



# The Chinese Economy

Giorgio Prodi – Federico Frattini

## What we will do

- Understand (a bit) China
- Connecting the dots...
- How to deal with China today

# The Chinese Economy

## Lectures

- Tuesday 1 00 pm 3 00 pm
- Wednesday 9 00 am 12 am

## Office Hour

- Wednesday 4 00 pm 5 00 pm (or upon request / at the end of each lecture)

## Final exam

- Attending students: discussion of papers in class + final thesis (or written exam as you prefer)
- Non attending students: written exam 1,5 hour. 3 questions.

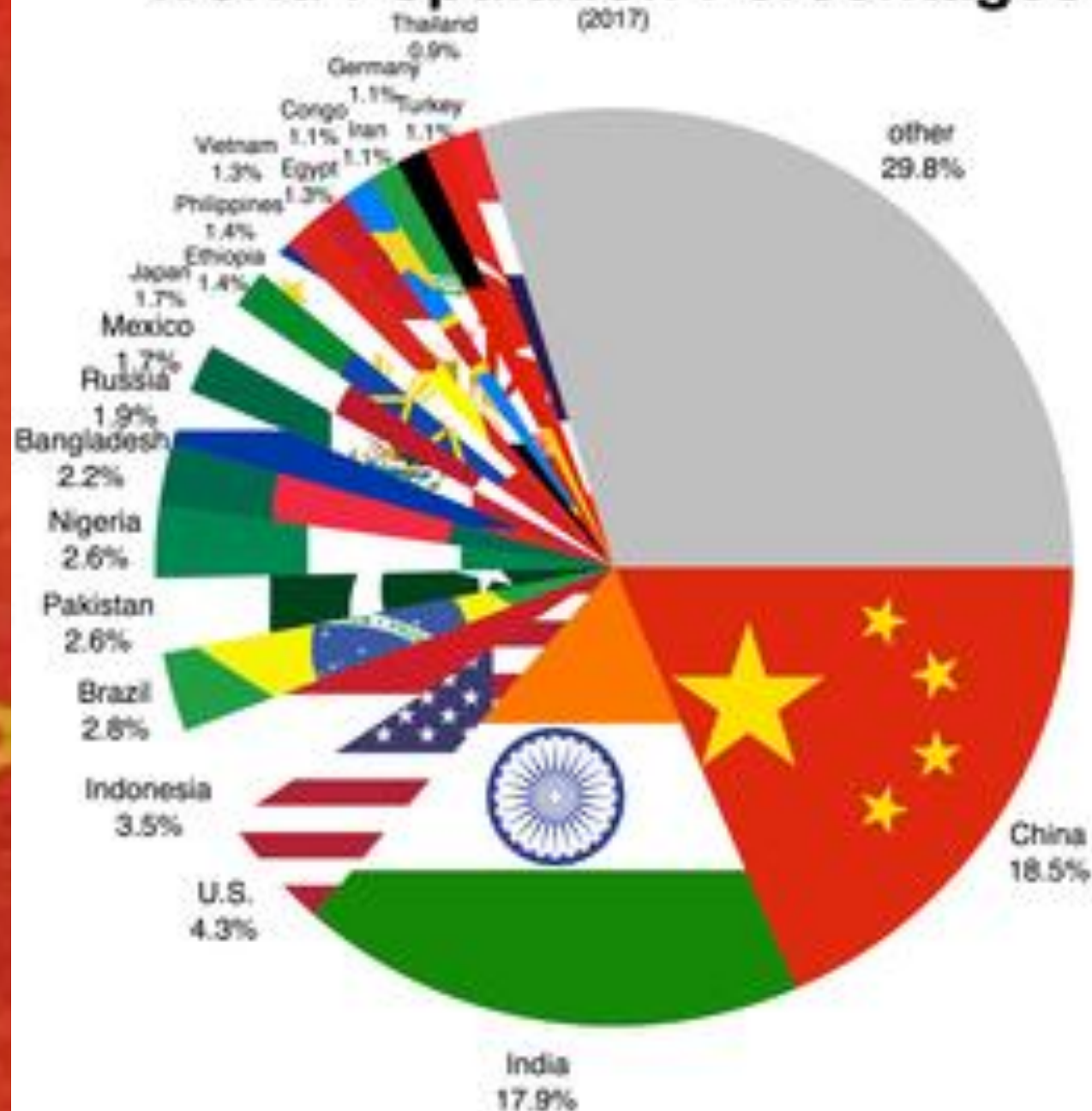


Why you cannot avoid China, like it or not, and why you need a strategy



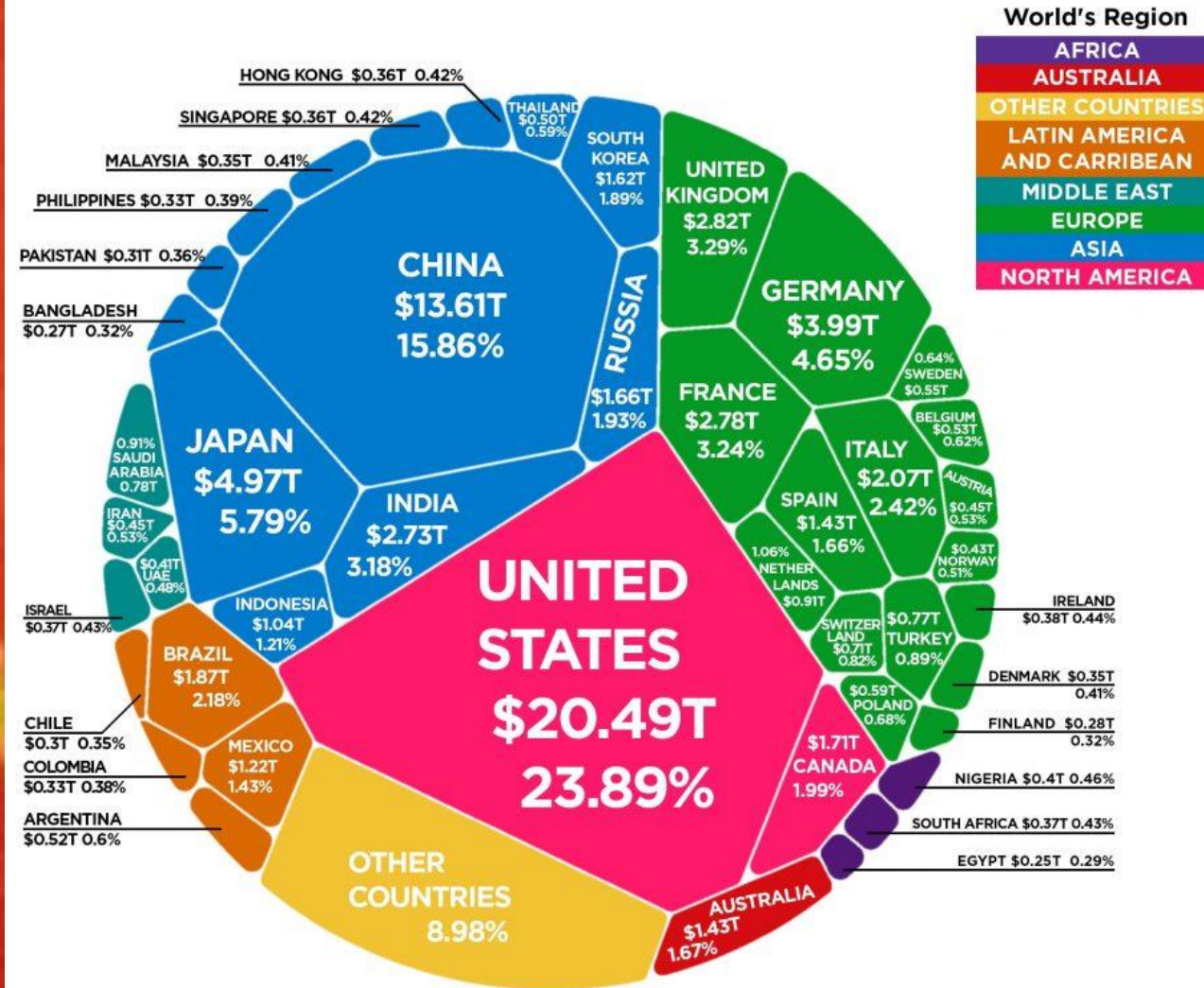
# World Population Percentages

(2017)



# The World Economy

## Gross Domestic Product (GDP) by Country 2018



### Article & Sources:

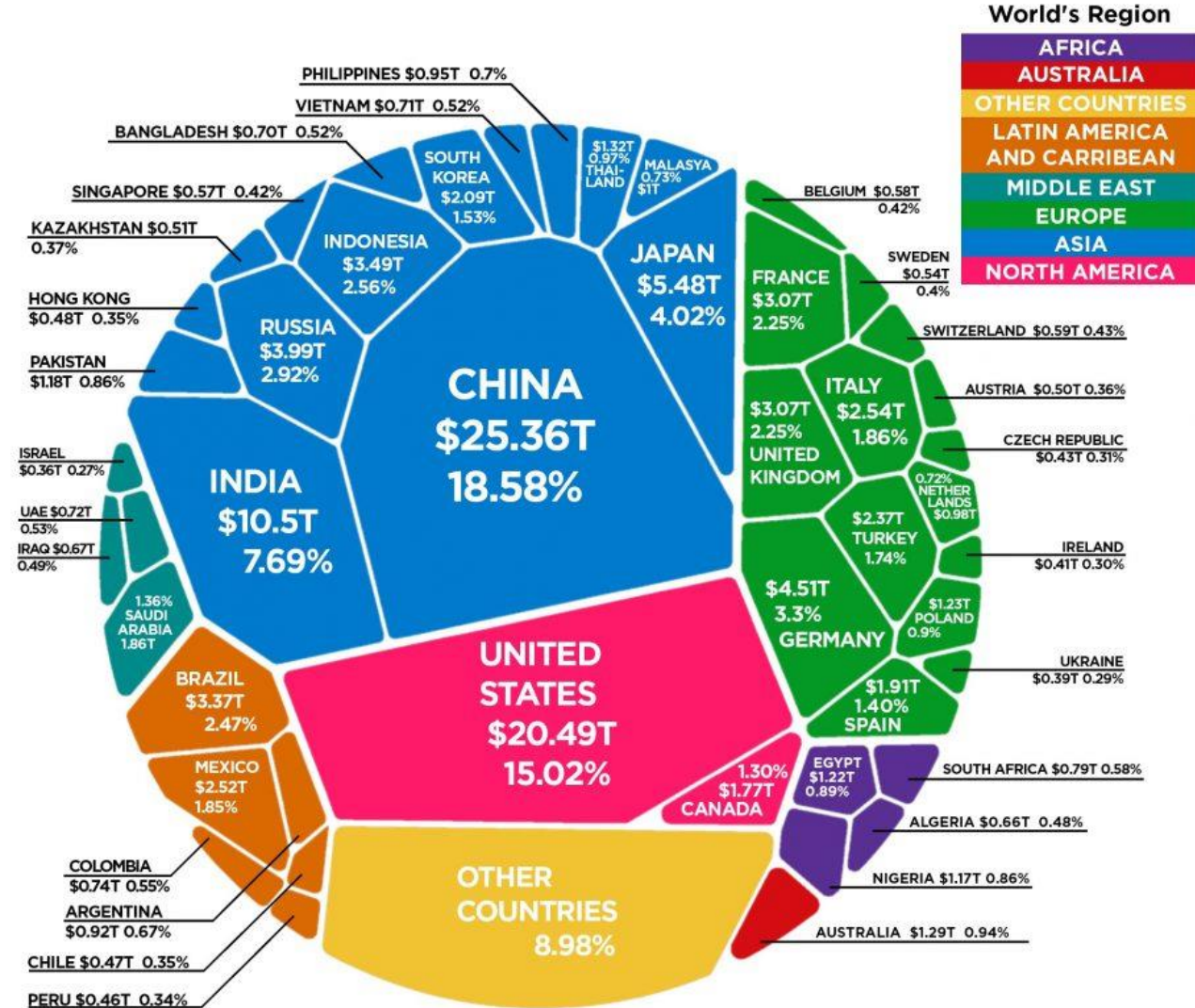
<https://howmuch.net/articles/the-world-economy-2018>

