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Trial and Error in Economic Planning

by Professor Karel Holbik, Boston

The defeat of the Japanese in the summer of 1945 confronted the National Government of China with the problems of reconstruction. One must consider the chronic economic problems which were rendered acute by many years of war; a growing population already beyond the means of subsistence under prewar economic conditions; a transportation system insufficient before the war, and now very much deteriorated; and the overwhelming burden of continuing inflation. No wonder the beginnings of industrialisation had suffered in China.

The questions to be answered are: what economic planning was instituted by the Communist government in rebuilding China, and how successful has this planning been in removing China from the class of an underdeveloped nation to that of a modern industrial state?

Reconstruction Period

When the Chinese Communists came to power in 1949, they took over an underdeveloped economy which had been greatly disrupted and destroyed by many years of war, inflation, and weak, inefficient government. Roughly 85 p.c. of the population was engaged in agriculture or in occupations closely related to agriculture¹. Methods of cultivation were intensive, but modern scientific techniques of farming were almost unknown to the average peasant. Output per acre was fairly high but output per man was low and agriculture barely supported minimum subsistence standards of life for the peasantry².

The only significant heavy industry in China was that fostered by Japan in Manchuria in the 1930's which the Soviets looted during the final phase of World War II, from 1945–1946.

The first objectives of the new Chinese government were those of achieving economic stability and restoring productive capacity to the country. The first task in accomplishing these objectives was that of achieving a stable currency. By very

stringent fiscal and monetary measures the Communist were able to put a halt to inflation. They were also successful in establishing unified political control, repairing the transportation facilities, and renewing domestic trade. All of this resulted in the recovery of the agricultural and industrial output during this three-year period.

By the end of 1952 the government announced the end of the period of reconstruction and the start of the period of construction. The authorities claimed that the output of 33 major industries had risen 26 p.c. above the prewar peak levels; 16 p.c. in capital goods and 32 p.c. in consumer goods³. Data—they are actual Communist data—show a 70 p.c. increase⁴ in national income for the years 1949–1952. Other and different figures were given by various authors. Nevertheless, they all agree that the period 1949–1952 was one of successful economic recovery for Communist China.

Single Track System Planning

The question remains unanswered as to what degree economic planning aided during this recovery period. Before answering it, it will be necessary to comment briefly on the Communist Chinese approach to the formation of a national economic structure. The Chinese Communists, like all of the Communist countries eulogising the Soviet example as their guide for the transformation of their national economies, formulated the country's basic economic policies in accordance with the Marxist-Leninist theory.

Once the initial efforts to gain economic stabilisation were in effect in mid-1950, the government was able to turn its attention to the long-term rehabilitation of the economy in preparation for the start of the first Five-Year Plan. Reform of the tax system increased the Central Government's revenue and introduced direct participation of the Central Government in an area where delegated powers had formerly operated. The government

¹ Chu-yuan Cheng, *Communist China's Economy, 1949-1962*. Seton Hall: Seton Hall University Press, 1963, p. 22.

² Leslie T. C. Kuo, *Agricultural Mechanisation in Communist China. Industrial Development in Communist China*. New York, Praeger, 1964, pp. 134-136.

³ Mary C. Wright, *Modern China in Transition, 1900-1930*. Government of Communist China. San Francisco, Chandler Publishing Company, 1966, p. 375.

⁴ Ta-chung Liu, *The Tempo of Economic Development of the Chinese Mainland 1949-65. An Economic Profile of Mainland China*. US Congress. Joint Economic Committee, Washington, US Government Printing Office, p. 55.

established centralised economic management and control of national finances. In general, the economic position of Communist China had been stabilised in 1952 through tight controls and a programme of rebuilding.

Early in 1952 an overall reorganisation of the state-controlled sector of the economy was conducted with the purpose of bringing about a more rigid control of production and distribution. The Committee of Financial and Economic Affairs issued a directive to all state enterprises to submit a detailed inventory of their assets and quarterly plans for accelerating the turnover of their working capital. The Committee was legally responsible to issue sets of control figures together with appropriate instructions to the economic ministries and to the regional economic organs. These would in turn send control figures and instructions to the units operating under their jurisdiction. These units would then draft annual plans which were to be examined and coordinated, first by the central economic ministries and regional economic organs, then by the Committee on Financial and Economic Affairs, and finally by the State Administrative Council. This process is better known as the single track system of annual planning.

