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FOREWORD

Li Daokui

What a tumultuous time the year 2005 has turned out to be. “Rethinking of the reform” was the proper name of it labelled by those long in the tooth.

A poignant scene to revisit, but it was not without its plausibility. As it is, the country at present is in the middle of the transition. Clearly, something somewhere at some opportune moment has to be evoked just to help set their unsettled minds more or less at ease.

What really boggles the mind, however, is of their actual prey that took the form of the eggheads of academy rather than the fatheads of the powers that be who are, in fact, the can-doers frequently caught red-handed. Well, part of the clarity may lie with the state of the regime that still renders it a nervy and pricey bent of wagging and pointing the finger at the Party reign. Plus, it was not entirely unjust, as they may have insisted, to take the economists as fall guys picking up all the tabs. After all, the blueprint of the reform was the handiwork of that brainy tribe that has since been accused of being bought over by the vested interests.

Hitting a sticky patch, all right. Yet, that cacophonous clamour won't be noisy enough to take the shine off the sure-footed stride that has at length seen those little arcane models of the dismal science greatly tailored to the domestic use. In the year alone, there were at least three areas where we have witnessed the progressive headways sustained. First was the up-tick of a notch or two in the quality of recruitment. Thanks to rapid economic growth and improved conditions in home research, a lot more fully trained talents blooded in teaching and research overseas were attracted to home-grown outfits in the trade.

Then, it was the cerebral ambiance, so rich has it grown that there are now more pleasant places for the highbrows of the profession to dawdle their hours away, hobnobbing, back-patting, or simply pressing the flesh around. Indeed, it is no longer a head-scratching undertaking, typically for members of chattering class, to get a foot in some economic conferences, periodic gatherings, or even a few noisy jamborees if one chooses. Finally was the continued change for the better in the appraisal system for the papers produced. Not only has it measured up, or in some cases got closer, to some international norm, but also been taken up by broader society and spreading. The papers enclosed in this book, for example, no longer crop out of one or two majors of the field. Rather, they are widely scattered across the landscape.

That said, this edition of *Economics in China*, with all the flying colours of papers, is another way of peppering up those

that unwittingly took the rap on the knuckles over the year. Altogether, there are 18 pieces chosen in line with the principle similar to that of the previous editions, which takes in three benchmarks. One is the focus of study that ought to be closely related with the on-going reform. Two is the rigor as well as the norm applied to *modus operandi* in either academic or practical endeavour. And the last is the general value inherent that would lend itself to the build-up of knowledge and experience in the line of specialty. Long-winded, all the same. Give or take here and there, however, it sounds not far from “localisation of alien culture”, does it? Well, in economics of course.

And finally, some words spared for the culling process that, in the minds of some readers, could be flawed one way or another as I may have missed out some of the worthy while bundled in others of the lesser. No holding forth in ifs and buts over it, since it happens from time to time in this kind of work. Wouldn't it be true, as the old saying goes, that the beauty is in the eyes of the beholder? What is weighing more heavily on my mind, however, is my gratefulness to such Journals and magazines as *Economic Research*, *World Economy*, *Administrative World*, *Economic Quarterly*, *Economics Daily*, *China Social Sciences Review*, and *New Political Economic Review*, as they have offered crucial support for the success of the task. And also my appreciations of such individuals as Messrs Liu Linlin, Mei Song, Feng Junxin, Yi Xingzhong, and others for their professional assistance throughout.

Now, at long length comes what we have to pen for in this space. Admittedly, the entire courtship went fiendishly hard with me. Yet, there has been little love lost between me and the stories in the bag, which, unlike the harshness on the way, should be easy on the ears. Or, should they? Read on to get the sense of it.

