

CHINA: DECENTRALIZATION AND REGIONAL COOPERATION

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ABSTRACT

Measured both in terms of population and territory, China is one of the largest countries in the world, and is now emerging as an important economic power (See Appendix 1 for economic data on China). There are, however, diverse opinions about the reasons for China's rapid economic growth. Some argue that this growth is the result of central government control. In fact, the opposite is closer to the truth. The rapid growth of recent years has resulted in sectors that are not controlled by the central government, and power continues to move from the central government to lower level governments and the private sector.

The purpose of this thesis is to describe how China has been transformed from a nation controlled over two thousand years by the center into a decentralized society through a peaceful evolution. The focus is on the economic and institutional reasons for this transition which began in the 1970s.

The terms "centralization" and "decentralization" used by political scientists are used here to refer to changes in the locus of economic power in China. Decentralization has resulted in large measure from the industrialization process. It is an important element in the development of the "post central planning economic nation" such as exists in China today. There is a strong correlation between decentralization, the market economy, privatization and the open economy. In China, regional economic development has motivated decentralization which has in turn contributed to regional economic development and national economic "boom". Indeed, decentralization has contributed significantly to the quality of life of Chinese citizens and supports new institutions in China.

As a student in the Sloan Business School, the author hopes this thesis can provide a macro-historic and economic view of China's progress and as such, will be useful to the international investment community.

Thesis Supervisor: Lester C. Thurow
Title: Professor at Sloan School, MIT

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**List 1: Abbreviations for China's Provinces, Municipalities,
and Autonomous Regions:**

AH	Anhui
BJ	Beijing
FJ	Fujian
GD	Guangdong
GS	Gansu
GX	Guangxi
GZ	Guizhou
HA	Hainan
HB	Hubei
HE	Henan
HI	Hebei
HL	Heilongjiang
JL	Jilin
JS	Jiangsu
JX	Jiangxi
LN	Liaoning
NM	Inner Mongolia
NX	Ningxia
QH	Qinghai
SA	Shaanxi
SC	Sichuan
SD	Shandong
SH	Shanghai
SX	Shanxi
TJ	Tianjin
XJ	Tibet
XZ	Yunnan
ZJ	Zhejiang

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Chapter I The Evolution of the Chinese Centralized Tradition

A. Agriculture Society and the Centralized System

In 221 B.C., the king of Qin state, Ying Zheng, who had just conquered all of China and established Qin Dynasty (see Appendix 2). In the same year, he made two decisions: one was to declare himself Emperor and establish imperial despotism; the other was to divide China into 36 prefectures and form an administrative system of prefectures throughout the country thereby centralizing political control (See Appendix 3). These two historic decisions profoundly influenced China's economic, political and social structures for the next two thousand years.

Imperial despotism consisted of a power-restricting, centrally controlled system. The emperor's power was nearly absolute, only somewhat balanced by officials called prime ministers. However, since the Qin Dynasty, the emperors gained power. During the Ming Dynasty, emperors were also prime ministers: the head of state and head of government were consolidated, which led imperial despotism to develop into an extreme form. Imperial despotism ended with the fall of the Qing Dynasty.

During this period of imperial central control, government was divided into administrating regions of various levels. Regional governments were established in these areas, and regional government officers were appointed, directly or indirectly. The central government gave or granted regional governments certain administrative, military, financial and judicial powers. This power structure allocation between the central government and the regional government was the main trend in China's political system for two thousand years, and was continuously strengthened. By the time of the Song Dynasty, the administrating regions formerly governed by regional governments had become administrating regions ruled by the central government. The centralized power system had reached its summit. This form of government prevented different regions of the country from separating and forming independent governments, and allowed the central government to maintain control over these local regimes for three dynasties beginning with the Yuan dynasty through the Ming and Qing Dynasties.

Between the Qin and Qing Dynasties the form of administration underwent all kinds of changes, but the principles and element by which these regions were divided remained basically the same. The so called elements of an administrative region include the size of the region, its boundary and geographic area and location. Since the Qin Dynasty the form of administration has undergone all kinds of changes, but the principles and elements by which these regions were divided remained Dynasties, the basic unit on the lowest level in the centralized system was the county. In the earliest days, counties were divided into 2500 sq. kms. varying somewhat depending on the size of the population. Densely populated counties had smaller units and sparsely populated counties had larger units. Above the county level, the division of administration regions changed throughout the dynasties. In terms of size, administration units remained relatively stable after the Ming

Dynasty. Provinces were the administrative unit just below the central government. There were fifteen provinces in the Ming Dynasty. This provincial system was adopted by the Qing Dynasty, though the number of provinces was increased to eighteen. The division of provinces in the Ming and Qing Dynasties have changed little as of the present time (See Appendix 4). Administration regions were divided according to geographical regions. So, for example, administration regions of lower levels were sub-geographical regions of administration regions of higher levels. During the Qing Dynasty, provinces were sub-geographical regions of the state, prefectures were sub-geographical regions of provinces, and counties were sub-geographical regions of prefectures. Since administration regions consisted of political space divided on geographic lines there was a relation between man-made administration regions and natural geographical environments which was both harmonious and conflicting. In other words, China's administration regions were unable to escape the restriction of natural geography on the one hand, and they were bound to be influenced by political elements on the other. It is not difficult to observe this jigsaw-like feature of the boundary of China's administration regions on a map. It is proof that the division was influenced by political factors.

It is obvious that the establishment of a centralized system based on a hierarchy of administration regions was closely connected with the fact that China was an agricultural society. Managing vast lands and ruling scattered populations required a stratified, well-defined division of regions. At the same time, the natural economy based on households required stability. The most important governmental function of these administration regions was to unify scattered households under the central government to provide a stable political and social environment. As agriculture expanded and population increased the number of administration regions increased. When agricultural production decreased and population declined, administration regions were revoked. For example, in the Qin and Han Dynasties the economic and cultural centers were in the North of China. But from the end of the Han Dynasty to the end of the Song Dynasty, China's economic and cultural centers transferred to the South. From that time on economic and cultural control has remained in the South. This historic transformation was reflected in the geographic division of administration regions. Starting in the Sui Dynasty, the number of administration regions in the North and in the South began to change: more administration regions were divided in the South than in the North. During the Song, Ming and Qing Dynasties, Jiangsu, Zhejiang, Jiangxi and Fujian administration regions in the Southeast became the densely divided administration regions. This is very similar to today's China.

In summary, from the earliest days, agriculture was the economic foundation of China. By the Qin and Han Dynasties, China had become a typical agricultural society, which lasted more than two thousand years until the late nineteenth - early twentieth century. That was the historic macro economic background upon which China's centralized political system was established and developed. China's centralized system and its supporting administrative regional system changed as the structure of China's traditional agricultural society changed. There was a direct, historic and logical relation between China's centralization political system and administrative regions and traditional agricultural social structure. Without understanding this relationship, it is impossible to understand the basis

of China's centralized political system or to understand the reasons why China's contemporary centralization system will end.

B. The Crisis of the Centralized System in the Transition Towards An Industrialized Society

The history of China's economy indicates that China's transition toward an industrialized society started in the Song Dynasty. Traditional commercial and handicraft industries developed rapidly and led to the emergence of new economic centers, though this development did not change the dominant status of the self-sufficient agricultural economy, nor the structure of the administration. These economic centers were located in the cities of former administration counties and in newly emerged cities or towns. For example, the famous town of Jingdezhen in Jiangxi province was set up in the Song Dynasty. Some towns created more revenue through commerce and handicrafts and paid higher taxes than counties. Some towns had a greater population than counties. Though cities and towns did not become an administration region and remained surrounded by vast rural areas, the crisis of the centralized system started with these new economic centers.

This modern so-called Industrialization Movement started in the late Qing Dynasty. It was a direct result of the defeat of the Qing government during the Opium War, which forced an open-door policy and the introduction of Western technology and capital. Modern machine industries were quickly developed in China, first in the eastern coast and river regions. This was followed by the emergence of densely populated, prosperous commercial and industrial centers. Shanghai developed as a modern economic center at this time. Clearly, such vast economic changes could not be accommodated by the old geographic administrative regions. In the late Qing Dynasty, the government began to establish new administration regions at the city level. However, history did not give it the chance to do so.¹ This administrative change was accomplished in the early days of the Republic of China during the 1910s.

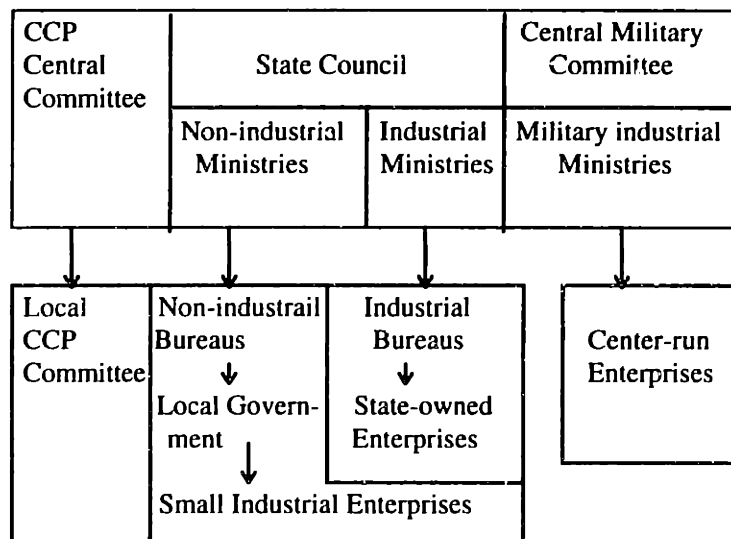
The historic process is very clear: industrial and commercial cities emerged with the development of modern industrial machinery and factories. The growth of cities led to the establishment of new, city-based administration regions. Thus China's administration system was transformed into a combined system of geographic administrative regions and city administrative regions. This mixed system was not easily accommodated into the traditional geographic administration region system sustained by the centralized system. The centralized political system was beginning to lose its stability.

In 1949, the Chinese Communist Party gained political power and established a socialist system of government based on state ownership. From 1950 through the 1970s, China's economy was based on a planned economy, pursuing industrialization and sustaining China's centralized political tradition under modern autocratic rule. The next section discusses the features of an integrated planned economy, state ownership, industrialization and a centralized political system in China.

¹ See Zhou Zhenhe, *China's Politics and Economy*, China Press, 1990, p.229.

From the Qin Dynasty to the Republic of China, China never broke away from centralized political control mainly represented by regional governments, but economic control was separate. However, after 1950 China's centralized political system acquired a strong economic significance. The central government not only sustained the regional administration political system, but also directly controlled economic activities from the central government down to the provincial and county levels through a highly centralized planned economic system. Specifically, economic activities of provincial and county governments such as investments and price and income levels of residents were all controlled by the central planned economic system. Meanwhile, nationwide enterprises of all kinds, but mainly industrial enterprises, were managed directly by the central government (See Figure I-1).

Figure I-1: Center-Locality Relationship



China's centralized system created by the first emperor of the Qin Dynasty reached its full development after the introduction of the planned economy. Now the centralized political system totally controlled all China's economic activities, from the central to the local level. Soon, however, industrial development grew to the point that the central political system could no longer control it. At first this was represented as a conflict between industrial development and the rigid planned economy. Then the conflict deepened to a struggle between industrial progress and central control. This struggle can be traced by reviewing the transformation of the planned economic system since the 1950s.

The "First Five Year Plan" (1953-1957) divided China into two economic regions: the coast region and the inland region based on their industrialization level. By the late 1950s and early 1960s, the country was divided into seven economic regions: Northeast, North China, East China, Central China, South China, Northwest and Southwest. By the middle of the 1960s, the country was carved into three frontiers: the first, second and third based on the need of preparing for war, especially nuclear war based on the strategy and

geographic location of the frontier. At the same time, the central government combined the Central China and South China regions into one Central-south region, thus reducing the number of cooperative economic regions to six. With the exception of dividing China into three frontiers, all the adjustments made by the central government were based on the realization that though the geographic administration regions were the foundation of the centrally planned economic system and the centralized political system, they were no longer easily adapted to the economic development in these regions.

The central government as forced to give provincial governments more economic power on several occasions. Officially, this was termed an adjustment of the relationship between "verticals and horizontals". The so-called "verticals" were the central government controlled economic sectors down from every department of the state council to their subcommittees at local levels. The so-called "horizontals" were local governments, mainly provincial regions. Put another way, these were decentralizing actions. Two major ones occurred between 1950 and 1970.

The first decentralization occurred in 1957-1958. In these two years, the central government transferred most of the light and textile industrial enterprises, some of the heavy industrial enterprises and some of the transportation and harbor enterprises to the management of local government. Concurrently, they increased the power of local government. By 1959, the kinds of industrial products controlled by the State Planning Committee decreased from more than 300 to 250. The proportion of taxes collected directly by the central government decreased from 40% to 20%. In addition, more than 8% of enterprises controlled by the central government were transferred to local governments.²

The second decentralization took place between 1964 and 1976. In this period, the products of five mini enterprises (mini steel, mini cement, mini fertilizer, mini coal and mini machinery) were transferred to local governments to allocate and use. From 1970 to 1976, more than 2600 key enterprises formerly controlled by the central government were transferred to local governments nationwide. Mini industrial products formerly controlled by the State Planning Committee decreased from 340 in 1965 to about 60 in the 1970s. Materials controlled by the state decreased from 326 to 49 in 1972.³

While state ownership and a planned economy tend to strengthen centralization, industrialization produces a reverse tendency of decentralization and reduced restrictions enforced by geographic administration regions. By the end of the 1970s, local governments had gained considerable administrative and economic power. Once the overall economic reform started, this shift in power not only led to the collapse of the planned economy, but also to a crises in the centralization system that eventually resulted in the formation of a decentralization system.

² Zhao Suisheng, "Changes in the Relations Between the Central Government and Local governments", in *Intellectuals*, Summer, 1994, pp.35-36.

³ *Idid*. pp.35-36.

The economic reform in contemporary China started in the late 1970s. In the ensuing 15 years remarkable achievements have been attained:

- 1) the market economy has replaced the planned economy;
- 2) the opened national economic system has replaced a closed national economic system;
- 3) the separation of local financial systems from the central financial system has replaced a centrally monopolized financial system; and
- 4) the separation of local international trade and foreign exchange systems from a centrally controlled international trade and foreign exchange system has replaced the central control.

All these changes suggest that China's centralization tradition has ended. The central government essentially no longer has its traditional compelling power over local governments. The relation between the central government and local governments has gradually become a bargaining relation between politics and economics, though the central government still needs to sustain its apparent authority.

The formation of decentralization can be measured economically by the following index:

- 1) compared with the central government, local governments' revenue and expenditure increased proportionally from a non-dominant to a dominant position (See Table I-1);

Table I-1: The Center-Locality Ratio in State Budgets

Period	Revenue		Expenditure	
	Center	Local	Center	Local
"First Five -Year": 1953-57	45.41	54.59	74.11	25.89
"Second Five-Year": 1958-62	22.70	77.30	48.13	51.87
"Third Five-Year": 1966-70	31.24	68.76	61.07	38.93
"Fourth Five-Year": 1971-75	14.71	85.29	54.22	45.78
"Fifth Five-Year": 1976-80	15.61	84.39	48.96	51.04
"Sixth Five-Year": 1981-85	30.56	68.44	48.84	51.16
"Seventh Five-Year": 1986-90	39.51	60.49	39.55	60.45
"Eighth Five-Year": 1991-	38.76	61.24	39.80	60.20

Source: *Statistical Yearbook of China*, 1992, China Statistics Press, 1993. pp.227.

- 2) the central government's investment specified in the state budget decreased from a dominant to a non-dominant proportion of the country's fixed capital investment. In 1985, the ratio of the state

budget investment was only 16% of the country's total investment. By 1991, it declined to 7%;⁴

- 3) local governments exceeded the central government in absorbing and using foreign capital. This has been very clear since 1990, when the total foreign capital used by provincial and city governments was 7% higher than the central government. And 1991, this figure rose to 17%;⁵
- 4) the contribution made by central government controlled state-owned enterprises is declining as a percent of total industrial output, while the contribution made by local government controlled non-state-owned businesses (private, cooperative, collective, joint venture, foreign investment, etc.) is increasing. By 1991, the total output made by non-state-owned enterprises was over half the total industrial output (See Table I-2).

Table I-2: Ownership Share as Percent of GNP, 1979-1991

	1979	1980	1985	1991	1992
State-ownership	78	77	62	58	45
Non-state-ownership	22	23	38	42	55

Source: State Statistical Bureau, World Bank Report, 1993

C. The Direct Economic Reasons leading to Decentralization

There are four related but different economic theories that explain how rapid industrialization led to decentralization:

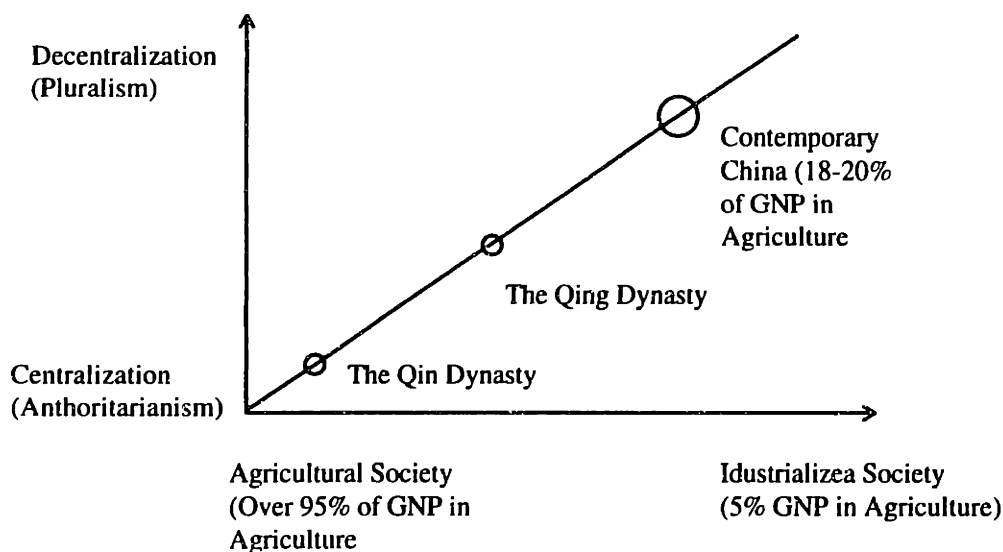
1. The Stages of Economic Development.

The existence of China's centralization system depended on the existence of China's traditional agricultural society. In the transition from an agricultural society to an industrial society, the centralized system began to decline and decentralize. This trend is illustrated in the following model:

⁴ *Statistical Yearbook of China*, 1992. China Statistics Press 1993. p.145.

⁵ *Idid.* p.643.

Figure I-2: The Correlation Between the Decentralization and Industrialization



Today agricultural output is about 20% of GNP, and the non-agricultural output is over 80% of the total. This provides an unshakable foundation for the formation of decentralization.

2. Big Leaps of Economic Scale.

The reason the Chinese Communist Party was about to successfully carry out the planned economy and strengthen the centralized tradition in 1949 was because, after the Chinese-Japanese war between 1937-1945 and the four year civil war, China's economic output greatly declined to below the 1937 level. A small, stagnant economy favors the establishment and strengthening of a centralized system. However, when the economy expands, decentralization is strengthened. In 1952, national income reached 59 billion yuan. From 1958 to 1962, for three consecutive years, the figure reached 100 billion yuan each year. During this period, decentralization developed quickly. In 1971, the national income exceeded 200 billion yuan. Decentralization again increased. By 1982, the national income was more than 400 billion yuan, and decentralization was firmly established. The national income was more than 800 billion yuan in 1987, and the decentralization trend could not be reversed. By 1991, when the national income reached 1600 billion yuan, decentralization had been institutionalized.⁶

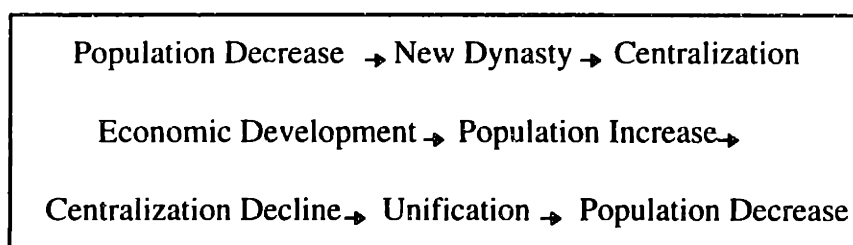
3. Population Expansion.

During the first two thousand years of Chinese history, from the pre-Qin Dynasty to the end of the Qing Dynasty, the population had undergone eight periodic fluctuations. An

⁶ All calculated according to those years' prices. *Statistical Yearbook of China*, 1992. China Statistics Press, 1993. p.703.

astonishing coincidence can be seen between these population fluctuations and the fluctuations of power of the central government. Usually at the beginning of a new dynasty when centralization was strengthened, population had declined. The end of every period of fluctuation when population increased to new levels, usually corresponded with the end of a dynasty - a time when the centralized system could hardly be sustained. This was followed by societal collapse from unification which, in turn, led to a decrease in population. A new age of unification would come, population would increase and the cycle would repeat itself. In other words, population fluctuations accelerated the rise and decline of China's dynasties, and affected the strength or weakness of the centralized system. This cycle is illustrated as follows:

Figure I-3: The Impact of Population on China's Centralization



This trend is further elaborated in Table I-3.

Table I-3: Population Sizes of Different Period in China's History

Period	Year	Population	Cycle/duration	% Change between
The Warring State (peak)	350 B.C.	3,000	First/239 years	100
Late Qin and early Han	205 B.C.	1,500		
Mid West Han	1	6,000	Second/190	
Early East Han	25	2,500		
Late East Han	150	6,000		
The Three-Kingdom	216	1,500	Third/366 years	-27.7
West Jin	290	2,500		
The South-North (peak)	510	4,700	Fourth/39 years	6.4
Early Sui	581	3,500		
Mid Sui	608	5,000	Fifth/360 years	43.8
Early Tang	620	2,500		
Mid Tang	752	8,000		
The Anshi Rebellion	760	5,000	Sixth/310 years	21.7
Late Tang	850	6,000		
Early Song	980	4,000	Seventh/270	192.9
Mid North Song	1110	10,000		
Song-Jin (peak)	1210	11,000		
Yuan	N/A	N/A	N/A	
Early Ming	1370	6,000		
Mid Ming	1570	14,000		
Late Ming and early Qing	1640	7,500		

The opium war	1840	41,000	Eighth/271	
Late Qing	1911	37,000		

Sources: Hu Huanyong and Zhang Shanyu, *Demographical Geography of China*, Shanghai: Huadong Normal University Press, 1984

After 1949, China's population expanded unprecedently. In 1952, it was 575 millions; in 1978, it was 963 million, and by 1992, 12 billion. The population in 1978 was 1.7 times of that in 1952. By 1992 it was 1.2 times greater than in 1978 and 2 times greater than in 1952.⁷ The formation of centralization in the early 1950s was consistent with the small population of that time. When the population increased by one or more times, the centralized system began to break down. The only remedy is to replace "unification" with "separation". Today separation means decentralization. China now has 12 billion people and 30 provinces. There are on average 40 million people in each province. Only a few countries have a population of 40 million. Centralization does not function in societies with large populations, as the history of China illustrates. Of course, countries with small populations need not adopt a centralized system.

4. The Relative Advantages of Regional Economies in the Industrialization Process.

China is vast, consisting of diverse geographic regions with different economic advantages. These regional economic advantages had little chance to develop during the period of the traditional agricultural society. However, once industrialization began relative regional advantages emerged. In China, this happened in the late 1920s through the late 1930s when the Chinese-Japanese war started. Regional economic advantages were restricted in the 1950s because of the implementation of the centrally planned economy. However, as industrialization progressed, especially since the reform and open-door policy were carried out the 1970s, market mechanism brought about regional advantages, which naturally promoted the tendency of economic Regionalization. The result was the rapid spread of decentralization, because decentralization is consistent with the requirement of regional economic advantages. Once regional economic advantages began to be established, the centralized plan, which required every province to establish its own relatively independent economic system, was questioned.

In summary, China's centralization system was based on a slow growing agricultural economy with a stable and modest population. Regional economic advantages could not be exploited. But now all these conditions have greatly changed. These changes will unavoidably destroy the centralized system. The economic development models that are emerging under a decentralized system are discussed in the next chapter.

D. The Role of Infrastructure in the Process of Decentralization

China is a vast and complex country geographically, with a land surface of 9.6 million sq. kms and a sea line of 4.7 million sq. kms. Over five and one-half million sq. kms of the land, or 59%, are plateaus and mountains, 12% are plains and the rest consists of basins

⁷ *Almanac of China's Economic*, 1993, Economic management Press, 1993. p.694.

and hilly terrain. There are 2.5 million sq. kms of plateaus over 3000 meters which is 26% of the total land surface.⁸ Facing the Pacific Ocean in the east and south, the land mass extends westward all the way to Altai, the Pamirs and the Himalayas.

Since China was unified under a central system by Emperor Qinshi more than 2,000 years ago, the country has shrunk and expanded many times, yet its basic contour has remained the same. It is extremely rare to maintain control over such a vast, geographically diverse territory for this period of time.

An important issue to note is that during its long history up to the beginning of this century, China never had a social infrastructure in the modern sense. The first railway was built in Shanghai in 1876: it was only 15 kms long. Telephones and telegrams were introduced at the beginning of the century. This suggests that administrative control did not require a well-developed infrastructure. Rather, the centralized system was sustained in the absence of such infrastructure. That is because modern infrastructure provides society with two possibilities: to develop cooperative horizontal relations and to develop an open system. Both work to undermine centralization. Only a backward society closed to the outside world, without modern infrastructure, few horizontal connections and with a widely scattered population can be effectively governed by a centralized political system.

Modern infrastructure has developed unevenly in China. The development of the transportation system is a good illustration of this (See Table I-4).

Table I-4: Transport Methods by Area, 1979

	Railway		Highway		River	
	Mileage	Percent	Mileage	Percent	Mileage	Percent
National	51,511	100	875,794	100	107,801	100
Southwest	5,930	11.5	171,345	19.6	10,014	9.3
Northwest	6,915	13.4	108,115	12.3	829	0.8
Middleeast	8,577	16.6	227,370	20.5	34,747	32.2
East China	7,237	14.1	160,530	20.6	52,609	48.8
North China	10,855	21.1	112,967	11.4	1,174	1.1
Northeast	11,997	23.3	95,467	21.6	6,021	5.6

Source: Ma Hong, Sun Shangqing, *China's Economic Structure Study* People's Press, 1981 pp. 385.

As can be seen, at the beginning of the economic reform in 1979, transportation the western region lagged behind the middle and eastern regions. While this gap has been narrowed in the past 15 years the pattern is the same. The railway and super highway systems build in the 1980s are concentrated in the east area (See Appendix 5 and 6).

⁸ *Statistics Yearbook of China*, 1992, the China Statistics Press, 1993, pp.4-5.

Harbors and airports are also predominantly concentrated in the east (See Appendix 7). Again development is uneven. As Table I-5 illustrates, the economically advanced areas have a greater communication network as can be seen by the number of telephones

Table I-5: China's Telephones by Province, 1992

Province	Total	Telephone Unit Per 1,000 People	Province	Total	Telephone Unit Per 1,000 People
Guangdong	1,554,259	24.14	Shaanxi	323,709	9.63
Jiangsu	899,433	13.14	Tianjin	317,824	34.94
Beijing	841,621	76.93	Fujian	312,600	10.15
Shanghai	790,267	58.98	Anhui	299,319	5.20
Liaoning	758,207	19.00	Inner	296,601	13.58
Shandong	734,705	8.57	Jiangxi	224,414	5.81
Zhejiang	692,327	16.48	Guangxi	203,640	4.71
Sichuan	567,188	5.20	Gansu	186,984	8.18
Hebei	543,192	8.73	Xingjiang	178,237	11.46
Heilongjian	515,866	14.43	Yunnan	177,758	4.70
Hubei	464,353	8.42	Guizhou	134,823	4.07
Henan	439,421	5.01	Qinghai	61,339	13.51
Jilin	421,494	16.80	Hainan	60,260	8.94
Hunan	338,844	5.46	Ningxia	53,059	11.05
Shanxi	328,930	11.18	Tibet	14,722	6.51

Source: *China Facts and Figures*, Academic International Press 1994 Vol. 18, pp. 187
Statistical Yearbook of China, 1992. China Statistic Press 1993, pp 79

China is now in the process of completely modernizing its infrastructure, both nationally and internationally. Horizontal connections among the regions will be strengthened. As a result, vertical dependence between local governments and the center will be weakened leading to further decentralization.

In fact, there is a strong correlation between modern infrastructure and decentralization. This can be illustrated by the shares of revenue generated by the post and telecommunications industries in different provinces. As can be seen in Table I-6, Guangdong has the most advanced postal and telecommunications network in the country. It amounts to 18% of the provincial revenue, a figure three times the provincial revenue of Shanghai and five to ten times that of provinces in the western regions. The eight provinces and municipalities in the table all generate more than 4% of their revenue from the communications industry. Guangdong has always played a leading role in China's decentralization process. Jiangsu, Zhejiang, Liaoning, Shandong, Sichuan, Beijing and Shanghai have also actively supported decentralization.

Table I-6: China's Post and Telecommunications Revenue by Province, 1990

Province/City	Million RMB	Percent Total	Province/City	Million RMB	Percent Total
Guangdong	1,484.6	18.2	Anhui	182.9	2.2
Beijing	583.3	7.1	Shaanxi	169.4	2.1
Jiangsu	505.2	6.2	Tianjin	160.8	2.0
Shanghai	475.6	5.8	Jiangxi	149.1	1.8
Zhejiang	454.0	5.6	Guangxi	142.4	1.7
Liaoning	435.4	5.3	Shanxi	136.0	1.7
Shandong	394.0	4.8	Yunnan	127.5	1.6
Sichuan	353.6	4.3	Inner Mongolia	117.3	1.4
Fujian	307.0	3.8	Xinjiang	102.6	1.3
Hebei	278.8	3.4	Gansu	101.9	1.2
Henan	278.7	3.4	Guizhou	78.6	1.0
Hubei	269.3	3.3	Hainan	50.7	0.6
Hunan	257.1	3.1	Qinghai	34.6	0.4
Heilongjiang	255.6	3.1	Ningxia	24.8	0.3
Jilin	213.8	2.6	Tibet	10.1	0.1

Sources: *China Facts and Figures Annual 1994*, pp.190.

In summary, it can be concluded that a modern infrastructure system does not strengthen the central government; instead, it paves the way for the demise of such a system by replacing the hierarchical "pyramid-like" political structure with a horizontal "network-like" system. •

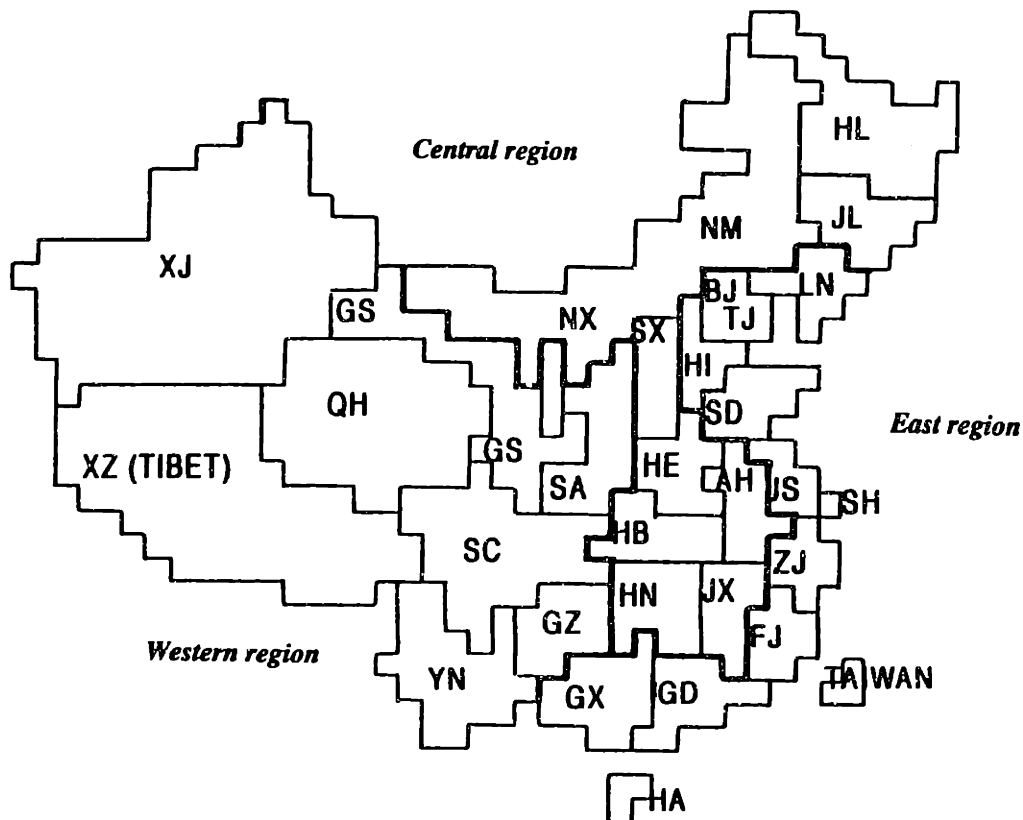
Chapter II The Patterns of Regional Economic Cooperation

A. Formation One: The East, Central and Western Regions

The division of China into three economic regions - East, Central and West was widely accepted by the middle of the 1980s. The division was based on the regions' productive forces and their level of economic development. If we consider the three regions' economic and technological development levels as three ladders, they coincidentally fit China's natural geographic regions.

