent by Comintern to Yugoslavia in 1937; reorganized communist party and led partisan resistance.
 - Initial policies included land redistribution and nationalization of foreign-owned capital, but resistance to Stalinist pressures for collectivization and withdrawal from trade relations with West.
 - First FYP used Soviet-style detailed planning and state ownership, initially successful.
 - Break with Stalin in 1948-1949 over foreign trade and investment.



Economic Reform under Tito

- The “Visible Hand” Reforms in 1951:
 - Decentralization of power to local and republic governments, workers’ councils.
 - Reduction of administrative pricing, more markets in rural and urban areas.
 - State enterprises set own output targets but planners retained control over investment and trade.
 - The idea was that state enterprises would be controlled through workers’ councils, and sell on markets, not for state quotas.
 - As in the Soviet NEP, this sparked a debate between the “left/conservative” faction and the “right/liberal” faction, but the liberal faction won!

Market Socialism, 1965

- More decentralization: investment decisions were transferred to *Basic Banks*.
- Workers were organized into *Basic Associations of Organized Labor* – perhaps many in a large enterprise, responsible for own contracts and self-management agreements.
- Price liberalization, enterprise autonomy, indicative planning, exchange rate devaluation and simplification, foreign trade reform, et cetera.
- But can the labor-managed economy succeed?

The Ward-Vanek-Domar Model

- Assume the capitalist firm maximizes profit
 $\pi = p \cdot Q - r \cdot K - w \cdot L$:
 - $p \cdot MPL = w$, $p \cdot MPK = r$: this determines optimal L^* , K^* .
 - If p rises, Q , L^* , and K^* all rise.
- Assume the labor-managed enterprise maximizes average residual $y = (p \cdot Q - r \cdot K) / L$:
 - $p \cdot MPL = y$, $p \cdot MPK = r$.
 - If $y > w$, then $L < L^*$; if $y < w$, then $L > L^*$.
 - If p rises, $y = (pQ - rK) / L$ rises more than proportionally, so L^* falls. Unless K increases more than enough to compensate, this means Q falls – a perverse price response!
- Furubotn (1976): the effect of investment on growth leads to a reliance on debt, not equity.
- The Property Rights solution – explicit share rights lead back to a two-class workforce.

Performance and problems

- **On one hand:**
 - Improving growth rates, worker productivity, and technology relative to traditional planned economy.
 - The Yugo was the only major industrial product from a socialist economy ever exported to the West.
- **But on the other hand:**
 - Bureaucracy became a significant portion of the BOAL. Inflation from reliance on debt from basic banks combined with BOAL control over lending, bad debts, and central bank bailouts.
 - High unemployment rates (>10% in 1980s).
 - Merger movement, rising industrial concentration, and many instances of monopoly pricing – a paradox.
 - Chronic balance of payments deficits.
 - Regional inequality issues led to transfers.

The End of Yugoslavia

Death of Tito led to collective presidency and regional conflicts in economic policy (esp. Slovenia vs. Serbia).

- By 1990s, Yugoslavia came apart – Slovenia and the Croatia seceded – and Serbian President Milosovic (who controlled the army) joined with local Serb populations to begin a brutal war on Croatia, then Bosnia, and finally Kosovo.
- After NATO war in Kosovo, Milosovic stole an election from his rival Kostunica and was then pushed from power.
- Serbia and Montenegro joined under a new constitution, but finally split apart in 2005. Kosovo is still officially part of Serbia but is administered by the UN. Bosnia-Herzegovina is divided into a Muslim/Croat Federation and Republika Srpska. Croatia and Macedonia are independent, along with Slovenia – which has joined the EU.