<https://databank.worldbank.org>



# The World Economy Under Price Parity

GDP at Power Purchase Power Parity (PPP) by Country in 2018

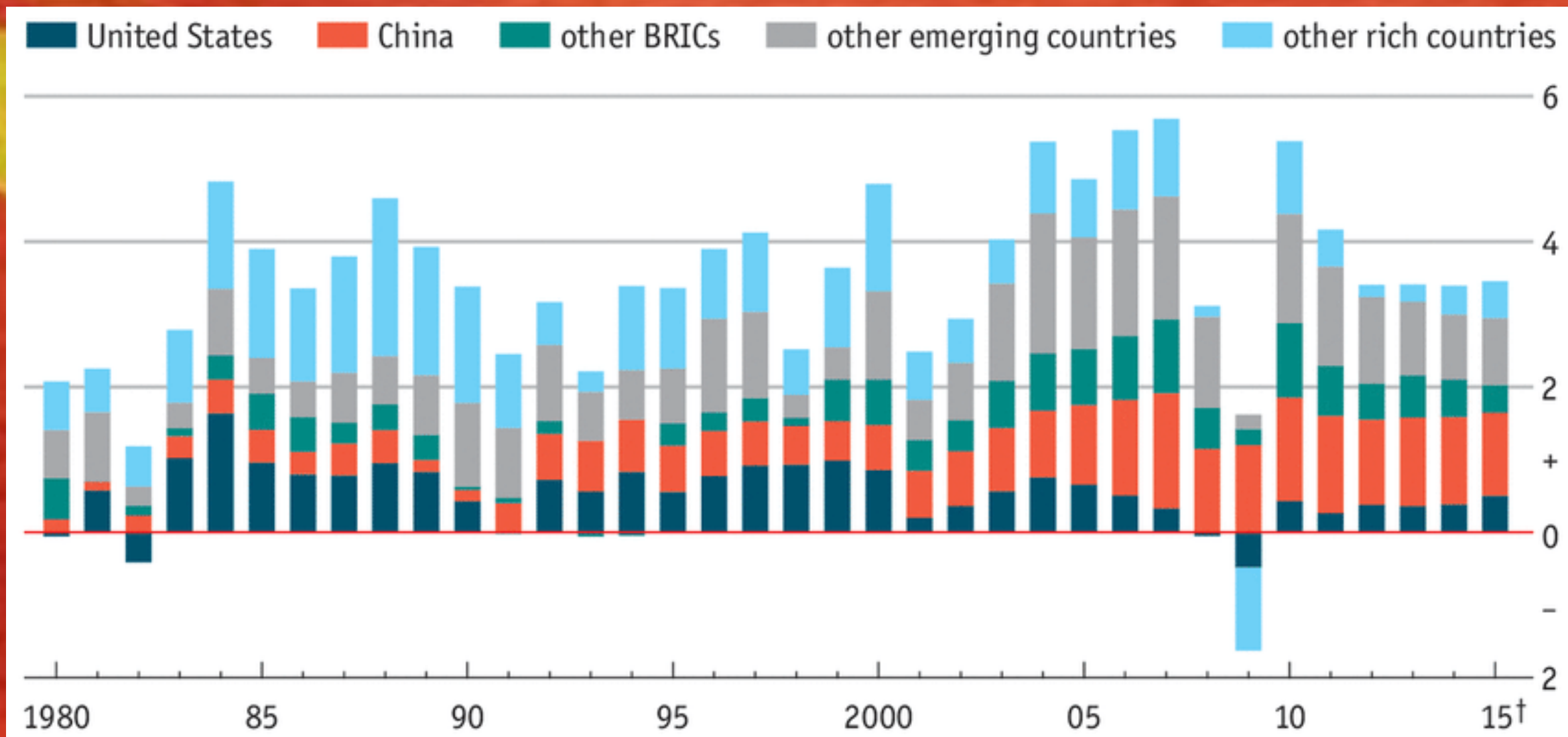


## Article & Sources:

<https://howmuch.net/articles/the-world-economy-ppp-2018>  
The World Bank - <https://databank.worldbank.org>

howmuch.net

# World GDP contribution to Growth

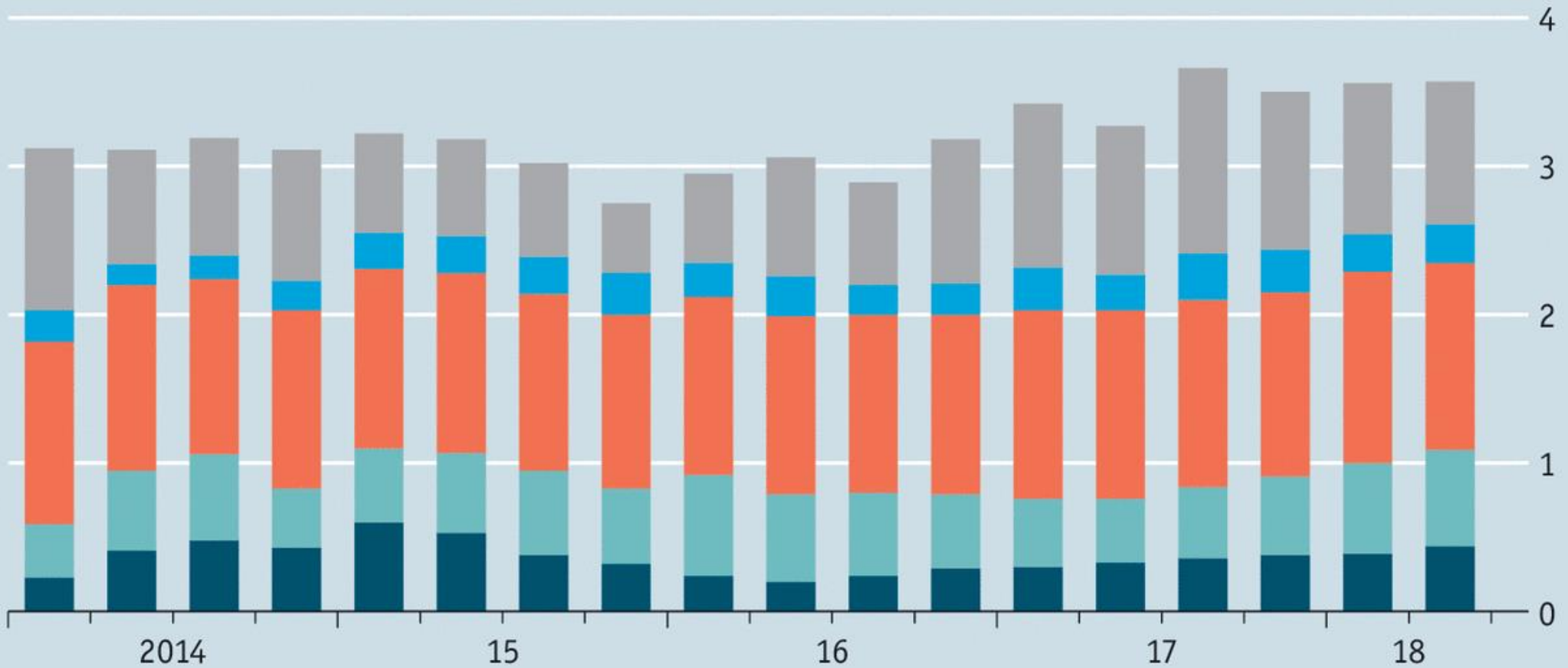




# World GDP

Contribution to growth\*, percentage points

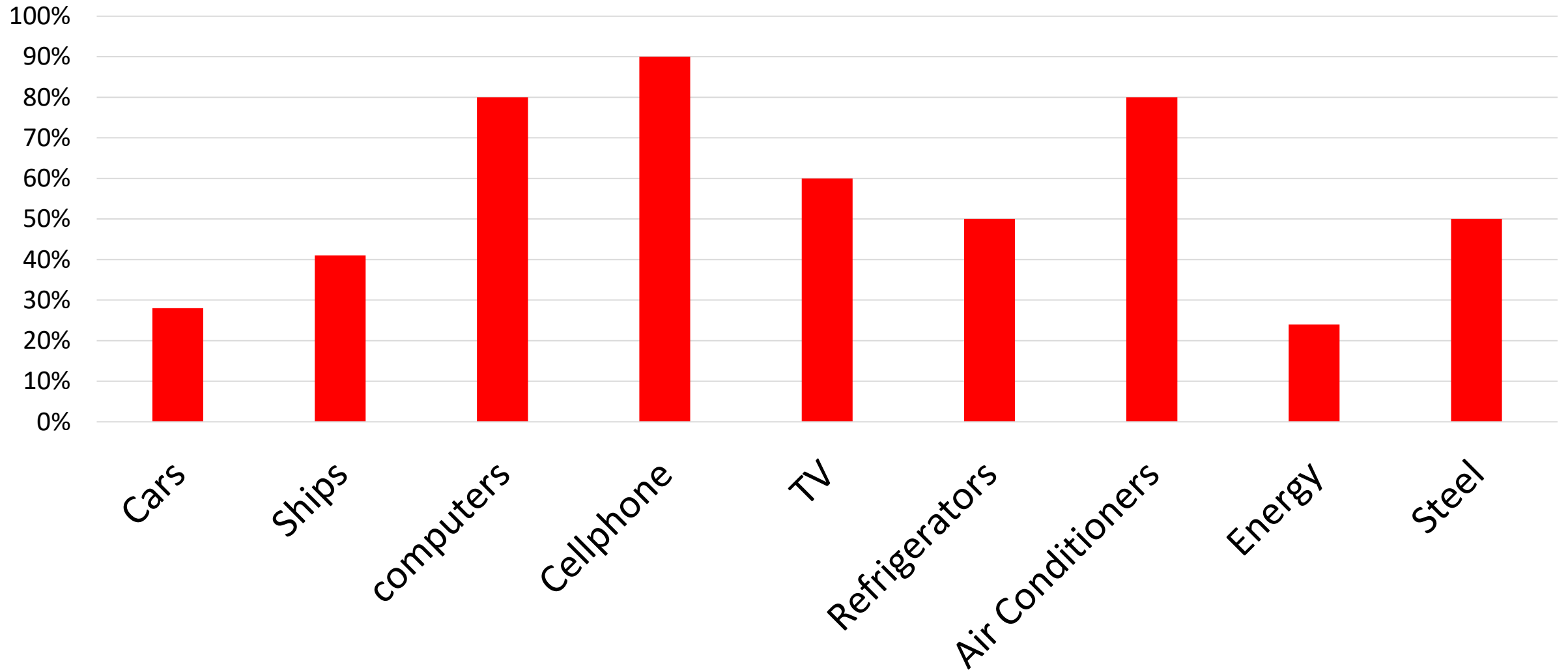
United States India China Euro area Rest of world