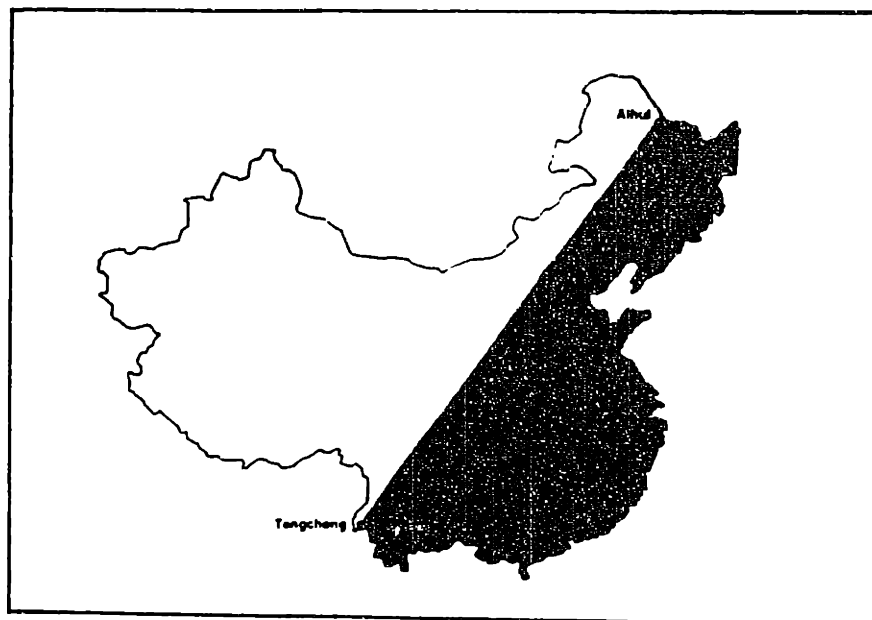
The Eastern region includes Liaoning, Hebei, Tianjin, Beijing, Shandong, Jiangsu, Shanghai, Zhejiang, Fujian, Guangdong, Hainan and Guangxi - all together 12 provinces, numerous cities and autonomous areas excluding Taiwan, Hong Kong and Macao. The Central region includes Heilongjiang, Jilin, Shanxi, Inner Mongolia, Anhui, Jiangxi, Hubei, Hunan Henan - nine provinces and autonomous areas. And the Western region encompasses nine provinces - Sichuan, Guizhou, Yunnan, Tibet, Shaanxi, Gansu, Qinghai, Ningxia, Xinjiang nine provinces, autonomous areas (See Map II-1).

Map II-1. The East, Central and Western Regions in China



The population distribution is much concentrated in the eastern region. (See Map II-2).⁹

Map II-2: Distribution of China's Population, 1992



The major economic indicators can be seen in Table II-2. (Appendix 8 provides more detail information about the three regions).

Table II-1 The Major Indicators of East, Central and West Region, 1992

	Population (Million)	% of Nation	Urban Pop (Million)	% of Nation	Illiterate Pop	% of Nation
East	468.07	42.5	100.34	45.7	161.16	55.3
Central	404.14	35.7	79.69	36.2	70.14	24.1
West	258.30	22.8	39.90	18.1	60.19	20.7
Total	1130.51	100.0	219.93	100.0	291.50	100.0

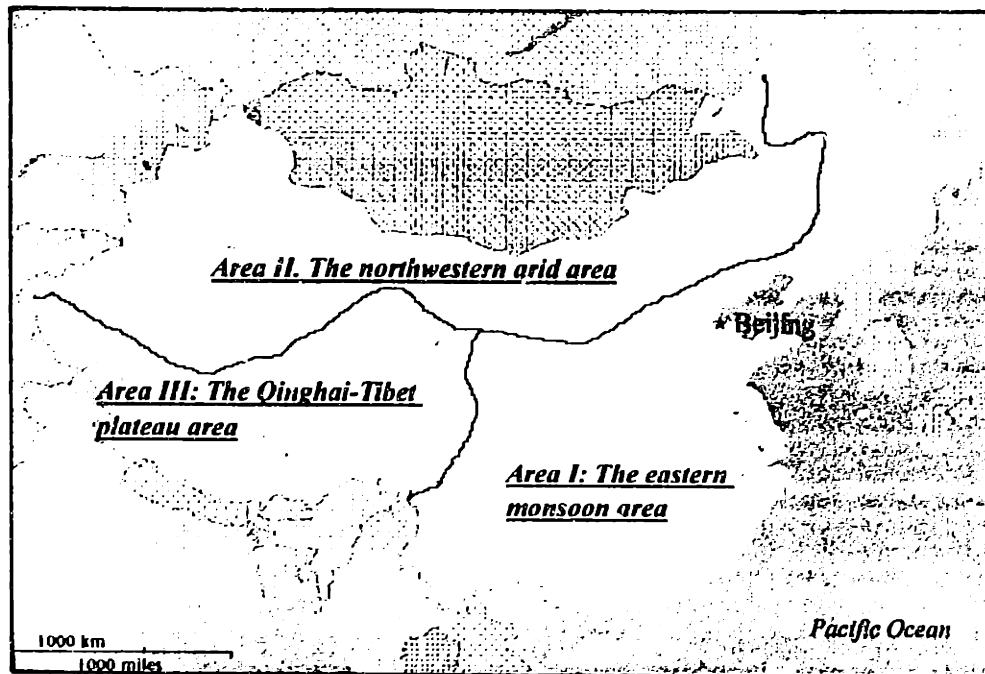
	National Income (Billion)	% of Nation	GNP (Billion RMB)	% of Nation	Import & Export (Billion)	% of Nation
East	766.89	53.4	2202.12	58.3	79.88	79.6
Central	433.00	30.1	1043.86	27.6	13.96	13.9
West	236.50	16.5	535.88	14.1	6.56	6.5
Total	1436.39	100.0	3781.86	100.0	100.40	100.0

Source: *Statistical Yearbook of China, 1992*, China Statistical Press

⁹ This line is named Hu's line after Chinese demographer Hu Huanyong. Hu's line illustrates the extreme population concentration of China, according to *China Population Today*. About 94 percent of China's population live east of the line, in an area comprising 45 percent of the country's territory, while only 6 percent of the population live west of the line, on more than half of China's territory.

Further China can be divided into three natural geographic regions, i.e., the Eastern monsoon region, the Northwest arid region and the Qinghai-Tibet plateau region. These three regions are divided into seven natural regions and 33 sub-regions (See Map II-2). Comparing the three economic regions (east, central and western) with the three naturally formed geographic regions, similarities are found in that both follow an east-west direction. The eastern geographic region is larger than the eastern economic region, but by and large, the division of the three economic regions is consistent with China's economic geography.

Map II-3: The Natural Areas of China



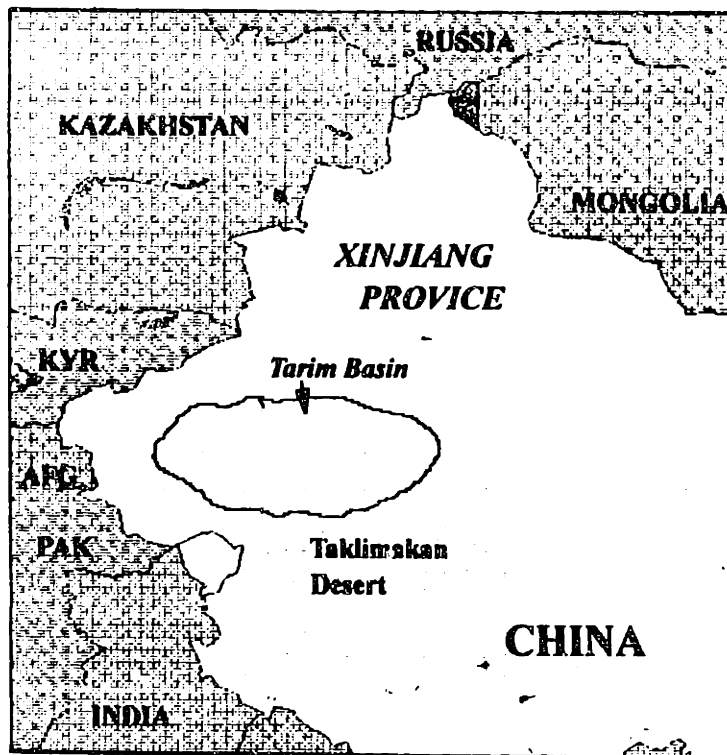
The eastern region lies on the mainland, facing the ocean. Its main geographic feature is a plain spotted by many hills. As such, it has a lot of rainfall during the monsoon season. The soil is rich and covered with vegetation so conditions are good for agricultural production. However, the eastern region lacks mineral resources. Except for the exploited crude oil, iron, boron, some construction materials and non metal resources, all other resources are poor. It only has 15% of the nation's coal deposits, and it is dependent on the central and western regions or imports for the supply of nonferrous metals and chemicals for industrial development.

Lying inland between the eastern and western regions, the central region has a continental monsoon climate featuring extreme differences in rainfall and temperature from season to season. It is China's grain basket, and has rich energy, metal and nonmetal mineral resources. Of the more than 40 major mineral resources to be found in China, the central region has more than half of them, and that amount consists of more than 30% of natural

resources in the country. They are coal, natural gas, gold, silver, molybdenum, aluminum, zinc, iron, etc.

The vast western region is a high elevation region. It includes the Yellow Earth, Yunnan-Guizhou and Qinghai-Tibet Plateaus. There are many mountains and deserts in this region. Most of the land cannot be cultivated because of the high elevation, cold temperatures and lack of water. Some areas in the Yunnan, Guizhou, Sichuan and Shaanxi provinces are an exception. The already exploited mineral resources in this region are crude oil, coal, natural gas and iron. Many kinds of nonferrous metals and rare metals also can be found. Crude oil reserves in Xinjiang's Tarim Basin has attracted major international oil exploration companies to participate in its exploration. On October 10, 1994, *the Wall Street Journal* reported about crude oil exploration at Tarim Basin and pointed out that many foreign companies thought this region may have as much oil as Saudi Arabia(See Map II-4).

Map II-4: Tarim Basin Xinjiang, China



In comparing eastern, central and western economic regions, the following issues should be emphasized:

- 1) The overall features of the three economic regions. Generally speaking, the three economic regions from the east to the west have developed, underdeveloped and non developed features. In 1990, their output as a percent of the country's GNP were 53%, 30% and

17%, respectively. Their shares in the gross industrial output were 61%, 26% and 13%, respectively. And their shares in gross manufacturing output were 46%, 35% and 19%, respectively. Because the speed of economic development in the three regions is unbalanced, i.e., the eastern region is developing faster than the central region which is developing faster than the western region, the proportion of the three regions total output will change continuously with the eastern share increasing and the central and western regions decreasing.

- 2) The features of the industrial structure in the three regions. Presently, China's major economic activities are agriculture, manufacturing industries, construction, transportation and commerce. There are obvious differences in the industrial structure in the three regions (See Table II-2).

Table II-2: Percentage Shares of Different Economic Sectors in the GNP, 1992

Region	Agriculture	Industry	Construction	Transportation	Commerce
National	16.3	66.4	9.3	3.2	4.8
Eastern	18.61	63.96	n/a	17.43	n/a
Middle	25.29	57.67	n/a	16.04	n/a
Western	28.27	48.18	n/a	23.45	n/a

Source: *Statistics Yearbook of China*, 1992, China Statistics Press, 1993 pp. 713

- 3) The form suggests that agriculture still enjoys one fourth or even more of total output in the central and western regions. As to industrial production, it is over half the total output in the central region and less than half in the western region. This relatively high level of industrial production is due to state investment in construction of heavy industries in the central region in the 1950s. And since the 1970s, this region has become the nation's key energy industry base. It should be emphasized that while there is a big difference in the three region's industrial structure, this gap has been reduced in some industrial products in the past ten years or so (See Table II-3).

Table II-3: Major Industrial Products and Output by Region

Products	East Region		Middle Region		West Region	
	1981	1989	1981	1989	1981	1989
Steel	60.41	57.54	27.88	30.12	11.71	12.36
Coal	27.50	22.46	54.06	57.58	18.44	19.96
Crude Oil	36.60	42.56	57.30	50.46	6.01	6.98
Electricity	50.02	48.13	33.27	34.30	16.71	17.57
Automobile	37.02	49.73	60.35	42.37	2.45	7.90
TV	73.49	75.42	17.28	11.85	9.23	12.73

Fertilizer	47.24	41.30	32.23	35.91	20.52	22.79
Ethylene	87.65	70.91	12.15	25.28	0.20	3.81
Chemical Babric	73.05	76.35	19.23	18.80	7.72	4.85
Sodium Carbonate	86.32	69.45	7.48	18.89	6.20	11.66
Caustic Soda	69.38	65.13	20.54	23.37	10.08	11.50
Cement	51.17	53.35	32.70	29.91	16.13	16.54
Glass Sheet	62.60	52.76	30.21	32.51	7.19	10.23
Cloths	57.44	59.91	29.67	28.26	12.89	11.83
Salt	79.89	66.70	8.34	9.31	11.77	23.99
Sugar	65.86	61.45	21.00	21.36	13.14	17.19
Cigarette	42.37	32.35	41.67	37.45	15.96	30.20
Ferroadlloy	35.57	30.64	45.48	41.61	18.95	27.75
Calcium Carbide	54.50	37.44	34.40	40.23	11.10	22.33

Source: *China Industry in 1990's*. Economic Management Press, pp.268

- 4) The economic division of the three regions. Due to the industrial infrastructure already formed in the three regions and the development of the country's market system, the economic division among the three regions is well established. The eastern region depends mainly on high tech industries, high value added processing industries and services. The central and western regions mainly depend on mineral, energy and some traditional heavy industries.
- 5) The enlarging gap in income in the three regions. The income gap among the three regions is increasing. Presently, more than 90% of China's population in poverty live in the central and western regions, around 80 million people. About 130 million rural people have an average income below 400 yuan annually. There are 33 counties classified as poverty counties in the eastern region, while there are 295 poverty counties in the central and western regions. And the average per capita income in the eastern poverty counties is two times that in the western region. In the eastern regions basic survival needs of housing and food have been provided, this is not the case in the western region.¹⁰ (See Table II-4, it illustrates these points).

Table II-4: GDP Per Head, 1992¹¹

Regions	Population (Million)	Per Head GDP (USD)
Shanghai	13	1,880
Guangdong	65	810
East coast	125	780
East interior	186	310
West interior	144	290
China total	1,165	470

Source: World Bank Report, 1993

¹⁰ *China Times Weekly*, Jan 30 -Feb 12, 1994, pp. 60.

¹¹ East coast includes Jiangsu and Zhejiang provinces; East interior includes: Henan, Anhui and Jiangxi provinces; West interior includes: Sichuan, Guizhou provinces.

- 6) Due to the existing gap and different economic growth rates among the three economic regions, the gap will grow dynamically. Given this situation, the overall government economic interest should be to adjust policies among the regions to reduce the gap. However, the intervening power of the central government has dramatically reduced. People in the eastern region do not want the central government to increase their taxes to subsidize the central and western regions. And people in the central and western regions do not support the central government's natural resource pricing policy which is structured to support rapid industrialization in the resource poor eastern region. Consequently, the central and western regions have adopted protective policies to prevent low price resources from going to the eastern region and restricting products from the eastern region from entry. They are using the freed-up capital to invest their natural resources in industrial development. This is a good example of the type of reconstruction that has occurred as a result of decentralization. No doubt, this kind of reconstruction has some passive aspects. However, it illustrates that the central government's ability to intervene effectively in the economic interaction among the three regions is limited. The regional development policy which originally had limited effectiveness has been further weakened.

In summary, the division of mainland China into three economic regions is theoretically and statistically significant: it is based on economic reality. As can be seen from this first phase of economic reform the hegemony of the central government is in the process of being replaced by a system of decentralized regional control. This is the first reconstruction from centralization to decentralization: others will follow.

B. Formation Two: Opened Coast Regions and Inland Regions

The eastern coast region of China was the first to be industrialized. In the late Qing Dynasty the government ended its closed door policy and opened its south eastern coast and some coast cities in the North to foreign trade. Until 1949 when the Chinese Communist Party gained power, China's coast region (184,000 kms of coast line) had been the vehicle for exchanges with the outside world especially the West, although there were periods of trade interruptions. The main function of the coastal cities was to provide the inland region with new technologies, raw processing materials, capital and a new market. What Mao Zedong said about the "ten relationships" in 1956 which included the relation between the coastal region and the inland regions was based on a closed economic system.

Since the reforms in the late 1970s, China has opened its borders again. The reform policy was designed to expose China to the outside world, while the objective of the new open door policy was to permit China to participate in the world economic system and avoid long-term capital shortages and lack of advanced technology. China's eastern coast region was again dominant in this new open door policy. In other words, when China opened its door in the late 20th century it opened them first in the eastern region.

The open region spreads through 11 provinces- Liaoning, Tianjin, Hebei, Shandong, Jiangsu, Shanghai, Zhejiang, Fujian, Guangdong, Guangxi and Hainan - and numerous cities and autonomous regions. The eastern province occupies 14% of the nation's land, is home to 41% of the total population. But the open region in the province only occupies 417 thousand sq. kms, which is only 4% of the entire country. The population is 200 million or 20% of the nation's total population.

There are some obvious advantages in setting up an open coastal region. They include:

- 1) easy access to foreign capital and advanced technology;
- 2) a tradition of international economic cooperation;
- 3) a developed industrial basis and complete industrial infrastructure; and
- 4) an advanced education system and research and development capabilities.

This eastern open region has played an increasingly important role in international trade. In the middle of 1980s, the gross value of purchases of the foreign trade sector of the 14 coastal cities and five economic zones reached 25% of the nation's total export value.¹² The role of the whole coast region in China's international trade sector is more important. The proportion of the coast region's total export value was 73% of China's total export value in 1987. This figure was 73% in 1989, and exceeded 75% since the 1990s.¹³ In contrast to the open coastal region is the inland region. In a narrow sense, the inland region includes the central and western economic development regions.

In the last decade the open door policy has expanded. According to the State Statistical Bureau, following the first five special economic zones, there are five catalogues of open economic zones in China now (See Appendix 9):

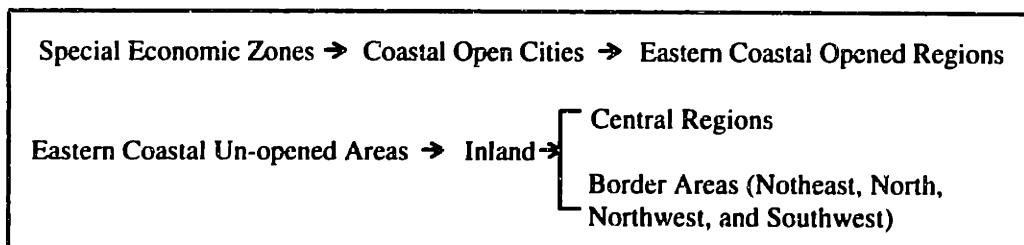
- 1) five special economic zones with 35.7 thousand sq kms of land and eight million people;
- 2) fourteen coastal cities with 51.2 thousand sq. kms of land and 38 million people;
- 3) five open coastal economic zones with 330 thousand sq. kms of land and 101 million people;
- 4) five open cities along the Yangtze River; and
- 5) thirteen open border cities.

In a wide sense, this historic process can be seen from the following Figure II-1:

¹² Fang Sheng ed.: *China's Opening Economy*, Economy Daily Press, 1991, pp. 285

¹³ *Strategic Studies in Economic Development of China's Coast Region in 1990s*, China Planning Press, 1993, pp. 173.

Figure II-1: The Expanding of Opening Areas

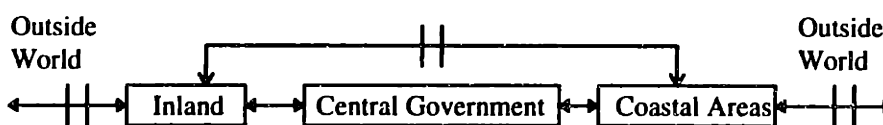


China has more than 23,000 kms of inland borders with other nations. When China opened its door in the eastern coastal region and subsequently all provinces, it also opened the door to all its neighboring nations. That is the so-called "all dimensional opening". Today there are more than 180 border trading centers - Dandong, Heihe, Manchuria and Herguosi are among the most well-known. In 1989, the total value of China's border trade exceeded 1 billion US dollars.¹⁴ The booming of border trade is bound to stimulate the economic development and market economy in these areas including minority areas.

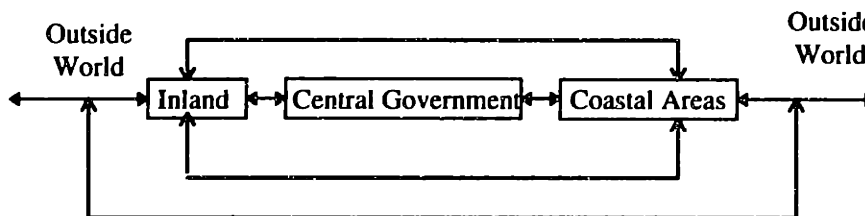
While the central government opened the coastal region to international trade before the inland regions the historical differences and conflicts between the regions are beginning to appear as they struggle to increase their share of trade. In order to gain more control over imports and exports, all regions will intensify their efforts to break away from control by the central government, resulting in further decentralization. The following Figure illustrates the dynamics of a transition from a closed, centrally controlled economic systems to an opened economic systems.

Figure II-2: Comparison Between Closed and Open Economic System

A. A closed economic system



B. An open economic system

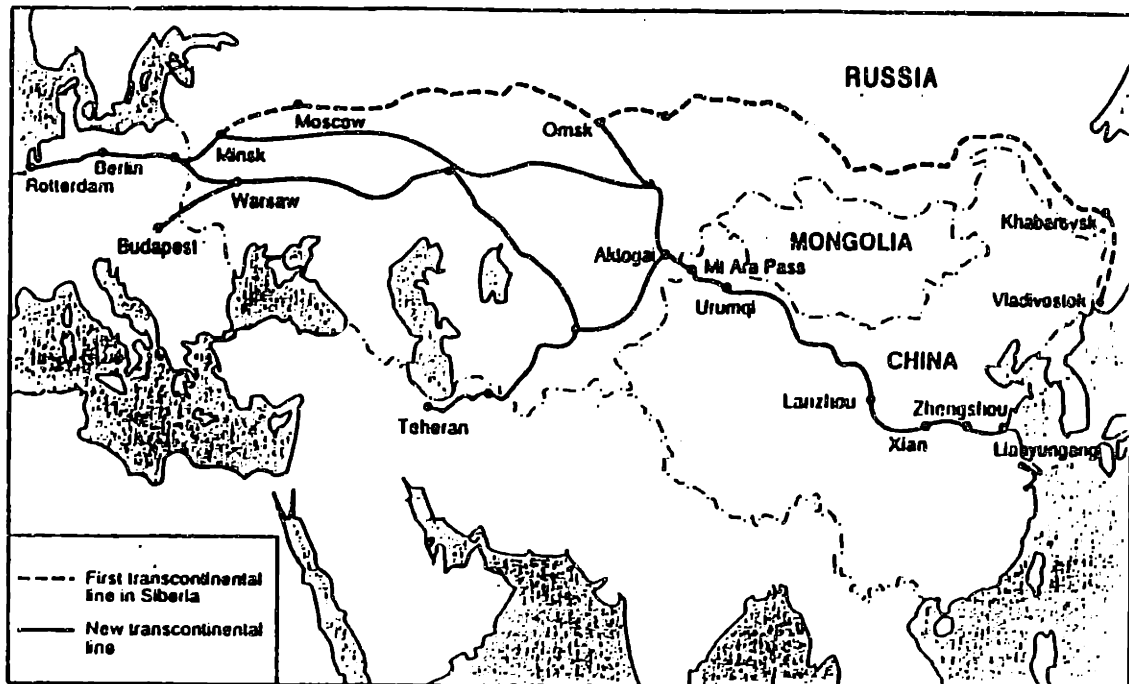


¹⁴ *Strategic Studies in the Economic Development of China's Coast Region in 1990s*, China Planning Press, 1993, pp. 305.

An important aspect on the inland trade is the so-called European-Asian continental bridge. When the railroads between Xinjiang and Russia are connected, China's inland region will have direct access to central Asia and Europe.¹⁵

This railroad begins in Tianjin, Dalian, and Qingdao on the east coast, transverses central China to Xinjiang and then moves through to Rotterdam and Hamburg. The new route: the bolting into place of a rail line between Russia and China promises a resurgence in the economy of central Asia. (See Map II-5).

**MAP II-5: The New Transcontinental Line
(Euro - Asia Continental Bridge)**

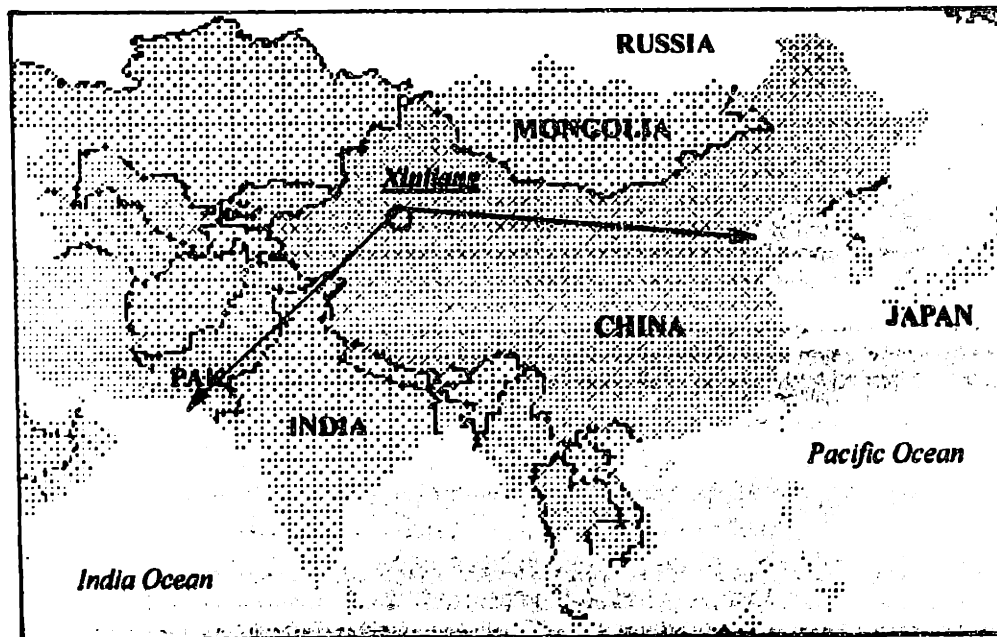


The railway, some ten thousand kilometers, would shorten travel time through the northern Siberia truck by two thousand kilometers. In addition, it is nearly ten thousand kilometers shorter than the sea route, and could save more than ten days' voyage. By connecting the Pacific and Atlantic oceans, China's inland provinces, once the cradle of Chinese civilization but now lags for behind the developed coastal regions, might gain access to many new markets and prospects. China's inland will no longer depend on the east coast for trade. The inland region, especially Xinjiang, also has direct access to the

¹⁵ China's railways were connected with those of the former Soviet Union through Xinjiang in September, 1990. The European-Asia continental bridge was formally open. It is 10,800 kilometers from China's Lianyungang to Holland. This is the third transcontinental bridge. The first one was North American transcontinental bridge built in 1950s. The second one was the European-Asia Siberia continental bridge starting from former Soviet Union's Vladivostok to Holland's Rotterdam. The third one is the European-Asia continental bridge starting from China.

Indian Ocean by China-Pakistan international highway.¹⁶ It is only 1500 kms from Kashi to Karachi, one-third of the distance from Xinjiang to China's major eastern harbors (See Map II-6).

Map II-6: Distance Central Northwest China to the Indian and Pacific Oceans



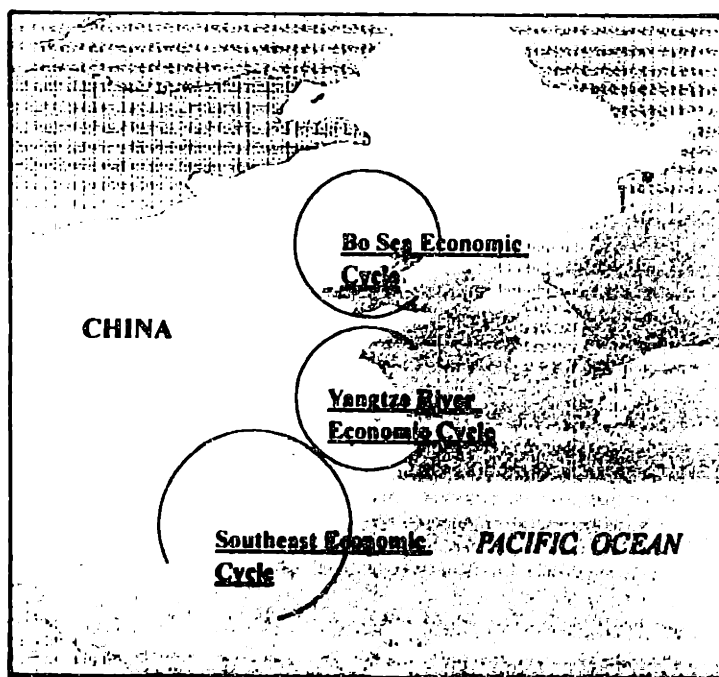
In summary, as China gains access to the world through trading channels on all fronts -the Pacific Ocean in the East, the European-Asian continental bridge in its West and border trading - continued decentralization is inevitable.

C. Formation Three: The North, Central, and South Economic Circle within the Coast Opening Region

It is not difficult to see by analyzing the economic development of the eastern coast region that three economic circles have developed in the last 15 years. These areas, the north, central and south, have their own special industrial structures. The northern area is centered around the Bo Sea Economic Circle; the central economic circle is centered in the Yangtze Delta with Shanghai as its heart; and the southern economic circle includes Guangdong, Fujian, Guangxi and Hainan, with the Pear River Delta the most active area. Hong Kong is surrounded by this economic circle (See Map II-7)

¹⁶ The highway was finished in October 1988. Karachi Harbor can anchor ships of ten thousand ton weight. The harbor's handling capacity is more than 70% of Pakistan's foreign trade and transit trade capacity. It is benefit to China to transit its products from Karachi to western Asia, North Africa, and Mediterranean countries.

Map II-7: North, Middle and South Economic Cycles in Eastern China



1. The Bo Sea Area

The Bo Sea economic circle includes areas and cities around the Bo Sea, i.e., Tianjin, the Liaoning Peninsula, the Shandong Peninsula and the Qinghuangdao-Tangshan-Cangzhou area in Hebei province. The region consists of Tianjin City and 18 provincial cities (Shenyang, Dalian, Dandong, Yingkou, Panjin, Jinzhou, Anshan, Liaoyang, Qinghuangdao, Tangshan, Cangzhou, Jinan, Qingdao, Yantai, Weihai, Weifang, Zibo, Rizhao) and counties governed by these cities. It covers 150 thousand sq. kms or 1.5% of the country's total area. The population is 69 millions, slightly more than 6% of the nation's total population.

This economic circle has many unique advantages. Geographically it is located at the junction between North China, Northeastern China, and East China. It is the nearest access to the Pacific Ocean from North China, Northeast China, Northwest China and neighboring Mongolia.¹⁷ All the eastern harbors which serve as terminals for the "European-Asian Continental Bridge" are located in this region.

Rich resources are located in the region. Shengli, Liaohe and Dagang have coastal oil fields. Ocean oil reserves so far exploited represent more than one-third of China's total oil reserves. Anshan and East Hebei have more than 40% of the nation's total iron. Kailuan, Shenyang, Zibo and Longkou have large coal reserves. The Kailuan mine alone has about 2.6 billion tons of coal, which is the largest coal mine field in China. There are also many

¹⁷ Republic of Mongolia has made an agreement with China in utilizing Tianjing Harbor. The country is part of Northeast Asia Economic Cooperation Zone.

other mineral resources. In addition, Bo Sea is the largest inland sea in China, having more than 100 kinds of fish. And there are vast areas of sea beach and slatterns.¹⁸

It has been the most important industrial region in China for the past hundred years of industrial development. In 1990, estimated steel production was 25% of China's total production; crude oil was 40%; crude oil processing capacity was 30%; pure alkali was 60%; machine tools were 20%; cement was about 15%; chemical fiber was about 16%; cotton yarn was about 20%; and salt was about 40%. By the end of the 1980s, this economic circle's gross industrial production was 350 billion yuan based on that time's price, which was 15% of China's GNP.¹⁹

Agriculture is also highly developed. The warm, monsoon climate suitable to crop production. Vast plains and mountains on one side and seas on the other mixed with warm temperatures and ample rainfall make this area China's most important farming area. In addition to exporting food, any kinds of raw materials are produced for light industry. Approximately one third of the population work in agricultural relative activities earning one fourth of the areas' GNP. This level is higher than China's average level.²⁰

Moreover, the area has highly developed transportation facilities, in fact, the best in China. A complete transportation network covers the Bo Sea economic circle, including railways, highways, water and air transportation and pipelines. To illustrate the extent of this system, the density of this region's railway network is two times that of the national average. And, in 1990, there were more than 110 berths capable of anchoring ships of ten thousand tons which was 37% of the total capacity of China.²¹ Key harbors like Tianjin, Qinhuangdao, Dalian, Qingdao and Shijiusuo are directly connected with the main railways, forming a land-ocean transportation network which in turn links China with the world. The highway network is the densest in China. Large airports were built in Tianjin, Shenyang, Dalian, Jinan, Qingdao and other cities. Also pipelines which linked the Shengli, Liaohe and Dagang oil fields directly to oil refining factories in east Liaoning, Dalian and Qinghuangdao and a harbor were built.