Right through the country's nice and easy run of "peaceful rise", as some folks would like to intone, one of the glaring streaks of home economy has been its sustained level of high rate of saving and investment in the midst of the neck-breaking pace of growth. Intuitive, though, it has been short of the proof in numbers. *High Rate of Saving, Investment and Growth over the Period of Transition in Labour Force*, by Li Yang and Yin Jianfeng, is one attempt to make up for it with the help of their little contraption dubbed "vector auto-regression model" (VAR). The study not only rolled out the perceived origin of the phenomenon, but also came up with a novel account of the economy availing itself of external capital markets to its advantage.

Just as a witty remark has it that many hands make the light work, so is the run-away economy that has by far been fuelled with influx of cut-rate coolies on hand from the backwoods of the land. High rate of growth begot high rate of saving as extra income got tucked away under a mattress, now that there were not many a place worthy of investment with a shabby state of the financial system. Yet, without high rate of outlays in plants and tools, the speedy expansion would be

curtailed with the consequence of oodles of the labour left idle. It became, in point of fact, the case of needs must of cozying up to the capital markets offshore while awaiting thousands of flowers to blossom on the home turf. There, then, came in the picture of state officials bending over backwards to pull in foreign direct investments while their central bank comrades scrambling to pile up stocks of US treasuries, Euro bonds, or things of that ilk by shovelling out loads of savings the other way.

What a topsy-turvy world of activity. Yet, we have to leave there and get down to the nitty-gritty of scholastic task of a different sort. For a long while, the fief of the comparative literature on firm performance has been in the state of triumvirate, dominated by three schools of thought. Each, though, dwells on one of the three measures as competition, ownership and governance while ignoring the rest with the pedantic hubris. Not surprisingly, they have been taken down a peg or two in recent time as gathering doubt reaches its crescendo over the predicting power and hence, usefulness of their much ado.

In the work, *Competition, Ownership, Corporate Governance: Their Importance and Interactions*, Messrs Hu Yifan, Song Min and Zhang Junxi were poring over the World Bank statistics of 736 native firms, across seven sectors over the period of 1996-2001, to assess the relative importance of the three measures. Their findings are quite intriguing. While, as expected, all three did pay their ways to the per-

formance with a lesser tribute from the competition, the ownership in the form of privatisation was somehow paired up with each of the other two in a zero-sum play-out. Counter-intuitive? Not that it makes the state of nature count. Nonetheless, the study does suggest that the three schools of view are indeed lack of sorcery by themselves, as some kind of combos is needed.

A brilliant idea you may say. Yet, it could have hit its cul-de-sac, languishing in the limbo of paper world, save that Messrs Lu Ting and Liu Xiaoxuan had come along with their empirical study, *A Model of Ownership Structure—Reform and its Impact*. The work, focusing on the impact of privatisation on the firm performance, has literally seen to that little pretty at long last basking in the sun. Based on the survey data in the later half of the 90s, they found that efficiency gains between the privatised and the non-privatised firms were seriously large enough to merit some market-based fix in ownership structure. And most importantly, it was a type of privatisation and its resulting governance structure that mattered most in the firms' performance.

Care, however, has to be taken in these number-crunching exercises since there are always drawbacks, such as data limits, factor oversights, formular choices and many others intrinsic in this kind of modelling. The similar inquiry, *Ownership Structure Reform of SOEs*, by Mr. Li Ji and his colleagues, for example, have produced quite an opposite brain-wave with different set of data collected from 500 or so corpo-

rations. Oddly as it goes, the fully privatised firms under the present market conditions did not possess the supposed cost-advantage over their state-owned counterparts in welfare largesse, except that they were more likely to take on higher risk by diversifying their operations. The upshot was then clear that the strategy of going private should be taken with the extent of market maturity in mind.

A mortal blow to the spirited *laissez faire*? Certainly, it does not make a comfortable reading for them. Still, room remained for a swift comeback as they might yet be embroiled in the fracas over the proper way of assessing the issue of the kind. One idea is to take a state-owned firm as a public project whose appraisal result is then weighed against its actual stock value so as to see the net effect of state intrusion on its market performance. A commonly used method in gauging public projects is that of cost-benefit analysis(CBA) that could, in this case, drag in such values as welfare, operational risks, budget constraint, and what have you. With social fallouts in mind, a little CBA could thus have a big role to play, wielding the telling pixie-dust of NPVs (net-present value) in its projecting charm for any of state-owned something it comes across.