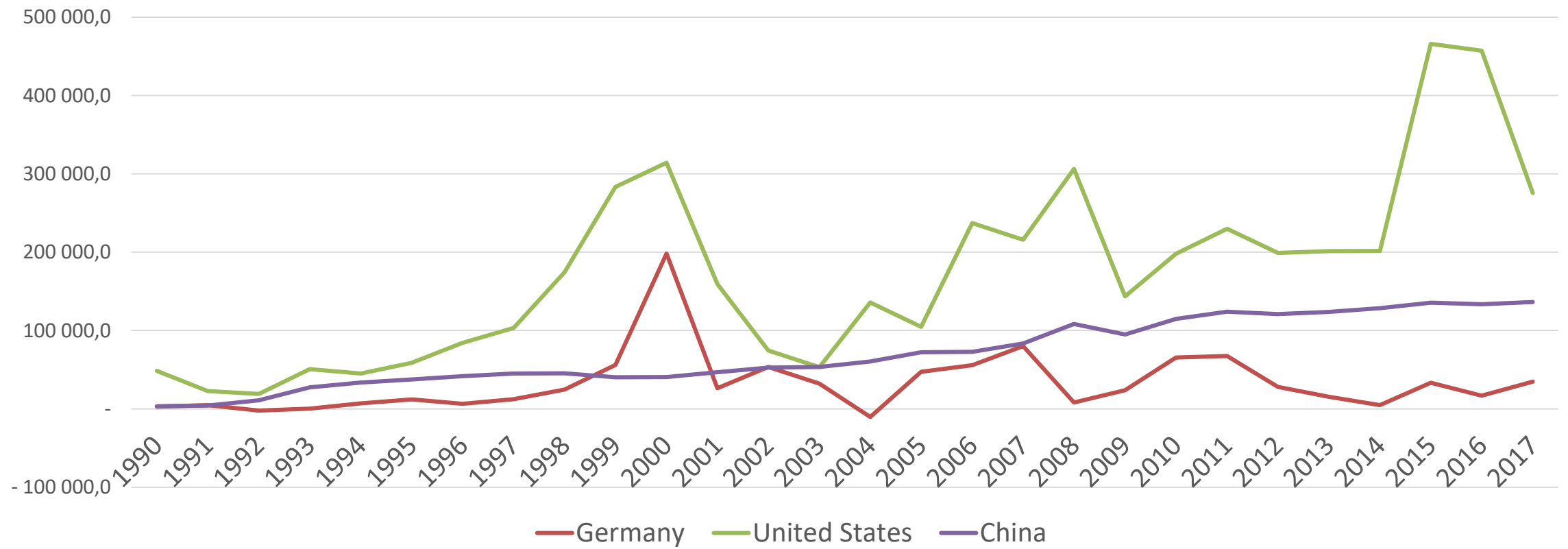
Sources: Haver Analytics;  
IMF; *The Economist*

\*Estimates based on 63 economies representing 87% of GDP.  
Weighted GDP at purchasing-power parity