The People's Republic of China Under Chairman Mao Zedong

Historical Background:

- Longest continuous civilization: at least 4000 years of good history.
- Empire unified in 221 BC from warring states
- Dynastic Cycle: stable imperial autocracy divided by periods of chaos. Internal power struggles before Song, foreign invasion: Mongolians, Manchus (Qing Dynasty).
- China was the world's most advanced economy for much of human history. Also cheap labor, premodern agricultural technologies, gentry-supported backward-looking imperial state, Malthusian tensions.
- The Opium Wars (1840-42, 1862) coincided with decline of Qing power (Taiping Rebellion).
 - Century of Humiliation: unequal treaties, indemnities.
 - Slicing the Melon: missionaries, foreign concessions.

Revolutionary China

- Scholar Protests (1898): Kang Youwei, Liang Qichao, the Guangwu emperor, and the Hundred Days (put down by Ci Xi).
- 1911 Wuhan Uprising (1911), abdication of boy emperor; 2nd, 3rd revolutions; Nationalist Party (Guomindang, or KMT). Sun Yatsen, Chiang Kaishek.
- May 4th Movement (1919), disillusion with western democracy, CCP founded.
- Warlord Period; CCP-KMT alliance, 1927 Northern Expedition, CCP-KMT split, Nationalist Nanjing government.
- CCP: Jiangxi Soviet, Long March, Zunyi summit, Yan'an redoubt; kidnapping of Generalissimo, alliance with KMT.
- Japanese encroachment: War over Taiwan, Korea (1895), War with Russia (1905), Manchuguo, invasion (1937); Rape of Nanjing, retreat to Chongqing.
- Civil War (1945-49). KMT better armed, but morale low, corruption and hyperinflation rampant.

The "High Tide of Socialism"

- October 1, 1949: Chairman Mao announced that "The Chinese people have stood up." PRC founded.
- Common Program (1949) – very inclusive approach.
- Land Reform (1950-53) – brutal, political.
- Mutual Assistance Treaty (1950)
- Korean War (1950-53) – confidence, status, radicalization
- First FYP (1952-57):
 - Nationalization, gradual collectivization – big push to complete both in 1955-57.
 - Soviet advisors, loans, turnkey factories, etc.
 - Soviet-style planning, heavy industrialization – difficult, "learning by ruining," still successful. Plan not actually completed until 1955.
 - Hundred Flowers (1957) followed by Anti-Rightist Campaign.
 - Agricultural production reached 1937 levels, economy growing.

Mao Zedong Thought



- Peasants, not workers, the Chinese revolutionary class: landlords, not capitalists, are the exploiters.
- People's War: guerrilla warfare techniques
- Mass Line rather than reliance on Party; Emphasis on Campaigns to educate, arouse the masses; Anti-intellectualism (vs. Chinese traditional respect for the scholar).
- Continual Struggle (not harmony), even after revolution; inherent contradictions.
- Self-Reliance: denies comparative advantage, division of labor, need for central planning.
- Egalitarianism.
- Need to adapt Socialism to Chinese circumstances.

The Great Leap Forward (1958-61)

Following Announcement of 2nd FYP, Mao announced switch to "Da Yue Jin." Turned Marx on his head.

- Plan for "three years of bitter struggle" to overtake UK in steel production, rapid industrialization.
- Agriculture: giant communes, mass production methods, direction from top, communal kitchens consumed surplus.
- Rural industrialization: backyard steel furnaces, push for "appropriate technology."
- Urbanization: rural workers, agricultural surplus taken to cities.
- Politics in Command: little planning, pressure on cadres to overstate success, feedback loop.
- **Break with the Soviet Union** (1960); Khrushchev's denunciation of Stalin, Mao's rejection of Soviet methods.
- **Initial news very good, truth was awful**: 30 million starved in famines (first rural, then urban), estimated 50 million fewer Chinese by 1961.
- Lushan Conference: ouster of Peng Dehuai, Mao admitted some errors. Policies slow to change.