This economic circle has the most densely located cities in China. There are 18 cities in the region: only one is administered directly by the central government. Ten are harbor cities. Most of those non-coastal cities like Shenyang and Jinan are industrial and communication centers. Most have strong industrial, transportation and communication facilities. In 1990, there were 35 cities in all of China and 20 cities in China's coastal region whose GDP exceed 10 billion yuan.²² Nine of these cities were located on the coast. They are Tianjin, Shenyang, Dalian, Qingdao, Weifang, Yantai, Jinan, Tangshan

¹⁸ *Strategic Studies in the Economic Development of China's Coastal Region*, China Planning Press, 1993, pp. 512.

¹⁹ *Idid.* pp 512.

²⁰ *Idid.* pp 513.

²¹ *Idid.* pp 514.

²² *Idid.* pp 514.

and Zibo. In short, this group of cities is totally linked together in a network of industrial, cultural and transportation facilities

The region is the gateway to the outside world and inland regions. In 1984, five city harbors along the Bo Sea Coast - Tianjin, Dalian, Qinhuangdao, Yantai, Qingdao were opened to the world, and in Hebei province, East Liaoning Peninsula, Shandong Peninsula and Qinhuangdao-Tangshan-Cangzhou were opened to external trade. At the same time, economic and technical development zones were established in Tianjin, Dalian, Qinhuangdao, Yantai and Qingdao. And one duty Free zone was established in Tianjin. These measures stimulated trade and exports, made more foreign currency from non-trade sectors available and created an agreeable environment for foreign investments. According to incomplete statistics, by 1991, more than three thousand projects using foreign capital valued at more than US DOLLAR 5 billion had been invested.²³ And economic cooperation with inland provinces were established with most inland provinces.

2. Yangtze River Delta Economic Circle

The Yangtze River Delta economic circle includes Shanghai and its nine cities - Lianyungang, Yancheng, Nanjing, Zhenjiang, Yangzhou, Suzhou, Wuxi, Changzhou and Nantong cities with their 47 counties, and Hangzhou, Jiaxing, Huzhou, Shaoxing, Ningbo, Zhoushan, Wenzhou cities with their 27 counties and 3 counties of Taizhou. It ranges from Lianyungang in the North to Wenzhou in the South and up the Yangtze River to Nanjing. The region is shaped like a "T" that faces the ocean. It covers 109 thousand sq. kms (7.4% of the nation's land), and has a population of 84 million, or 1% of the total population. It is China's largest coastal open economic region.

The Yangtze River Delta economic circle has a common culture and history, similar geographical condition and close economic and social relations. Shanghai is the epicenter; Jiangsu and Zhejiang are the two wings. There are interdependent, complementary economic relations among the cities and towns. Since the 1980s, the economy in the area has increased dramatically as a result of the implementation of the economic development strategy along the coastal regions and the opening of the Pudong region in Shanghai.

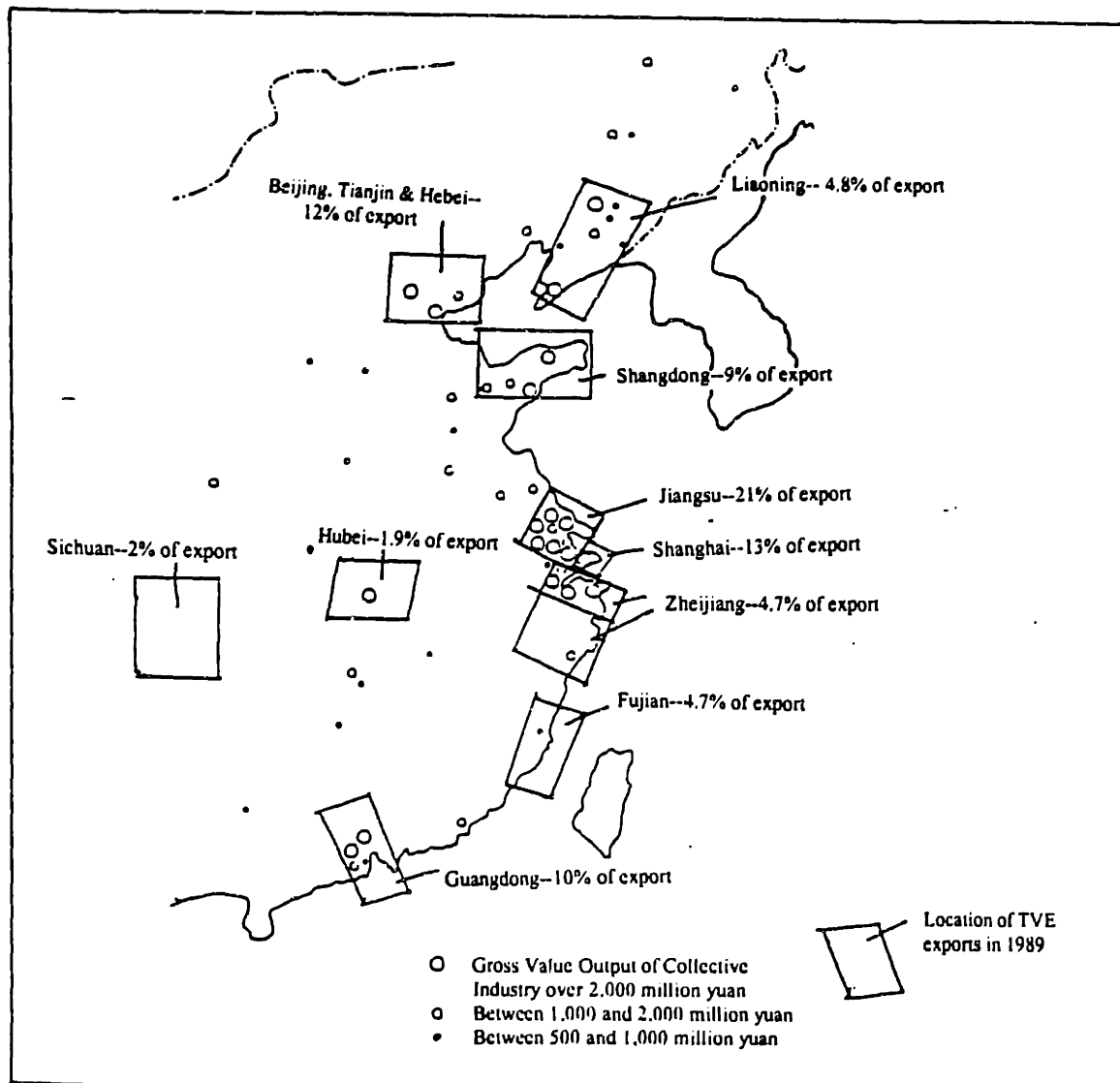
The Yangtze River Delta has become China's key economic region in 1990s. This comprehensive regional economic system has five coastal cities as the "window" to the outside - Lianyungang, Nantong, Shanghai, Ningbo and Wenzhou - and numerous supporting cities with business connections throughout the counties - Nanjing, Zhenjiang, Yangzhou, Suzhou, Wuxi, Changzhou, Hangzhou, Jiaxing, Huzhou, Shaoxing, Zhoushan, etc. The development has been multidimensional. Six economic and technological economic zones have been constructed in Lianyungang, Nantong, Caohejing, Minhang, Hongqiao and Ningbo. These high tech zones have become priority areas for foreign investors.

²³ *Strategical Studies in the Economic development of chin's Coastal Region*, China Planing Press, 1993, pp 514.

By 1990, this economic circle had established economic and trade relations with more than 160 countries and regions throughout the world. Trade increased from 5.7 billion US dollars in 1980 to 13.7 billion US dollars in 1989, a 140 % growth. Exports amounted to US dollars 9.2 billion or 21% of all exports. Sixty percent of goods exported consisted of light industrial products and textile; 20% consisted of heavy industrial and chemical products. The proportion of elementary and semi-processed products decreased. Finely processed products like electronic equipment and machine equipment were greater than processed goods like minerals and hardware. This increased the competitive capacity of the region because they export finally processed products in the world market.

Historically, village and town enterprises have been pillars of the national economy. With the development of the open economy, village and town enterprises have grown rapidly in this region since 1980s, especially in the area of export. (See Map II-8)

Map II-8: Export Distribution of TVE by Regions, 1989

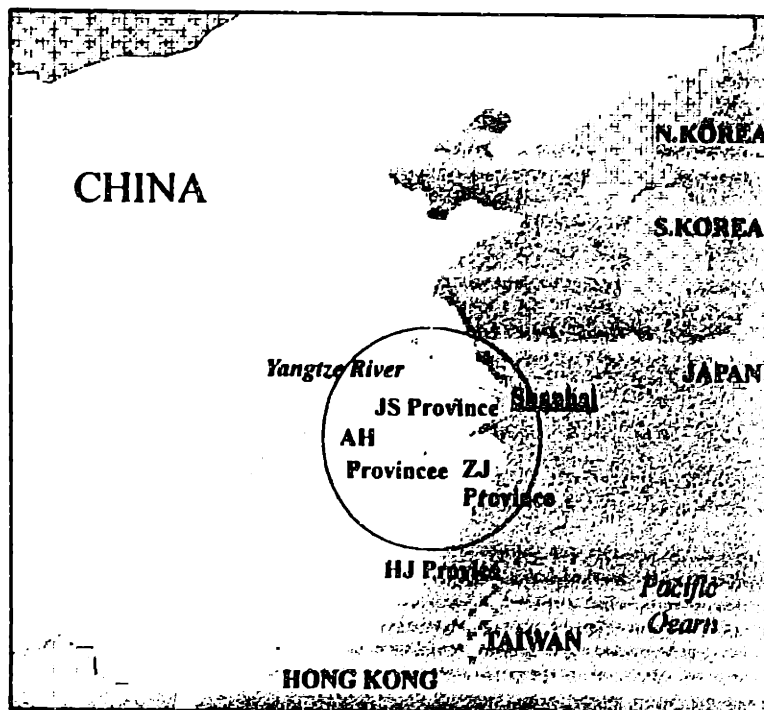


The above map illustrates that : the production value of the town enterprises in Suzhou, Wuxi, Nanjing, Yangzhou and Yancheng was 42.9 billion yuan, which was 18% of China's total, and the production value of the village enterprises in this area was 186.9 billion yuan, which was 46% of China's total.²⁴ Village and town enterprises have become economic pillars in rural areas and an important source of exports.

At the same time, the region introduced many new technologies and attracted significant foreign capital. By the end of 1990, 2800 foreign enterprises had been approved, US dollars 4.4 billion agreements had been signed and US dollars 1.8 billion were actually introduced, amounting to 18%, 11%, and 9%, respectively, of China's total foreign investment.²⁵ Clearly, foreign investment is becoming more and more important in China's economic development.

Geographically, Shanghai is located on the coast of the East Sea on the east side of the Yangtze River Delta. Situated in the middle of China's coastline, it controls the entrance of the Yangtze River, China's main inland water route (See Map II-9).

Map II-9: Shanghai and Yangtze River Economic Zone



²⁴ "Shanghai is Trying to Become an International Financial Center", in Central Daily, October 9, 1994.

²⁵ *Strategic studies in the development of Chin's coastal Region in 1990's*, China Planning Press, 1993, pp. 426.

It is also situated on both sides of the Huangpu River. The lower reach of the Huangpu River is deep and wide; ten thousand ton ships can navigate it. Wusong River (or Suzhou River) originates in Tai Lake and flows to the Huangpu River through Shanghai. This forms a water network connecting the inland rivers of Anhui, Jiangsu and Zhejiang provinces. Shanghai is also the center of China's two major railways from the North to the South, i.e., the Beijing-Shanghai and Shanghai-Guangzhou lines

Economically, Shanghai has always been one of the key industrial cities in China. It produces more than 7% of all industrial products. The scope, depth and scale of Shanghai's industrial system is incomparable to any other industrial city in China. It is also China's most important consumer market. Residents have a higher than average income in the country and there is a huge population. Shanghai is China's largest city, and one of the largest cities in the world. It is worth emphasizing that when the construction of the Pudong Economic Zone is completed, Shanghai will become the center of foreign investment in this economic circle, perhaps even in South China and all China. Now, Shanghai is carrying out this ambitious project to become an international financial center locally, regionally and internationally in three stages over a period of 25 years.²⁶ The growth of Shanghai's economy is no doubt a huge impetus to this circle's economic growth regardless if the Pudong project can be accomplished.

3. Southeast Coast Economic Circle

The southeast coast economic circle includes Guangdong, Fujian, the coastal areas of Guangxi and Hainan Island. In the 1950s and 1960s, this region was a defense frontier. Agriculture and agricultural processing dominated the economy. Economically it was not as important as the Bohai Sea and Yangtze River Delta regions. With the implementation of China's reform and open door policies and the changes in international politics and economy in the late 1970s and early 1980s, this region became China's first open region. Because this region is near Hong Kong, Macao, Taiwan and southeast Asia where a large Chinese population live and because the region was always commercially prosperous, it quickly became the target region in China's economic development strategy. During the 1980s, the southeast coast economic circle had the most open and flexible economic policies in China. The Shenzhen Special Economic Zone and the Pearl River Delta region experimented with unique development models, and economic development there exceeded the speed of the "takeoff stages" of Asia's four small dragons. This economic circle occupies four provinces. Though geographic neighbors, their economic relations and development are relatively independent. There are a variety of development patterns in this circle.

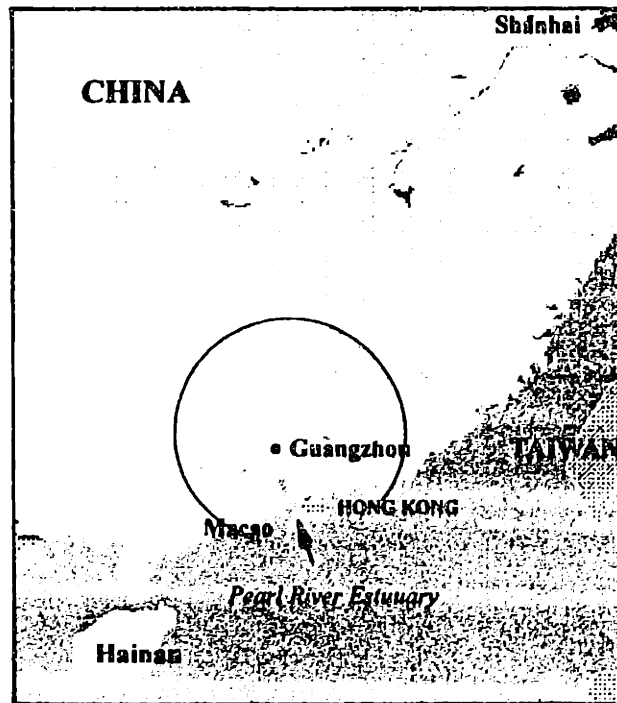
i. Guangdong Coastal Opening Region

Guangdong was one of the first open provinces in China. In 1979, three special economic zones (Shenzhen, Zhuhai, and Shantou) were established, and Guangzhou, Zhanjiang, the Pearl River Delta and areas in east Guangdong and west Guangdong have been opened to the outside world. Now, there are 15 cities and 42 counties opened. According to one

²⁶ "Shanghai is Trying to Become an International Financial Center", in Central Daily, Oct 9, 1994

survey, the total value of GDP per capita of Guangzhou, Shenzhen, Zhuhai, Foshan, Dongguan and Zhongshan in 1990 was equal to that of Britain, France, West Germany and Japan in the early 1960s or South Korea and Taiwan in the middle of 1970s.²⁷ The center of the Guangdong coastal open region is the Pearl River Delta which includes Guangzhou, Shenzhen and Zhuhai (See Map II-10).

Map II-10: Pearl River Delta Open Economic Zone



In terms of the net value of fixed assets, the largest 100 enterprises are concentrated in the Pearl River Delta. Of the 611 village and town enterprises in Guangdong province whose production exceeded ten million yuan, there are 555, that is more than 90% concentrated in the Pearl River Delta region.²⁸ The region has been so productive because of rapid industrial and agricultural production, large inflows of foreign currency, growth in per capita income, increase in sales of retail value in the society and the expansion of village and town enterprises. Even more fundamental in the growth of the Pearl River Delta is its geographic location. Hong Kong and Macao are favorably situated to carry out the open door policy in this region. And Shenzhen, Zhuhai and Shantou were the first special economic zones established in China giving Guangdong an advantage in attracting both overseas and domestic capital.

²⁷ *Strategic Studies in the Economic development of China's Coastal Region in 1990s*, China Planning Press, 1993, pp.378.

²⁸ *Strategic Studies in the economic development of China's Coastal region in 1990's*, China Planning Press, pp. 379.

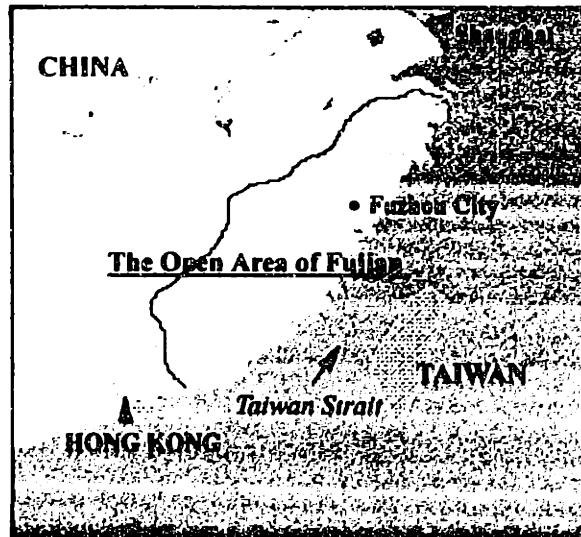
Village and town enterprises were established as a result of the open economy. They fostered an interactive process between the growth of village and town enterprises and the growth of the open oriented economy. This high growth in the Pearl River Delta accelerated the integration process of Hong Kong and Macao, and that affected the entire South China coastal region as well as distant economic regions.

ii. Fujian Coastal Open Region

The Fujian coastline of 3051 kms, with many deep harbors, includes Xiamen, Fuzhou, the South Fujian Delta and other part of Fujian. There are 33 cities, counties and areas in this region encompassing 41.6 thousand sq. kms, which is 34% of the province's total area. The area has a population of 17 million, or 60% of the province's population. Industrial and agricultural production and revenue account for three-fourths and three-fifths of the province's totals, respectively.

The region is close to Taiwan, only divided by the Taiwan Strait. More than 80% of the inhabitants of Taiwan are descendants of Fujian. This unique geographic and social relationship gives Taiwan an important role in the development of the area (See Map II-11).

Map II-11: The Open Areas of Fujian Province



According to incomplete statistics, Fujian descendants residing abroad represent one-fourth of all Chinese overseas residents. Living in more than 90 countries, they are, next to Guangdong residents, the second largest Chinese overseas population

Up to now, reasonable cooperation and mutual advantageous complements have been formed within the Fujian coastal open region. The region of the lower reaches of the Min River centered by Fuzhou, the region of the lower reaches of the Jiulong River centered by Xiamen and Meizhou Bay region, have become three economic centers in the Fujian coastal open region.

The South Fujian Delta region developed by utilizing the Xiamen special economic zone and its advantageous geographic location and its opening economic development zone.

During the past 15 years, especially since 1990, the complementary economic relation between Fujian and Taiwan as strengthened. In essence, the region has become the door for Taiwanese capital influx into mainland China, and also it has become a hinterland of Taiwan's expanded economy. Naturally, Guangdong and Fujian took the dominant share of Taiwan's investment in China. (See Table II-5).

Table II-5: Geographical Distribution of Investments by Taiwanese Firms, 1988-92

Region	Investments (Million USD)	No. of Firms
Guangdong	121.1	411
Shenzhen	111.6	378
Guangzhou	55.9	146
Dongguan	15.7	188
Shantou	12.0	39
Zhuhai	11.3	42
Shanghai	87.0	78
Beijing	25.0	30
Jiangsu	24.6	56
Shandong	18.0	46
Zhejiang	14.8	56
Hainan	15.0	49
Fujian	42.4	204
Xiamen	87.0	275
Fuzhou	44.9	119

Source: *Sino-American Relations at a Time of Change*
1994, Edited by Gerrit W. Gong and Bih-jaw Lin, PP. 224

For this reason economic growth in the region has exceeded China's average level. In 1992, GDP increased 218% over the 1991 level, fixed asset investment increased 49% and exports increased 39.4%. The foreign capital investment increased 100%.²⁹ This growth was the largest among the coastal provinces.

There are three economic centers in the lower Min River: Fuzhou, Xiamen and Meizhou Bay. The Min River area has established a comprehensive economic system of trade, industry, agriculture and R & D by utilizing the economic strength and preferential trade policies of the economic and technological development zones of Fuzhou and Mawei. The Meizhou Bay region developed an industrial base of petroleum chemical products, power, steel, construction materials and shipbuilding, and took advantage of an excellent natural harbor and rich labor resources. Construction currently underway in Xiamen harbor and in the Xinglin -Taiwan investment zone and the Fuzhou - Mawei Taiwan investment zone will enlarge the economic relations between Fujian and Taiwan.

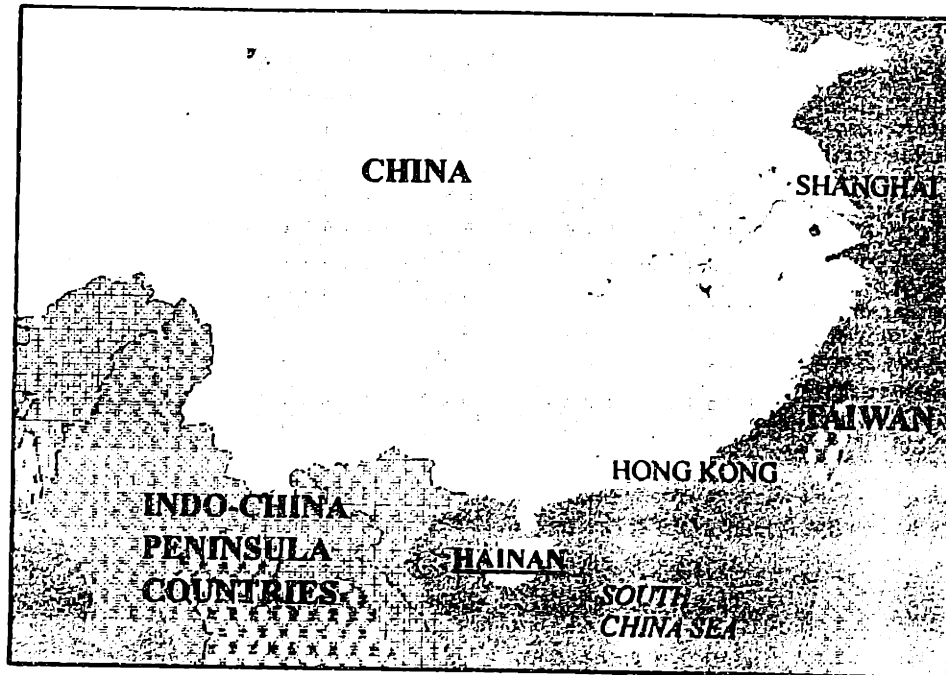
The economic significance of this region cannot be underestimated. As government relations normalize between mainland China and Taiwan, direct air and marine transportation will open and the economic ties between Fujian and Taiwan will be further strengthened and integrated.

²⁹ *Economic Yearbook of China, 1993*, Economy Management Press, 1993, pp 433-434.

iii. Hainan Province

Hainan Island, located in the South China Sea, is vital both strategically and commercially for it is the link between East Asian and Southeast Asian. (See Map II-12)

Map II-12: Hainan Province



Development was slow in the past because it was isolated from the mainland. However, in 1988 Hainan became an independent province: since then, its economy growth has been more rapid than the average in China, mainly because it has become China's largest special economic zone.

This special economic zone receives preferential policies in terms of autonomy in investment, trade, finance and land development. After it became an independent province a number of separate economic development zones were formed: Haijiang, Sanya, Yangpu, Qinglan and Basuo. A long-term foreign investment strategy as designed to exploit resources and to develop a high-tech, export oriented industrial structure. This strategy has been successful: in the past few years huge amounts of capital has been invested in Hainan, both from abroad and inland provinces.

iv. Guangxi Coastal Opening Region

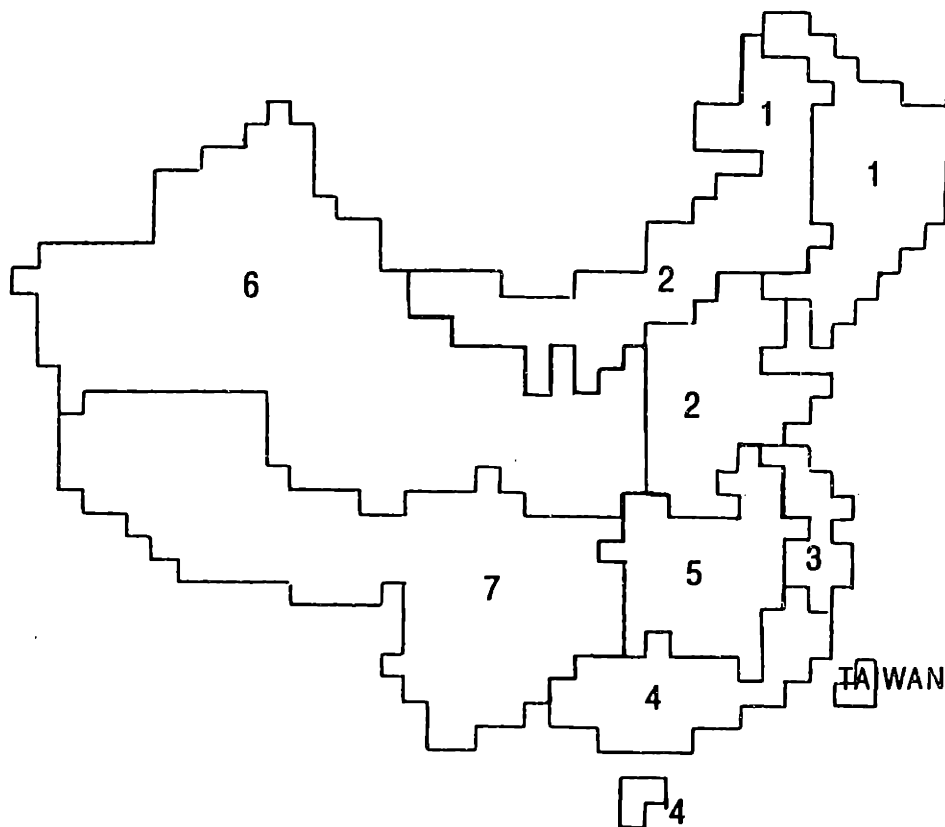
Guangxi coastal open region is located in southeast Guangxi. It includes Beihai, approved as one of 14 coastal open cities in 1984, and Wuzhou, Cangwu, Yulin, Qinzhou, Hepu and Fangcheng cities and counties approved as open areas in 1988. Geographically, the region faces the North Bay and has 1595 kms of coastline and two well-located harbors. One is Beihai city (including Fangcheng Harbor). When the Nanning-Kunming railroad is finished, it will be the nearest cargo exit to the sea for the provinces of Guangxi, Yunnan, Guizhou and Sichuan. These four provinces will be connected by this railway and harbor

Guizhou and Sichuan. These four provinces will be connected by this railway and harbor with China's other coastal provinces, Southeast Asia and the world. This is most significant for the development of the rich coal, iron, phosphorus, sulphur, nonferrous metals and water resources in these provinces. The other is Wuzhou city located at the river thoroughfare of Guangxi. It has been historically the river transportation thoroughfare for cargo from Guangxi, Yunnan, and Guizhou to Guangdong, Hong Kong and Macao. The region is relatively underdeveloped. Undoubtedly the rapid development in the Pearl River Delta region, Hong Kong and Macao in the east and Zhaoqing, Maoming, Zhanjiang and the open cities in west Guangdong and Hainan and neighboring Vietnam and other Southeast Asian countries will influence economic trends in this area.

D. Formation Four: Seven Economic Zones

In China, provincial administrative regions have played a very important role regardless if whether the system is centralized or in the process of decentralization. The above sections analyzed three reconstruction patterns: provincial, trans-provincial and inter-provincial. Now we turn to another form of reconstruction based on geo-political and geo-economic units. This kind of reconstruction can be divided into seven economic zones (See Map II-13).

Map II-13: The Seven Economic Zones



The major economic indicators can be seen in Table II-6. (Appendix 10 provides more detail information about the seven economic zones).

Table II-6: The Major Indicators of East, Central and West Region, 1992

Region	Population (Million)	% of Nation	Urban Pop (Million)	% of Nation	Illiterate Pop	% of Nation
Zone 1	110,063,675	9.74	43,231,599	19.66	13,730	4.71
Zone 2	279,372,746	24.71	47,486,587	21.59	46,287	21.22
Zone 3	121,844,679	10.78	27,794,240	12.64	108,493	11.34
Zone 4	141,680,976	12.53	25,153,548	11.44	20,852	10.71
Zone 5	90,250,910	7.98	19,256,382	8.76	20,762	11.87
Zone 6	208,519,675	18.44	33,117,149	15.06	40,023	18.91
Zone 7	178,777,977	15.81	23,892,475	10.86	41,361	9.66
Total	1,130,510,638	100	219,931,979	100	291,496	100

Region	National Income (Million)	% of Nation	GNP (Billion RMB)	% of Nation	Import & Export (\$ Million)	% of Nation
Zone 1	180.15	12.54	472.34	12.49	16,900	16.83
Zone 2	354	24.64	965.95	25.54	12,080	12.03
Zone 3	248	17.28	791.03	20.92	21,008	20.92
Zone 4	193	13.46	489.21	12.94	37,465	37.32
Zone 5	93	6.47	221.48	5.86	3,532	3.52
Zone 6	213	14.80	500.69	13.24	5,919	5.90
Zone 7	155	10.81	341.16	9.02	3,496	3.48
Total	1,436	100	3,781.86	100	100,400	100

Source: *Statistical Yearbook of China, 1992*, China Statistical Press 1993

1. The Northeast Economic Zone

Located in East Asia, this region borders Russia and Mongolia and has links with Korea and Japan. The northeast economic plank includes Heilongjiang, Jilin, Liaoning and part of Inner Mongolia. It is China's most developed industrial region and includes huge, modern enterprises. It is the base of China's heavy industry and an important agricultural area. There are rich coal, iron and other mineral resources here. Dense railway and highway networks link the region internally and externally.

Since the open door policy, the northeast economic zone has become a focus of investment from Japan and South Korea. The zone has formed an economic cooperative network with Russia and Mongolia along the border cities of Suifenhe, Heihe, Manchuria, Erlianhaote and with the center cities of Harbin, Changchun, Shenyang, etc. The challenge facing the northeast economic zone is how to adapt former state owned enterprises to the rapidly growing open economic system.

2. North China Economic Zone

The North China economic zone includes the coastal provinces and cities at the lower reaches of the Yellow River: Beijing, Tianjin, Hebei and Shandong. It also includes

Henan, Shanxi and part of Inner Mongolia. There are dense railway networks, developed infrastructure and modern harbors within this plank. Shanxi is the center of China's energy, heavy and chemical industries. In addition to coal, there are also rich aluminum, "rare earth" and copper reserves. And this region possesses strong industrial processing capacities.

This zone has directly benefited from China's open door policy. The Bo Sea economic circle is in this plank, and the Shandong and Korean peninsulas have been connected as a potential economic cooperative unit.

3. East China Economic Zone

This zone includes Shanghai, Jiangsu and Zhejiang. While it lacks energy and mineral resources, its location at the lower reaches of the Yangtze River connects it with the outside world by sea and to inland regions by rivers. Major railways provide access to Tianjin-Shanghai, Shanghai-Nanjing, Shanghai-Hangzhou, Zhejiang-Jiangxi, etc. This is China's most developed region. With mild temperatures and abundant rainfall, the agricultural sector is highly developed. Shanghai's industrial system supports much of China's industrial construction. It has advanced technology and processing industries and management systems. In fact, it is the most comprehensive industrial base in China for light and processing industries.

4. South China Economic Zone

This zone includes Fujian, Guangdong, Guangxi and Hainan provinces. With a long coastline and numerous harbors such as Zhenjiang, Guangzhou and Xiamen it faces both the East Sea and South Sea. Railroads from Beijing-Guangzhou, Yingtian-Xiamen, Hunan-Guangxi, Guizhou-Guangxi connect the area with East, Central and Southwest China. There are rich mineral resources in this region including iron, aluminum, manganese, lead and zinc, providing the region with the capacity of developing raw material industries. Located in a tropical zone on the ocean, the region has a rich variety of tropical biological resources and seafood. The only restriction to development is the lack of energy resources, especially coal and natural gas.