Priority of Industry

By the end of 1952 the government planners felt that the government had sufficient control of the major sectors of the economy and was therefore ready to operate a national economic plan. The First Five-Year Plan was inaugurated in 1953. Its fulfilment was the primary focus of national life in Communist China.

It should be restated that China, although introducing significant innovations in methodology and timing, accepted the Soviet concept of rapid, forced industrialisation, under state control and direction. The First Five-Year Plan was the initial step and was patterned on the Soviet model in its basic approach including the principles that investment should have priority once minimum defense and consumption needs had been met; and that investment in industry should outrank investment in agriculture and that, within industry, investment in heavy industry should be several times as great as investment in light industry.

Nevertheless, demands were placed upon agriculture to provide necessary food grains for home consumption, raw materials for industry, as well as a surplus for export to help finance industrial development. Individual consumption was to remain at a low level⁵.

Through lengthy negotiations with the Soviets beginning in 1950, the USSR agreed to transfer to China, over the period of three 5-year plans, 1953–1967, the following economic aid:

⁵ Peter S. H. Tang, *Communist China Today*. Washington, Research Institute on the Sino-Soviet Bloc, 1961, pp. 298–300.

□ a package of 300 industrial plants worth a total of almost \$ 3 billion;

□ a high proportion of the whole spectrum of Soviet technology, and

□ the administrative know-how necessary for running a modern economy.

By the end of the last 5-year plan, Communist China would have 300 modern steel mills, electric power, machine tool and aircraft plants, and agricultural machinery factories. All of these plants would be phased and interrelated so that they would be both suppliers and consumers of each other. This gigantic undertaking would be so well planned that at the conclusion of the last phase, Communist China would be a truly developed economic power, the leader in Southeast Asia and an example to the world⁶.

Success under the First Plan

The question arises, just what did the Chinese Government succeed in accomplishing during the First Five-Year Plan, and how much did the Soviets aid China during this period? A look at the gross national product in Communist China in 1950 shows its value at about 55 billion yuan — valued at constant 1952 market prices. In 1957 the GNP was in excess of 102 billion yuan. Its total increase during the period 1950–1957 came to 86 p.c. which corresponded to an average yearly increment of about 9 p.c.⁷ The index of per capita GNP (1950 = 100) increased in the same time to 162, assuming a population growth of 2 p.c. per year⁸.

The agricultural sector's share of the national product declined from 47.9 p.c. in 1952 to 40.0 p.c. in 1957. This is not surprising when one considers that during the First Five-Year Plan the government allocated about 8 p.c. of total state investment funds to agriculture, forestry, water conservancy, and meteorology compared with over four times that amount for industry. The agricultural development programme was to be co-ordinated with the socialisation programme to have been completed by the end of 1967. However, current estimates extend this period up to 20 to 30 years⁹.

On the other hand, large-scale industry increased greatly in importance; in 1952 its share amounted to 11.5 p.c. of the net domestic product, in 1957 it attained 20.4 p.c., that is slightly more than half of that for agriculture. With the exception of construction, more than 50 p.c. increase, the remainder of the areas remained fairly stable. The

⁶ William W. Hollister, *Capital Formation in Communist China. Industrial Development in Communist China*, New York, Praeger, 1964.

⁷ William W. Hollister, *China's Gross National Product and Social Accounts 1950–1957*. Illinois, Free Press, 1958, pp. 1–7.

⁸ *Ibid.*, p. 3.

⁹ Marion R. Larsen, *China's Agriculture Under Communism. An Economic Profile of Mainland China*. US Congress. Joint Economic Committee, Washington, US Government Printing Office, 1967, p. 236.

decline of small-scale industry during this period might be accounted for by the government's continued programme of abolishing all private enterprises.