The Cultural Revolution

- Recovery (1962-65) under Liu Shaoqi, Zhou Enlai, Deng Xiaoping: return to central planning, party control, agricultural decentralization.
- Socialist Education Movement (1965), development of Mao's personality cult (little red book).
- Great Proletarian Cultural Revolution: red guards, attacks on "four olds;" elimination of Mao's competitors; breakdown of education, public order, and planning; near civil war in 1967, order then re-established by PLA.
- Continuation of radical policies until Mao died (1976):
 - "Gang of Four" radicals, extreme uniformity.
 - Conflict with USSR, rapprochement with USA (Shanghai Communiqué, 1972), triangulation.
- After Mao's death, Hua Guofeng new chairman: two whatevers, arrest of Gang of Four, Great Leap Outward.

People's Republic of China After Chairman Mao

- ❑ In 1972, Mao Zedong met with Nixon and relations with the rest of the world began to normalize.
- ❑ Mao Zedong, Zhu De, and Zhou Enlai died in 1976. Hua Guofeng was new Chairman, and arrested "Gang of Four."
- ❑ Deng Xiaoping – a small, intelligent, pragmatic, and popular figure within the CCP – was admitted back into circles of power after being purged twice.
- ❑ In Dec. 1978, Deng Xiaoping emerged as "paramount leader" after his proteges (Hu Yaobang, Zhao Ziyang) were elected to highest formal positions.

Deng Xiaoping



- ❑ End of "Politics in Command" -- managers promoted on the basis of skills, rehabilitation of rightists, end of class labels.
- ❑ Political restructuring to end personality cults: no more CCP Chairman, term limits on highest positions of General Secretary, Premier, et cetera.
- ❑ Party legitimacy still depended on Mao's reputation, so party repudiated most of his policies with repudiating him.
- ❑ Pragmatic "black cat, white cat" approach.

China's Economic Reforms

- ❑ Open Door Policy (by 1980): Joint-Ventures, Special Economic Zones, foreign exchange retention, tourism, et cetera. China granted "MFN Status" by U.S. and other developed countries, but still subject to textile and other quotas along with annual MFN Review.
- ❑ Rural Reform (by 1980): Household Responsibility System, decollectivization, rural and urban markets, new rural enterprises (TVEs), and the eventual release of surplus labor.
- ❑ Industrial Reform (by mid-1980s): Decentralization, SOE autonomy, profit retention, two-tier pricing system, banking reforms, *getihu* system, et cetera. SOEs improved productivity in 1980s but also started to borrow heavily from state banks, and by late 1980s competition, rising productivity from other sectors, and SOE inefficiency was leading to falling profits and falling market shares.

Chinese Policy after 1989

- By late 1980s, inflation was rising and many inside and outside the CCP were becoming dissatisfied.
- Zhao Ziyang pushed for tolerance of private sector and wholly-owned foreign firms, but was blamed by CCP conservatives for reform problems.
- Student protests in 1987 led to ouster of Hu Yaobang, and large Tian'anmen protests after death of Hu led to a crackdown in June 1989, ouster of Zhao, and worsening of international relations. New leadership included Jiang Zemin and Li Peng.
- Retreat from reform in 1989-1991 did not help SOEs but did lead to millions of rural job-seekers coming to the cities.
- Deng Xiaoping pushed for return to reform with his trip to SEZ in Shenzhen.
- In 1992, the CCP announced that China would seek to create a "Socialist Market Economy" (*Shehuizhuyi Shichang Jingji*), effectively renouncing traditional communist objective. Prior attitude was that reform was temporary.

The Socialist Market Economy

- Initial reforms included:
 - Efforts to improve SOE management through limited liability incorporatization and creation of stock markets, but state retained controlling share.
 - Tax and fiscal reform to prevent rising deficits.
 - Simplification of exchange rates and devaluation to black market rate, full convertibility of current account by 1996.
 - Separation of state banks into commercial banks and policy banks.
- SOEs were to be the "cornerstone" of the SME, but their profits, shares, and performance plummeted.
- NPL problem in state-owned banks 25-50% of loans, but state banks continued to lend to SOEs.
- Inflation accelerated in mid-1990s, wiping out real effect of devaluation. Zhu Rongji named vice-premier (later premier) and began to tighten money and credit growth and tried to reduce NPL problems.