State ownership, Operational Risks, Soft-budget Constraint and Firms' Performances, by Li Tao, is one of bold cracks, which has gone to great lengths to do just that. Based on the statistics of listed state-owned companies, it found that amongst the poorest performers—the bottom 30% of the firms investigated, all values in NPV were popping up high in the

positive area, whereas no clear evidence of net-plus from the similar activities shown in the top 10% of them. It was blindly obvious that the state meddling, for whatever purposes or intents, had taken its toll on the firms' internal rate of return. The question that follows is: what is the purpose for a state to own firms? If merely as tools of servicing its social and political ends, fine, keep them albeit unwieldy and expensive. But otherwise loose them. That finding, in its own right, might well tip the balance of the debate over the validity of the state ownership.

The tendency of regional protectionism is closely related to the economic activities of local officials. There have always been controversies about the extent of regional protectionism and its impact, but there lacks systematic empirical evidence. *Regional Protectionism in China: Direct Micro-evidence* by Gong Binglin, Xu Lixin and Chen Guangyan filled this blank. By using a new survey specifically designed for the topic of regional protectionism, the paper found that phenomena of regional protectionism notably declined as time passed by. Regional protectionism also varied a lot with regard to different provinces and different industries, among which the tobacco industry and beverage industry (including alcohol) were the most badly hurt. Moreover, the development of impoverished inland regions met the most obstructions from regional protectionism. Therefore, the economic return from eliminating regional protectionism was quite obvious. What's more, the lesser the extent of regional protectionism, the higher the rela-

tive prices of goods in other regions, and therefore the more attractive the commercial environment of other regions and the higher the export value to other regions. These findings remarkably expand our discussion and deepen our understanding of relevant issues.

Meanwhile, the issue of RMB exchange rate becomes a hot issue as well as an important economic research topic in recent years. Here we selected three representative papers. *The Equilibrium Exchange Rate of RMB and Maladjustment of the Exchange Rate : 1991 ~ 2004* by Shi Jianzhun and Yu Haifeng synthetically utilized models of equilibrium exchange rate universally used in the world and conducted a systematic research on the issue of RMB exchange rate. Equilibrium exchange rate is based on the hypothesis that the exchange rate is an important influence to macro-economic equilibrium. Either overly high or overly low exchange rate will result in the dislocation of the macro-economy. We define the equilibrium exchange rate as the exchange rate under which the macro-economy is at equilibrium. The paper not only utilized the concept of equilibrium exchange rate, but what it used was a relative new method—behavioural exchange rate method. The paper demonstrates a skilled treatment of data, including the consideration of possible roots of unity of various macro-data. Further, the findings of the paper are quite interesting. For example, during 1992 to 1994 RMB was undervalued and from the forth quarter of 1994 on the real exchange of RMB was in the state of appreciation. Similarly, from 1995 to 1999 the exchange

rate of RMB was higher than its equilibrium rate, so its value started to decline. The paper is a rare masterpiece with regard to methodology among relevant domestic literature. There is one point that requires further discussion and exploration: under the circumstance that the Chinese economy has not been fully marketized, does the exchange rate have such a huge impact on the balance of Chinese macro-economy? The question is whether there is an inner connection between the level of exchange rate and the balance or imbalance of the macro-economy, though statistically the connection exists. The answer to this question is the theoretical basis of RMB equilibrium exchange rate which requires further investigation.