Fujian and Guangdong are close to Taiwan, Hong Kong and Macao, an advantage for introducing foreign capital, foreign technology and expanding international trade. As mentioned above, the large population from this area living abroad facilitate this economic exchange. Since the establishment of the special economic zones of Shenzhen, Zhuhai, Shantou and Xiamen in 1980s, the opening of another four harbor cities in this region and the establishment of the Pear River Delta as an open economic zone in 1984, the South China economic zone has become the fastest developing economic zone in China. After World War II and the economic miracle in the Asia-Pacific region and since the economic take-off of Japan and the "four small dragons", South China's economic zone, Hong Kong and Taiwan have become the latest economic boom area.

5. Central China Economic Zone

This region includes Anhui, Jiangxi, Hubei and Hunan. It is located in the middle of Yangtze River which flows across the region from west to east. The Beijing-Guangzhou railway transverses the region from north to south. Among its natural resources are copper, lead, zinc, tungsten, antimony, nonferrous metals, iron, coal and abundant water. It is the repository of 22% of China's phosphorus reserves. Climate wise, it is warm and has abundant rainfall. Agricultural systems are well developed (rice, cotton and linen), and the extensive transportation facilities offer advantageous conditions for industrial development.

Wuhan city, located at the middle of the Yangtze River holds a special position in this economic plank as it is a central junction of north-south and east-west transportation. Water and inland transportation connect it to Beijing in the north, Guangzhou in the south, Chongqing in the west and Shanghai in the east. It is connected with nine inland provinces and coastlines.

Although there is no direct sea harbor in the Central China economic zone, the harbor at Wuhan provides passage from China's southwest and northwest regions to the ocean. In 1980s, Wuhan reopened its customs office after it had been closed for 25 years. In the following 15 years, the total value of imports and exports through Wuhan increased very rapidly, at least double the period before customs were reopened.

6. The Northwest Economic Zone

This is China's largest economic zone and includes the five provinces of Shaanxi, Gansu, Ningxia, Qinghai and Xinjiang and several autonomous regions. More than half the natural reserves in China are in this region. They include coal, iron, vanadium, titanium, nickel, molybdenum, gold, manganese, zinc, lead, aluminum, copper and so forth. In addition the area has abundant water energy, tourism potential and biological resources. High mountains and the Gobi desert make the area ideal for space and nuclear industries. Presently, this is the most backward region in China in terms of its industrial development. The region is known historically for the silk road which helped Europe and Asia establish economic links and promoted the growth of trade locally. Presently, the area is not linked to the eastern regions. However, this disadvantage will quickly change when the European-Asian continental bridge and the China-Pakistan International Highway are opened.

7. The Southwest Economic Zone

This zone includes Sichuan, Yunnan, Guizhou and Tibet. Since the 1950s, this region has constructed the following railways linking the area with central China and strengthening local transportation networks: Hunan-Guizhou, Yunnan-Guizhou, Sichuan-Guizhou, Chengdu-Kunming Baoji-Chengdu and Xiangyang-Yunnan. River navigation has expanded after lengthy reconstruction of rivers in Sichuan province. With the improvement of backward transportation conditions the potential for resource exploitation and economic development is promising.

The area has rich mineral and energy resources including the second largest iron reserve in China. Vanadium and titanium mines have not yet been fully explored. Aluminum, copper, lead, zinc, tin and mercury reserves are between 15-75% of China's total reserve, respectively. Large quantities of gold, silver and other rare metals, and significant reserves of phosphorus and salt minerals like sulphur iron and asbestos are unexplored to their full potential. The area has rich water resources, calculated at 70% of China's total exploitable water resource. It has the richest coal reserve in the Yangtze River region. It has more than half of China's natural gas reserve. This combination of rich mineral and energy resources, together with an advantageous geographic location makes this plank an ideal region for developing energy and raw material industries.

Moreover, the climate is suited to agriculture production. Crop production includes silkworm, linen, tobacco, tea, tung oil and medical herbs. Other agricultural products include live stock. The defense industry was established here in the 1960s: now this industry has, to a large extent, be converted to civil industries.

By contrast, the industrial production and technology levels of the Southwest economic zone are developed compared to neighboring Mekong countries. Underdeveloped industrial production in the Mekong provides a market for the Southwest economic zone. Therefore, the major markets for this region are south Asia, the central south peninsula and the south ocean islands. Tibet, Yunnan and Guangxi represent the major trade and investment frontier and Guizhou and Sichuan are the back up provinces. To promote and strengthen China's economic role in this region by exporting technology and products, and by opening new international trade market in the surrounding areas trade arrangements were developed, that would adjust inequitable balances of trade with other economic zones.

The formation of these seven economic zones has had a positive impact on the decentralization process in China. They are as follows:

- 1) There are deep rooted geographic, economic and historic linkages within each economic zone;
- 2) Each economic zone has a common interest in participating in the international economic system in China's economic take-off process;
- 3) Every economic zone has effective cooperation within their provinces in areas of resources, population, markets, industrial foundation and infrastructure; and,
- 4) Every economic zone has its own effective bargaining strength with the central government and other economic zones.

According to some data, these formal and informal alliances among provinces based on economic planks are getting stronger. This trend will lead to further decentralization in China.

Of course, it should be noted that the economic development level among the seven economic planks has widened in the past ten years. However, the only way to reduce this gap does not lie on the restoration of the centralized system, but in giving more autonomy to the economic zones to pursue China's multi-development economic patterns.°

Chapter III Urbanization and Regional Integration

A. Features of China's Urbanization

China was one of the first countries in the world with large urban populations. According to archaeologists' findings, as early as 3000 years ago in the Yin-Shang Dynasty, there were cities located near today's Anyang in Henan province. Historical records tell us that in the first century there were 650 thousand people living in Luoyang, then China's capital. This city was the same size as Rome, the largest city in the West at that time.³⁰ By the seventh century, the population of Changan, the capital of the Tang Dynasty, had exceeded one million. From the eighth to the eighteenth century, the growth of cities in China, in terms of scale and number, was rapid.

However, by the nineteenth century, when urbanization developed dramatically in the West, China's urban population was only 6% of its total population.³¹ Compared with the West, China's urbanization level was low at that time. Between the 1950s and 1980s, urban growth in China remained slow. And in the 20 years from 1960 to 1980, there was nearly no urban expansion. Only 20% of the population lived in urban areas in 1960, this number decreased to 19% in 1980.³² However, urbanization has developed rapidly since then.

Once urbanization began and urban administrative regions were established, China entered a mixed system of regional and urban administration. The centralized system is regionally administered. When the regional administrative system began to break down the central administrative system began to decline.

Urbanization worldwide shares many features, but China has several unique features which may be summarized as follows.

1. Concentrated Urbanization.

Fluctuations in urbanization have been observed throughout the world. China is no exception. In the early stage of industrialization and urbanization, rural populations continuously moved to cities. At this initial stage of urbanization, the cities functioned efficiently. Gradually, population and industrial concentration accelerated. Between 1978 to 1988, cities with a population of more than one million people increased from 13 to 28, a rate of 115%. The urban population increased from 30 to 57 million an increased of 91%.³³ Although China has policies restricting urban concentration it is clear that many big cities are still expanding and becoming megalopolis.

³⁰ *Patterns of the Growth of Urban Population*, UN International Economy and social Affairs Department, 1980, p.6.

³¹ Skinner, G. William: "China's Regional Urbanization in the 19th Century", in *The City in late Imperial China*, Stanford University Press, 1977, p.225.

³² *Report on China's national Conditions*, Liaoning People's Press, p.780.

³³ Idid.

2. Urbanization Levels Lag Behind Industrialization Levels

Due to China's policies controlling urban growth, urbanization lags behind industrialization when compared to other countries. The following table compares urban China with other countries.

Table III-1: Measures of China's Urbanization and Industrialization

Year	Urban Population %	Industry as % of GNP
1950	11.2	14.1
1955	13.5	22.7
1962	17.3	32.8
1965	18.0	36.4
1970	17.4	40.1
1975	17.3	44.5
1978	16.6	46.8
1980	17.8	45.8
1985	19.2	41.5

Source: *Statistics Yearbook of China*, 1986, pp. 51, 91

3. The Development of Village and Town Enterprises and the Formation of Scattered Small City Groups

Since the end of the 1970s, China's urbanization pattern has changed. It has broken away from the traditional pattern of simultaneous industrial and urban growth. Now excess rural inhabitants have moved to non-rural areas in new villages and town enterprises. Approximately 80 million rural people relocated to non-rural areas between 1978 to 1987. Non-farming laborers in rural areas increased from 11% to more than 20%.³⁴

Village and town enterprises were scattered in the beginning. Gradually they concentrated based on central government policy, specialization, coordination, coalition and efficiency. A lot of small towns were thus formed. Peasants working in village and town enterprises were the main source of this population. These enterprises became the financial foci of the area, and the main financial source for the construction of all kinds of public facilities and infrastructure in these small towns. By the end of 1987, there were 11,103 new small towns in China, which became the link between cities and wide spread rural areas. Some of them even merged with cities.

This kind of urbanization played an important role in easing the population flow between rural areas and cities:

- 1) by providing job opportunities for excess rural labor;

³⁴ Idid.

- 2) by developing the rural economy;
- 3) by increasing peasants' income; and
- 4) by speeding China's urbanization process.³⁵

4. Obvious Regional Differences in China's Urbanization

Due to China's unbalanced economic development, urbanization varies from region to region (See Table III-2).

Table III-2: The Urban Population, 1988

Province/ Municipality/ Autonomous Region	Total Population (10,000)	Share of Urban Population	Province/ Municipality / Autonomous	Total Population (10,000)	Share of Urban Population
Beijing	1,001	67.8	Henan	8,094	16.6
Tianjin	843	66.6	Hubei	5,185	39.2
Hebei	5,795	20.7	Hunan	5,890	24.1
Shanxi	2,755	25.8	Guangdong	5,028	24.3
Inner	2,094	29.1	Guangxi	4,088	17.3
Liaoning	2,373	50.4	Hainan	628	12.1
Jilin	2,373	48.1	Sichuan	10,576	17.5
Heilongjiang	3,466	43.7	Guizhou	3,127	17.3
Shanghai	1,262	53.0	Hunnan	3,594	17.3
Jiangsu	6,438	30.1	Tibet	212	9.2
Zhejiang	4,170	36.9	Shanxi	3,135	24.3
Anhui	5,377	17.7	Gansu	2,136	26.3
Fujian	2,845	17.9	Qinghai	434	17.0
Jiangxi	3,609	23.4	Ningxia	445	26.0
Shandong	8,061	37.0	Xingjiang	1,426	30.7

Source: *Statistical Yearbook of China*, 1989. China Statistics Press 1989
Urban Statistics Yearbook of China, 1989. China Statistics Press 1989.

Generally speaking, urbanization is more advanced on the east coast than in the central and western regions, because of the high level of industrialization and economic development on the east coast. But, there are cases of intense urbanization some provinces in the west where the economy is relatively backward. This suggests that there are other factors, in addition to economic factors, influencing China's urbanization.

5. The Distribution of Urban Regions is Unbalanced

Urbanization in China is not balanced. The most economically developed region, the east coast, is the region, not surprisingly, with the dense urban centers. In 1988, there were 162 cities in nine provinces on the east coast, which represents 37.4% of all cities in China located on only 13% of the land mass. Among the 162 cities, there are six "super cities"

³⁵ *Idid.*

with more than two million inhabitants, eight cities with between one and two million inhabitants and 14 cities with one-half to one million people. Compared with all of China, the "super cities" represent 67% of all "super cities", the large cities 42%, and the smaller cities 47% of the same scaled cities in China, respectively.

Compared with the nine provinces in the west which encompasses 55% of the land mass, there are 91 cities less than 21% of the country's total number of cities, and only eight have a population of more than one-half million people. To put this in perspective, on the east coast there is approximately one city every 10 sq. kms kilometers and one "super" city within every 20 thousand sq. kms; in the west, there is one city about every 60 thousand sq. kms and one large city about every 70 thousand sq. kms.³⁶

Urban density is high in central Liaoning, Beijing-Tianjin-Tangshan and Shanghai-Nanjing-Hangzhou regions. These areas are also the most industrialized parts of the country however, the distribution of cities within regions is uneven. In the Northeast Region, where urbanization is among the highest in China, urban centers are scattered. And in Liaoning province, the central part of the region has the highest urban density in China, while in its west, urban density is very low.

6. The Reasonable Trend of Urban Structuring

The term "reasonable trend of urban structuring" refers to urban growth patterns since the end of the 1970s. In essence, large-sized cities and small-sized cities have tended to develop economically, while middle-sized cities have tended to decline economically (See Tables III and IV).

Table III. Structural Change's in Populations of China's Cities, 1978-88

Scale	1978	1978	1988	1988	1978-88	1978-88	1978-88	1978-88
	Number of Cities	Pop (10,000)	Number of Cities	Pop (10,000)	Increase in Number of Cities	Increase in Pop (10,000)	Increase in Number of Cities	Increase in Pop (10,000)
Above 1 million	13	2,995	28	5725	15	2730	115.3	91.2
500,000 - 1 mil	27	1,997	30	2979	3	82	11.1	4.1
200,000 - 500,000	60	1,821	110	3321	50	1500	82.3	86.4
Below 200,000	92	1,058	266	2909	174	1824	189.1	168.1

Source: *China's Cities Statistic Yearbook*, and *The Manual of the China's Cities*.

³⁶ Idid.

Table III-4: The Change of Population Shares in Different Sized Cities

Year	Total	Above 1 Million	500,000 - 1 Million	200,000-500,000	Below 200,000
1951	100	40.0	20.4	17.0	17.6
1978	100	37.9	25.3	23.1	13.7
1988	100	40.7	14.8	23.6	20.7

Source: *China's Cities Statistics Yearbook* and *The Manual of the China's Cities*

This trend is the result of reforms in the economic system. High tech industries, large-scale modern processing industries and other new industries are concentrated in cities with a population of more than one million people because these cities provide advantageous investment opportunities. In contrast, handicraft, low-level and elementary product industries re moving to small cities and towns from middle-sized cities because these small cities have the capacity to produce these products. The result of these shifting production centers are:

- 1) the economic development of small cities ill help strengthen the economic and technological relations between large and middle-sized cities and rural regions
- 2) the expanding development of large cities will accelerate the construction of modern technology and promote China's economic development; and
- 3) Rapid development of both large cities and small cities will push the development of middle cities. Otherwise, there would be no base for developing middle-sized cities.

China has formed a pyramid city system consisting of "super large" cities as centers and small cities and towns as bases.³⁷ This structure meets current national requirements that both large and small cities be vigorously developed so as to form a reasonable urban system. By 1988, China had developed 28 "super large" cities, 30 large cities, 110 middle cities and 266 small cities. They represent 6%, 7%, 25% and 61% of China's cities, respectively. In addition, there were more than 1000 small towns. The ratio of "super" cities, to large cities to small cities to towns was 1:1.07:3.93:9.5, respectively.³⁸

B. Urbanization, Economic Centers and Decentralization

China adopted measures to make cities administrative units have jurisdiction over counties in the 1950s. Beijing and Shanghai were the first cities given this power in 1958. By the middle of the 1980s, this system was widely implemented throughout China. In 1988, there were 169 cities governing 724 counties. Among them, 22 counties were governed

³⁷ *Idid.*

³⁸ *Idid.*

by Beijing, Tianjin and Shanghai. The remaining 702 counties were governed by 166 cities. Today, there are three kinds of cities: cities directly governed by the central government; regional cities; and county cities. Most regional cities govern counties, but county cities do not have jurisdiction over counties. There were 248 county cities by the end of 1988.³⁹ It is worth noting that, from the middle of the 1980s, the central government set up some independent planning cities in major provinces like Liaoning's Shenyang and Sichuan's Chongqing. These cities exercise the same major economic autonomy as provinces do. These changes reflect the key role exercised by cities at different levels in China's urbanization process.

Once cities held the dominant position in the mixed regional administrative system and cities functioned as complete economic centers, the non-centralized governmental system began to take form. The fundamental differences between the centralized system and the non-centralized system are as follows:

- 1) the centralized system is pyramidal: the central government governs provinces, provinces govern cities (counties), counties govern towns and towns govern villages, or in reverse from the bottom to the top. The non-centralized system forms a network in which many large economic centers promote sub-level economic centers.
- 2) under a centralized system the main function of sub-level government is administrative. Under a non-centralized system the main function of cities at different levels is economic.
- 3) under a centralized system cities are restricted by the borders of the administrative region. Under a non-centralization system cities' economic radiation could exceed the restriction of regional administration.

In the 1990s, it can be seen that city economic networks were established in China (See Appendix 11).

In the Northeast Region, Shenyang is the center. Shenyang, Changchun and Harbin have formed a city group in a column. And a city group has been formed from Shenyang to Dalian in a row. In North China, the two "super" cities, Beijing and Tianjin, are only 100 kilometers apart. As they expand, they are gradually merging into one huge metropolis. In terms of economic strength, size and population this metropolis will be unique in the Asian-Pacific region as well as in the rest of the world.

In East China, Shanghai's influence radiates in all directions. It is connected with Nanjing and innumerable cities along the Yangtze River and by the Shanghai-Nanjing railway. Shanghai and Hangzhou are connected by a series of cities along the coast, and by highways and railways. Shanghai, Nanjing and Hangzhou have formed a "V"-shaped urban belt that has become the economic center of the eastern region in China.

³⁹ Zhou Zhenhe: *China's Politics and Economy*, China Press, 1990, pp.299-300.

Guangzhou is the focal city in the southern region. But Shenzhen is important because it was China's first special economic zone, and the economy is rapidly being integrated with that of Hong Kong. After 1997, when Hong Kong is returned to China, Hong Kong and Shenzhen will become another big economic metropolitan in South China (See Map III-1).

Map III-1: The Future Metropolitan of Hong Kong -- Shenzhen



Of course, Hong Kong is already an important economic center in the Asian-Pacific region: it is one of the "four small dragons" in Asia. With free open port, an all purpose international financial center and a modern information industrial base, Hong Kong's role cannot be replaced in the foreseeable future.

In Central China, Wuhan is the most important economic center because it is located at the heart of China. It is connected by the Yangtze River and railways and is the largest port on the Yangtze River. It has an extensive industrial foundation and rich scientific and technological resources. As this region's economic center, soon it will become its commercial, industrial, financial and transportation center as well.

In the Northwest, Lanzhou and Xian are the two most important economic centers because they are the thoroughfares that connect the northwest with other economic regions. And Chengdu and Chongqing in Sichuan are the two economic centers in the Southwest province of Sichuan, the most populated province in China.

The importance of these cities in China's national economy is illustrated in the following table.

Table III-5: The Role of China's Major Cities in the National Economy, 1991

Cities	Population (Million)	GNP (100 Million)	Sphere of Influence
Shenyang	8.14	185.0	Northeast+Nation
Harbin	5.27	97.8	Heilongjiangz+ Northeast
Changchun	3.79	58.4	Jilin+Northeast
Beijing	12.77	447.7	Nation
Tianjin	10.34	253.0	Nation
Shanghai	15.33	511.7	Nation
Nanjing	4.59	128.8	Southeast
Hangzhou	2.44	85.1	Zhejiang+Southeast
Guangzhou	6.49	258.6	South
Hong Kong	6.01	8,476.0	South+Nation
Wuhan	7.03	122.6	Central
Lanzhou	2.7	63.5	Ganshu+Northwest
Xian	4.72	78.9	Shannxi+Northwest
Chengdu	4.52	96.4	Southwest
Chongqing	5.25	97.4	Southwest

Source: *Statistics Yearbook of China* 1991, The Statistics Press, pp.653 - 668. The figures about HK come from *Hong Kong*, 1994, published by Chines Affairs Administration of HK

government. The GNP of HK is calculated on basis of HK dollars. China's total GNP was 1767 billion yuan in 1990, of which 259 billion yuan or about 15% was created by cities, excluding Hong Kong.⁴⁰

As mentioned before, China's rapid urbanization includes the expansion of large cities that are integrating into even larger metropolis. In this process, China's major economic cities and the decentralized system will be further developed. This development will reallocate and reconstruct economic resources horizontally, rather than in the top-down administrative structure of the past.

Development of the market and urbanization is simultaneous and mutually promoting. Market formation (capital, futures and raw materials) will eventually be connected with the division of labor among cities. In fact, this division among cities has been formed, by and large, during normal processes of urbanization and market formation in the past 10 years. For example, Shanghai is being transformed into the financial center of the East China region, perhaps even of all of China and the Asian-Pacific rim. Wuhan is becoming

⁴⁰ *Statistic Yearbook of China*, China statistics Press, 1992, p.18.

a goods collection and distribution center in the Central China region. And, as the function of Shenzhen's financial market is strengthened, Shenzhen is becoming an important place in maintaining Hong Kong's influence in international finance and trade. Historically, cities have had different industrial advantages and traditions: urbanization and market formation have strengthened these industrial advantages. Thus different economic centers developed different key industries with different features. This has promoted the formation of industrial divisions among cities.

The conclusion is obvious that urbanization has led to the emergence of regional and national economic centers. These economic centers reflect natural divisions in a market economy and the demands of industry. The fundamental feature of economic centers is that they radiate outward into the surrounding region. This radiation constitutes an economic network. This new trend does not exclude cooperation among provinces and cities under the regional administrative system, but provides a stronger backing for this kind of cooperation. In fact, regions with a strong market formation also have regional autonomous cooperation, as is illustrated in the east coast region. In another words, regions with a high density of cities are regions where non-centralized systems are mature. The typical examples are the Yangtze River Delta region and the Peal River Delta region.

In the past 40 years, China's population has doubled and the urban population has increased four times to nearly 300 million people. According to the most conservative projections, China's population will reach 1.3 billion by the year 2000 and the urban population will reach 400 million at least. The urban population will be 30% of China's total population. At this new level of urbanization, China's non-centralized economic and administrative systems will dominate. •

Chapter IV The Institutional Factors in the Process of Decentralization

A. Property Rights of Localization

Since the mid-1980s, one of the key aspects of China's economic reform has been the delegation of power from the center to local governments, provinces in particular. Such delegation has taken two forms: first, the transfer of governmental responsibilities and powers ; and second, the transfer of responsibilities from government to non-governmental organizations, i.e., to enterprises and the market. These transfers have proceeded hand in hand, providing impetus to the creation of localities and enterprises and leading to a remarkable growth of regional economies and an unprecedented expansion of non-state ownership.

A much emphasized goal in the property rights of localization is the separation of governmental responsibilities from those of enterprises. To accomplish this goal, the central government has relegated a large number of national enterprises to localities, giving up direct administration and resorting to financial and monetary measures as a means of controlling them. Against this background, the interaction between local governments and local economic activities has intensified. Local governments have increased control over, and intervention into, individual enterprises' internal affairs through a so-called "responsibility system". This system allows the local government to become the owners of the property rights and the local enterprise to become the executor of those rights. Faced with an inequitable tax structure, (state-owned enterprises are taxed more heavily than collectively or privately owned businesses) local governments are inclined to invest in non-state businesses, e.g., collective and private enterprises, in pursuit of greater profits. In turn, the expansion of the non-state sector accelerates the localization of property rights. Also this trend has personally benefited local government officials. As local enterprises take on many of the characteristics of private corporations, government officials act like members of boards of directors. This phenomenon is evident everywhere in China, but most pronounced in the coastal provinces of Guangdong, Zhejiang and Shandong.

Local governments have demonstrated the following investment patterns:

- 1) giving priority to short-term projects;
- 2) giving priority to projects being confined to the areas directly under their jurisdictions; and
- 3) giving priority to small enterprises, especially ones run by townships and villages.

There is no doubt that the property rights of localization is far from ideal, but in comparison with national ownership, it has several obvious advantages. Local governments know local market conditions and consumer needs. Their developmental goals tend to be more realistic and feasible. They are in a better position to communicate effectively with the local enterprises, clarify mutual responsibilities and make them pay

attention to environmental concerns. And they can train personnel to meet the special needs of their regional developments.

The property rights of localization has worked to accelerate the process of decentralization in the followings ways:

- 1) it strengthens the economic position of the localities *vis-à-vis* the center;
- 2) it helps shape a local identity; when local governments control their economy they go to great lengths to look after their interests; the inhabitants identify increasingly with their local government over the center, particularly in the more developed regions;
- 3) as local governments become stronger they gain legitimacy with the local population; and
- 4) cooperation among the local governments increases and regional integration deepens. In the early stages of economic reform and localization of property rights, local governments compete to grant beneficial policies to their businesses. As market conditions mature, local governments give more attention to cooperation than protection.

In short, localization of property rights has been at the core of China's economic reforms. While not a perfect solution to centralized economic control, it is a unique, unprecedented form of ownership, differing from a planned or private economic structure. Since it is impossible to find a perfect form of ownership, the most important issue should be how to minimize the various adverse effects of localized property ownership. The combination of the property rights of localization and the market economy provide prerequisites for government, the market and property ownership to function together to bring about an economic take-off, as has happened in the coastal provinces of China.

Chinese provinces can be divided into three categories according to the degree of the property rights of localization. This categorization helps clarify the correlation between localization and decentralization. The most important criterion for this categorization is the relative strength of a local government in the local GNP. The three categories are spelled out as follows:

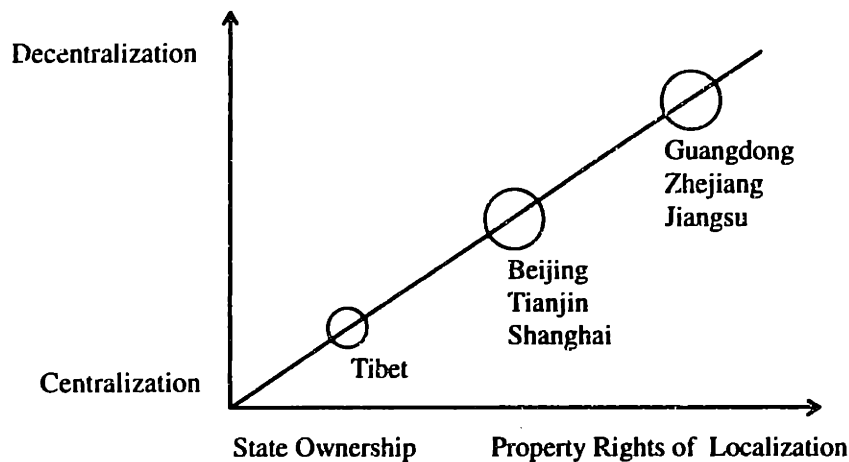
- 1) Category one: Low Level of Localization -- Local governments only influence local GNP at a modest level and, therefore, have minimum bargaining power with the central government, as is exemplified by the provinces (regions) in western China, Tibet in particular.
- 2) Category two: Intermediate Level of Localization -- Local governments have considerable economic strength with which to bargain with the center, but the center still has considerable capacity to intervene and penetrate into local economic activities,

as is exemplified by the directly-administered municipalities of Beijing, Shanghai and Tianjin.

3) Category three: High Level of Localization -- Local governments have strong economic power to bargain effectively with the center and the center has only limited influence over local economic activities.

The correlation between localization and decentralization is illustrated in Figure IV-1.

Figure IV-1: The Correlation Between Localization and Decentralization



B. The Evolution of the Ownership Structure

Before the economic reforms, state-owned enterprises dominated the national economy. Since the reforms, dramatic changes have taken place in China's ownership structure. Unlike the former Soviet Union and East European countries which witnessed an abrupt process of privatization, China has incrementally enlarged non-state portions of the national economy in step with the decrease of state-ownership. For example, in 1978 the industrial sector accounted for just over 20% of the total, but in 1991, it was close to 45%. If other economic sectors are included, the proportion of non-state businesses is even larger.

Looking at individual localities, it is not difficult to conclude that those provinces and directly-administered municipalities and regions with a high proportion of non-state businesses are closely correlated with the tendency for decentralization. The chain of cause and effect is this: a high proportion of non-state businesses leads to rapid economic growth which, in turn, gives rise to a higher degree of decentralization (See Table IV-1).

Table IV-1: The Ownership Structures of the Three Economic Regions, 1992

	State	Ownership	Non-State	Ownership
Regions	Products	% of GNP	Products	% of GNP
	(Billion RMB)		(Billion RMB)	
Eastern	787.74	57.05	592.34	42.95
Central	431.57	77.58	124.69	22.42
Western	217.86	79.64	55.68	20.36

Source: *Statistics Yearbook of China*, 1992, Beijing: China Statistics Press, 1993

As is shown in Table IV-1, the proportion of non-state businesses in the eastern region is twice as large as that of the western region, and nearly twice as large as that of the central region.

In China today, the growth of town and village enterprises (TVE) has had a direct impact on the overall condition of the non-state economy. A breakdown of the geographic distribution of TVE in Table IV-2 illustrates this point.

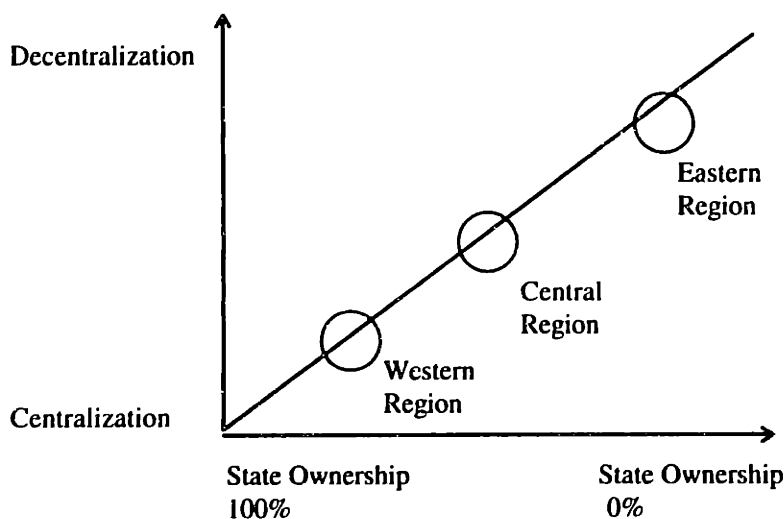
Table IV-2: The GNP Percentages of TVE Products in the Three Regions, 1992

Regions	Number of TVE Enterprises	Value of TVE Products (10,000 RMB)	% of GNP
Eastern	695.80	48,699.520	74.55
Central	509.69	11,700.844	17.91
Western	236.19	4,919.995	7.53

Source: *Statistics Yearbook of China*, 1992, Beijing: China Statistics Press, 1993

The same tendency can be demonstrated by a linear correlation (See Figure IV-2) in which the horizontal line represents the ownership structure of the national economy starting from 100% state ownership toward 0% state ownership and the vertical line represents the degrees of decentralization.

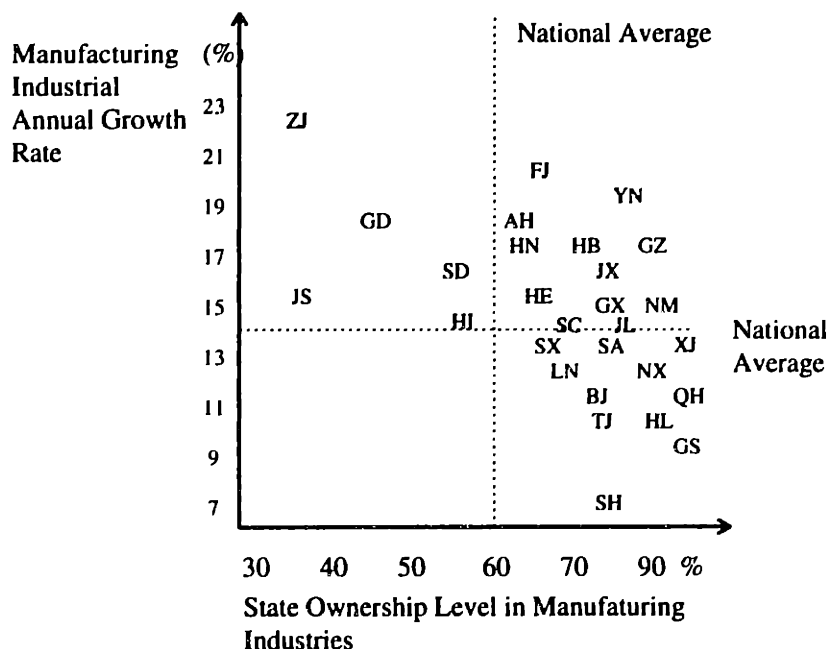
Figure IV-2: Correlation Between Ownership Structure and Decentralization



A similar conclusion was reached by the International Monetary Fund (IMF) in its research on decentralization and regional development. In a recent report, the Fund observed that in rapidly developing provinces like Zhejiang, Jiangsu, Guangdong, Fujian and Shandong the share of national ownership has declined dramatically. By 1991, the share of state enterprises in these five provinces decreased almost by half, down to 30-40%, while the share of the non-state economy activities reached the dominant position. However, such changes have hardly taken place in the western provinces. For example, in Qinghai, Guizhou, Ningxia, Inner Mongolia and Heilongjiang, the share of state enterprises shrank only by 10%, remaining above 75% of the total economy.⁴¹ Obviously, the change in the ownership structure has had a direct impact on the process of decentralization. These changes in the ownership structure at the provincial level has been dramatically since the middle 1980s (See Appendix 12).