# China % of world production 2015

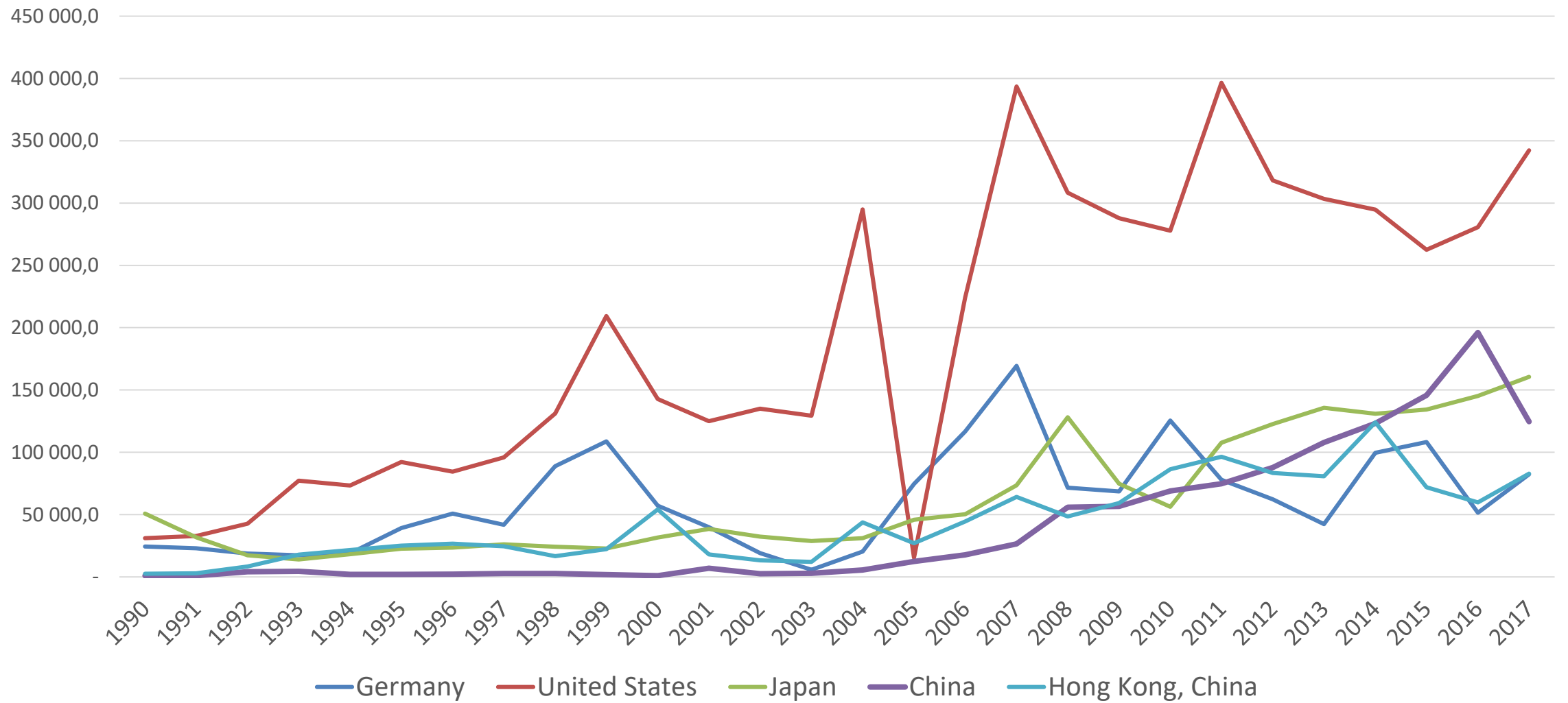


## Inward FDI

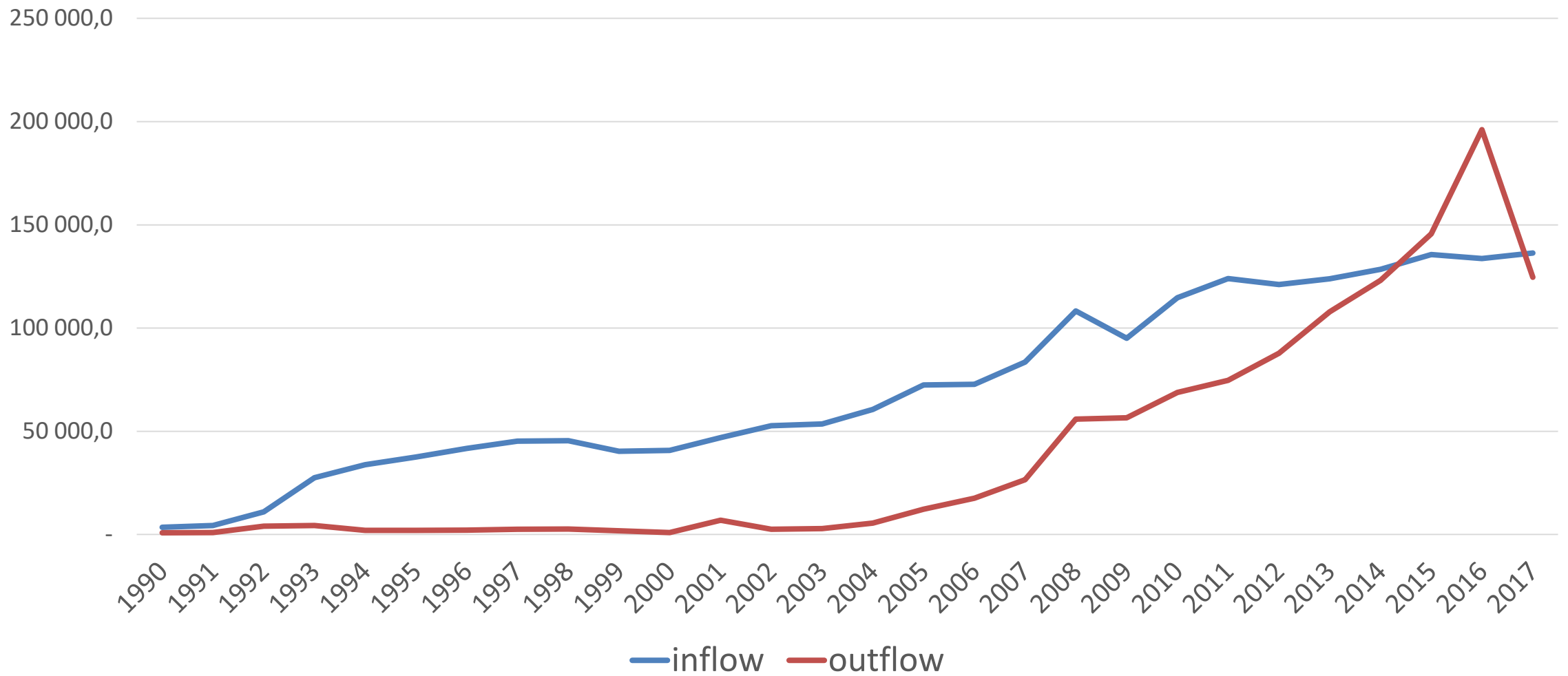




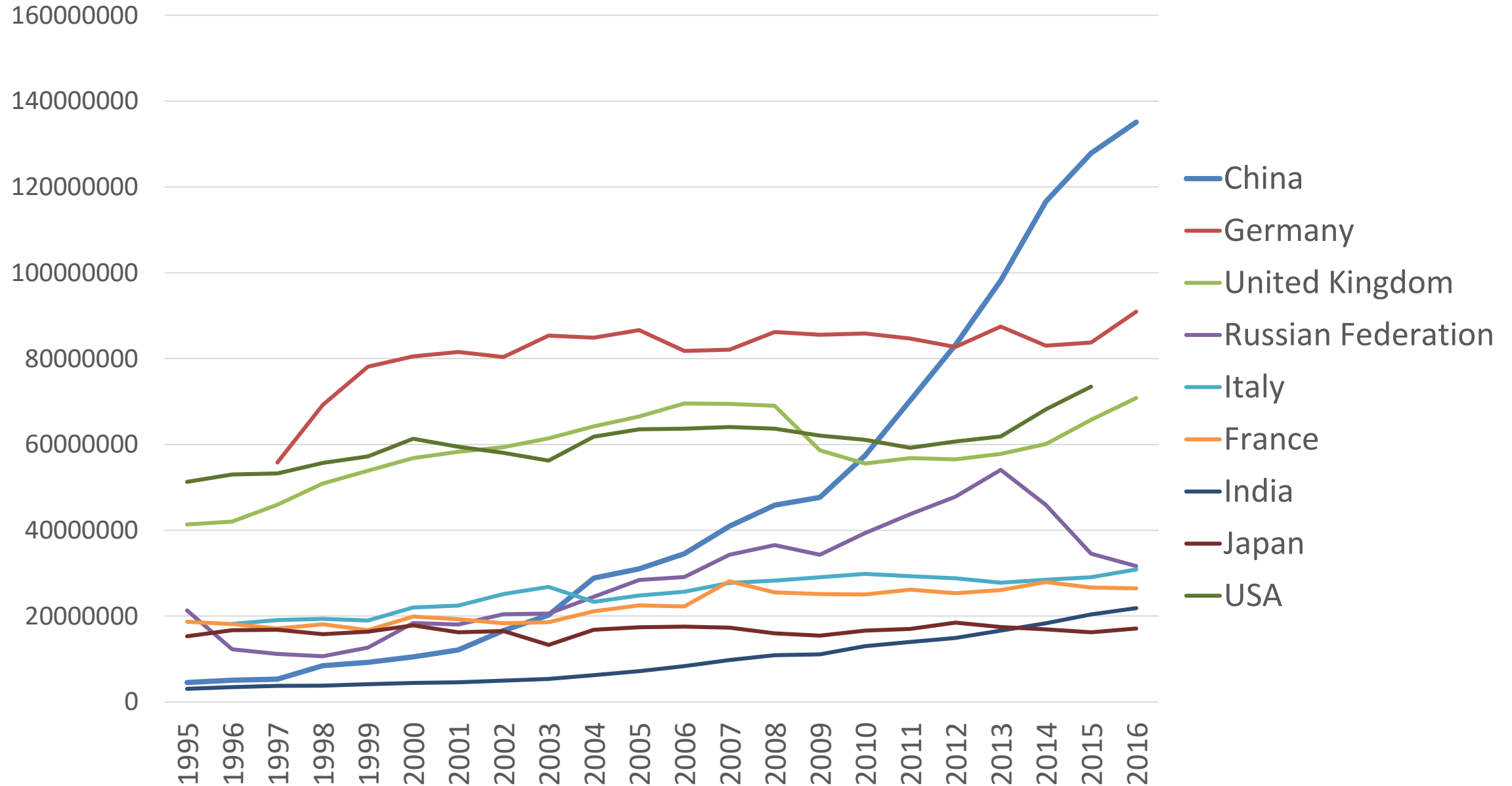
# OFDI



# China FDI



# International tourists departures

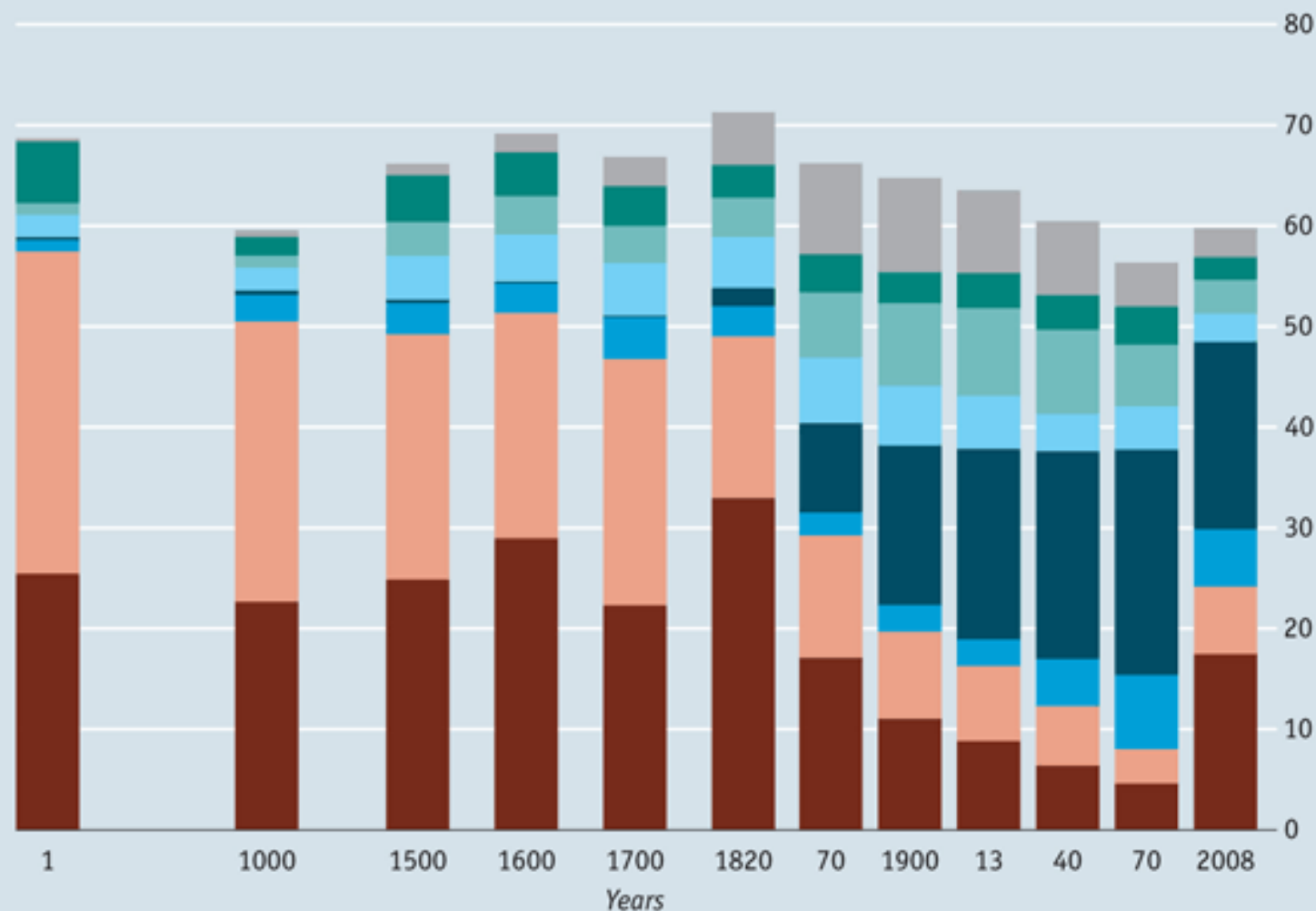




## A history of world GDP

Percentage of total, 1990 \$ at PPP\*

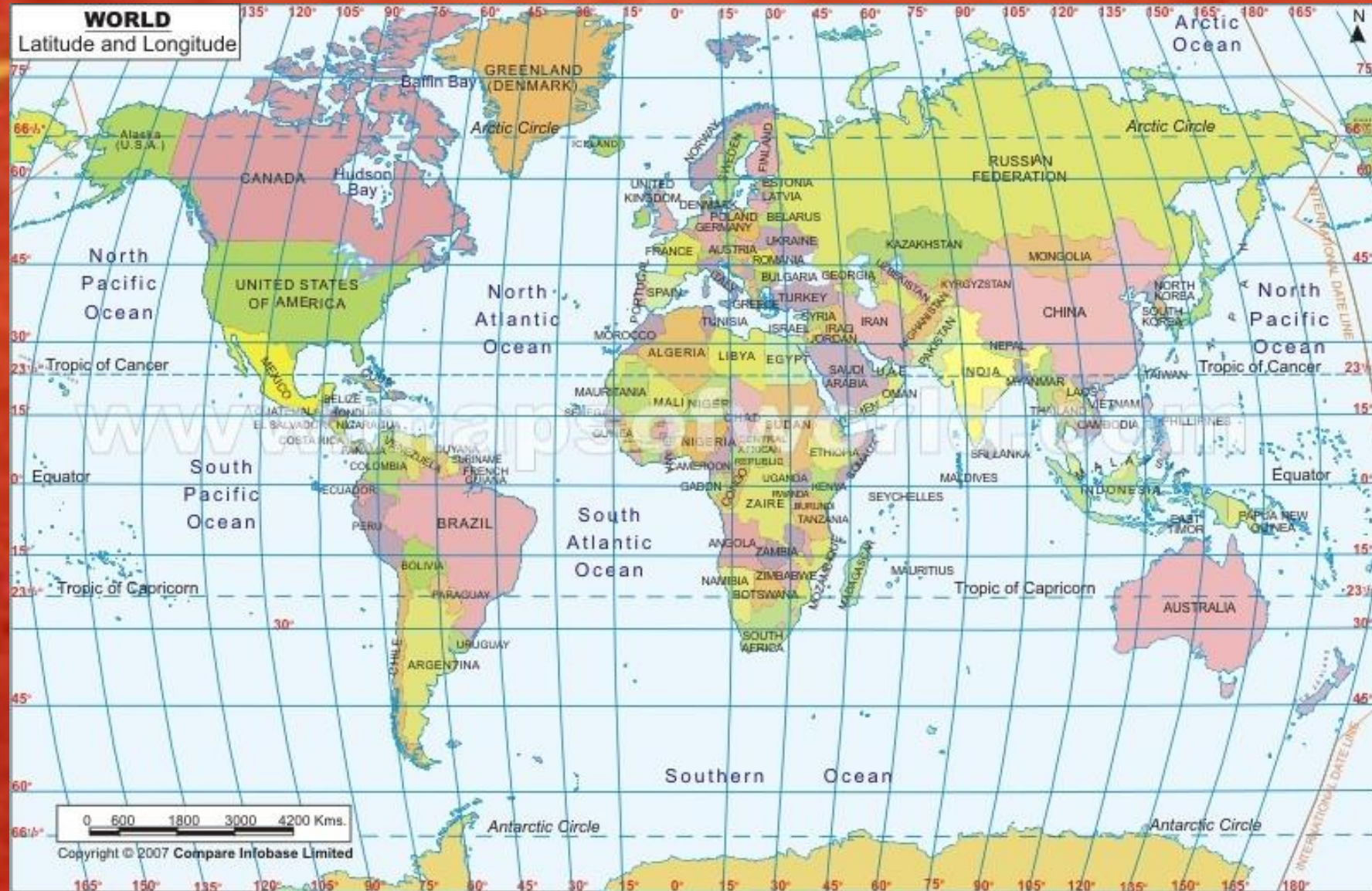
China India Japan US France Germany Italy Britain



Sources: Angus Maddison, University of Groningen; *The Economist*

\*Purchasing-power parity

# Deal with China in the wrong way

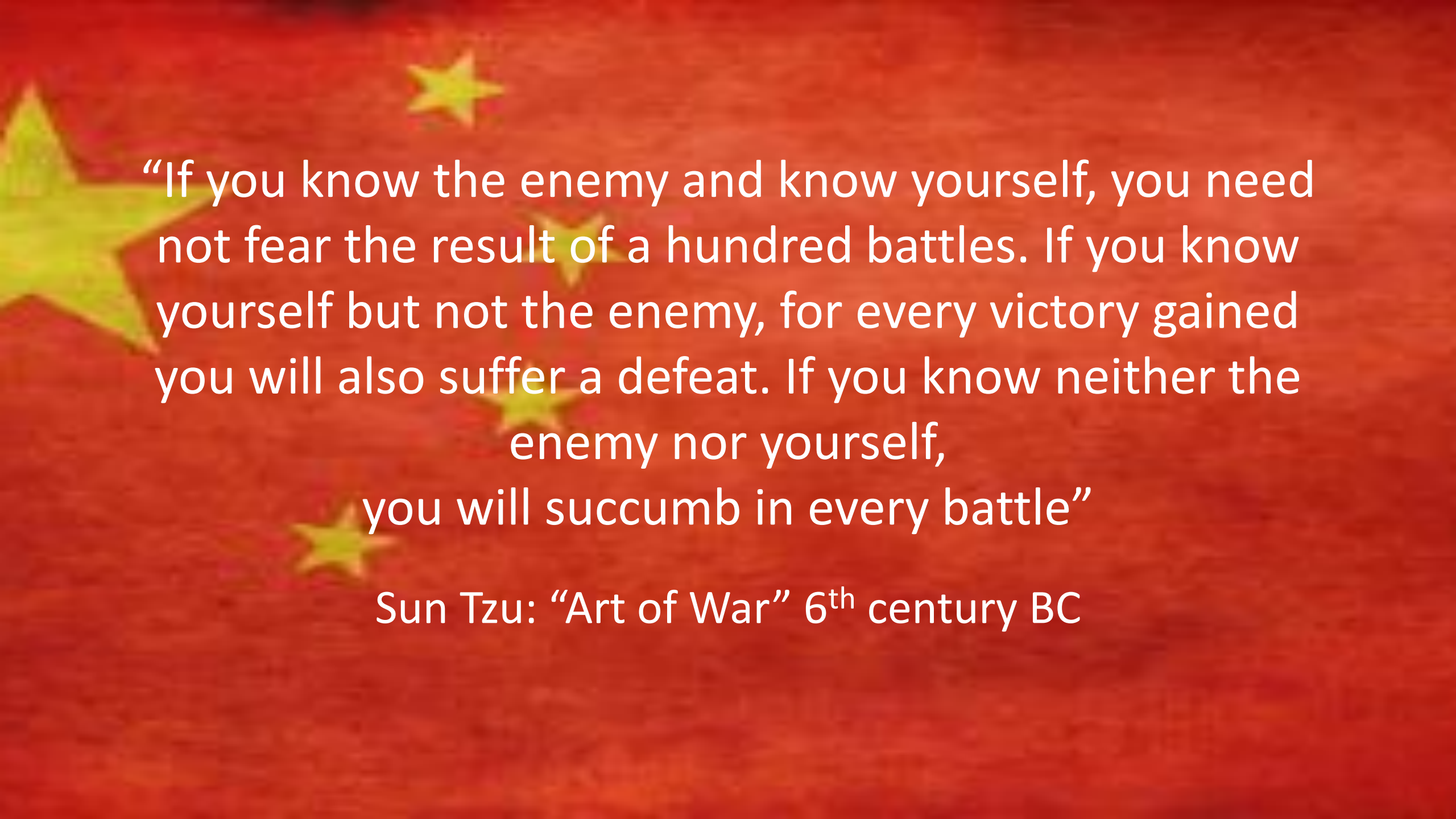




# Go to China Right







“If you know the enemy and know yourself, you need not fear the result of a hundred battles. If you know yourself but not the enemy, for every victory gained you will also suffer a defeat. If you know neither the enemy nor yourself, you will succumb in every battle”

Sun Tzu: “Art of War” 6<sup>th</sup> century BC

# What we will do

History

Chinese  
reforms

China  
today

Doing  
business in  
China

# China Strategy

- Geography matters
- History matters
- Politics matters
- Economy matters
- Business strategy matters too



The background of the image is the flag of the People's Republic of China, featuring a red field with five golden-yellow stars. One large star is positioned on the left side, and four smaller stars are arranged in an arc towards the fly. The word "Geography" is written in a bold, golden-yellow, sans-serif font, centered horizontally and partially overlapping the stars.