In the process of China's rapid development individual industries advanced more rapidly than others. This is attributable largely to the planning priorities assigned to the various types of industry. Especially, advancement and growth in electric power generation, petroleum, metallurgy, engineering, and chemicals is most noticeable. These sectors were those areas most underdeveloped in relation to the technical requirements of industrialisation and had to be improved to be able to support Soviet foreign aid. Even if one allows for the low level of the starting point, the First Five-Year Plan saw a most remarkable growth in industry, and particularly in heavy industry¹⁰.

By the end of 1957 the Soviets, as the sponsor of China's industrialisation programme, had thousands of technicians there. Moreover, thousands of Chinese technical students were in the USSR for training and education. Chinese scientists were working with Soviet scientists in nuclear research, and much material aid was flowing into China.

Decentralisation of Planning

By the middle of 1956 socialisation of the whole Chinese economy had almost been completed. Industrialisation based on the development of heavy industry, built around the core of Soviet aid, was proceeding satisfactorily. It was against this background that the Central Committee of the Chinese Communist Party set up the Second Five-Year Plan for economic development (1958–1962)¹¹.

The Second Five-Year Plan was, however, superseded in early 1958 by the Great Leap Forward, which was a complete turnabout in the Chinese economic policy. It was a scheme to drive the economy ahead at a much faster rate. It was the complete abandonment of the Soviet model of economic development.

In early 1958, a directive was published which changed the planning structure for the Chinese economic administrators. The reform of the planning system was an attempt at decentralisation of the planning process. Up to 1959 the process of drafting annual plans was known as the single track system, or, a system of centralised planning mainly for the benefit of the centrally controlled state enterprises. The new double-track system had the local authorities draw up a coordinated plan for all of the enterprises in their area. This local plan would handle the problems of

☐ balancing needs between different enterprises, different economic sectors, and different areas,

☐ defining targets and scopes of planning, and
☐ maintaining proportionate development between different sectors. Plans were controlled and supervised by various government agencies and committees and the People's Bank.

Under this system the planning unit was a geographical area and every unit aspired to become as self-sufficient as possible. This, of course, resulted in the disruption of the normal, regular flow of supplies between areas or regions¹².

The main feature of the Great Leap Forward was that its fundamental goals could not be tackled by economic policies alone. The first major principle of the programme was that China's huge population was an economic asset. Yet this could not be farther from the reality in a country that was already hard pressed against the limits of its existing agriculture to obtain food.

A second element in the economic thinking of China's leaders was that the country's population, especially in the rural areas, was underemployed a large part of the year. The government's position was that the key to a reorganisation was the mustering of these people in a huge pool of unused labour from which manpower could be used for such manual and communal efforts such as repairing dikes, construction of irrigation ditches, building roads and producing industrial or handicraft goods.

In the urban areas the same economic estimate was made. Housewives could be used in industry at small cost and the whole urban labour force could step up the tempo of work.

The third element of the economic thinking in China, which fostered the Great Leap Forward, was the great emphasis placed on ideological motivation as compared to the normal economic elements of material incentives, steady technological advancement on the basis of research and testing and the simple matter of cost effectiveness.

No "Great Leap Forward"

At the end of the first year of the Great Leap Forward the government claimed that industrial production had been 65 p.c. higher than in 1957. The great claims of the accomplishments of the Great Leap, which were issued from time to time throughout 1958 and early in 1959, were discredited when the government announced great success in April 1959, and four months later admitted exaggeration of its claims. Thus for the past decade the validity of all Peking statistics have been open to serious question.

¹⁰ Roland Hsia, *Economic Planning in Communist China*. New York, Institute of Pacific Relations, 1955, p. 89.

¹¹ Choh-ming Li, *China's Industrial Development, 1958-1963*. Industrial Development in Communist China. New York, Praeger, 1964, p. 3.

¹² Audray Donnithorne, *China's Economic System*, New York, Praeger, 1967, pp. 457-470.