Furthermore, a correlation between the speed of economic growth and the ownership structure can be revealed by a close examination of the various provinces in the 1980s. It can be seen that the ownership below 50% is correlated with an industrial growth rate higher than 13% (See Figure IV-3). As the following table suggests, provinces experiencing rapid economic growth are invariably among the most decentralized ones.

Figure IV-3: Correlation Between the Share of State Ownership and Industrial Growth Rate in the 1980s



Source: Marayama Nobuo: *The Economic Cycle of Southern China*. Asia Economic Research Center Press, Tokyo, 1992, pp. 34.

⁴¹ *China at the Threshold of a Market Economy*, Washington, D.C.: IMF, september, 1993, pp. 47-48

C. Fiscal System Relationships Between Central and Lower-Level Governments

A major moving force behind China's process of decentralization has been the continuous restructuring of the central-local fiscal system.

Prior to the 1980s, local governments turned over all revenues to the central government, which then distributed the financial resources back to the provinces, based on their expenditure needs as well as the fiscal condition of the central government. Since the 1980s, however, this centralized fiscal system has been restructured several times.

It was modified for the first time in 1980 when a general revenue sharing agreement was made between the center and the local governments. During the period of 1980-1984, about 80% of the local revenue was turned back to the central government: local entities retained about 20%. One drawback of this arrangement was that it benefited well-off provinces but hurt poor ones or those suffering financial losses.

Then, in 1985, the fiscal system was restructured again, and another agreement was made between the center and the provinces. This time, different proportional revenue-sharing contracts were drawn with different provinces. The center collected more revenue from wealthy provinces or directly-governed municipalities, such as Shanghai, Beijing, Tianjin, Liaoning, Jiangsu and Zhejiang, while allowing the poor provinces to retain a larger share of their revenue. This practice also had a serious disadvantage in that it hurt well-off areas.

The fiscal system was changed once again in 1988. The central government mandated a formal proportional revenue-sharing system that divided the country into six categories (See Appendix 13). This new system granted larger revenue retention rates to the localities, particularly to those that were the primary revenue-generating provinces and municipalities. This system has functioned since 1990. Without it, local governments would have lost their motivation to generate more revenue.

Since 1992, the central government has attempted to implement a separate taxation system in different localities based primarily on the US system of taxation, and has actually experimented with it in nine provinces and municipalities.

This fiscal restructuring has resulted in a reduction in the importance of the central government, measured either in terms of central government revenue or expenditures as a percent of GDP (See Appendix 14). At the same time, the role of the central government relative to local governments also declined.

It is important to note that since the late 1970s, as economic reform accelerated, the proportion of extra-budgetary governmental revenues increased dramatically compared to budgetary governmental revenues (Table IV-3).⁴²

Table IV - 3: China - Governmental Budgetary Revenue and National Extra-Budgetary Revenue, 1978-1990

Year	Budgetary Revenue (100 Million RMB)	Extra-Budgetary	Revenue
		Amount (100 Million RMB)	As % of Budgetary Revenue
1978	1,121.12	347.11	31.0
1979	1,067.96	452.85	42.4
1980	1,042.22	557.40	53.5
1981	1,016.38	601.07	59.1
1982	1,083.94	802.74	74.1
1983	1,211.16	967.68	79.9
1984	1,467.05	1,188.48	81.0
1985	1,837.16	1,530.03	83.3
1986	2,184.52	1,757.31	79.5
1987	2,262.42	2,028.80	89.7
1988	2,489.41	2,270.00	91.2
1989	2,803.81	2,658.83	94.8
1990	3,134.34	2,708.64	86.4

Source: *Statistics Yearbook of China*, 1992, Beijing: China Statistic Press, 1993, pp. 228. The governmental budgetary revenue does not include foreign borrowings.

As Table IV-4 illustrates, the share of extra-budgetary revenue almost tripled against that of budgetary revenue during the period of 1978-90. This suggests that central fiscal control has weakened dramatically.

In addition, an examination of sources of governmental revenue reveal a decrease in the percentage of state ownership in the national economy as compared with the corresponding increase of non-state ownership (See Table IV-4).

Table IV-4: China - Sources of Government Revenue, 1978-1987

YEAR	Fiscal Income (100 Mil RMB)	State	Owned	Non-state	Owned
		Amount (100 Million RMB)	%	Amount (100 Million RMB)	%
1978	1,121.1	973.65	86.85	147.45	13.15
1979	1,103.3	923.62	83.71	179.27	16.29

⁴² Extra-budgetary funds refer to those which, not included in the governmental budgets, are raised directly by individual work units, primarily through taxation, revenue retention, and toll collection, and which the work units are entitled to expend at will.

1980	1,085.2	889.58	81.97	195.42	18.03
1981	1,089.5	858.05	78.76	231.45	21.24
1982	1,124.0	884.47	78.69	239.53	21.31
1983	1,249.0	969.85	77.65	279.15	22.35
1984	1,501.9	1,156.85	77.03	345.05	22.97
1985	1,866.4	1,314.81	70.45	551.52	29.55
1986	2,260.3	1,685.49	74.57	574.71	25.43
1987	2,368.9	1,690.25	71.35	678.65	28.65

Source: *China's Statistics Yearbook*, 1992, Beijing: China Statistic Press, 1993.
According to an estimate, between 1987-94, revenue from non-state enterprises had risen to 50% of the total governmental revenue.

As is known to all, the growth of the non-state economy is a driving force behind China's process of decentralization as well as a major feature of that same process.

In a word, against the background of economic reform and marketization, the Chinese fiscal system has undergone some fundamental changes. Such changes may appear to be merely a matter of different sharing arrangements between the center and the localities but, in fact, they reflect an irreversible trend toward decentralization. History has proved that the new revenue-sharing system has provided strong incentives for the development of the regional economies, thus constituting a major driving force behind the economic take-off of China in the 1990s.

D. The Outward Orientation

During the past 15 years, China has opened herself up in virtual every aspect, in order to integrate its economy gradually with the world system. (See Appendix 15). Significantly, this process has gone hand in hand with the process of decentralization. An outward-oriented economy is reflected in the following three major aspects:

- 1) the share of foreign trade in the GNP or the GDP;
- 2) the share of direct foreign investment in the total capital investment; and
- 3) the share of foreign-run enterprises, joint ventures, and foreign-assisted enterprises in the GNP.

Among the thirty provincial-level regions, those which are strong in the above three aspects are all inclined toward greater decentralization; conversely, those which are weak in the three aspects tend to support the old centralized system. Let us look at the three aspects more closely.

1. The Share of Trade

Examples are selected mainly from the eastern, central, and western regions (Table IV-5).

Table IV-5: The Share of Exports in the GNP in the Eastern, Central, and Western Regions, 1992

Regions	GNP (Billion RMB)	Imports & Exports (Billion RMB)	% of GNP
Eastern	220.21	42.50	19.30
Central	104.39	7.43	7.11
Western	53.59	3.49	6.51

Sources: *Statistics Yearbook of China, 1992*, Beijing: China Statistic Press, 1993, pp. 18; *Almanac of China's Foreign Economic Relations and Trade*, pp. 1023

* the average exchange rate in 1992:100 USD to 532 RMB.

It should be pointed out that amid the economic reform, the rapid growth of the township and village enterprises (TVE) is closely related with the rise of the volume of China's export (See Table IV-6).

Table IV-6: TVE Exports by Province, 1987 and 1989

Area	Total (mil.)	Export (RMB)	Percentage of	National Total
	1987	1989	1987	1989
National	16,195.77	37144.33	100	100
Beijing	496.86	1,081.75	3.1	2.9
Tianjin	789.63	2,042.95	4.9	5.5
Hebei	770.62	1,404.29	4.8	3.8
Shanxi	120.98	373.97	0.7	1.0
I. Mongolia	240.50	51.29	1.5	0.1
Liaoning	600.02	1,766.59	3.7	4.8
Jilin	46.40	123.38	0.3	0.3
Heilongjiang	74.62	192.90	0.5	0.5
Shanghai	2,190.51	4,702.78	13.5	12.7
Jiangsu	3,253.22	7,857.27	20.1	21.2
Zhejiang	1,647.99	4,462.95	10.2	12.0
Anhui	102.71	270.71	0.6	0.7
Fujian	652.19	1,755.45	4.0	4.7
Jiangxi	158.66	276.41	0.9	0.7
Shandong	1,090.32	3,378.49	6.7	9.1
Henan	225.80	747.47	1.4	2.0
Hubei	278.22	688.94	1.7	1.9
Hunan	371.98	706.56	2.3	1.9
Guangdong	2,489.50	3,881.45	15.4	10.5
Guangxi	161.46	216.11	1.0	0.6
Hainan	N/A	5.15	N/A	0.01
Sichuan	412.59	750.17	2.5	2.0
Guizhou	47.18	80.80	0.3	0.2
Yunnan	60.21	110.41	0.4	0.3
Tibet	N/A	N/A	N/A	N/A
Shaanxi	36.75	67.33	0.2	0.2
Gansu	30.09	59.92	0.2	0.1
Qinghai	9.32	46.11	0.05	0.1
Ningxia	15.53	19.78	0.09	0.05
Xinjiang	8.36	22.96	0.05	0.06

Source: 1987 data: *Township and Village Enterprises Yearbook 1978-1987*.
1989 data: *Township and Village enterprises Yearbook 1989*.

Table IV-6 indicates clearly that Guangdong, Shandong, Jiangsu, Shanghai and Fujian are the provinces/municipality where township and village enterprises prosper most. A the

same time, these are the places where the share of the TVE products is the highest in the foreign trade. furthermore, the same conclusion is reached when samples are collected from counties whose foreign trade volume has surpassed 100 million yuan. In 1992, there were 197 such counties across China, of which 42 were in Jiangsu, 34 in Zhejiang, 34 in Shandong and 28 in Guangdong, accounting for 70% of the total (See Table IV-7).

Table IV-7: Numbers of Counties Whose Export Volume Surpassed 100 Million RMB in 1992

Province	Number	Province	Number
Beijing	11	Jiangsu	42
Tianjin	8	Zhejiang	34
Shanghai	9	Fujian	6
Hebei	9	Henan	2
Liaoning	2	Hubei	8
Jilin	3	Hunan	2
Shandong	34	Guangdong	28

Source: *Almanac of China's Foreign Economic Relations and Trade*, pp.1023

The above table demonstrates that decentralization, the open economy and non-state ownership are positively interrelated.

2. Geographic Distribution Pattern of Direct Foreign Investments

The geographic pattern of direct foreign investment is illustrated in Tables IV-8 and IV-9 below.

Table IV-8: Geographical Structure of Direct Foreign Investment, 1992

Area	Total (10,000)	Utilization (US Dollar)	Loan Foreign	From Countries	Foreign Investment	Direct and Others
	Amount	% of Total	Amount	% of Total	Amount	% of Total
National	1,305,937	100	205,218	100	1,100,719	100
Beijing	36,159	2.8	1174	0.6	34,985	3.2
Tianjin	26,259	2.0	15,481	7.5	10,778	1.0
Hebei	11,309	0.9	n/a	n/a	11,309	1.0
Shanxi	5,384	0.4	n/a	n/a	5,384	0.5
I. Mongolia	828	0.1	308	0.1	520	...
Liaoning	68,012	5.2	16,370	8.0	51,642	4.7
Jilin	7,534	0.6	n/a	n/a	7,534	0.7
Heilongjiang	7,269	0.6	52	...	7,217	0.7
Shanghai	89,929	6.9	40,568	19.8	49,361	4.5
Jiangsu	146,324	11.2	n/a	n/a	146,324	13.3
Zhejiang	27,664	2.1	3,686	1.8	23,978	2.2
Anhui	5,466	0.4	n/a	n/a	5,466	0.5
Fujian	146,561	11.2	4,197	2.0	142,364	12.9
Jiangxi	12,179	0.9	2,207	1.1	9,972	0.9
Shandong	102,685	7.9	2,343	1.1	100,342	9.1
Henan	5,316	0.4	n/a	n/a	5,316	0.5
Hubei	21,057	1.6	744	0.4	20,313	1.8
Hunan	13,521	1.0	250	0.1	13,271	1.2
Guangdong	474,641	36.3	104,530	50.9	370,111	33.6
Guangxi	19,881	1.5	1,680	0.8	18,201	11.6
Hainan	51,480	3.9	6,225	3.0	45,255	4.1

Sichuan	11,214	0.8	n/a	n/a	11,214	1.0
Guizhou	1,979	0.1	n/a	n/a	1,979	0.2
Yunan	2,875	0.2	n/a	n/a	2,875	0.3
Shaanxi	4,553	0.3	n/a	n/a	4,553	0.4
Gansu	35	...	n/a	n/a	35	...
Ningxia	352	...	n/a	n/a	352	...
Qinghai	68	...	n/a	n/a	68	...
Xingjiang	5,403	0.4	5,403	2.6	n/a	n/a

Source: *Almanac of China's Investment*, 1993. China Financial Press 1994. pp.559

Table IV-9: Geographical Distribution Pattern of DFI Projects, 1979-1992

Region\Project	Contracted Project	Percentage as of Nation	Contracted Foreign Capital (100 Million USD)	Percentage as of Nation
Coastal Area				
Subtotal	77,319	85.16	941.56	85.24
Beijing	3,761	4.14	36.84	3.34
Tianjin	2,616	2.88	20.28	1.84
Hebei	2,084	2.30	22.45	2.03
Liaoning	3,861	4.25	39.25	3.55
Shanghai	3,304	3.64	63.63	5.76
Jiangsu	10,113	11.14	89.33	8.09
Zhejiang	3,705	4.08	36.59	3.31
Fujian	8,080	8.90	111.81	10.12
Shandong	5,856	6.45	54.90	4.97
Guangxi	1,951	2.15	17.55	1.59
Hainan	3,368	3.71	33.21	3.01
Guangdong	28,620	31.52	415.72	37.63
Inland Areas	12,454	13.72	99.92	9.05
Ministries	1,018	1.12	63.14	5.71

Source: *Almanac of China's Investment*, 1993. China Financial Press 1994. pp.23

The above two tables make it amply clear that the coastal open areas (provinces, municipalities, and regions) occupy the dominant place in terms of geographic distribution and number of projects. In Table IV-9, Beijing, Tianjin, Shanghai, Shandong, Jiangsu, Zhejiang, Fujian and Guangdong account for nearly 80% of the national total of direct foreign investment in 1992. In Table IV-10, the same localities account for 65% of the national total number of foreign investment projects during the period of 1979-92. Significantly, those coastal provinces and municipalities, best exemplified by Guangdong, are the major supporters for decentralization.⁴³

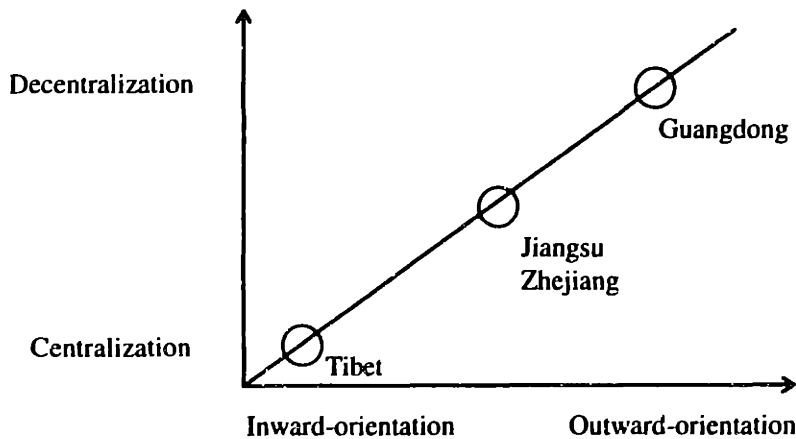
⁴³ Guangdong is cited as the primary example by the IMF in its research on China's decentralization. According to its findings, in 1990 Guangdong accounted for one third of the national total of Foreign investment, and contributed to one fifth of the national exports. See *China at the Threshold of a Market Economy*, Washington, D.C.: IMF, September 1993.

As a matter of fact, the reason for this phenomenon is very simple. Centralization has to be sustained by exercising tight control over budgetary revenues of localities, but the opening up and influx of foreign investment provide the localities with alternative sources of revenues and capital. As a result, the localities dependence on the center is weakened, thus giving a further impetus to decentralization.

3. The Place of Foreign-owned Enterprises, Joint Ventures, and Foreign-Assisted Enterprises in Regional Economies

It is only logical and amply clear that because the eastern coastal region is in a better position to attract foreign investment, foreign-owned enterprises, joint ventures and foreign-assisted enterprises multiply and prosper there. Statistics indicate clearly the following features: First, foreign-related enterprises register a higher rate in productivity, per capita profit generating, and foreign currency earning than their domestic counterparts. Second, foreign-related enterprises grow more rapidly in terms of percentage of the local GNP, the local industrial GNP in particular, than their domestic counterparts. Third, foreign-related enterprises require a shorter investment/construction cycle than their domestic counterparts. These three features are illustrated in Figure IV-4 below.

Figure IV-4: Interrelationship Between an Outward-Oriented Economy and Decentralization



Chapter V Regionalization and Neighboring Countries

A. Historical Review of the Relationship Between China and Neighboring Countries

China, the United States and Russia are the larger sized nations in term both territory and population. However, China has complicated relations with its numerous neighbors compared to other large countries. The United States and Canada enjoy much simpler relations and have fewer neighbors. Even Russia is better off than China, although the number of its neighbors has multiplied following the breakup of Russia, because it has virtually no neighbors to the north.

China's land boundary of over 20,000 kms borders 16 countries, which are, from east to west, Korea, Russia, Mongolia, Kazakhstan, Kyrgyzstan, Tadjikistan, Afghanistan, Pakistan, India, Sikkim, Nepal, Bhutan, Bangladesh, Burma, Laos and Vietnam. The coastline is more than 18,400 kms long, with the Philippines and Malaysia, among others, as close neighbors.

In its long history, international relations between China and its neighbors has been rather primitive compared to Europe. For the most part China followed a policy of isolationism with the exception of neighbors to the north with which they constantly fought. This was particularly true during the Ming and Qing Dynasties, up to the Opium Wars in the middle of the nineteen century. These two dynasties, pursued an absurd policy of "closing off the sea". Nevertheless, there was a remarkable exception to this general pattern, which was during the "Silk Road" era, a references to the times when commercial trade was active between Asia and Europe along the north-south "Silk Road". The most prosperous international trade of this type occurred in he Tang dynasty.

From the late 1870s up to the late 1940s, China followed an "Open-door" policy. Under this policy, trade was opened to western industrialized countries and Japan. Little trade occurred with neighboring countries because those countries were economically even worse off than China.

When the communist regime was established in 1949 and for the ensuing 30 years, China followed an extreme form of the "close-door" policy. The policy was carried out in the name of promoting self-reliance and building "an independent and self-integrated national economic system,". During these 30 years of isolation, China was characterized by a combination of centralization, totalitarianism, planned economy and a closed socio-economic system. Against this general background, China only managed to maintain a minimal trade with its neighbors punctuated by occasional military conflicts. For example, from the early 1960s to the late 1970s, China had military border confrontations with the former Soviet Union, India and Vietnam.

Not until the 1980's did China's economic exchange with its neighbors gain momentum. Since then, those bordering provinces or regions have had a dual economic identity. On

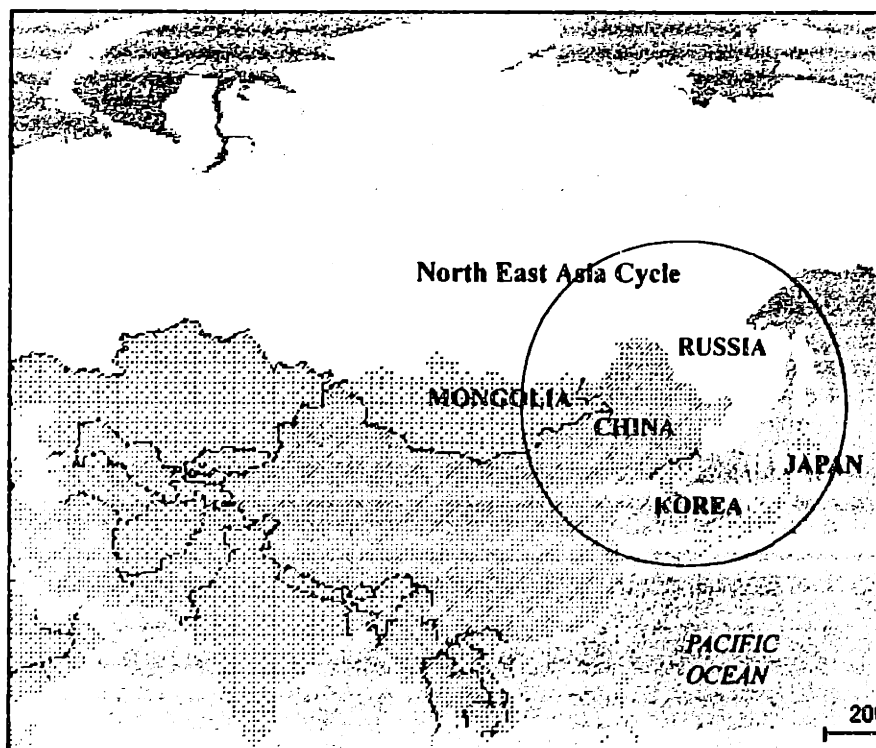
the one hand, they are part of China and its economic system; on the other hand, they have become part of cross-border economic zones. At present, five such zones deserve particular attention:

- 1) the one between the three northeastern provinces of China and Northeast Asia;
- 2) the one between China's northwestern economic region (Xingjiang in particular) and the Muslim neighboring countries to the west;
- 3) the one between China's southwestern economic region and Burma and the three Indo-China countries;
- 4) the one between China's southeastern economic region and those countries in the South China Sea (also called the South China Sea economic cooperative zone); and
- 5) the one between the Shandong peninsula and South Korea (also called the Yellow Sea economic cooperative zone).

B. Northeast China and Northeast Asia

Northeast Asia is geographically defined as the area lying between 38 and 60 degrees north latitude and 120 and 150 degrees east longitude. It covers north Russia (primarily Siberia), Japan, the Korean peninsula and the Chinese northeastern provinces of Heilongjiang, Jilin and Liaoning and part of Inner Mongolia (See Map V-1).

Map V-1: Northeast Asia

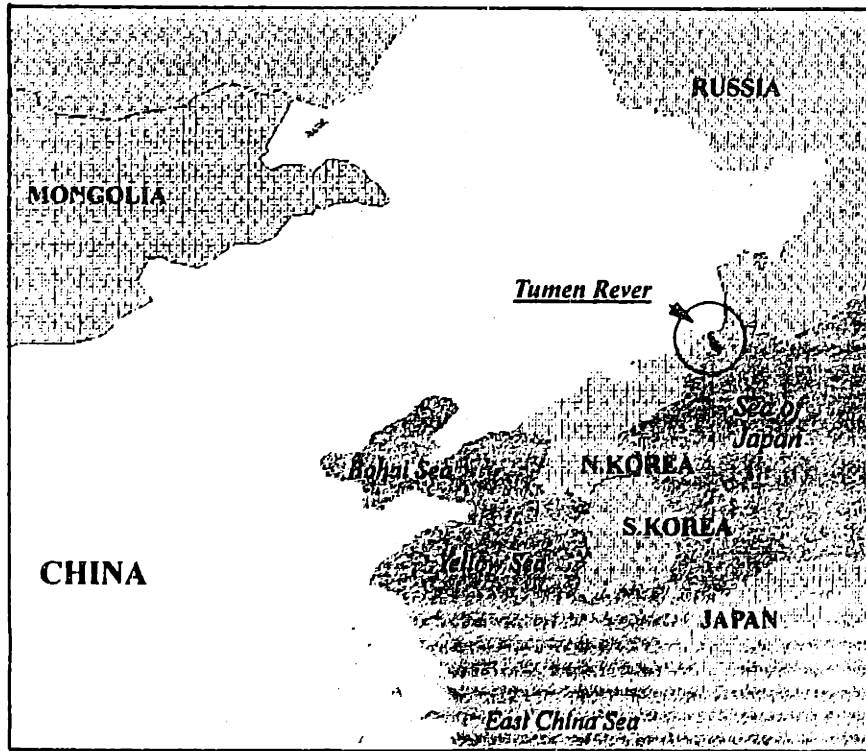


The major natural resources and economic strengths of Northeast Asia are as follows:

- 1) solid industrial infrastructure, which is mainly in Japan, South Korea and the three Chinese northeastern provinces;
- 2) rich natural resources, which lie primarily in Siberia and the three Chinese northeastern provinces;
- 3) abundant human resources, which lie primarily in the three Chinese northeastern provinces;
- 4) great market potential, which lie primarily in the three Chinese northeastern provinces, Japan and South Korea; and
- 5) well-developed ocean, land and air transportation infrastructure.

This economic cooperative zone is linked by the sea of Japan, which also connects it to the northwest Pacific.⁴⁴ China hopes to open the Tumen River directly into the sea (See Map V-2). To accomplish this goal, China has to negotiate with North Korea and Russia which flank the river upstream. Once the river has an outlet into the sea, the three Chinese provinces can ship their natural resources directly to the northwest Pacific through the sea of Japan all the way to the west coast of North America.

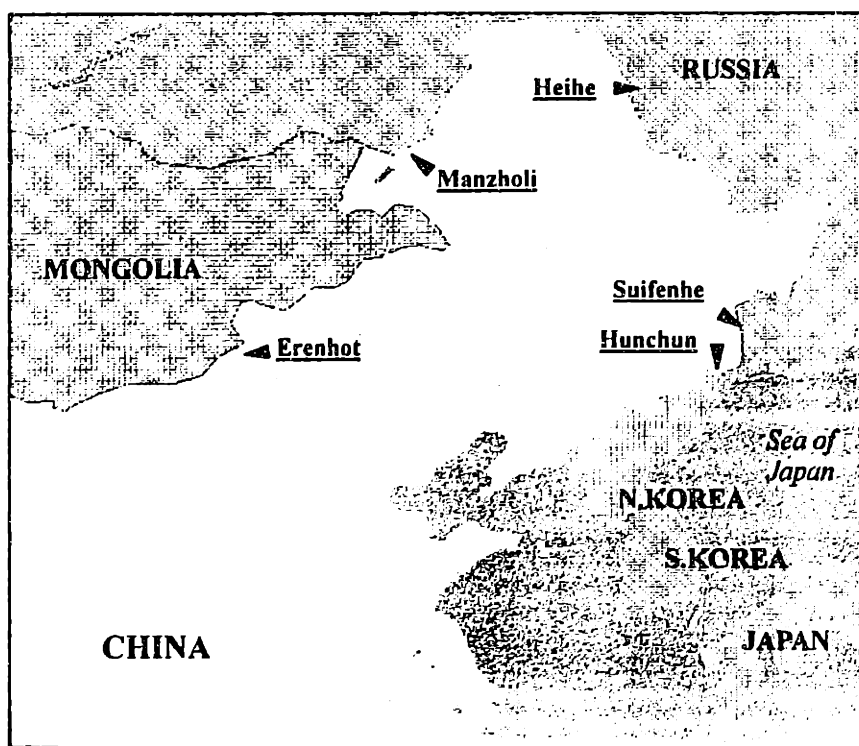
MAP V-2: The Tumen River in Northeast China



⁴⁴ A heated debate took place during the symposium The Project of Northwest Pacific hosted by the United Nations in the spring of 1994 and attended by representatives of Japan, S. Korean, China, and Russia. The S. Korean representatives insisted that the name of Sea Japan be changed to East Sea, while the Japanese representatives objected adamantly. It is unlikely that this debate will be resolved anytime soon.

Presently, exchanges between the three Chinese provinces and North Asia include trade (conventional and barter), mutually investment and exploration of each other's natural resources. These forms of economic cooperation became possible only after border cities in these three Chinese provinces were opened in early 1992. The cities opened for trade were Huihe and Suifenhe of Heilongjiang province, Huichun of Jilin province and Manchuria of Inner Mongolia. In the summer of the same year, another decision was made by the central government to open Erenhot city (See Map V-3). These border cities form a geographically well distributed network of outlets, supported by economic production from Haziwan and Changchun. This network has given a great impetus to the economic exchange between China and Russia.

MAP V-3: The Five Open Border Cities In Northeast China



The trade is complementary to the needs and production of both countries. Russia needs light industrial products, edible oil, foodstuffs, textiles and livestock. China needs steel, lumber, machinery, coal, natural gas, oil, cement, chemical fertilizers and other construction materials. Furthermore, Russia is short of laborers for construction, mining and lumbering, which China can supply in abundant numbers. Since the Sino-Russian border trade is based on barter, both sides can save a great deal of much-needed hard currencies. In addition, the three Chinese northeastern provinces are well situated to participate in the various exploratory projects for natural resources in Siberia, which are now being undertaken by Japan and South Korea.

The creation of this economic cooperative zone is attracting direct investment by the Japanese and South Koreans in the three Chinese provinces. In 1992, South Korea ranked

number two in terms of the amount of direct investment in Jilin province, surpassed only by Hong Kong and followed by the United States and Japan.⁴⁵ South Korea again ranked second in investments in Heilongjiang, with Japan taking sixth place.⁴⁶ In Liaoning, both South Korea and Japan are among the top five foreign investors.⁴⁷

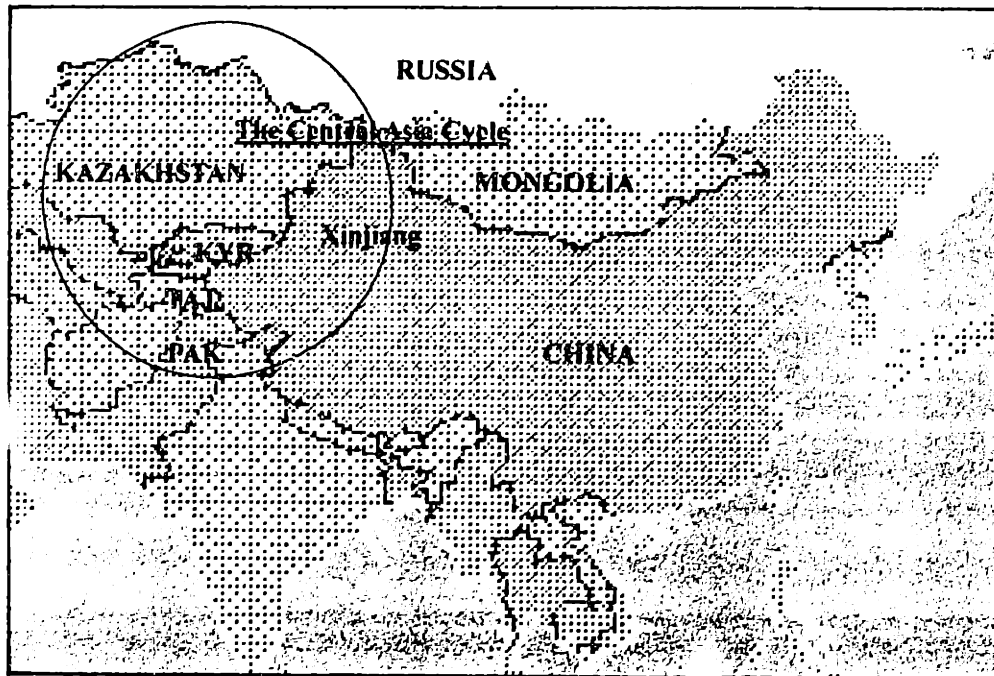
It is obvious that China's northeastern economic block and the neighboring countries in Northeast Asia will own a mutually complementary, integrated cross-border economic system based on a set of well-recognized regional interests.

C. Northwest China and its Muslim Neighbors

This economic cooperative zone covers in area lying between 35 and 50 degrees north latitude and between 60 and 95 degrees east longitude, encompassing Kazakhstan, Kyrgyzstan, Tadjikistan, Afghanistan and Pakistan. As the heartland of Eurasian economic prosperity, this economic zone is blessed with an abundance of natural resources and a high level of economic development.

The Chinese western economic block is, in reality, the Xingjiang Autonomous Region, which accounts for one sixth of China's total territory. This economic zone can be connected with the Indian Ocean through several ports (See Map V-4).

Map V-4: The Central Asia



⁴⁵ China Investment Yearbook, 1993, China Financial Press, 1994, p. 135.

⁴⁶ Idid. p. 141.

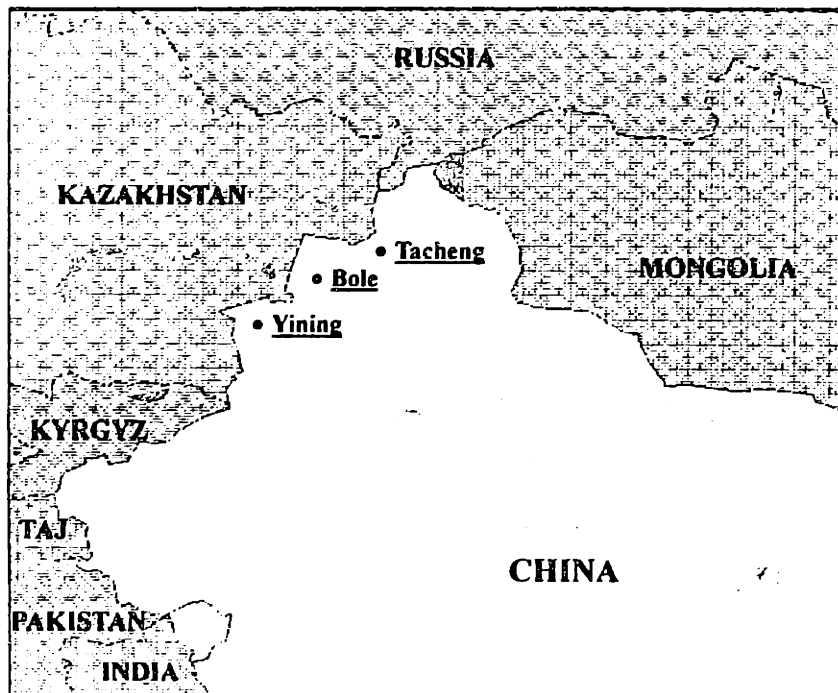
⁴⁷ Idid. p. 123.