# Geography

# Geography

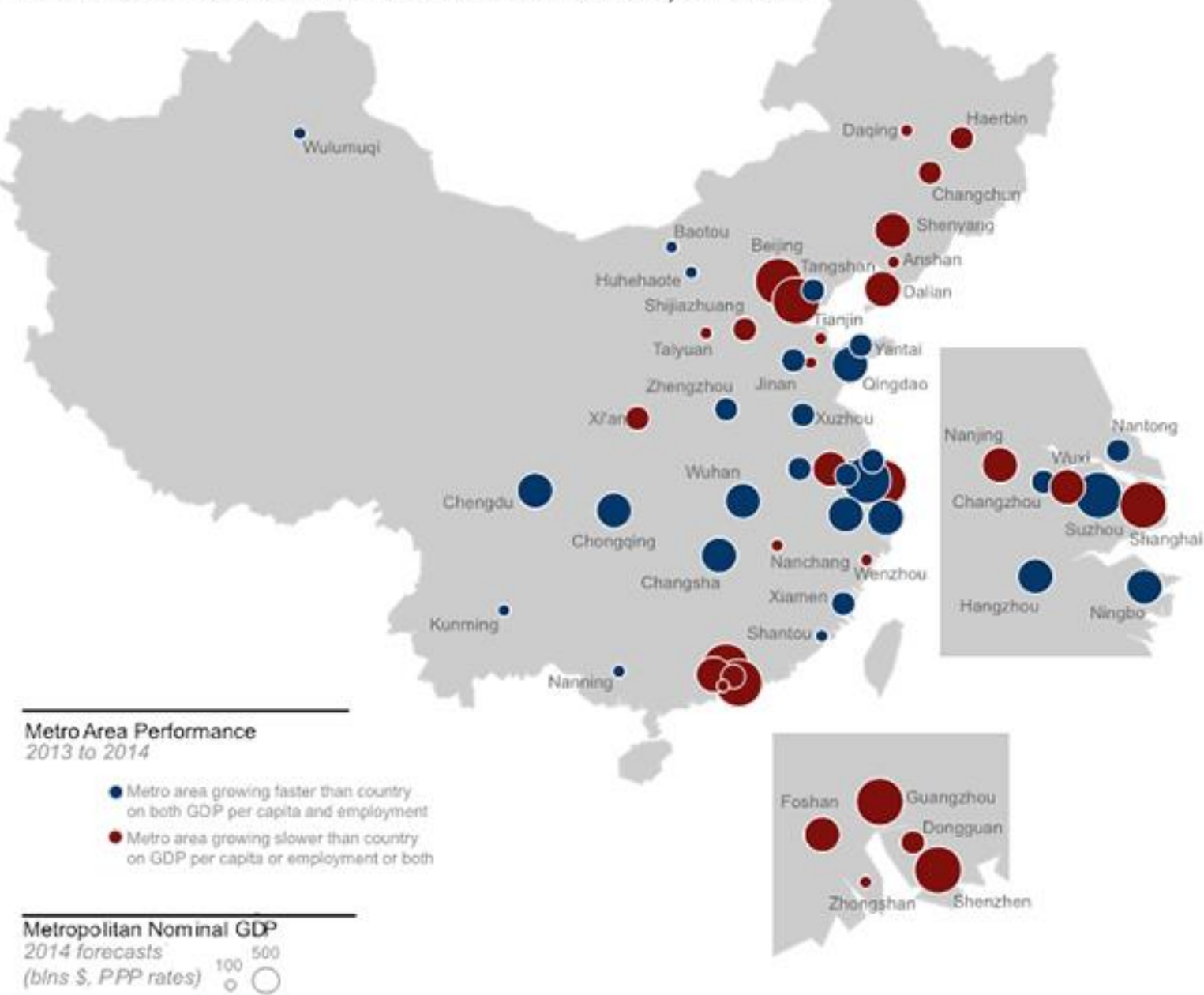




## China Major Rivers Map



**MAP 3. METRO ECONOMY-COUNTRY GROWTH DIFFERENTIAL,  
CHINA'S 48 LARGEST METROPOLITAN ECONOMIES, 2013-2014**

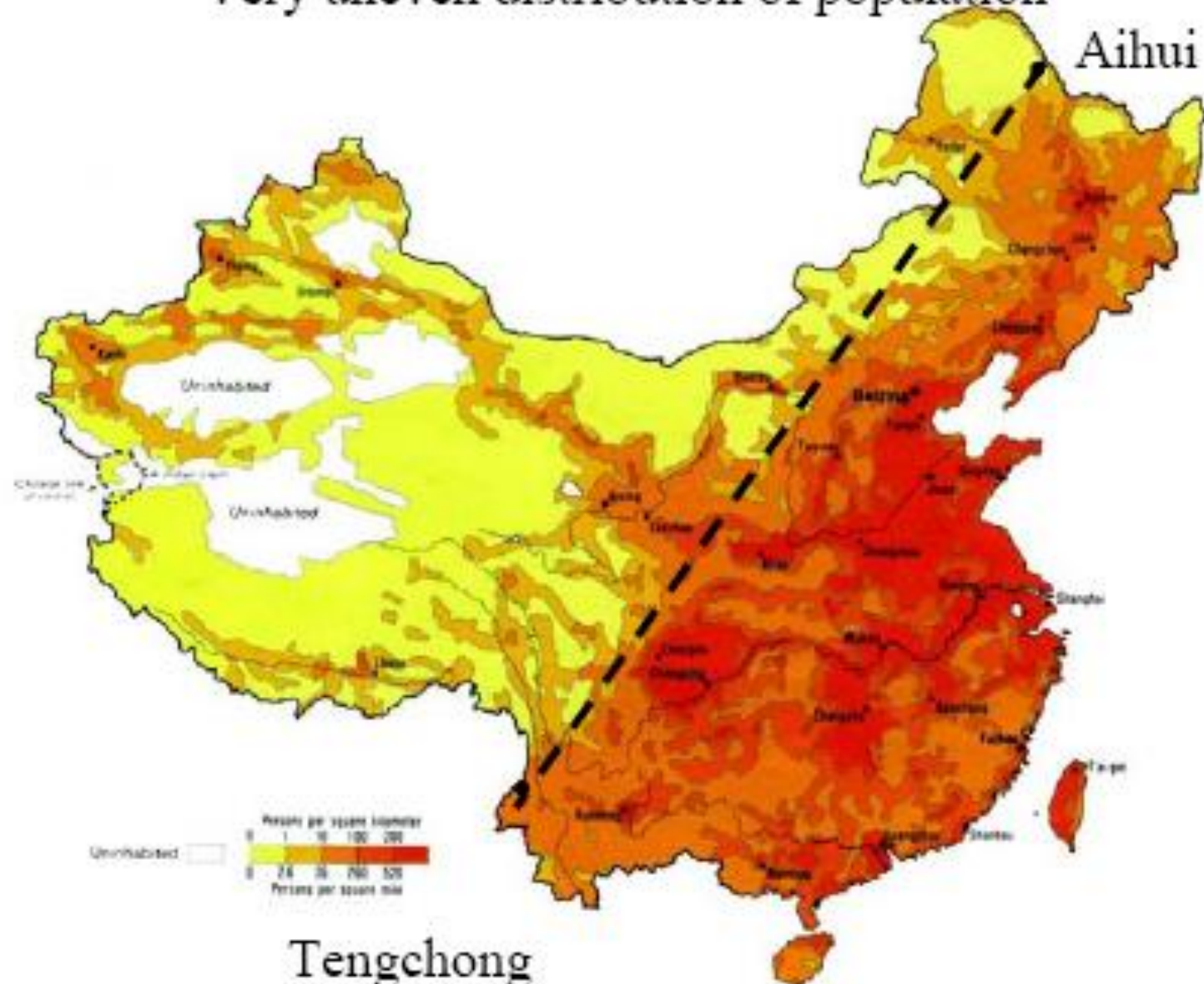




China: Population Density

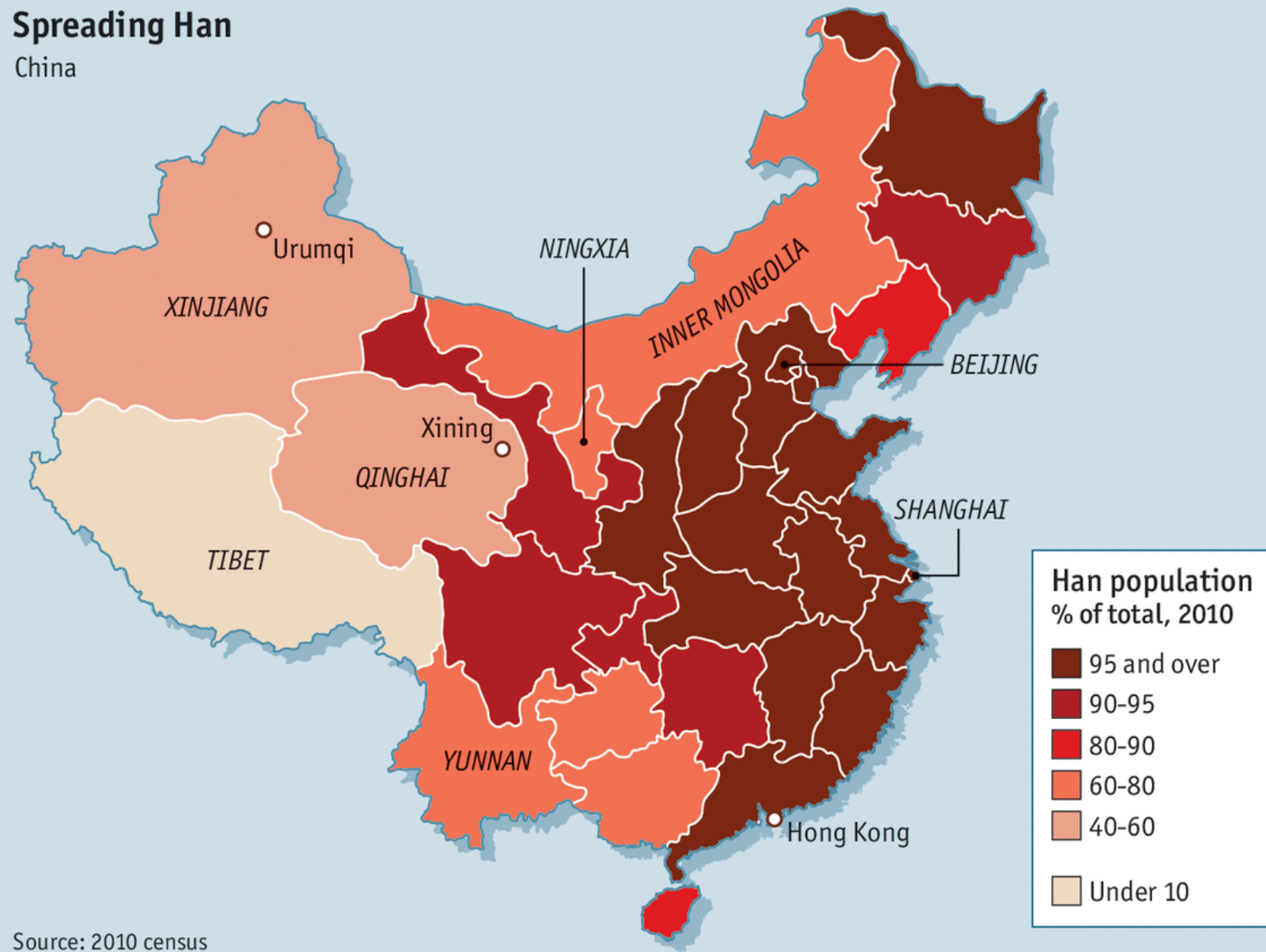
# A-Population

Very uneven distribution of population



## Spreading Han

China



Source: 2010 census

The background of the slide is the flag of the People's Republic of China, featuring a red field with five golden-yellow stars. One large star is positioned on the left, and four smaller stars are arranged in an arc to its right.