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GERMAN PRISM

Relaxation of German Credit Restrictions

As had been anticipated, the Central Bank Council at Frankfurt has released the Federal Bank's credit restrictions, i.e. by lowering the minimum reserve ratio. The 100 p.c. minimum reserve on the increase of liabilities vis-à-vis foreign countries is being eliminated. Furthermore, the reserve ratios for liabilities vis-à-vis foreign countries are adjusted to the ratios for domestic liabilities. And, thirdly, the general minimum reserve ratios are reduced by 10 p.c. All these measures are becoming effective retrospectively as of November 1, 1969. With that about DM 2.5 bn should be released for the market.

After the temporary release of the exchange rate on September 30, and particularly after the fixing of a higher DM-parity on October 27, considerable amounts of speculative money that had flown in, returned to other countries. The big loss of liquidity is to be particularly compensated for by the general lowering of minimum reserve ratios. Together with the DM-revaluation the cause for the different treatment of foreign and domestic liabilities as regards minimum reserve obligations ceased to exist.

German Stock Exchange after the DM- Revaluation

Neither the new Government nor the high revaluation rate of the DM have made the German stock exchange nervous. This leads to the conclusion that neither a social-democrat government is thought to be an economic disaster nor is the revaluation considered to be a shock to the economy. While after the Bundestag elections in the first week of October a bullish mood even set in, a few days ago authoritative export quarters stated freely that they do not fear the consequences of revaluation but in spite of it anticipate further high rates of expansion.

Measured against the official stock market index the average level of quotations rose by 5.2 p.c. during the last month. With that the index at the end of October reached with 153.3 a new peak for this year and marks a medium market profit of 15.5 p.c. since the beginning of the year.

The overall index is not at all typical for all market sectors. Some securities, e.g. the Volkswagen shares, experienced even lower quotations in October and other shares were thrown back to the previous month's level after the decision to reevaluate. Above all the internationally known ex-

port-oriented shares of the chemical, electro-technical, automotive and engineering industries suffered set-backs after the revaluation rate of 9.3 p.c. became known. Mainly foreigners sold their shares. but this wave of sales was not impressive, all the more since domestic investors were hardly impressed by the revaluation. Quite the contrary, the shares of branches not effected by revaluation and showing a high import ratio—i.e. banks, insurances, department stores and suppliers of electricity, gas, etc.—were even firm after revaluation.

Not All Industrial Prices Have Been Rising

The rising index of industrial producer prices must not make us ignore the fact that prices of a number of industrial manufactures—especially important to the consumer—have in September 1969 been lower than in the preceding year's corresponding period. Apart from mineral oil products and high-grade coal derivatives (−7.0 p.c.) as well as some building materials, these were especially electromotive household equipments (−0.9 p.c.), chemical products (−0.7 p.c.) and a number of products of the food processing industry as e.g. nutritive cereals, starch products, margarine, beer and feeding stuffs.

German Foreign Trade with Develop- ing Countries

In 1968 the Federal Republic's imports from developing countries amounted to DM 81.2 bn and its exports to the nations of the Third World were DM 99.6 bn. While the Federal Republic's total imports have been rising by 15.7 p.c. from 1967 to 1968, imports from developing countries outside Europe increased by only 13.7 p.c. to DM 15.6 bn. Thus the share of developing countries in total imports declined slightly from 19.5 p.c. to 19.2 p.c. A similar development was to be noticed in exports to the developing world, whose share of 13.4 p.c. in 1967 decreased to 13 p.c. in 1968. The growth rate of exports to less developed nations with 10.5 p.c. (to DM 12.8 bn) was also smaller than that of total exports (14.4 p.c.). The long-term trend towards a declining share in German foreign trade of developing countries has continued again—after a short interruption regarding imports in the period of 1966/67.

Most important partners in the exchange of goods with the Federal Republic showing a turnover of more than DM 1 bn in 1968 have been Libya, Iran, Brazil, Saudi-Arabia, Chile, and Argentina.

Adding 12 other producer and consumer countries, each of which reached a turnover of more than DM 500 mn, these countries' share in West-Germany's total foreign trade with developing countries was 62 p.c.