Here again, the economic needs are complementary.

- 1) China enjoys some superiority in industrial processing of textiles, machinery and hardware as well as in technology in general, so it can export both processed industrial products and technologies to its Muslim neighbors.
- 2) China has an abundant labor supply and the Muslim neighbors have a Shortage.
- 3) the Muslim countries are rich in agricultural products and natural resources, which are in demand in northwest China.

In the northwest, Xingjiang is the only region which has direct access to neighboring countries. It lies at the center of the Eurasian land bridge, which opened in the 1990s. Kashi and the Pamirs are connected by the Sino-Pakistan international highway to Karachi, thus connecting China's northwest region with the Indian Ocean. Moreover, Xingjiang has several open metropolitan, including Urumqi, and three exit ports (Yining, Bole and Tacheng), which have placed Xingjiang strategically in a good position to expand international trade. As a result, Xingjiang is the frontier of this economic block See Map V-5).⁴⁸

Map V-5: The Major Opening Cities in Xingjiang Province



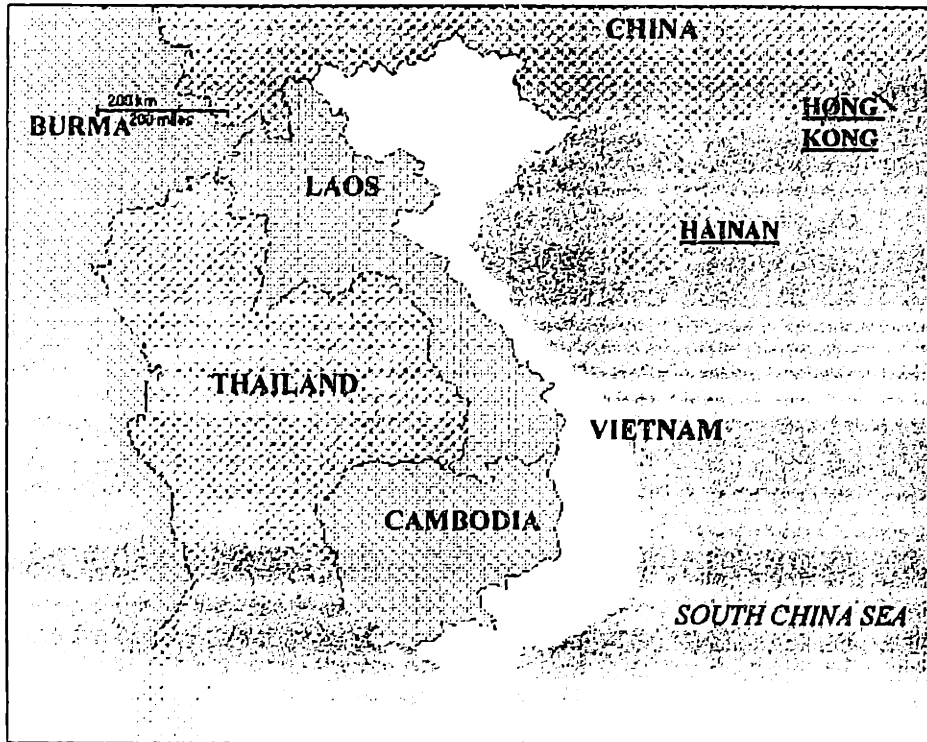
Beyond the economic perspective, this area has a deep-rooted Muslim cultural heritage, which cannot but help integrate and solidify economic cooperation in this region.

⁴⁸ The opening up of these metropolises and cities was sanctioned by the State Council document issued in June of 1992.

D. Southwest China and Mekong Countries

This economic zone is defined geographically as an area between 10 and 30 degrees north latitude and between 95 and 110 degrees east longitude. It encompasses Yunnan, Guizhou, Sichuan and parts of Guangxi in China and neighboring countries such as Burma, Laos, Cambodia and Vietnam. And Thailand has come to have direct impact on this economic zone. Since the end of the "Cold War", this economic zone has undergone the most remarkable economic recovery and development in Asia.(See Map V-6).

MAP V-6: The Southwest China and Mekong Countries



Economically, the economic zone is characterized by the following features:

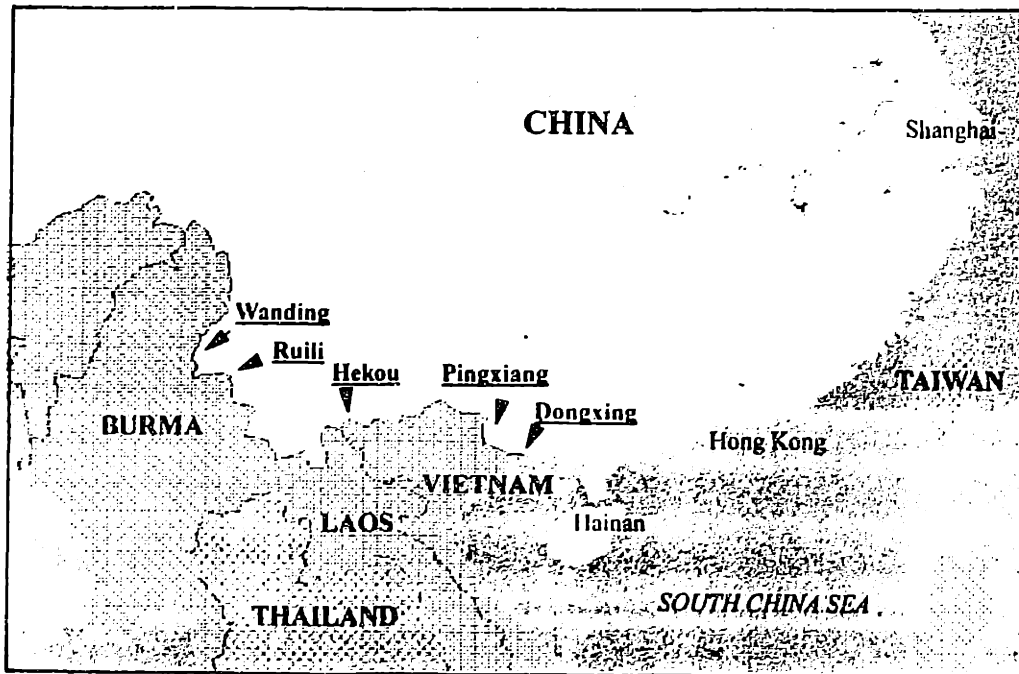
- 1) abundant natural resources;
- 2) ideal climatic conditions for agriculture;
- 3) abundant, low-cost labor
- 4) excellent river transportation provided by the Mekong River; and
- 5) excellent opportunities or capital investment.

Complimentary economic opportunities can be easily identified between China's southwestern region and Burma and the three Indo-China countries. China can benefit in three ways.

- 1) the stresses created by the serious bottlenecks in the transportation system of this region can be alleviated by trading with neighboring countries and gaining access to the Indian Ocean and South China Sea.
- 2) China enjoys considerable advantages in industrial production and technology over its southern neighbors. Exports of these industrial products will facilitate the industrialization of the southwestern economic block.
- 3) China can import from these neighboring countries much-needed agricultural products and raw industrial materials, which will facilitate the structural rationalization of the southwestern economic block and promote its processing industry.

The economic center of open trade is located at Kunming in Yunnan province, with Ruili, Wanding, Hekou and some other cities serving as border ports. In the Guangxi Zhuang Autonomous Region, a similar center is located in Xining, with Pingxiang and some other cities serving as border ports (See Map V-7).

MAP V-7: The Major Open Cities in Yunan Province of Southwest China



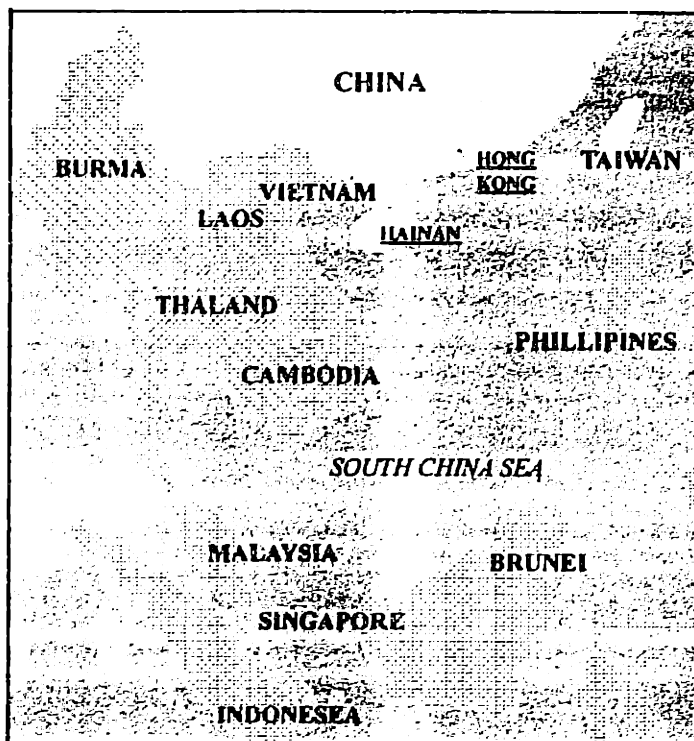
From the perspective of the neighboring countries, China is no doubt their largest trading partner and largest market or their primary products. Furthermore, with the strengthening of its economic power, China will surely become a major investor in this area.

In sum, the economic, social and ethnic ties between China's southwestern region and the neighboring countries can be traced far back into history. So the opening of this Chinese region and the full-scale economic recovery of Indochina will inevitable help the economic cooperative zone develop even more rapidly.

E. Southeast China and the South China Sea Economic Zone

As a part of Southeast Asia, the South China Sea economic zone is located between 50 and 25 degrees north latitude and 110 and 125 degrees east longitude. The countries and regions lying on the rim of the South China Sea include: mainland China (Fujian, Guangdong, Hainan and parts of Guangxi), Hong Kong, Taiwan, Vietnam, Singapore, Malaysia, Indonesia, Brunei and the Philippines (See Map V-8).

MAP V-8: The Economic Cycle in South China Sea



Since the 1960s, this economic zone has seen some of the fastest growing economies in the world, and has been the model for miraculous economic take-off globally. For instance, three of the "Four Dragons" in Southeast Asia. Taiwan, Hong Kong and Singapore completed their economic take-off during the 1960s and the 1970s. Guangdong province of China began its economic take-off during the late 1980s. Around the beginning of the 1990s, Fujian province of China, Vietnam, Malaysia and Indonesia entered their stage of high-speed economic growth. The mid-1990s are also witnessing economic take-off in Hainan of China and the Philippines. Globally speaking, most of the newly-industrialized countries and regions are concentrated in this economic zone.

This economic zone has well-educated, technically trained population and economic resources, as can be illustrated by Table V-1 below.

Table V-1: Distribution of Economic Strengths in the South China Sea Economic Zone, 1992

Countries/ Regions	Surface (sq. 1000 km)	Population (10,000)	GNP (Billion USD)	Growth Rate of GNP (%)	Per Capita GNP (USD)	Foreign currency reserves (Billion USD)
China:						
Fujian	120.00	3.08	27.28	28.90	886.00	n/a
Guangdong	180.00	6.44	96.84	30.70	1.50	n/a
Hainan	34.00	674.00	2.55	22.40	330.00	n/a
Guangxi	230.00	4.32	20.16	26.90	466.00	n/a
Hong Kong	1.10	589.00	91.40	5.20	15.75	n/a
Taiwan	38.00	2.10	210.50	6.10	10.21	n/a
Vietnam	329.00	589.00	n/a	8.30	n/a	82.30
Singapore	0.60	276.00	48.80	5.80	15.03	39.40
Malaysia	330.00	1.83	54.30	8.00	2.97	19.40
Indonesia	1909.0	18.78	120.20	6.50	645.00	10.40
Brunei	6.00	23.00	3.40	n/a	13.66	n/a
Philippines	300.00	6.23	52.90	6.00	835.00	4.8
Total/Avera	1568.7	2193.78	728.33	n/a	n/a	156.30

Sources: *Statistics Yearbook of China*, 1993, Economic Management Press, 1994, pp. 443-494; *The Economic Atlas 1989*, pp. 232-247. IMF, *International Financial Statistics*, March 1993; The Taiwan Economic Construction Association and the Taiwan Economic Council, *International Economic Information Weekly*, issue no. 977, April 1, 1993; Asian Development Bank, *Asian Development Outlook, 1993*, pp. 62-129.
The exchange rate is based on the average of 1992: 100 US dollars = 551.49 RMB

An important development in the South China Sea economic zone is the discovery of rich deposits of oil and natural gas in the continental shelf, extending into the Gulf of Tonkin and to the offshore areas of the Mekong Delta, as well as in the continental shelf of Indonesia and Brunei. Right now, the South China Sea has become a hot spot for oil exploration and, unfortunately, led to territorial disputes over rights to the Spratley Islands.

In the South China Sea economic zone, Hong Kong plays a pivotal economic role for a number of reasons:⁴⁹

⁴⁹ Currently the future of Hong Kong after its reversion to China is being widely debated and worried about, but it surpasses the scope of this study.

- 1) Hong Kong enjoys tremendous geographic advantages, being adjacent to China, occupying a strategic position for ocean transportation between the Pacific and the Indian Ocean and boasting an excellent deep-water seaport -- Port Victoria, which, unfrozen all the year round, is one of the three best ports in the world. Furthermore, Hong Kong is an economic center and axis for trade in the Asian Pacific area.
- 2) Hong Kong has free trade and a free port. Depending on world trade for survival and development, it had no choice but to open itself completely to the world market. Hong Kong is actively engaged in international exchanges of commodities, energy, technology and information -- all without any protective tariffs or barriers. Even more remarkable, as an "unguarded" free port market, Hong Kong is open in a wide scope of economic activities, unlike some other free ports, free trade zones or special economic zones, where usually only a few sectors are open. In Hong Kong, virtually every sector is open and anybody, regardless of nationality, is free to legally invest, open a business and enjoy equal tax benefits.
- 3) Hong Kong can provide all the transportation and communication facilities and other conveniences to access their financial market with the international financial system. It operates as the principal financial center for the Asian-Pacific area, being one leg of a tripod together with New York and London. Due to the time differences among the three places, the world financial market can remain open around the clock.

Another development worth close attention in this economic region, is the growing economic ties between the four southeastern provinces of China and Hong Kong and Taiwan. Since the beginning of the 1990s, Taiwan has played an increasingly important role in the economic development of the southeastern economic block of China through direct and indirect trade and direct investment (See Table V-2).

Table V-2: Trade Between Taiwan and China

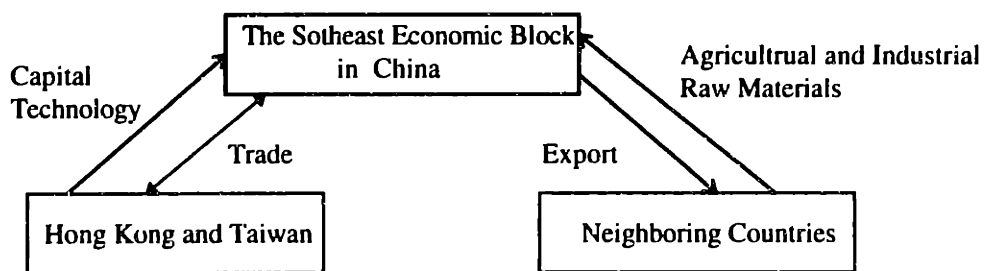
	Taiwan to	China	China to	Taiwan
Year	Amount	% Growth	Amount	% Growth
1978	0.2		218.9	
1979	106.5	5315.0	279.2	27.5
1980	1205.4	1031.8	390.3	39.9
1981	2182.3	81.0	426.6	9.2
1982	1,263.9	-42.1	546.1	28.0
1983	1,226.5	-3.0	698.3	27.9
1984	3,327.5	171.3	998.7	43.0
1985	7,697.3	131.3	904.0	-9.5
1986	6,328.4	-17.8	1124.9	24.4
1987	9,556.9	51.2	2253.7	100.3
1988	17,489.3	82.8	3773.8	65.7
1989	22,592.6	29.2	4577.8	22.6
1990	25,570.4	13.2	5969.8	30.4
1991	36,403.8	42.4	8782.3	47.1
1992	49,046.0	34.7	8782.0	-0.6

Source: Census and Statistical Department, Hong Kong.
 Edited by Gerrit W. Gong and Bih-jaw Lin: *Sino-American
 Relation at a Time of Change*. Taipei pp.223.

In 1991, Taiwan ranked as the fourth largest investor in mainland China, but in 1992, it was second, surpassed only by Hong Kong and followed by the United States and Japan. By acting as the transit station, Hong Kong plays an indispensable role in the Taiwan-China economic exchange. According to statistics issued by the Hong Kong government, in 1984 indirect cross-strait trade via Hong Kong amounted to 500 million US dollars; in 1986, the volume rose to 9.5 million US dollars, or 7.4 billion HK dollars. In 1987, China's exports to Taiwan via Hong Kong were worth 289 million US dollars, or 2.3 billion HK dollars, while Taiwan's exports to China via Hong Kong were worth 1.2 billion US dollars, or 9.6 billion HK dollars, with the total two-way volume at 1.5 billion US dollars, or 11.8 billion HK dollars. In 1989, China's exports to Taiwan via Hong Kong were worth 587 million US dollars, or 4.6 billion HK dollars, while Taiwan's exports to China via Hong Kong were worth 2.9 billion US dollars, or 22.6 billion HK dollars, with the total two-way volume at 3.5 billion US dollars, or 27.2 billion HK dollars. In these three years, the total value of the exports increased by 2.7 times.⁵⁰

Obviously, the Chinese southeastern economic block has to depend on cooperation with Hong Kong, Taiwan and the other neighboring countries in the area in order to modernize its own industrial structure, explore and expand its world trade and complete its transformation to an export-oriented economy. This interrelationship is illustrated in Figure V-1 below.

Figure V-1: Economic Cooperative Relations Among the Chinese Southeastern Economic Block, Hong Kong, Taiwan and the Other Neighboring Countries



Politically, the increasingly close economic ties within the South China Sea economic zone will pull China's southeastern economic block further away from the rest of China, thus driving forward the process of decentralization. If this economic zone continues to play a

⁵⁰ *Hong Kong Review of Overseas Trade in 1989*, Table, 23. According to *Almanac of China's Foreign Economic Relations and Trade 1993/1994*: In 1989, the volume of the indirect cross-strait trade via Hong Kong to 7 billion US dollars, of which 6 billion US dollars was from Taiwan to China with 1 billion US dollars going the other way (pp. 403).

leading role in the Asian and global economy then the development of China's
southeastern economic block will take on unusual historical significance.°

Chapter VI How Economic Integration of China, Taiwan and Hong Kong Has Contributed to China's Decentralization

A. Integration Between the Three Chinas Over the Last Two Decades

The picture of China's decentralization will not be complete without examining the process of economic integration between China, Hong Kong and Taiwan.

The process of economic integration between Hong Kong and China, Guangdong and the Pearl River Delta in particular, got under way in the early 1980s. The same process between Taiwan and China, centered in Fujian province, did not start until 1987, when the Taiwanese government officially lifted the ban on non-governmental exchanges across the Straits.

Nevertheless, many political and legal barriers still exist, and so much of the cross-strait economic exchange has to go through Hong Kong, hence the so-called "trilateral economic interdependence". Since the beginning of the 90s, the trilateral economic exchange has expanded dramatically.

The role of Hong Kong in this trilateral interaction can be specified in three aspects.

- 1) Hong Kong is the largest trading partner of China. The volume of the Hong Kong and China trade grew at a rate of 9% in the 1960s, 21% in the 1970s and over 40% in the 1980s. Between 1978 and 1988, the volume increased nearly 20 times. For China, Hong Kong is by far the most important transit port; for Hong Kong, China is its largest source of transit exports. In 1988, for example, China accounted for 84% of such exports by Hong Kong to the outside world. Moreover, China is also the largest market for Hong Kong's transit trade, accounting for 35% of the total volume.⁵¹
- 2) Hong Kong has transferred its labor-intensive technologies to China, beginning in the Pearl River Delta (town and village enterprises in particular) and moving to the Yangtze Delta and beyond. This has enabled Hong Kong to reduce labor costs enhance its competitiveness internationally and expand its trade further into inland China.
- 3) Hong Kong is the largest foreign investor in China, as is shown in Table VI-1. The Hong Kong investment has facilitated China's participation in the international economic division of labor and transformation to an export-oriented economy.

⁵¹ Yang Qi (ed.), *A General survey of Hong Kong*, Hong Kong: Sanlian Press, 1993, pp. 281-286.

Table VI-1: The Top Ten Foreign Investors in China, 1979-1992

Country or region	Number of Contracts	Foreign Investment (\$ 100 Million)	As a % of total investment	Country or region	Number of Contracts	Foreign Investment (\$ 100 Million)	As a % of total investment
Hong Kong	61,078	208.42	60.8	France	242	4.61	1.3
Japan	3,694	38.79	11.3	Singapore	1,371	4.41	1.3
U. S.	5,269	31.74	9.3	Macao	2,201	4.00	1.2
Taiwan	10,034	19.17	5.6	Britain	268	3.57	1.0
Germany	249	4.71	1.4	Australia	541	2.28	0.7

Source: *China's Investment Yearbook, 1993*, Beijing: China Financial Press, 1994, p. 20.

- 4) Hong Kong is the most important and steady source of hard currencies for China. At present China suffers a trade deficit with the Western developed countries, and yet it enjoys a trade surplus with Hong Kong. In 1986, the surplus was 2.9 billion US dollars; in 1987, 3.8 billion US dollars; in 1988, 2.9 billion US dollars; and in 1989, 6.4 billion US dollars.⁵²
- 5) As a fully-developed international financial center, Hong Kong offers a convenient place for China to raise capital from abroad. Since 1993, Chinese enterprises have sold their stocks in the Hong Kong securities market. As of August 1994, a total of 11 Chinese enterprises, including the Tsingtao Brewery, have issued stocks in Hong Kong, with a total market capitalization at close to 20 billion HK dollars (See Table VI-2).

Table VI-2: Chinese Companies and Their Market Capitalization in the Hong Kong Stock Market

Company Name	Listing Date	Issue price in HK \$	Closing price at Oct. 25, 1994	Market capit'n Oct 25, 1994 HK \$ Million
Tsingtao Brewery	July 17, 1993	2.80	5.6	1,942.36
Shanghai Petrochemical	July 26, 1993	1.58	2.5	4,200.00
Beiren Printing Machinery	August 6, 1993	2.08	3.525	352.50
Guangzhou Shipyard	August 6, 1993	2.08	3.875	609.92
Maanshan Iron & Steel	Nov 3, 1993	2.27	2.4	4,159.03
Kunming Machine Tool	Dec 7, 1993	1.98	3.2	208.00
Yizheng Chemical Fibre	March 29, 1994	2.38	2.925	2,925.00
Tianjin Bohai Chemical	May 17, 1994	1.20	1.26	428.40
Dongfang Electrical	June 6, 1994	2.83	4.25	722.50
Luoyang Glass	July 8, 1994	3.65	4.125	1,031.25
Qingling Motors	August 17, 1994	3.07	3.125	3,062.50

Source: *FT Statistics, Hong Kong*

⁵² *Idid.* p.286.

- 6) the flow of capital between Hong Kong and China has taken numerous forms. What is striking, is that capital from China has begun to play an increasingly significant role in the Hong Kong economy, and to have an impact on the economic prosperity of Hong Kong. Capital flows serve as an important link between China, Hong Kong and the rest of the world.⁵³
- 7) Hong Kong serves as an indispensable transit center in the Taiwan-China trade.
- 8) Hong Kong is a hot spot for Taiwanese investment. As of 1989, Taiwan had invested more than US dollars 2 billion in Hong Kong.⁵⁴ Between January and October of 1993, Taiwan exported US dollars 15 billion to Hong Kong, making it the largest recipient for Taiwan's capital exports.⁵⁵ This flow of Taiwanese capital into Hong Kong is partially motivated in hope of further strengthening economic ties with China.

Now, let us turn to an examination of the role of Taiwan in the trilateral economic integration. As mentioned previously, Taiwan is becoming rapidly a major trading partner with China.

- 1) since the beginning of the 1990s, China and Taiwan have been each other's fastest growing trading partner.
- 2) since 1993, Taiwan has been the second largest overseas investor in China. Because it has long enjoyed a trade surplus in international trade, Taiwan now has a huge foreign exchange reserve so it can invest extensively in China, thus helping China to restructure its industry, create more jobs and export more products.
- 3) Taiwan is trying to become the center of operation of multinational corporations in the Asian-Pacific area. No matter how successful these efforts will be, Taiwan's economic weight in this area will continue to rise.
- 4) Taiwan is in a position to offer lessons in management and administration which are suitable to Chinese conditions.
- 5) Taiwan is a major source of advanced scientific knowledge and technologies for China.

Next, let us look at the role of China in the three-way economic integration.

- 1) Since 1985, mainland China has been the largest trading partner of Hong Kong accounting for the largest share of its imports and its transit trade and for the second largest share of its exports.
- 2) China has always been the principal supplier to Hong Kong of foodstuffs, fresh water, construction materials, coal, raw materials and intermediate goods at

⁵³ The top Chinese capital groups operating in Hong Kong are: Zhongyin, Huarun, Zhoushangju, Zhong'u, Zhongxing, Guangda, Yuehai, and Huamin.

⁵⁴ Yang Qi (ed.), *A General Survey of Hong Kong*, Hong Kong Sanlian Press, 1993, pp.281-286.

⁵⁵ The Economic Investment Review committee, *The Republic of China Statistics Monthly*, October, 1993.

advantages rates. This has enabled Hong Kong manufacturers to maintain low costs and gain competitiveness in the international market.

- 3) China supplies inexpensive labor for Hong Kong processing industries and receives, in exchange, labor-intensive technologies from Hong Kong. The Pearl River Delta has become the major processing base for many of these products, enabling Hong Kong to restructure its industry and become more technology-intensive.
- 4) while rapidly becoming a major trading partner with Taiwan by exporting foodstuffs, raw materials and semi-finished products, China also promises to become the largest market for Taiwan's exports.
- 5) China is becoming a major processing base for Taiwanese products, due to its large labor supply and land resources.
- 6) the two economies complement each other in that compared to Taiwan, China is strong in primary products and production of raw materials but weak in machinery, consumer goods, service industries (finance, commerce, trading, etc.) and transportation and communications. In these aspects, Taiwan is in an excellent position to offer assistance with capital, technologies and skills. Moreover, China possesses a remarkable pool of talent in science and technology, and if it can be combined with the one Taiwan has, then both sides can elevate their places internationally in economics, science and technology.

In sum, China, Hong Kong and Taiwan are clearly undergoing a process of economic integration characterized by ever greater economic interdependence. Bilateral and trilateral trade has taken up an increasingly important place in the GNPs of the parties involved. Direct bilateral or trilateral investment represents an increasing share in their overseas investments. Bilateral, trilateral and joint ventures and cooperative projects have increased both in numbers and in importance in their respective GNPs.

B. Patterns of Integration Between the Three Chinas

The trilateral economic integration of China, Hong Kong and Taiwan has attracted widespread attention nationally and in the international community. In the past several years many scenarios have been proposed about the form this integration should take. They include the following:

- 1) "the Chinese International Community", or "the Chinese economic community";⁵⁶
- 2) "the Chinese Sphere";⁵⁷

⁵⁶ Huang Zhilian, *The 203 years of the United States of American*, Vol. II, Hong Kong: Zhongli Press, 1980, p.924.

⁵⁷ Wen Yong, *The future of the Asian-Pacific area and the chinese sphere: a visit with professor Chen Kunyao*, *Jingji daobao*, No. 2047, November 30, 1987, Hong Kong.

- 3) "the Greater China Common Market";⁵⁸
- 4) "the Chinese Economic Area";⁵⁹
- 5) "the Asian Chinese Common Market";⁶⁰
- 6) "the South China Economic Area";⁶¹
- 7) "the Natural Economic Zone of Hong Kong, Taiwan and Mainland China";⁶² and
- 8) "the Chinese Economic Cooperative System".⁶³

All the suggested names reflect approval of the trilateral integrating process.

According to the historical experience, economic integration has followed one of five forms:

- 1) a free trade zone, where no internal tariffs are levied;
- 2) a tariff consortium, under which no internal tariffs are levied and external tariffs are unified;
- 3) a common market, where production elements are circulated freely;
- 4) an economic consortium, under which unified policies are exercised in monetary, financial and other affairs; and
- 5) a complete economic integration, in which unified economic policies are exercised.

When it comes to the trilateral integration of China, Hong Kong and Taiwan, the most feasible arrangement is to start with a free trade zone. Hong Kong and Macao will be returned to China July 1, 1997, and December 1999, respectively. Both will become special administrative zones of the People's Republic of China, thus making it feasible to turn them into free trade zones with mainland China. Furthermore, as bilateral relations between China and Taiwan improve on all levels, this will also become a possible *modus operandi*.

Internationally, trilateral integration is attracting attention. In April 1993, the World Bank and the International Monetary Fund issued a joint report stating that China, Taiwan and Hong Kong would be treated as a single economic unit (regardless of political differences) called the Chinese Economic Area (CEA). It predicted that in ten years the CEA would rival Germany, Japan and the United States, and become a fourth economic pole in the global economy.

⁵⁸ Zheng Zhuyuan, *The Design of the Great China Common Market*, Hong Kong Daily, June 13, 1988.

⁵⁹ Gao Xijun, *How Should Chinese Face the Economic Blocks?* Yuanjian, Taipei, October 15, 1988.

⁶⁰ Idid.

⁶¹ *The South China Economic Area*, 1992.

⁶² Fu Dongchen, *The New economic Territory of the Greater china*, China Times Weekly, January 5-7, 1992.

⁶³ It was suggested during the Symposium on the Chinese Economic Cooperative System, held in January, 1992, reported by the Xinhua Hong Kong Agency, on January 21 and 22, 1992.

This projection was based on three factors. First, the total volume of imports of the CEA was almost two-thirds that of Japan and, at current growth rates, would surpass Japan in 2002. Second, China's GDP should be smaller than is alleged according to current official exchange rates. Even so, by 2002 the actual GDP of the CEA will far exceed the present GDP of France, England and Italy (members of the G-7), and will be four times that of India, or that of all the members of the former Soviet Union put together.⁶⁴

Moreover, according to 1992 GATT statistics, the foreign trade volume of the CEA was about US dollars 560 billion, or 7% of the world total, equaling that of Japan, which ranked third. The Taiwanese government even predicted in 1993 that their international trade would probably surpass that of Japan by the end of the year.⁶⁵ It is even estimated that if mainland China's official GDP reflects true value, the GDP of the CEA will have a high probability of surpassing that of the United States, thus becoming number one in the world. Nonetheless, one should not forget that for a rather long time to come, the economic and political systems of the three parties will remain vastly different, thus setting some limits to the trilateral integration.

Realistically speaking, trilateral integration, in the short term, will continue to be based on the principles of complementary production needs, circulation of production elements, exchange of tariff benefits and mutually beneficial cooperation. The business community will play the leading role, with governments playing an assisting part in the process of economic integration. As the process develops, a unified Chinese trade zone will become more and more likely. One example of how this zone might operate would be to follow the structure of the free trade treaty signed between Argentina and Brazil a few years ago. This agreement identified several industries that would be open for free trade. Another example of this approach was the formation of a steel consortium prior to the formation of the European Common Market. This tactic minimized economic repercussions during the integration process

Absence major political conflicts, the economic integration between mainland China and Taiwan will probably develop in stages. In the first and current stage, individuals will cooperate on mutually beneficial schemes. In the second stage, collective actions will be taken by industries and businesses. Production elements will freely circulate and reciprocal tariffs will be granted. In the third stage, the same groups will unite to promote mutual benefits. And in the fourth stage, government free trade agreements will be ratified establishing a free trade zone, tariff consortiums and eventually a common market.

C. Trilateral Economic Integration and Decentralization

Trilateral economic integration will weaken further the centralized system of China. Geographically, trilateral integration primarily involves the coastal region in the southeast. As stated previously, Taiwan's and Hong Kong's foreign investment is concentrated in the

⁶⁴ Lianhe Bao, Taiwan, April 17, 1993.

⁶⁵ Idid. April 19, 1993.

coastal provinces. Linguistically and culturally there are historical ties between the mainland and the two islands. In a sense, integration is already occurring naturally and spontaneously, apart from international economic and political actions. This integration is creating a gigantic economy, as is illustrated in the following table.