# History



# Chinese technology superiority

## innovation

	China	Europe America
• Rotating fan	180	1556
• industrial bellows	1310	1757
• wheel barrow	231	c.1200
• cast iron	II century. a.C.	XIII century
• sternpost-mounted rudder	VIII century.	1180
• gun powder	c.850	XIII century
• Paper	105	1150
• movable type printing	740	c.1400
• Porcelain	III - VII century.	XVIII century



Source: Seeds of change, Henry Hobhouse





## why does china go into crisis?

- Isolationism
- A close society that doesn't evolve and miss all the social and technological innovation of the XIX century)
- The growth potentiation of an agrarian society (although with high yields) was close to be ended
- The population growth made the economy even weaker.
- Foreign invasion / colonialism
- The decline of China started well before the rising of the CCP
- (china didn't have one real day of democracy in 5000 years )
- but....



but....

- Agriculture well developed (high yields per acre but not if you consider manpower)
- A good network of rural markets
- Advanced Institutions (paper bills since 1820)
- A complex contract system
- Legal institutions that worked also at interprovincial level
- Good banking system
- Small firms but well interconnected (silk as an example)
- Competitive markets and a fairly good social mobility even if poverty was a problem.



# Collapse of the Imperial System in China



- 1911 = End of the last (Qing) dynasty
- 1912 = China became the Republic of China
- Republic of China ruled from 1912 until 1949
  - First president of the Republic of China = Sun Yat-sen (died in 1925)
- (general Yuan Shi-kai in real power till 1916)

# ★ Last emperor Pu Yi

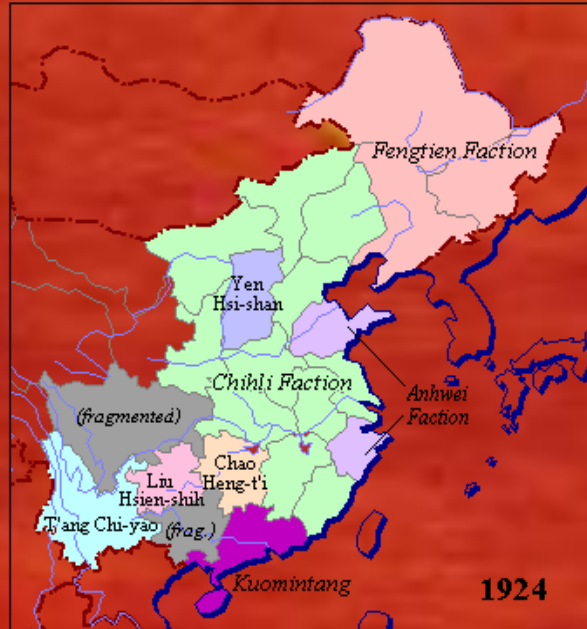


- Born in 1908 – emperor till 1911
- ★ Puppet emperor of the Manchukuo state (controlled by the Japanese Army) from 1932 to 1945 (taken prisoner by the Russians)
- ★ Condemned in China as a criminal. Pardoned in 1959
- Lived in Beijing working in a mechanical repair shop of a botanical garden and later as a researcher in the institute of literature and history under the Chinese People's Political Consultative Conference

# Warlords in the 1920s



- 1916 – 1928 = China's central government fractured and various warlords ruled different sections of China



China in 1924



# Whampoa Academy



- Established in 1924 by the Nationalist Party
- Both member of the Nationalist and Communist party studied at this military academy (like Liu Shaoqi, second president of the Chinese republic)
- Mao Zedong made some seminars

# The Nationalist Party



- 1928 = The Nationalist Party gained control of China and reestablished a unified central government
- Under the leadership of Chian Kai-shek, a military officer
- He led the Nationalist Party until 1949

# The Nationalist Party



*Chiang Kai-shek*

- Promoted modern development
  - Railroads, banking, airline services, etc.
  - Early industrial development mainly in coastal cities (light industry, foreign and Chinese companies). Heavy industry in Manchuria, Japanese companies.
  - In 1945 The Nationalist Party took control of all these firms (90% steel industry , 45% cement, 2/3 Electric production)



# The Nationalist Party



*Chiang Kai-shek*

- Problem: Impacts of these achievements only in the cities → rural areas (where most of the population lived) were still impoverished
- Problem: Left the Nationalist Party with a limited base of support
  - Urban elites; rural landlords; Western powers

# The Nationalist Party



*Mao Zedong as a young revolutionary*

- Constantly faced opposition from the newly developed Chinese Communist Party (CCP)
  - Founded in 1921
  - Grew enormously over the next 28 years
  - Found a charismatic leader in Mao Zedong



# The Nationalist Party

- 1927 = Nationalist Party chased the CCP out of China's cities
  - CCP developed a new strategy = appeal to China's peasants for support
  - It was a strategy built on a weakness because CCP couldn't fight directly with the Nationalist Party in rural areas.





# Chinese Communist Party

- Slowly gained the respect and support of the peasants by:
  - Using guerrilla warfare tactics against the Nationalist Party
  - Experimenting with land reform in areas under communist control
  - Efforts to empower women
  - Creation of a communist military force to protect against Nationalist Party attacks



*Chinese Communist Guerrillas*

# Long March (1934 – 1935)

The map illustrates the Long March (1934-1935) across China. A legend in the top left corner indicates that the solid red line represents the 'Route of 1st Front' and the dotted red line represents the 'Route of minor commands'. A scale bar shows 0 to 400 miles. The map covers a large area of China, including provinces like Xinjiang, Ningxia, Suiyuan, Shanxi, Shaanxi, Gansu, Sichuan, Shaanxi, Hubei, Hunan, Guizhou, Yunnan, Guangxi, Guangdong, Fujian, Zhejiang, Anhui, Jiangsu, Shandong, Hebei, Henan, and Manchuria. Major cities like Beijing, Shanghai, Nanjing, and Chongqing are marked. The route of the 1st Front starts in the north, moves south through Shaanxi and Sichuan, and ends in the southwest. The route of minor commands branches off from the main route and moves towards the southeast. The map also shows neighboring regions like Outer Mongolia, Korea, and Taiwan.





# Chinese Communist Party



*Japanese Invasion of China, 1937*

- CCP gained an enormous amount of support during Japan's brutal invasion of China
  - Nationalist Party lost control over most of China and was forced to retreat to the interior
  - Nationalist Party seemed more concerned with eliminating the CCP than fighting Japan



# Chinese Communist Party



- CCP, with its communist-led People's Liberation Army, fought the Japanese vigorously
- Offered security to many Chinese faced with Japanese atrocities
- CCP membership grew from 40,000 in 1937 to 1.2 million in 1945

*The People's Liberation Army (late-1940s)*

# Chinese Communist Party



- The CCP gained even more support by doing the following in areas it controlled:
  - Reduced rents, taxes, and interest rates for peasants
  - Taught literacy to adults
  - Mobilized women for the struggle
  - Encouraged peasants to fight back against their landlords





Millions of people all of one mind vow to  
exterminate the Japanese enemy  
*Wanzhong yixin shimie Wokou*



- 1937 Japanese invasion  
(Nanjing massacre – 300 civil  
casualties in a few weeks)



# Chinese Communist Party



- In 1949, 4 years after WWII, the CCP swept to victory over the Nationalist Party
  - Most of the Nationalist Party's leaders fled to Taiwan
  - New leader of communist China = Mao Zedong



# Chinese Communist Party



- Industry and agricultural sector damaged after the war.
- Guomindang considered unfitted to run the economy (1945 – 1949 hyperinflation)
- Strong anti-western and Japanese sentiment
- Many industries already nationalized

And more

- CCP co-opted part of the former ruling class.
- Huge poverty but good human capital
- There was an industrial base that could be useful as a starting point



解放



毛主席永远和我们在一起



# Tibet



# Taiwan (province of China)



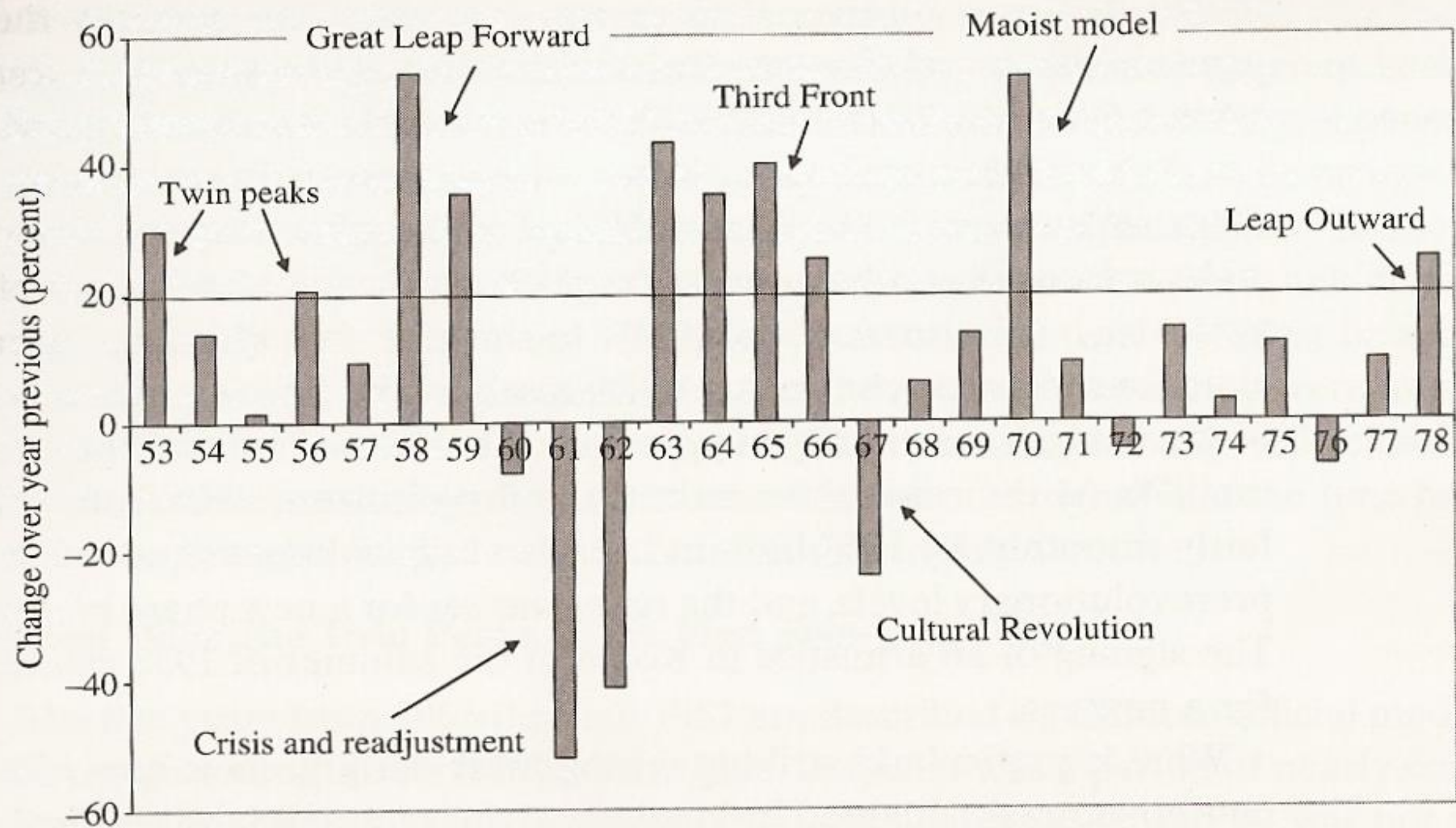
# The nine-dash line





## ★ From WW2 to 1978

- “Big Push” myth
- Command economy: 5 year plans started in 1953
- Focus on Heavy industry
- From 1952 to 1978 industrial production grew 11,5% per year
- Industry jumped from 18% to 44% of GDP
- Agriculture decreased from 51% to 28% of GDP
- strong economic and political instability (good moment and very bad moment but CCP always in control)