Supplementary Levy for One More Year Only

The Federal Government has already submitted the draft of a "Tax Amendment Law 1970" to Federal legislature. This draft is to realise in anticipation of a planned comprehensive tax reform two immediate measures becoming effective as of January 1, 1970: (1) The doubling of the employee allowance of at present DM 240 to DM 480 annually and (2) the gradual reduction of the supplementary levy to the income and the corporation tax.

The Federal Government is of the opinion that the of necessity different forms of taxation and systems of income ascertainment, in spite of equal tariff burdens, lead to tax disadvantages for workers and employees that are not sufficiently balanced by the employee allowance of DM 240. The Federal Government therefore proposes as a measure of social symmetry a doubling of the employee allowance from January 1, 1970, on.

The reduction of a supplementary levy on the income and corporation tax furthermore provided by the draft law takes into consideration that this levy is, according to its very nature, only a temporary measure for the elimination of former budgetary difficulties.

Government Statement on Develop- ment Policy

The Government of Herr Brandt, announcing its intention to increase public development aid (1968: DM 2,380.6 mn) by an average of 11 p.c. annually, and until the mid-seventies to double the number of development assistants and experts, has again emphasised the importance of development aid. It embraces the development policy as introduced by the Government of Herr Kiesinger and intends to continue it consequently. The continuity of this engagement to the Third World is also proven by the person of the old and new Minister for Economic Cooperation, Herr Eppler.

Further objectives mentioned by the Statement are quality improvement of development aid, its better organisation, promotion of non-government initiatives and additional granting of trade preferences. These targets are unfortunately formulated only very generally and require a better reification.

Even if no new concept of development policy is to be expected, another softening of the "Hall-

stein Doctrine" should come about. The Government did not oblige itself unambiguously in this respect. But the tendency of the Government statement indicates clearly a more flexible handling of the doctrine.

Particularly interesting is the statement of Minister Eppler that the developing nations will not suffer any disadvantage by the DM-revaluation. The less developed countries' liabilities—about DM 9.6 bn—have increased by the revaluation rate of 9.3 p.c. It remains to be seen what the regulations will be like.

Industrial Turnover Increased by DM 41 bn

In the first eight months of 1969 industrial turnover with DM 296 bn (excluding added value tax) surpassed by DM 41.0 bn (16.1 p.c.) the volume of the previous year's corresponding period. Approximately one half of the growth rate with DM 20.2 bn to DM 106.8 bn (23.4 p.c.) fell to the share of the capital goods industries. The turnover of the basic materials industries rose by DM 12.1 bn to DM 90.6 bn (15.4 p.c.), while turnover of the consumer goods industries increased by only DM 6.0 bn to DM 51.7 bn (13.1 p.c.), that of foodstuffs and luxuries industries by DM 2.3 bn to DM 40.6 bn (6.1 p.c.) and that of mining by DM 0.35 bn to DM 6.5 bn (5.6 p.c.).

Algae to Fight Hunger in the World

About 44 p.c. of the world's population is underfed, due mainly to the lack of protein. If efforts to supply these people with more and better protein-containing food succeed, it would be possible to improve their health considerably. While the carbohydrate gap prevailing in developing countries may probably be closed by the mid-seventies through the growing of improved cereals, more intensive cultivation and several crops, the protein gap requires much greater efforts. Research is therefore endeavouring to develop "unconventional" protein media, i.e. algae and yeasts.

The Federal Republic's most important contribution to the solution of this worldwide problem is the green alga *Scenedesmus obliquus* and its introduction into countries of the Third World. German development aid can now utilise this alga cultivated by the Carbon-biological Research Institute at Dortmund as well as the simple technological procedure to render it useful. This alga contains all important amino-acids and propagates particularly well. Besides it exploits almost without waste water, scarce as it is in most developing countries, as well as expensive fertilisers and, moreover, it is palatable.

In spite of Soviet hints that Chinese continuance of the Great Leap Forward could jeopardise the USSR aid program, the Peking government proceeded with the programme. The dispute lasted until July 1960 when the Soviets withdrew their technicians. The spirit of the Leap Forward was not sufficient to overcome the technological deficiency in the Chinese labour and management forces.