Table VI-3: Economic Strength of Fujian, Guangdong, Taiwan, Hong Kong and Hainan

	Surface (sq.km)	Populati on (10,000)	GNP (bln USD)	Foreign trade (bln USD)	Growth rate of GNP 1981-90
Fujian	120	3,074	272.8	65.75	
Hainan	34	674	25.5	12.86	
Guangdon	180	6,439	968.4	657.48	
Hong Kong	1.1	589	914	1,650	7.2
Taiwan	38	2,100	2,105	1,187	8.5
Total	373.1	12,891	4,285.7	3,573.09	

Sources: *China Statistics Yearbook, 1993*, Beijing: Economic Management Press, 1994, pp. 436-432, 478-479, 489; Asian Development Bank, *Asian Development Outlook, 1993*, pp. 62, 80; and the Taiwan Economic Construction Committee and the Taiwan Economy Council, *International Economy Weekly*, No. 997, April 1 (1993). The exchange rate is based on the Chinese official rate of 1992: 100 US dollars = 551.45 RMB.

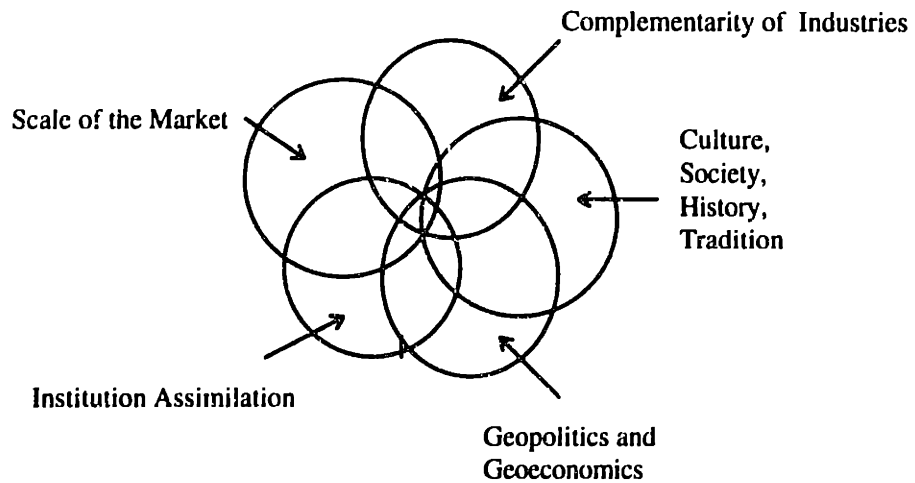
From the table above, it is clear that this Chinese economic area is formidable. It has surpassed the GNP of Brazil, which was US dollars 38 billion 1989.⁶⁶ It earns 42% of the GNP of China and accounts for 216% of the volume of Chinese foreign trade.⁶⁷ And it is continuing to grow at a faster rate than the rest of China, so it will be even more important in the Chinese economy in the future.

Finally, trilateral economic integration is accelerating the movement of the Chinese economy away from the center, and defining a new economic system. Chinese economic reform has been uneven: the coastal regions, Fujian, Guangdong and Hainan in particular, opened up, and moved to non-state ownership and the market economy faster than the rest of the country. As a result, the *de facto* economic system of this area is similar to that of Hong Kong and Taiwan, reinforcing their economic cohesion. This has intensified the centrifugal force within the economic cooperative zone and its centripetal tendency away from the centralized system, as is illustrated in Figure VI-1 below.

⁶⁶ The Central Intelligence agency, *The World Factbook*, 1990, p.46.

⁶⁷ In 1992, China's GNP was 5,584 billion yuan, which, at the exchange rate of 100 US dollars= 551 yuan, equaled 1,012 billion US dollars. In the same year, China's total volume of foreign trade was 165.61 US dollars.

Figure VI-1: Integrative Forces Among Fujian, Guangdong, Taiwan, Hong Kong and Hainan



Historically, the movement of economic activities to the South has been going on for over a thousand years, but only in the past century has the South been decidedly more developed economically than the North. With trilateral economic integration, Fujian, Guangdong, Taiwan and Hong Kong are becoming pivotal in China's economy. This development is more modestly reflected in the economic rise of the Yangtze Delta. All these developments will positively impact on China's process of decentralization. •

Chapter VII The Impact of Western Industrial Countries on China's Decentralization

A. The Impact of Foreign Direct Investment

Prior to 1979, when the policy of economic reform and opening up was adopted, historical, political and ideological reasons kept direct foreign investment (DFI) in China at a minimum. During the 1950s, DFI came, in the form of restricted technical cooperation and technology transfer, from the former Soviet Union and the East European countries. During the 1960s, the relations between China and the former Soviet Union deteriorated to the extent that the former Soviet Union withdrew all its technical advisors from China. China then received technical assistance from West European, Japan, but on a limited scale. As of 1987, the total volume of DFI was only US dollars 6.4 billion.⁶⁸

Since 1979, China has become the largest recipient of DFI among the developing countries. By the end of 1992, the total number of approved DFI projects was 90,791 with a value of US dollars 34.4 billion (See Figure VII-1).

Table VII-1: Foreign Investment in China
(\$ 100 Million)

Year	Foreign Commitment	Actual Foreign Investment
1979-82	60.12	11.68
1983	17.31	6.35
1984	26.50	12.58
1985	59.31	20.30
1986	28.34	18.75
1987	37.09	23.14
1988	52.97	31.94
1989	56.00	33.93
1990	65.67	34.14
1991	119.77	43.66
1992	581.24	110.08

Source: *Investment in China*, the China Business Press, 1993.

It is obvious that DFI had a big jump in 1992 in China, this can be illustrated in Appendix 15. The impact of DFI on the Chinese economy is evident, as is reflected in the following aspect.

- 1) DFI has compensated for China's shortage of capital. In 1992, for example, US dollar 11 billion of DFI came into China, accounting for 10% of the national total of fixed-asset capital investment.⁶⁹

⁶⁸ "World Bank Discussion Paper", No.130, 1991, p.7.

⁶⁹ *China Investment Yearbook*, 1993, the China financial Press, 1994, pp.24-26.

- 2) DFI brought new advanced technology, equipment and management skills into China.
- 3) DFI boosted China's export. In 1992, for example, foreign-invested companies in China exported a total of US dollars 17.4 billion, representing a 44% increase over the prior years and accounting for more than 20% of the national total volume of exports.⁷⁰
- 4) DFI enhanced the economic efficiency of indigenous enterprises.

In addition, DFI contributed to the progress of decentralization, in that it is concentrated overwhelmingly in the east coast open region, as has been discussed in section D of chapter IV. The world bank wrote about the role of DFI in China as follows.

“The geographical pattern of DFI in China is largely reflective of the government’s open-door policy which has been implemented gradually. In the early years of reform (i.e., 1979-82), the government solicited DFI in the four SEZs (late expanded to five) which were regarded as ‘experimental labs’ as well as windows for obtaining capital and modern technology and promoting exports. SEZs offered a more developed infrastructure, minimal controls by the government and tax incentives which made a big difference, compared to the rest of the country. During 1983-85, 14 coastal cities and three deltas along the east coast were also opened up for DFI, and the government issued new regulations in 1986/87 to encourage DFI. This was followed by the ‘gold coast’ development campaign of 1988. At the same time, the bulk of the investment that came from Hong Kong and Taiwan was directed mainly to Fujian and Guangdong provinces because of proximity and ethnic ties; although in later years other coastal cities were also significant beneficiaries of such investment. All the above factors led to DFI’s concentration in the SEZs and coastal cities. Such investment also had a spillover effect as adjacent non-SEZs learned from SEZs, and created attractive investment atmosphere for contractual joint venture.”⁷¹

It should be pointed out, that DFI has been largely responsible for the capital used for the development of the five special economic zones, the 14 coastal open cities, the 27 economic and technology development zones, as well as for the development of the other open economic systems composed of coastal or border cities.⁷² This development will further decentralization.

Under the planned economy, political centralization was clearly based on the center's monopoly of investment capital. After the reform, the center and localities were entitled to separate shares of fiscal revenues and the localities have some investment capital at their disposal. Nevertheless, the amount of revenue and capital that the localities can count on is unstable and inadequate, for the central government is still in a position to

⁷⁰ *China Investment Yearbook, 1993*, China Financial Press, 1994, pp. 24-26.

⁷¹ “*World Bank Discussion Paper*”, No. 130, 1991, pp.19.

⁷² Idid.

reduce the amount by tax rates in its favor. Therefore, only DFI can provide a stable source of investment capital which is totally free from control by the center.

An analysis of China's sources of investment capital for 1985-1992 reveals that DFI was among the fastest-growing sources (See Table VII-2).

TABLE VII-2. China's sources of investment 1985-92 (billion RMB)

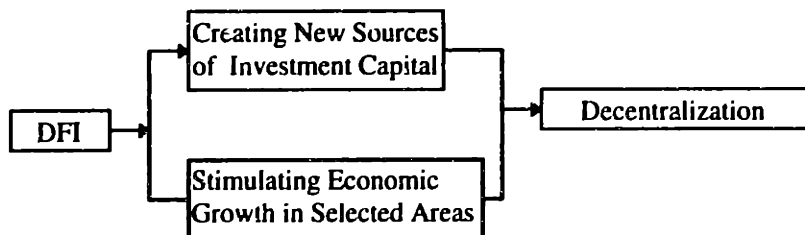
Source	1985	1988	1989	1990	1991	1992
Budgetary	40.78	41.001	34.162	38.765	37.295	33.42
Domestic loans	51.027	92.668	71.636	87.088	129.21	215.20
Foreign	9.148	25.899	27.415	27.826	31.627	45.714
Non-budgetary	153.36	290.08	235.55	232.94	287.86	402.46
Others			45.09	58.301	64.879	88.699

Source: *China Investment Yearbook*, 1993, The China Financial Press, 1994, pp 604

For the period covered in the above table, the share of state budgetary investment declined by 18 %, domestic loans increased by 302% and non-budgetary investments increased by 220%.⁷³

From a macro economic perspective, the impact of DFI on China's decentralization can be understood in Figure VII-1:

Figure VII-1: DFI and Its Impacts On Decentralization



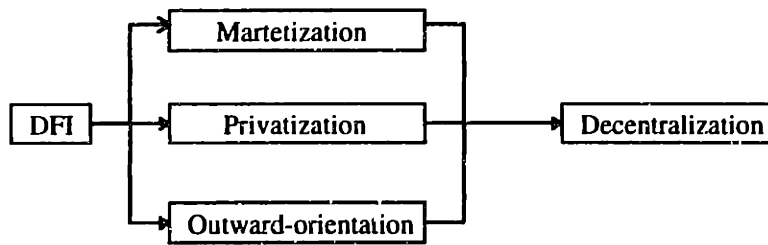
Take Guangdong for example. The province is the top recipient of DFI in the country. In 1992, the total fixed-asset investment of Guangdong was 92.2 billion yuan, whereas the total DFI was US dollars 3.7 billion, or 20,424 billion yuan at the exchange rate at the time, accounting for 22% of the total.⁷⁴ No wonder that Guangdong is the vanguard province in China's process of decentralization.

On a systematic level, the impact of DFI on China's decentralization can be understood in the following Figure VII-2:

⁷³ "Foreign investment" here include both DFI and loans. During 1979-1992, the total DFI was 110.46 billion US dollars, or 58% of total foreign investment, which was 191.1 billion US dollars for the same period.

⁷⁴ *China Investment Yearbook*, 1993, the China Financial Press, 1994, pp.223, 599.

Figure VII-2: DFI's Influence On Institutions and Decentralization



China's marketization for the past 15 years germinated in the Special Economic Zones and then extended to the 14 coastal cities and the rest of the coastal region and the entire country. DFI was the primary mover for this process and the most important media through which the contemporary world market economic system penetrated the Chinese economy.

B. GATT, China's Market Economy and Decentralization

Since July 1986, China has been negotiating to restore its membership in the General Agreement of Tariffs and Trade (GATT).⁷⁵ Eight years have passed since then, and China is very close to achieving its goal.

China's re-entry into GATT will have a profound impact on its economy. GATT is based on the principles of the market economy and international free trade. Once China becomes a member of GATT, it will be committed irrevocably to the market economy and free trade. This will require some restructuring of the current economic system.

- 1) to give full play to market-based pricing mechanisms, China must remove various arbitrary rates and differentials in its pricing system to make it compatible with international market pricing practices, and give up all projectionist measures based on tariffs and exchange rates.
- 2) it must rationalize its tax policy and reform its tax system to conform with international conventions. All businesses, whether owned by the state, collectivizes or individuals or by Chinese or foreigners, must be subject to a uniform tax code. Moreover, tax rates should be reduced and the tax base enlarged so that the tax burden on businesses and production costs can be reduced.
- 3) to restructure its foreign trade system to conform with both domestic and international markets, China must abolish the monopoly off stage-owned import and export companies. They should be turned into independent

⁷⁵ China was a founding member of the GATT, but since the founding the People's Republic of China its membership has been suspended. Since the mid of the 1970's, China has reestablished relations with the GATT. On July 10, 1986, the Chinese government officially submitted to the GATT secretary general its application to restore its membership. In March of 1987, the GATT board of director set up a special work team to review China's application. As of now, more than the teams has met more than ten times.

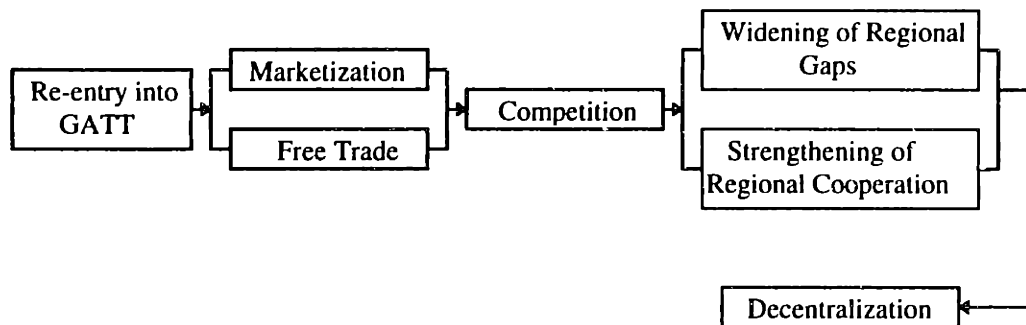
entities, and other enterprises should be given the right to trade internationally. China must also make its domestic market more compatible with the international market.

If these measures are taken, Chinese enterprises will be forced into the fierce competition in the world market and subjected to the brutal test of survival of the fittest. This challenge requires complete privatization of enterprises and a clear definition of ownership. It also means reorganization and mergers to form more competitive business conglomerations. The latter is necessary to overcome the weaknesses of capital shortage, technological backwardness, low productivity, low added value of products and slow technological upgrading.

These developments will intensify decentralization in China, for the following reasons:

- 1) the coastal provinces of China will benefit most from the re-entry into GATT cause they already have considerable experience in international market competition and are further along in the transition toward an outward-oriented economy and marketization.
- 2) most enterprises with clearly-defined ownership and an outward orientation relocated along the coastal, open area. They are capable of adapting to international standard practices, while the vast majority of the inland enterprises still have great difficulty moving away from the old practices under the centralized system.
- 3) the advantageous position of the coastal area will attract production businesses away from inland provinces. How these factors interact and affect decentralization is shown in the following Figure VII-3.

Figure VII-3: The Relationship Between Re-entry into GATT and Decentralization



At this stage, Western industrialized countries hold the final say over China's re-entry into GATT, thus wielding considerable indirect impact on China's decentralization process.

C. APEC's Impact on China's Decentralization

Ever since the 1940s, politicians and scholars have come up with one design after another for integrating the Asian-Pacific area economically. (see Table VII-3) The most

influential one - the Asian Pacific Economic Cooperation (APEC)- was proposed in 1989 by Australian Prime Minister Robert Hawke. In the same year, delegates from the United States, Canada, Japan, South Korea, Australia, New Zealand and members of ASEAN (Singapore, Thailand, Malaysia, Indonesia, the Philippines and Brunei) met for a ministerial-level conference at Canberra, the capital of Australia. After the conference, a joint communiqué was issued inviting China, Hong Kong, and Taiwan to participate in APEC conferences. And delegates from China, Hong Kong and Taiwan attended the APEC conference held in Seoul, South Korea in 1992.

Table VII-3: The Conception and Institution of Asian Pacific Economic Cooperation

Year	Advocating Countries	Conception and Institution
1942	Japan	Great East-Asia Co-prosperity Sphere
1960	Japan	Asian Development Fund
1965	Japan	Pacific Free Trade Area/ Pacific Economic Community
1965	Australia and New Zealand	New Zealand-Australia Free Trade Association
1967	Japan	Pacific Free Trade Area
1967	US Canada, New Zealand, Australia,	Pacific Basic Economic Council
1968	Academic Arena in the region	Pacific Trade and Development Conference
1980	Japan	Pacific Economic Cooperation Council
1983	New Zealand, Australia	Australia-New Zealand Closer Economic Relations Trade Agreement
1989	Australia	Asian Pacific Economic Cooperation
1990	Malaysia	East Asian Economic Group/ East Asian Economic Caucus
1993	ASEAN	ASEAN Free Trade Area

Source: *"The Interaction Between the Regionalism and Multi-lateralism"*, Zhou Tiancheng, Taiwan. *Theory and Policy* 1994 Spring, pp. 78.

During the second APEC ministerial-level conference representatives resolved that APEC should not become a trading group, and that trade among APEC members should conform to the principles of GATT

Although APEC was never intended to be a permanent organization, the Fifth APEC Conference held in Seattle in 1993 has brought it to a new important stage strengthening its standing among multilateral economic institutions

- 1) the organization authorized a "Declaration on Trade and Investment Structure", and made the informal regional trade liberalization group a formal trade and investment committee.
- 2) as is stipulated in the "Declaration of the APEC Leaders' Economic Forecast", the representatives decided to continue to convene conferences for economic and financial ministers to discuss overall economic development and capital circulation, and to coordinate general financial policies among member nations.
- 3) during the 1994 ministerial-level conference the special group on economic trends and issues was established as a permanent institution called "The APEC Economic Council". It had a mandate to strengthen policy and regional cooperation among member countries. At the same time, it was decided that APEC would continue to convene ministerial-level conferences on environmental protection and education policies.

Since the Fifth APEC Conference, the organization has moved in the direction of becoming another international organization such as the OECD (Organization for Economic Cooperation and Development). It is focusing on general economic and financial policies and economic promotion among members, and has established new committees and consultative networks, and signed agreements on standard customs procedures. In a word, APEC is no longer merely an informal forum, as it was originally intended to be. It will play an increasingly important role in coordinating economic integration and development and influencing public policy.

Motivated by a desire to enhance its prestige in the area, China is enthusiastic about becoming a member of APEC. However, once China becomes involved in the world economic system and in regional economic cooperation, it will have to liberalize the present market economy. This impetus will force economic blocks inside China further away from each other, since APEC promotes marketization, free trade, regionalism and multilateralism.⁷⁶ As a country undergoing decentralization, China will have to become more flexible. This is inevitable: China has little choice but to return to the world economic system, participate in regional economic cooperation and open its market.

D. Recommendations for a Western Investment Strategy

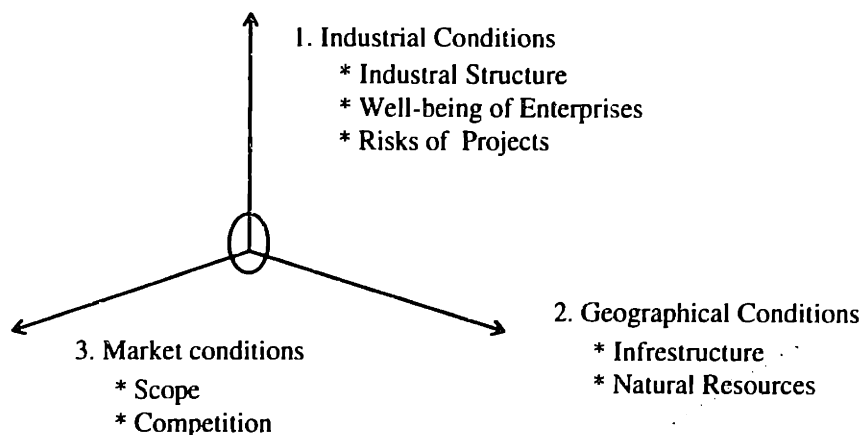
The most effective way for Western countries to influence China's decentralization is to invest in the country. In recent years, major industrial countries have not invested significantly in China. Between 1979 and 1992, Japan, the United States, Germany, France, England and Australia accounted for only 32% of the total direct investment of

⁷⁶ There are two opposing views among scholars regarding the relationship between regionalism and multilateralism: some regard it as contradictory, others as complementary.

the 10 major investors in China, this was only a little more than half of the total investment of Hong Kong in China during that period.⁷⁷

There are many explanations for the low rate of investment in China by Western industrial countries, but major ones lies in the follows areas: first is industrial conditions; second is geographical conditions; and third is market conditions. These are illustrated in the Figure VII-4.

Figure VII-4: Three Major Clusters of Conditions Affecting Direct Investment in China



It is difficult to achieve an ideal balance among the three clusters. Take the Chinese automobile industry. Objectively, potential for development exists, but that does not mean that there are no risks or that large profits are guaranteed. At present, there are three situations which mitigate against a profitable investment in the automotive industry. The market is not well developed, parts and supplies are inadequate and plants are not located strategically. The only automobile business in China which as a favorable market, supplies and location seems to be in Shanghai.

In reality, investors prioritize their investment strategy. If market conditions are general favorable, they will determine whether industrial or geographical conditions receive priority. In the former case, they should first decide on a project with favorable industrial conditions and then make efforts to improve the local geographical conditions, hence the "industry-inclined" strategy. In the latter case, they should decide on a location with favorable geographical conditions and then choose a particular industry and project to invest in, hence the "geography-incline" strategy. The first strategy is more common in practice, while the second strategy occurs usually when choosing a country for investment. This explains why investments have flown into the Asian Pacific area, where labor costs are low and the market potential is great.

In the case of China, geographic choices must be considered in making investment decisions. Economic development is very uneven in China, and the gaps have widened even while cooperation has strengthened due to the process of decentralization. Thus, it is

⁷⁷ *China Investment Yearbook*, the China Financial Press, 1994, p.25.

not appropriate to regard China as unified, but rather as composed of highly diversified environments for investment. To illustrate, the investment index for the same industry in different regions is usually different from that for different industries in the same region.

In adopting a geographic investment strategy, advantages of various regions should be compared closely. A hypothetical comparison of the Bohai Sea economic zone, the Yangtze Delta economic zone and the Pearl River economic zone, which all have strong industrial processing capacities, is used to illustrate this point (See Table VII-4).

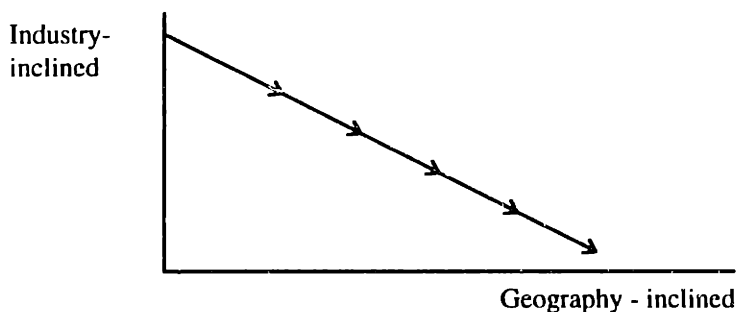
Table VII-4: A Hypothetical Comparison of Three Investment Candidates

	Industry A	Industry B	Industry C
Bohai	+	--	--
Yangtze	--	+	--
Pearl River	--	--	+

As indicated in the above Table, the same industry may present a very different investment opportunity in different regions. Industry A offers an ideal opportunity in the Bohai economic zone, industry B in the Yangtze Delta zone and industry C in the Pearl River zone.

Looking at Western investment practices in China, we can see that they are changing from the industry-inclined strategy to the geography-inclined strategy, the way investors behave internationally (See figure VII-5).

Figure VII-5: The Shift Toward the Geography-Inclined Investment Strategy



Now, the most crucial question is: What is the impact of this shift? The answer is obvious: it will effectively further decentralization in China.

Consistent with the shift in the Western investment strategy since the beginning of the 1990s, Chinese local governments have played an increasingly active role in attracting foreign investments. Now they attract more investments than the central government. In 1992, for example, the total foreign investment in China was US dollars 19 billion of which US 13 billion, or 68% was invested in local governments, while only US dollars 6

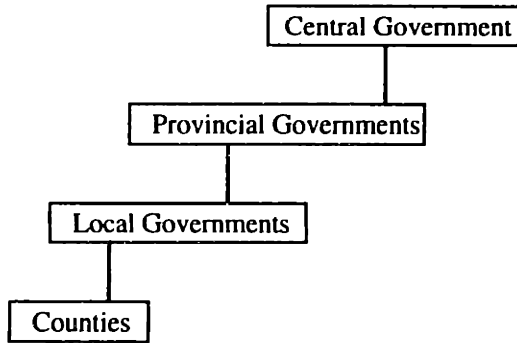
billion, or 32% was invested in the central government.⁷⁸ Five to ten years back, however, the central government received half of the foreign investments

In a word, the shift of Western investment in China to the "geography-inclined" strategy has gone hand in hand with China's decentralization.

⁷⁸ *China Investment Yearbook*, the China financial Press, 1994, p. 792.

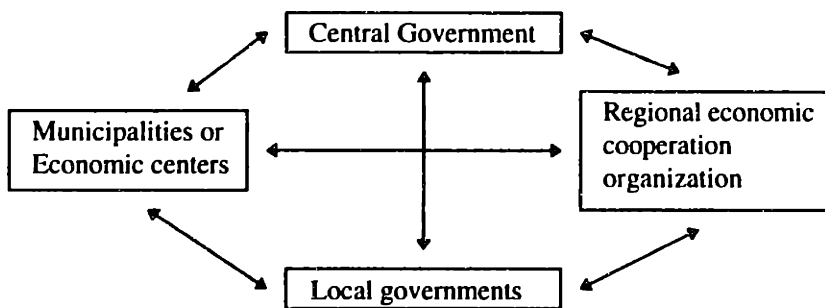
Conclusions

For decades after the Chinese Communist Party established its regime, public ownership and the planned economy in China, centralization proceeded to the extreme extent. The whole political economic system of this period can be depicted as pyramid in the following figure:

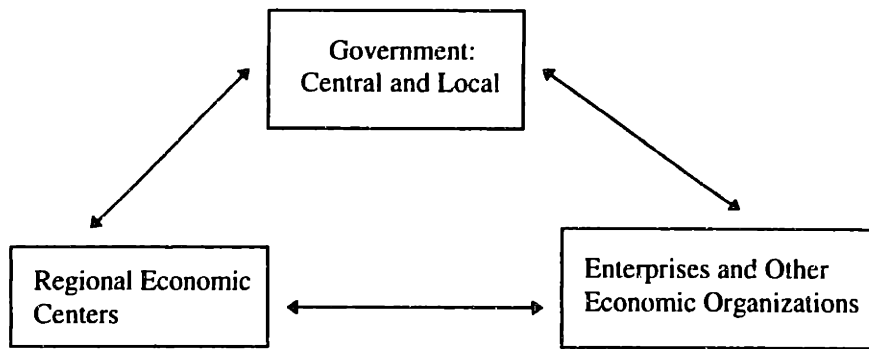


Under this “pyramid” model, the various departments and ministries of the central government were responsible for controlling everything for the sake of centralization.

After 15 years of reform China has largely returned to a market economy, with non-state ownership taking up the dominant place and the entire economy is moving toward Regionalization. A new “network” model is taking shape, as is represented in the following figure.



Under this model, the influence of the center is decreasing continuously. It should be emphasized that the “pyramid” model can be sustained only by self-isolation and autarky, while the “network” model thrives on decentralization and an open economy. So as the Chinese economic system evolves, the “network” will also undergo further changes, particularly with regard to the enhanced position of enterprises, as is illustrated below.



For about 2000 years since the Qinshi Emperor established the first centralized political system, the system has undergone the process of germination, growth, maturity, aging and dying. Since the 1980s, China has experienced rapid industrialization, economic marketization and liberalization and abolition of public ownership. At the same time, the Chinese economy has been undergoing the transformation from a closed, semi-closed to an open economy. All these changes are preparing it for the final death of centralization.

China may be one the earliest centralized states in human history, and it may be the last, that will have completed its transformation to decentralization peacefully. This will be great liberation of China. •

Appendix 1. The Major Data of China

Pattern of China's Economic Growth, 1978-1993

	Annual Compound Growth (%)	Share in Increase in GDP (%)
Investment	10.7	46
Consumption	7.9	53
GDP	9.0	100

Source: *Statistics Yearbook*, 1993: World Bank

Alternative Estimates of China's GDP

Source of Estimate	Year	Dollars Per- capita	Total GDP (\$'000bn)	Share of World GDP (%)
World Development Report 1994*	1992	470	0.55	2.4
Lardy (1993)*	1990	1,000-1,200	1.14-1.37	5.1-6.1
New York Times (20 May 1993)*	1992	1,600	1.66	6.0
World Bank (1992)*	1990	1,950	2.20	9.9
World Bank (1993)*	1991	2,040	2.35	10.9
Summers & Heston (1991)*	1988	2,308	2.56	15.0
Asian Wall Street Journal (31 May 1993)*	1990	2,598	2.90	13.0

* Based on the official exchange rate

* Based on the purchasing power of the Chinese currency

* Derived from IMF

* Update of estimates in the previous row

* Extrapolation/update of estimate in the previous row

Sources: Nicholas R. Lardy, *China in the World Economy* (Washington D.C. Institute for International Economics, 1994)

Changes of the Order of Precedence of Output of Major Industrial Products of China

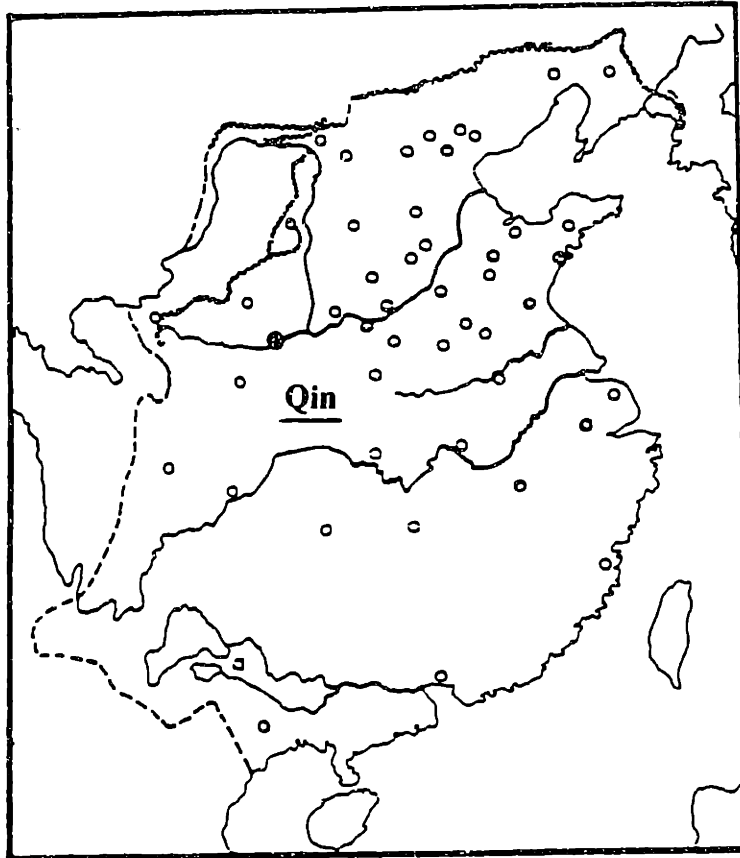
Products	1949	1965	1978	1985	1991
Steel	26	8	5	4	4
Coal	9	5	3	2	1
Crude Oil	27	12	8	6	5
Electricity	25	9	7	5	4
Cement		8	4	1	1
Ethylene		3	3	3	
Fertilizer		8	3	3	
Chemical Fibre			7	4	3
Cloths		3	1	1	1
Sugger		8	8	6	6
TVs			8	3	1

Source: *Statistical Yearbook of China*, 1992. China Statistics Press, 1993. pp. 855

Appendix 2. Chronological Table

Dynasties	Period
Shang	c 1600-1066 BC
Zhou	1066-221 BC
Qin	221-206 BC
Han	206 BC- 220
Tree Kingdoms	220-265
Jin	265-420
Northern and Southern States	420-581
Sui	581-618
Tang	618-907
Five Dynasties	923-979
Song	960-1279
Liao	907-1125
Western Xia	1023-1227
Jin	1115-1234
Yuan	1279-1368
Ming	1368-1644
Qing	1644-1911
Republic of China	1911-
People's Republic of China	1949-

Appendix 3. Map of Administration of Qin Danasty



- Capital
- Prefectures

Appendix 4. Evolution of China's Provinces from Ming, Qing to the Present

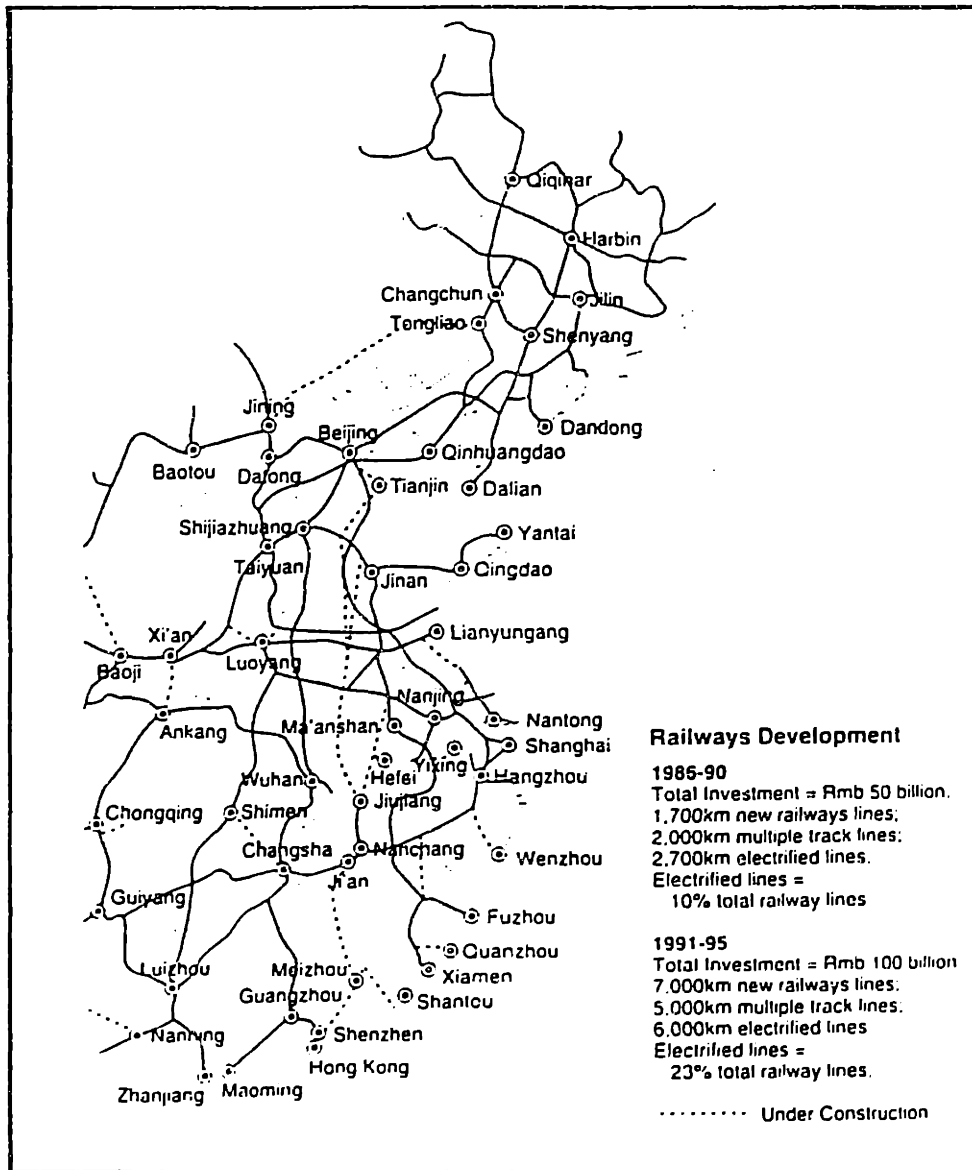
	Ming	Qing	Present
Beijing***	---	---	---
Tianjin**	---	---	---
Shanghai**	---	---	---
Hebai	---	---	---
Shaxi	---	---	---
Inner Mongolia*	---	---	---
Liaoning	---	---	---
Jilin	---	---	---
Helongjiang	---	---	---
Jiangsu	---	---	---
Zhejiang	---	---	---
Anhui	---	---	---
Fujian	---	---	---
Jiangxi	---	---	---
Shangdong	---	---	---
Henan	---	---	---
Hubei	---	---	---
Hunan	---	---	---
Guangdong	---	---	---
Guangxi*	---	---	---
Hainan	---	---	---
Sichuan	---	---	---
Guizhou	---	---	---
Yunnan	---	---	---
Tibet*	---	---	---
Shaaxi	---	---	---
Gansu	---	---	---
Qinghai	---	---	---
Ningxia*	---	---	---
Xingjiang*	---	---	---

* Minorities Autonomic Regions at Present.