**Figure 3.2**  
Growth of investment

# Command economy

- Control of all factories (excluded some SMEs) plus telecom and transport networks
- Agricultural collectives took over ownership of the land and management of the farm economy (1950 CCP started to give land before controlled by large Landholders. First redistribution, after collectivization)
- “**Big push**” : consumption squeezed – high investment to support industrialization (mainly heavy industry). Planned economy – price control. Factory products were expensive, farm product cheap. Price not defined by supply and demand
- Farms and factories have to achieve defined goals.
- Managerial career controlled by CCP



## 5 year plan

- “Material balance planning”
- Nomenklatura
- Monobank
- In China price control on 600 goods in USSR on 60000 – in China there was a much larger role of intermediate institutions



我們爲參加國家工業化建設而自豪

- We are proud of participating in the founding of our country's industrialisation 1954





大力支援农业



- "Provide Great Support to Agriculture"



Study the Soviet Union's advanced economy to build up our nation  
1953



學習蘇聯先進經驗建設我們的祖國



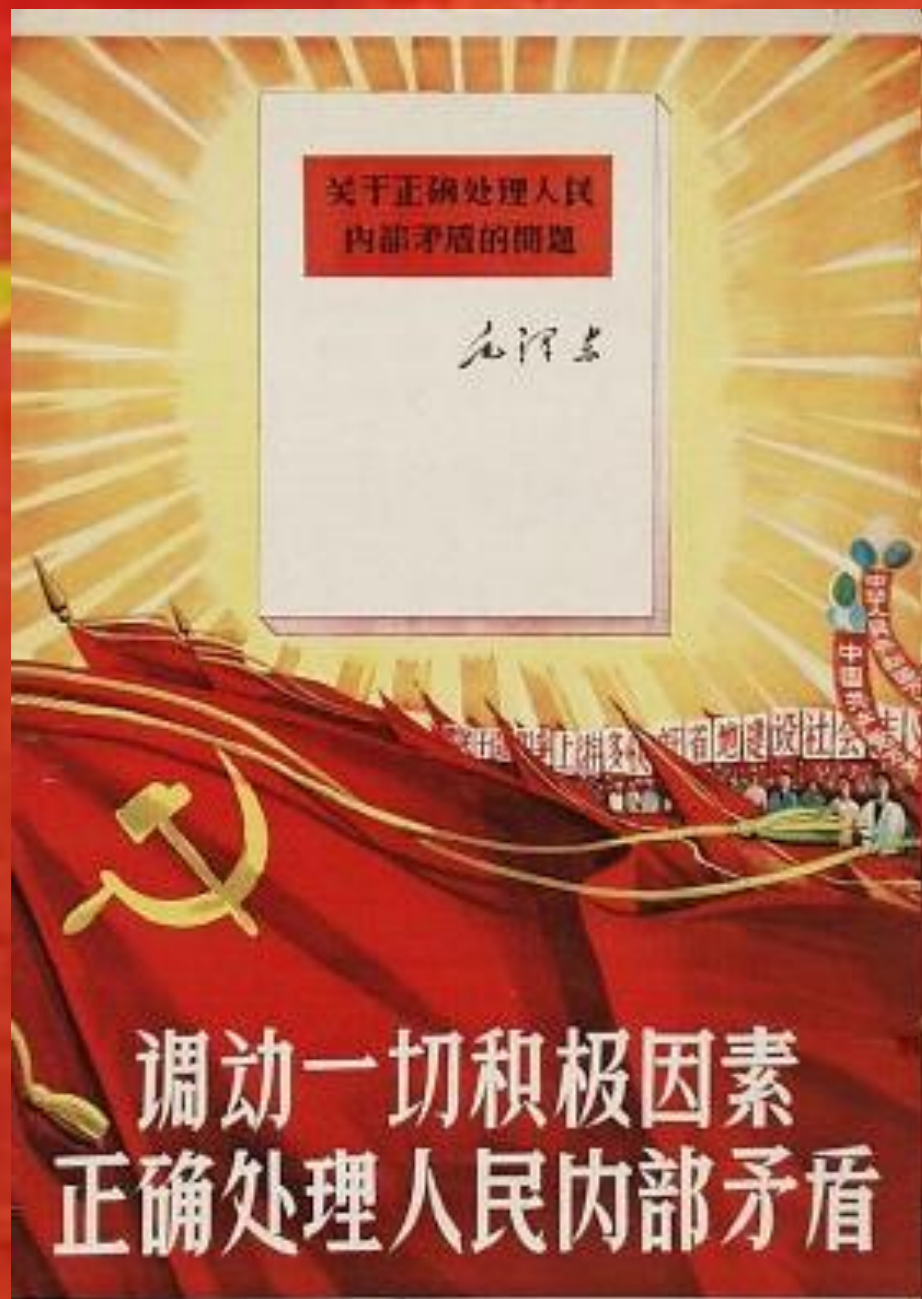
The life of the peasants is  
good after Land Reform



## ★ From WW2 to 1978

- 1949 – 1956: good economic growth but less than Hong Kong and Korea)
- 1956 – 1957: Hundred Flowers campaign
- 1958 -1961: Great Leap Forward (800.000 intellectuals sent to the countryside to labor camps.– Communes were established – material incentives and monetary rewards eliminated. No more free markets – more decentralization – «backyard steel mills»
- GLF ended in 30 million excess deaths for famine. 30 million for postponed birth.





- *"Letting a hundred flowers blossom and a hundred schools of thought contend is the policy for promoting progress in the arts and the sciences and a flourishing socialist culture in our land."*

Blast furnaces rise in level ground  
releasing red rays everywhere 1958







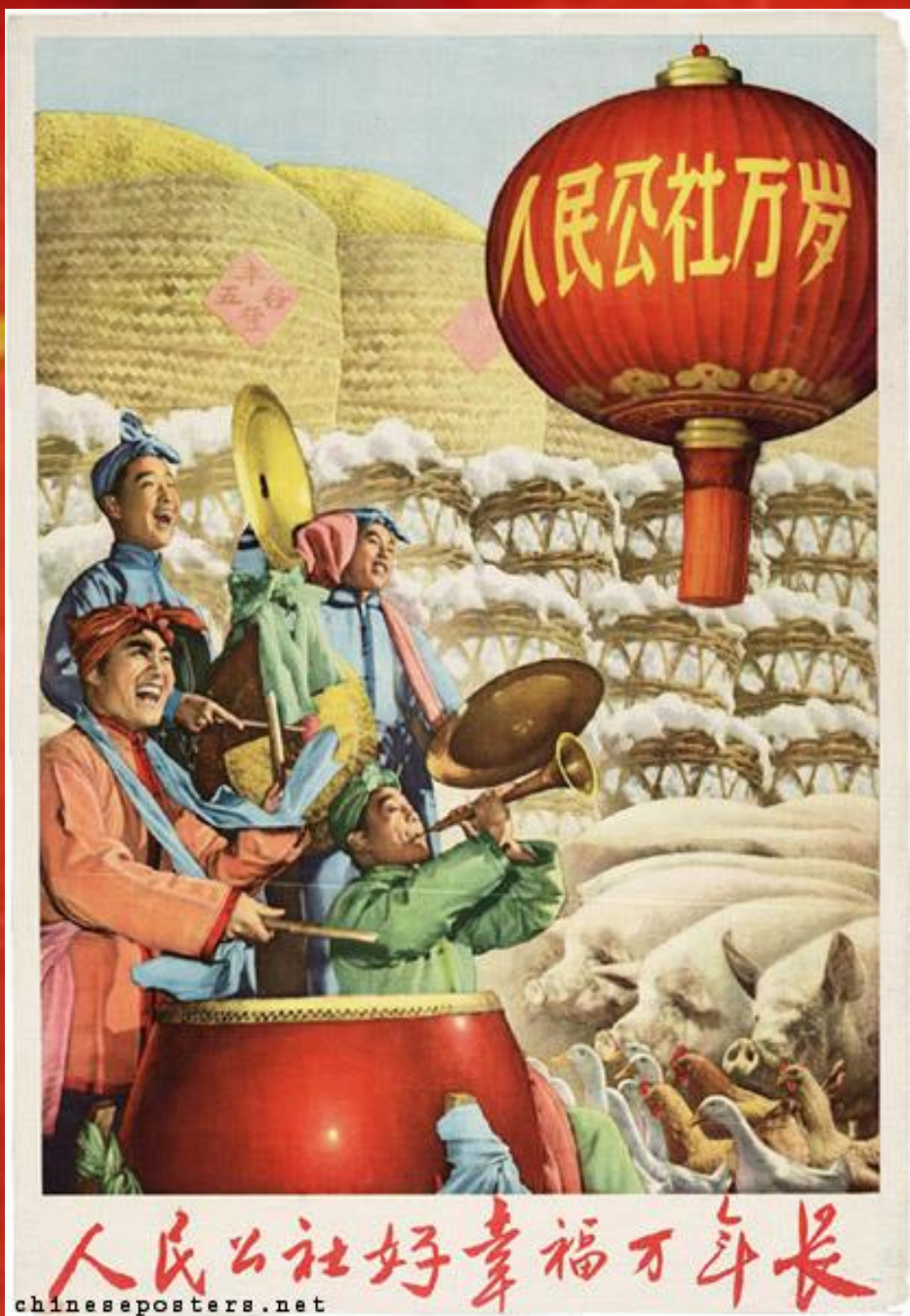
- The industry of the fatherland develops by leaps and bounds and frightens England so that it trembles with fear 1958



**Everybody comes to beat  
sparrows 1956**

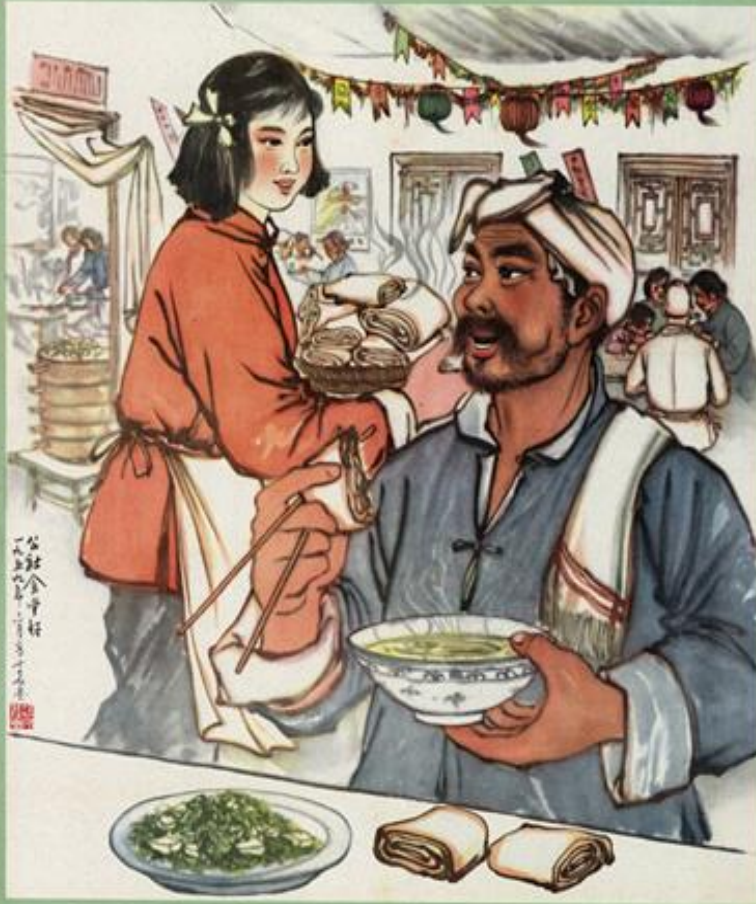
**(4 plagues rats, fly,  
mosquitos, sparrows)**