Two poor harvests in 1959 and 1960 closed the gap between total production and the subsistence requirements of the nation. Grave discontent among the population was evident throughout the country. The critical spirit needed to carry on the Great Leap was gone, it was time for a new economic policy. The events leading to the collapse of the Leap in 1961 made the Chinese government more conscious than ever that their ambitious aims in industrial development depended on the satisfactory solutions to the basic problems of economic development which led to the recovery and readjustment period.

Recovery Period

This period comprises the years 1961–1965. It was marked by a retreat from the economic policies of the Leap Forward and by significant changes in both economic priorities and in the style of economic management. Emphasis was to be placed on insuring the supply of food by concentrating rural labour on the growing of food crops, by commissioning industry to supply more fertilizer, and by importing grain from Canada and Australia. The government also abandoned the commune system, introduced in 1958.

Industrial recovery was geared to restoration of production in the areas of the greatest national importance and to improvement in the quality of industrial output. Industry was also to support agriculture through expansion of the production of chemical fertilizers and agricultural equipment. Petroleum refining was to reach the point of self-sufficiency at a rapid rate. Towards the end of this period a national birth control plan was put into effect in an effort to check the danger posed by the rapidly growing population¹³.

New Recession by Cultural Revolution?

As the Peking government regained control of the economy it announced the formulation of a Third Five-Year Plan to be effective over the years 1966–1970. Yet since this announcement was made nothing has been published which would indicate that it is anything like a detailed economic plan, such as the Soviet five-year plans have been. The information that has been released indicates, rather, that it is a preliminary sketch of major economic policy and contains output goals

for key commodities. There does not seem to be a detailed long-term plan for even major industrial establishments¹⁴. Economic planning in China is far from clear. Often economic planning appears to be a synonym for government control over the economy, commanding obedience from all enterprises, other units and individuals. The desire to minimise political difficulties, and not to run foul of current political trends, is likely on many occasions to exert more influence than either formal targets or material incentives.

This could have much meaning, particularly now, during the Proletarian Cultural Revolution underway in China. The big question remaining unanswered at this time is, will the aims of the Proletarian Cultural Revolution, which are mainly political, supersede the Third Five-Year Plan in the same manner that the Great Leap Forward did the Second Five-Year Plan?

Despite the political ferment and turmoil which is being caused by the revolution, the country seems to have functioned normally with little disruption to the national economy. According to the 1966 year-end official reports, the gross output value of industry rose 20 p.c. In the field of steel production there was a 20 p.c. increase in the first nine months of 1966 as compared with a like period in 1965. The government claimed self-sufficiency in crude oil and petroleum products. The output of chemical fertilizer showed a constant advance after 1963. Agricultural production has remained more or less in stagnation despite the fact that the 1965 grain output was 5 p.c. higher than the 1957 figure, although this represented actually a 5 p.c. decline in per capita availability of farm products¹⁵.

In December 1966 and January 1967 there were many work stoppages in various major industrial centers throughout China. There were also major transportation stoppages.

Although modernisation of the economic system in Communist China may not have progressed evenly in all sectors, one can be certain that the country's economic development will continue to move ahead. Two factors will be the driving forces for this continued progress. The first is the growth of the population. This will make it mandatory that the economy remain dynamic in order to remain stable. The political future of the country is actually at stake here. The people must be cared for if the government is to survive. The second factor that will assist in driving the economy ahead is the spread of modern science and technology. These two factors together will lead to further development of China's productive forces.

¹⁴ Arthur C. Ashbrook, *Main Lines of Chinese Communist Economic Policy. An Economic Profile of Mainland China*. US Congress. Joint Economic Committee. Washington, US Government Printing Office, 1967, p. 36.

¹⁵ Chu-yuan Cheng, *The Cultural Revolution and China's Economy*. *Current History*, v. 53, No. 313, September 1967, pp. 148-152.

¹³ Alexander Eckstein, *On the Economic Crisis in Communist China*. *Foreign Affairs*, v. 42, July 1964, pp. 655-668.