China After 1997

- Deng died in 1997, just before HK was returned to China.
- Asian financial crisis of 1997 did not happen in China because foreign exchange transactions were limited to exports and imports (foreigners were in segmented "B shares" market). But export growth did slow after other Asian economies devalued their currencies, and government has used fiscal policy to keep demand high.
- After Deng died, CCP General Secretary (and President) Jiang Zemin announced new "release the small, retain the large" policy for SOEs, and pushed to allow private entrepreneurs into the CCP.
- In 1990s, China became the largest less-developed recipient of FDI, and this funded China's growing export sector.
 - Many of these exports are in labor-intensive products that used to be produced by other Asian countries, though China is making signs of moving into higher-tech areas.
 - Export sector relied upon to deal with urban unemployment problem.
 - China now accounts for 10% of U.S. imports, and blamed by some in U.S. for loss of manufacturing jobs. The U.S. has lost 2 million manufacturing jobs since 1995, while China has lost 16 million. China runs a large current account surplus with the U.S. but a deficit with the rest of the world.

Comparative Statistics

	USA	Japan	China
Population (2000)	284.0	127.1	1271.9
GDP (billion US\$, 2001)	\$10,082	\$4,176	\$1,159
Avg. Growth Rate 1990-2000	3.3	1.4	10.1
Household Consumption Share	68	56	48
Health Expenditures Share	13	8	5
GDP Per-Capita 2001 US\$	\$34,870	\$35,990	\$890
PPP Per-Capita 2001 US\$	\$34,870	\$27,430	\$4,260
GINI	40.8	24.9	40.3
Life Expectancy at birth	77	81	70
Trade Ratio	26.2	20.3	49.2
Pop Share below \$2/day	0.0	0.0	52.6
Under 5 mortality /1000	9	5	39
Primary School Enrollment	94.9	100.0	93.2
Inflation Rate 1990-2000	2.2	0.1	6.3
Unemployment Rate	5.0	4.9	10.0
Total MMT CO2 Emissions	5448	1134	3108
Per-capita MT CO2 Emissions	19.2	8.9	2.4
Highest Marginal Tax Rate	39.6	37.0	45.0

China's Per-capita Growth Performance

Using Maddison's PPP estimates (international Geary-Khamis Dollars)

- 1 – 1850: 0.02% per year
- 1850-1913: -0.1%
- 1913-1950: -0.6%
- 1950-1959: 5.3% (Japan 7.1%, Korea 4.2%)
- 1959-1976: 1.2% (Japan 7.2%, Korea 6.9%)
- 1976-1989: 6.0% (Japan 3.4%, Korea 6.7%)
- 1989-2001: 5.8% (Japan 1.2%, Korea 5.2%)
- 1950-2001: 4.2% (Japan 4.8%, Korea 6.0%)

China Now

- China was finally admitted into the WTO after years of trying, and agreed to open its import, telecommunications, and banking sectors to foreign competition and investment. China is seen by many as dragging its feet, especially in banking.
- China's export growth (though imports are starting to catch up) → trade surpluses, FDI inflows → BOP surpluses invested in U.S. assets.
- Rural areas continue to have large surplus labor problem, and many worry about effect of U.S. agricultural imports.
- Price deflation from increased competition and rising money demand eroded real exchange rate and led to implicit insurance for domestic depositors and FDI investors.
- Exchange rate kept low through massive purchases of U.S. Bonds.
- China now pressured to allow currency to revalue or even float, but this is dangerous to banking sector. Alternative may be price inflation from BOP surpluses.
- Jiang Zemin stepped down as CCP General Secretary and President, replaced by Hu Jintao. Jiang also removed from CCP Military Affairs Commission.