- The people's commune is good, happiness will last for ten thousand years  
1960





公社食堂强

GONGSHE SHITANG QIANG

吃着心如意

CHIZHAO XIN RUYI

飯菜做得香

FANCAI ZUODE XIANG

生產志气揚

SHENGCHAN ZHIQI YANG

- the commune's canteen is powerful, the dishes are deliciously made. You eat like you wish, production ambitions are rising 1959

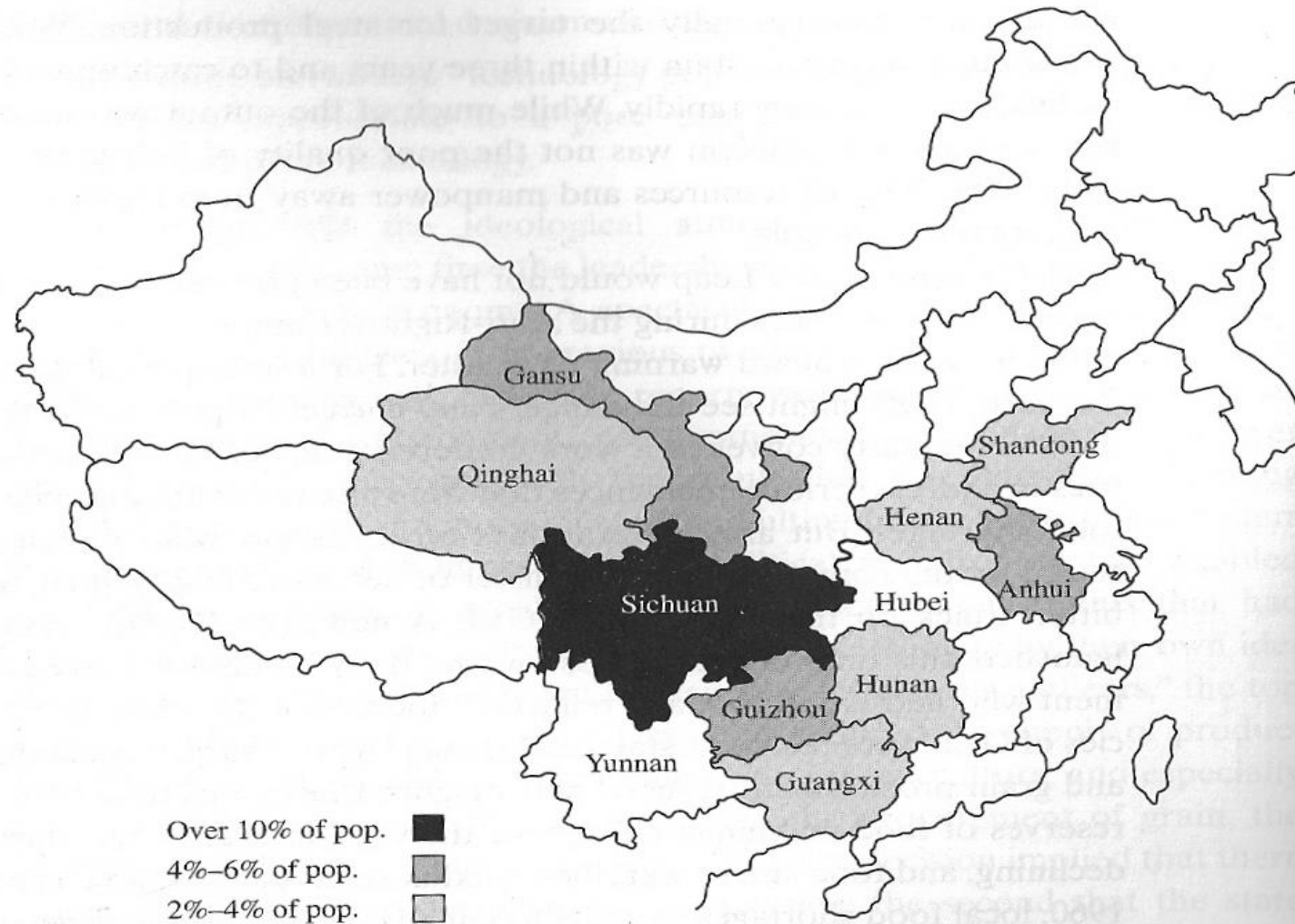




chinese posters.net

- The vegetables are green, the cucumbers plump, the yield is abundant 1959

## Famine in China



**Figure 3.3**  
The post-GLF famine



## From WW2 to 1978

- 1960 – 1963: end of the Soviet support – more power to Beijing authority – focus on the countryside (20 million workers went back to the countryside – small opening of rural markets)
- 1964 – 1966: new radicalism – “Third front Campaign” to develop inner provinces (easier to protect from a possible attack from USSR or the US)
- 1967 – 1976: Cultural Revolution (militarization of the economy – priority to national defense, support to industries to growth agriculture productivity, autarchy and austerity. Total control of the labour force. Few markets for a small number of products (no grain))

## **The Chinese economy as a bird cage**

“While reviving the economy, we must guard against the tendency to diverge from the state plan. Revitalisation should be under the guidance of the plan; it should not depart from the plan. This can be compared with a bird and its cage. A bird cannot be held tightly in one’s hand because that would kill it; it must be allowed to fly. But it can only fly within the cage; without the cage it will escape. If the bird represents economic revitalization, then the cage represents state planning” (Chen Yun).



# Cultural Revolution (1)

- 1966 1969: Mao encouraged the «red Guards», groups of young students that had the Goal to overthrow national leadership (Mao enemies, included Deng)
- Battle against the 4 “olds”: Old Customs, Old Culture, Old Habits, and Old Ideas
- No big change in economy
- 1969 – 1971: investment push like in the GLF but countryside is not abandoned
- Militarization of all the Chinese Society. A lot of Power to the PLA also to control the Red Guards that went too far.
- New decentralization especially for the industry linked to agriculture.
- Still no material incentive

## Cultural revolution (2)

- 1971: suddenly and mysteriously Lin Biao dies. He was the designated successor of Mao.
- 1972 – 1976: in 1971 new problems of food supply. Too many unproductive investments. Need to open the economy to other countries (very slow process)
- In 1974 Mao rehabilitated Deng (that works with Zhou Enlai very ill). Deng was considered a reformist
- Deng was obstructed by a group of powerful radicalists (later known as the Gang of four that included Mao's wife)
- Deng was again sidelined in 1976



# Cultural Revolution (3) – Leap Outward

- In January 1976 Zhou Enlai dies. He was Prime minister since 1949
- In September 1976 Mao dies. Hua Guofen took his place. (Mao took that decision: “With you in charge, I am at ease”)
- The Gang of Four is put in prison.
- This is the beginning of a slow redefinition of the economic system.
- China starts to buy technologies from abroad
- Still huge problems because past epurations completely destroyed a generation of leaders, managers, teachers, etc.
- Some projects, like the development of Oil field, don't perform as expected
- No money to pay for foreign technologies
- Finally in 1978 politic and economics are on the same path: 11 plenum of CCP. Deng come back to power
- Now we really start.....

Oppose economism: destroy the new counter-offensive of the capitalist class reactionary line 1967





高举毛泽东思想伟大红旗



彻底粉碎刘邓的反动路线

- Hold high the great red flag of Mao Zedong Thought, thoroughly smash the reactionary line of Liu and Deng 1966



Smash private ownership  
1968 [?]





Awakened peoples, you will certainly attain  
the ultimate victory! 1966



觉醒了的人民,必将得到最后的胜利!

The evil system of colonialism and imperialism arose and thrived with the enslavement of negroes and the trade in negroes, and it will surely come to its end with the complete emancipation of the black people.

1968





Resolutely support the anti-imperialist struggle of the  
Asian, African and Latin American people.

1967





- The fight against U.S. imperialism by people of the whole world will succeed!  
1965



Forging ahead courageously while following  
the great leader Chairman Mao! 1969



**紧跟伟大领袖毛主席奋勇前进!**

Long live chairman Mao! Long, long live! 1970



**毛主席万岁!万万岁!**





- Deepen the criticism of Deng Xiaoping, strike against the right deviationist wind of reversing verdicts (1976)

Workers, peasants and soldiers are the main force to criticize Lin Biao and Confucius.

1974





# Bombard the capitalist headquarters 1976



炮打资产阶级司令部 文化大革命以来革命斗争(二)

chinese-posters.net



# Hua Guofen



毛主席无限信任华主席  
全国人民热烈拥护华主席





- 1977
- Boundless confidence  
"With you in charge, I am at ease",  
Mao writes on a piece of paper that  
he hands over to Hua Guofeng. Hua  
uses this document - which may or  
may not be authentic - to prove  
Mao really appointed him as  
successor.



- Resolutely overthrow the anti-Party clique of Wang, Zhang, Jiang and Yao! 1976



1978



Resolutely liberate Taiwan, save the  
Taiwanese people from their misery!  
1955





We will definitely free Taiwan! 1971



**一定要解放台湾!**

chineseposters.net





notes



- ***Development as economic growth:***

Up and down

Chinese economy grew but less than in the western world or in the rest of Asia.

- ***Development as structural change***

Chinese society transformed from rural to an industrial one. China has been able to rebuilt its institutions after 1911. Problems in the seventies. *Industries were profitable but only for price distortion!*

- ***Development as welfare and quality of life.***

In the beginning life improves in the countryside

After that, strong limitation of personal freedom.

High level of alphabetization and a good healthcare network given the level of the country development.

# Capital

- Development investment led
- Government Investment in heavy industry
- Savings are form the countryside (countryside had to do the bigger effort)
- Human capital first has been developed and later destroyed
- No foreign capitals
- Improve of social capital in the 50ies. Decrease of social capital in the 70ies



# ★ People

- Very difficult aspect for growth
- First policies (sometime compulsory) to limit the birthrate.
- Need to limit mobility of people

# 'Practice Birth Control for the Revolution'. 1974







★ Marry late for the revolution!





## ★ Technical progress

- In early fifties exploitation of Japanese technologies left after WW2 in the north and by other foreign countries (Shanghai)
- Fifties and early sixties USSR technologies.
- Sixties and seventies stop relations with USSR and closure of universities
- Late seventies: impossibility to buy foreign technologies

# Trade

- Autarchy
- Minimum export of raw materials
- in 1978 Export was considered a crucial element for the “leap outward” but was not enough to buy foreign technologies



## When Mao passed away.....

- Chinese Growth model was already at the end of its possibilities like the one based on agriculture in the XIX century

# Cina Vs Taiwan and Hk

**Table 3.1**

Two contrasting industrialization strategies

	Heavy-industry–priority, PRC	Light-industry–priority, Taiwan, Hong Kong
Basic strategy	Strategic industries with most upstream and downstream linkages	Begin with downstream consumer goods industries; gradually work upstream
Saving done by	Government, state-owned enterprises	Households, private business, government
Investment decisions	Government	Private business, government infrastructure
Source of demand growth	Domestic industries, government investment projects	Foreign and domestic consumer-goods markets
Household income	Slow growing	Moderate to fast growing
Coordination by	Plan	Market, with some government “steerage”
Openness to world	Low	High