** Municipality Directly Under the Central Government at Present.

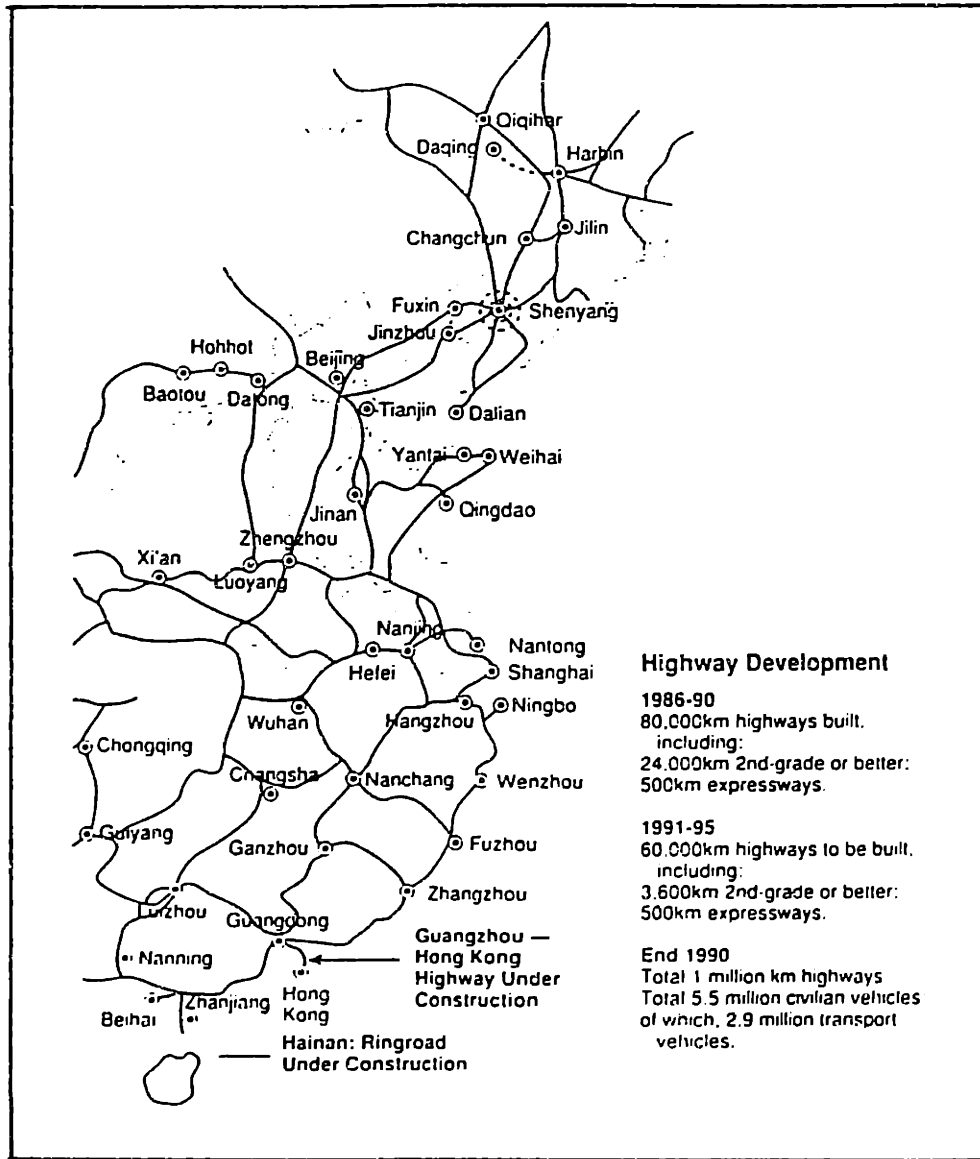
*** Beijing has been the capital city of China from Ming, Qing uptill today.

Appendix 5. Map of China's Railway Development, 1988-1995



Source: *China Facts and Figures Annual Handbook*,
 Academic International Press, 1994

Appendix 6. Map of Highway Development, 1986-1995



The Hong Kong-to-Guangzhou highway, scheduled for completion in 1994, will be the first six-lane super highway in China. The 76-mile long road has an estimated cost of 1.4 billion dollars US and will charge a 13 dollar/vehicle toll. The primary importance of the road is that it will merge Hong Kong, Shenzhen, and Guangzhou into a single, large metropolis after Hong Kong reverts to Chinese control in 1997. An estimated 30,000 vehicles a day will cross the frontier between Hong Kong and China when the highway opens.

Source: *China Facts and Figures Annual Handbook*, Academic International Press, 1994

Appendix 7. Map of Ports and Airports in China



Source: *China Facts and Figures Annual Handbook*,
Academic International Press, 1994

Appendix 8. Major Data of East, Central and West Regions in China

	East Region	Central Region	West Region	Total
Population (Million)	468.07	404.14	258.30	1,130.51
(% bloc of nation)	41.4	35.7	22.8	100
Urban Pop (Million)	100.34	79.69	39.90	219.93
(% bloc of nation)	45.6	36.2	18.1	100
Illiterate pop (Thousand)	161,162	70,149	60,185	291,496
(% bloc of nation)	55.29	24.07	20.65	100
City Numbers	188	196	94	476
(% bloc of nation)	39.50	40.76	19.75	100
GNP (Million RMB)	2,202.12	1,043.86	535.88	3,781.86
(% bloc of nation)	58.23	27.60	14.17	100
Structure of GNP:				
Manufacturing %	63.96	51.90	48.16	
Agriculture %	18.58	25.29	28.27	
Ownership Struture				
State owners:				
(Million RMB)	7,877.41	4,315.70	2,178.62	14,371.73
(% bloc of nation)	54.81%	30.03%	15.16%	100%
Collective				
(Million RMB)	4,450.86	1,201.50	525.72	6,178.08
(% bloc of nation)	72.04%	19.45%	8.51%	100%
Others (Million RMB)	1,462.51	45.44	31.11	1,539.06
(% bloc of nation)	95.03	2.95	2.02	100
TVE:				
TVE Numbers*				
(Million RMB)	695,797	509,688	236,183	1,441,668
(% bloc of nation)	48.26	35.35	16.38	100
TVE Income				
(Million RMB)	486.9	117.0	49.2	653.2
(% bloc of nation)	74.55	17.91	7.53	100
FCAU **				
(100 Million USD)	1,200.9	57.9	23.6	1,282.4
(% bloc of nation)	93.64	4.52	1.84	100
Imports & Exports				
(100 Million USD)	799	140	65	1,004
(% bloc of nation)	79.56	13.90	6.53	100
Patent Application				
(Million RMB)	35,317	14,369	8,021	57,707
(% bloc of nation)	61.20	24.90	13.90	100
Research Instituts				
(Million RMB)	2,880	1,788	1,186	5,854
(% bloc of nation)	49.20	30.54	20.26	100
Scientists & Engineers				
(Million RMB)	263,190	98,458	97,678	459,326
(% bloc of nation)	57.30	21.44	21.27	100

Note: * Town and Village Enterprises

** Foreign Capital Actual Utilization

Source: *Statistical Yearbook of China 1992*. China Stastics Press, 1993.

Appendix 9. The Categories of Open Economic Areas in China Since 1980s

Category I	Special Economic Zones (total 5 cities) 1. Shenzhen 2. Zhuhai 3. Shantou 4. Xiamen 5. Hainan*
Category II	Open Cities in China (total 14 cities) Dalian, Qinhuangdao, Tianjin, Yantai, Qingdao, Lianyungang, Nanton, Shanghai, Ninbo, Wenzhou, Fuzhou, Zhanjiang, Guangzhou, Beihai
Category III	Economic and Technological Development Zones (total 12 cities) Dalian, Tianjin, Yantai, Qingdao, Lianyungang, Nanton, Shanghai, Ninbo, Wenzhou, Fuzhou, Zhanjiang, Guangzhou,
Category IV	3 Coastal Open Economic Zones Liaoning Peninsular, Yangtze River delta, Pearl River Delta, Shandong Peninsular
Category V	High and New Technological and Industrial Development Zones (total 52 places)**
Category VI	Open Border Cities (total 13 cities) Hunchuan, Suifenhe, Heihe, Manzhouli, Erenhot, Tacheng, Bole, Yining, Wanding, Ruili, Hekou, Pingxiang, Dongxing
Category VII	The New Area of Pudong in Shanghai
Category VIII	Open Cities Along the Yangtze Rivers (total 5 cities) Chongqing, Yueyang, Wuhan, Jiujiang, Wuhu
Category IX	Bonded Areas (total 14 areas)***
Category X	National Tourist and Holiday Resort Areas

* Hainan become a province in 1985;

** There are 52 national development zones for high and new technology industries in China separating in almost every provinces.

*** 14 Bonded areas were created in 1990.

Source: *Investment in China 1994*, China Commerce Press, Beijing 1994.

Appendix 10. Major Data of Seven Economic Zones in China

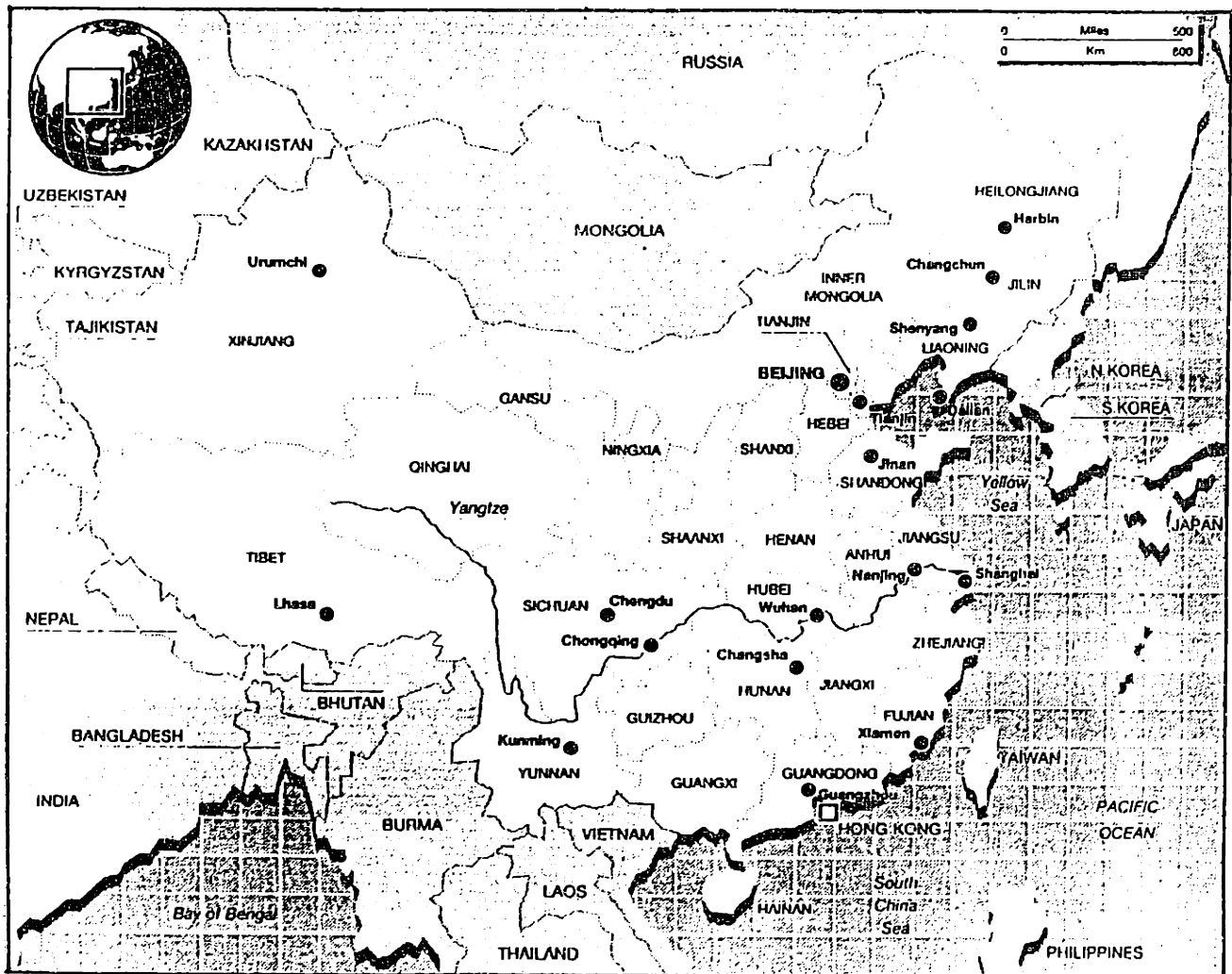
	Zone 1	Zone 2	Zone 3	Zone 4	Zone 5	Zone 6	Zone 7	Total
Population (Million)	110.06	279.03	121.84	141.68	90.25	208.52	178.78	1,130.51
(% bloc of nation)	9.7	24.6	10.7	12.5	7.9	18.4	15.8	100
Urban Pop (Million)	43.23	47.49	27.79	25.13	19.26	33.12	23.89	219.41
(% bloc of nation)	19.7	21.6	12.7	11.4	8.8	15.1	10.9	100
Illiterate Pop (Thousand)	13715.9	46,287	108,493	20,852	20,762	40,023	41,361	291,496
(% bloc of nation)	4.71	15.88	37.22	7.15	7.12	13.73	14.19	100
City Numbers	78	101	54	51	57	90	46	476
(% bloc of nation)	16.28	21.22	11.34	10.71	11.87	18.91	9.66	100
GNP (million RMB)	4,723.4	9,659.5	7,910.3	4,892.1	2,214.8	5,006.9	3,411.6	37,818.6
(% bloc of nation)	12.49	25.54	20.92	12.94	5.86	13.24	9.02	100
Structure of GNP:								
Manufacturing %	56.00	66.28	74.16	49.16	48.54	55.83	41.55	
Agriculture %	16.17	15.84	11.62	30.74	22.10	29.06	34.13	
Ownership Structure:								
State owners	2,402	3544	2764	14711	975	1900	1316	14,372
(Million RMB)								
(% bloc of nation)	16.71	24.66	19.23	10.24	6.78	13.22	9.15	100.00
Collective (Million RMB)	566	1527	2194	698	178	648	368	1,178
(% bloc of nation)	12.27	18.98	22.63	10.08	6.33	18.46	11.25	100.00
Others (Million RMB)	88	187	482	724	14	24	18	1,539
(% bloc of nation)	5.72	12.16	31.33	47.05	0.92	1.62	1.19	100
TVE :								
Numbers*	5.72	12.16	31.33	47.06	0.92	1.62	1.19	100.00
(% bloc of nation)	95,888	372,940	200,709	195,465	70,118	334,912	171,637	1,441,668
TVE Income	436	1,817	2,238	904	151	631	354	6,532
(Million RMB)								
(% bloc of nation)	6.67	27.81	34.27	13.85	2.32	9.66	5.42	100
FCAU **	75.9	179.8	263.9	692.6	10.1	46.8	13.5	1,282.6
(100 million USD)								
(% bloc of nation)	5.92	14.02	20.58	54.00	0.79	3.65	1.06	100.00
Imports & Exports	169	121	210	375	35	59	35	1004
(100 Million USD)								
(% bloc of nation)	16.83	12.03	20.92	37.32	3.52	5.90	3.48	100
Patent Application	8,215	17,987	9,508	6,688	3,731	7,033	4,545	57,707
(% bloc of nation)	14.24	31.17	16.48	11.59	6.47	12.19	7.88	100
Research Instituts	885	1,506	771	645	654	788	605	5,854
(% bloc of nation)	15.12	25.73	13.17	11.02	11.17	13.46	10.33	100
Scientists & Engineers	51,053	16,0707	76,734	24,773	51,584	45,599	48,877	45,326
(% bloc of nation)	11.11	34.99	16.71	5.39	11.23	9.93	10.64	100

Note: *Town and Village Enterpriss

**Foreign Capital Actual Utilization

Source: *Statistical Yearbook of China 1992*. China Statistics Press, 1993.

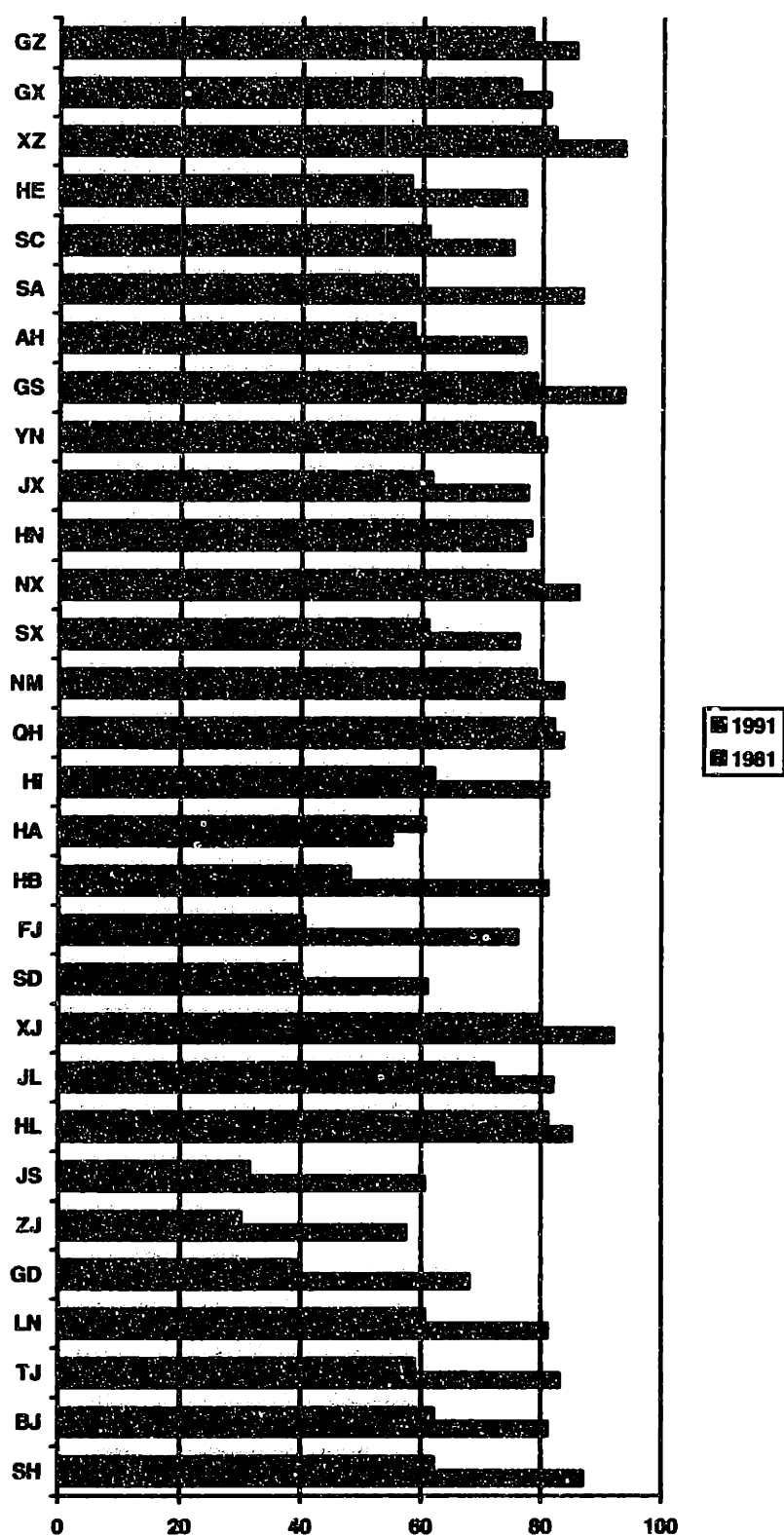
Appendix 11. The Major Cities Network in China



The Population in Major Cities (million, 1992):

- Shanghai 15.3
- Beijing 12.7
- Tianjin 10.5
- Shenyang 8.1
- Wuhan 6.9
- Guangzhou 6.4

Appendix 12. Provincial Ownership Structure*



* Share of state-owned industry in percent.

Source: *China at Threshold of a Market economy*, IMF, Sep 1993, pp.47

Appendix 13. Central-Local Resource-Sharing Contracts, 1988-1992 (1)

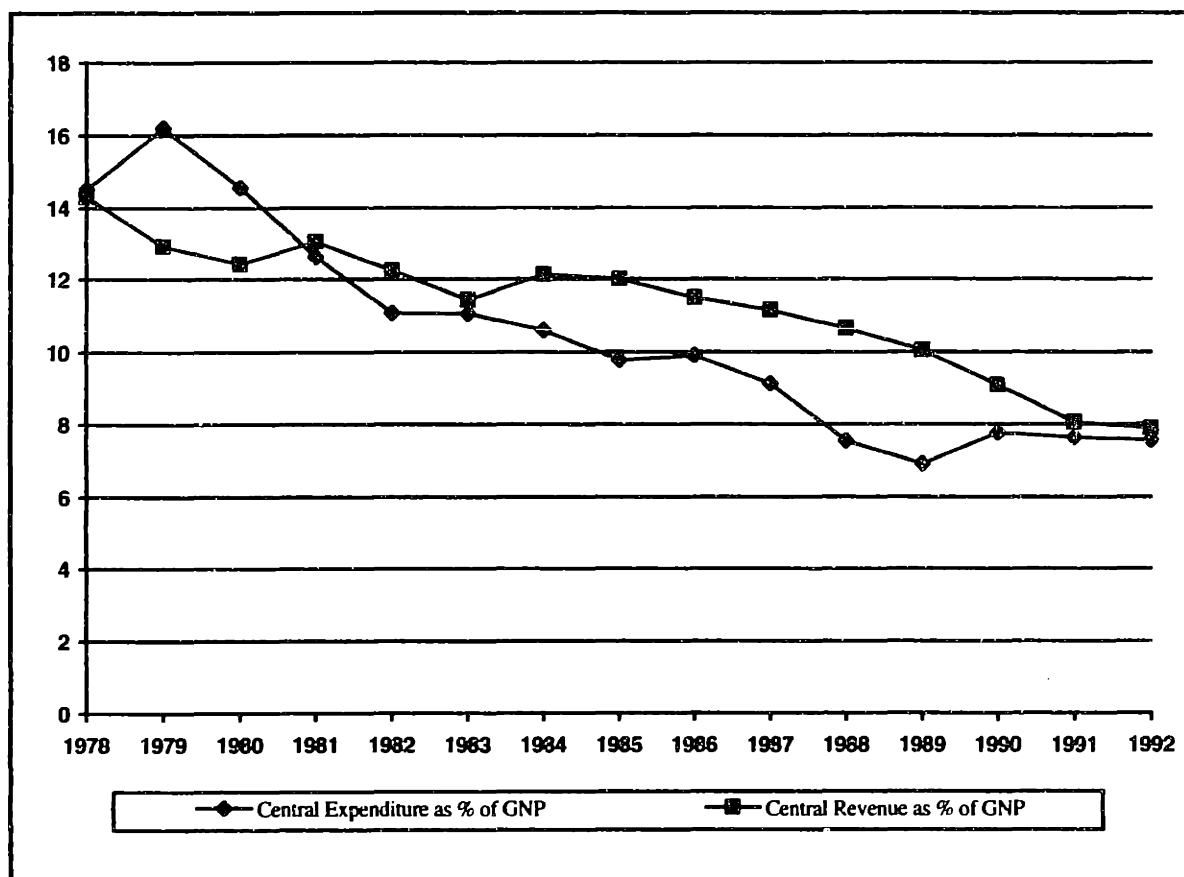
Tapes	Provinces or Major Cities
<i>Tape A</i> (2) Variable Retention by Formula	Beijing, Hebei, Liaoning, Shenyang, Harbin, Jiangsu, Zhejiang, Ningbo, Henan, Chongqing (2)
<i>Tape B</i> Fixed Rate of Retention	Tianjin, Shanxi, Anhui
<i>Tape C</i> Variable Remittance by Formula	Dalian, Qingdao, Wuhan (3)
<i>Tape D</i> Semi-Fixed Amounts to State	Guangdong (including Guangzhou), Hunan
<i>Tape E</i> Fixed Amount to State	Shanghai, Shandong, Heilongjiang
<i>Tape F</i> Contracts Transfer to Provinces	Jilin, Jiangxi, Shaanxi, Gansu, Fujian, Inner Mongolia, Guangxi, Tibet, Ningxia, Xinjiang, Guizhou, Yunnan, Qinghai, Hainan (4)

1. These contracts were intended to cover three years but have been extended annually in subsequent years.
2. The locality retained a specified proportion (local retention rate) of any revenue that was less than or equal to contracted rate of increase. Any revenue above this amount was retained locally.
3. After the cities of Wuhan and Chongqing were separate from Hubei and Sichuan provinces changed from net providers to the state to net recipients of subsidies from the state. The Difference between their expenditures and their income, which was made up from income that Wuhan and Chongqing sent to the provinces, served as central government subsidies to the local government. The percentage that Wuhan and Chongqing gave to the provinces was 4.8 percentage and 10.7 percentage, respectively.
4. Inner Mongolia, Guangxi, Tibet, Ningxia, Xinjiang are belong to be autonomous regions.

Source: *China at Threshold of a Market economy*, IMF, Sep 1993, pp.49

Appendix 14. Central Revenue and Expenditure As Percentage of GNP, 1978-1992

	1978	1979	1980	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992
Central Expenditure as % of GNP	14.52	16.19	14.56	12.61	2.00	11.1	10.66	9.81	9.93	9.15	7.53	6.91	7.76	7.52	7.57
Central Revenue as % of GNP	14.31	12.91	12.91	13.05	12.25	11.44	12.14	12.00	11.50	11.15	10.65	10.05	9.09	8.05	7.88



Source: *Statistic Yearbook of China, 1992*. China Statistic Press 1993.

Appendix 15. China's Total of Imports and Exports, 1980-1992

Total Value of Imports and Exports USD Million

Year	Total	Exports	Imports
1980	38,136	18,119	20,019
1985	69,602	27,350	42,252
1990	115,443	62,093	53,350
1992	165,525	84,940	80,584

Indexes of Total Value of Imports and Export

Year	Total	Exports	Imports
1980	100.0	100.0	100.0
1985	182.5	150.9	211.0
1990	302.7	342.7	266.5
1992	434.0	488.8	402.5

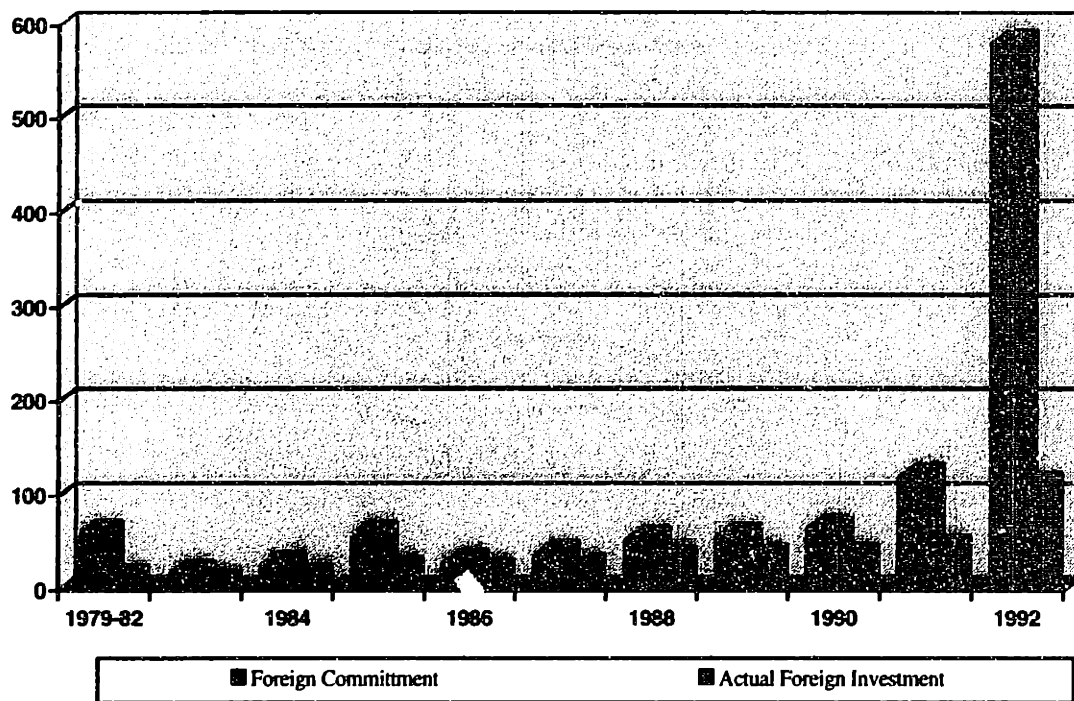
China Exports Share in GDP

Year	GDP (RMB Million)	Exports (USD Million)	Exports Propotion (%)
1980	447,000	18,119	6.0
1985	856,200	27,350	9.5
1990	1,768,600	62,093	17.0
1992	2,939,800	84,940	19.5

Source: *Almanac of China's Foreign Economic Relations and Trade*
1993/1994.

Appendix 16. Foreign Investment in China, 1979-1992

	1979-82	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992
Foreign Commitment (100 million USD)	60.12	17.31	26.5	59.31	28.34	37.09	52.97	56	65.67	119.77	581.24
Actual Foreign Investment (100 million USD)	11.68	6.35	12.68	20.3	18.75	23.14	31.94	33.93	34.14	43.66	110.06



Source: *Investment in China*, 1994 China Commerce Press 1994

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