Zhang Shuguang's paper *the Issue of RMB Exchange Rate: its Appreciation and Cost-benefit Analysis* first systematically reviewed the evolution of RMB exchange rate system since the Reform and Opening Up, and then suggested that the imbalance of macro-economy is demonstrated by the reciprocal circulation and mutual reliance of the real economy and the monetary economy. In real economy, the balance of macro-economy relied on both the export to external markets and investment, while in monetary economy, there existed a reciprocal circulation; on the one hand an enormous amount of savings flowed abroad, and on the other hand foreign capital was attracted. Using econometric analysis this paper discussed the influence of RMB exchange rate on China's import, export and attracting foreign capital. It also found that RMB exchange rate did have an influence on China's export though this influ-

ence had a lagging nature, and this influence tended to fade after 7 lagging periods. This finding is worth noticing because such systematic empirical research is quite rare since the RMB exchange rate became a hot issue. However, the paper can be improved in one aspect: its econometric analysis is a little crude in that the roots of unity of some macro-variables were not tested.

In the paper *to Ease the Pressure of Hot Money: Self-Regulation Mechanism of the Market and Policy Measures*, Sun Huayu and Ma Yue constructed a monetary model of sticky prices in a continual time setting with consideration of exchange rate expectations, and described a massive capital inflow effect of the expectation of RMB appreciation through such a normative model. One conclusion of this normative model is that the marketization of interest rate can to some extent ease the pressure caused by the expectation of RMB appreciation, and meanwhile, the expectation of RMB appreciation has a self-realization nature and multiple equilibriums. The significance of this paper does not lie in its detailed policy advice or vivid description of the reality, but in that it used very normative research method of international finance to study the topics of RMB appreciation and inflow of hot money, which is very commendable.

Social problems in the development of Chinese economy received a significant amount of attention in all social circles, and this is also reflected in economic research. Here we selected three papers with profound research results, covering topics

of property distribution, rural workers and medical needs. The paper *the Uneven Property Distribution of Chinese People and Empirical Analysis of its Reasons* by Li Shi, Wei Zhong and Ding Sai distinguishes itself because though the misdistribution of incomes receives much attention the uneven property distribution lacks systematic research due to lack of data. This paper by the three authors is pathbreaking in this field. They found in their survey in 1995 and 2000 that wealth growth of Chinese citizens was faster than GDP and income growth, and the disparity of wealth distribution enlarged quickly. This enlargement of the disparity was mainly due to the enlargement of disparity between cities and rural areas, and wealth disparity was caused by the privatization of publicly owned houses. There was no such privatization process in the rural areas, so the growth of wealth disparity and income disparity in rural areas was not as quickly as in cities. This finding is quite significant for studying various phenomena in the Chinese economic reform process and problems it brings.

The issue of rural worker is a unique phenomenon in Chinese economic development. Rural workers work in cities for a long term, have the right of use of land in the countryside, but do not have registered residence in cities. This phenomenon is different from the dual economic structure in the conventional economics for development. In fact, rural workers move between cities and rural areas constantly. Lack of rural workers in some regions in recent years is partly because some rural workers start to move back to the countryside. Zhang Luwen's

Theory and Case Study of Rural Workers' Moving Back systematically reviewed relevant literature in the international economic circle and proposed his own theory. The main point was that rural workers determined the direction of their own movement after a rational comparison of the relative returns between working in cities and staying in rural areas. The paper proved his theoretical discovery to a large extent by surveying rural workers. As an academic paper that specifically studies the movement of rural workers between cities and the countryside, this paper represents a relatively high level of economic research and it is worth further discussion by later literature.

The health and medical issue has become a social focus in China. The paper *Health Needs of Our Citizens and the Grossman Model—Evidence from the Interface Data* by Zhao Zhong and Hou Zhengang for the first time systematically studied the connections of people's health level, education level and income level by using China's 2000 Health and Nutrition Survey. Based on the survey of nutrition, the paper constructed a life quality index of an individual which is directly based on an individual's health level index including action index, physical activity index and social activity index. According to the long-term research of health economics, an individual's health level should be related to some of his or her characteristics, such as education level and income level etc. The paper came up with some interesting findings: the distribution of people's health level was more even than that of income level; women's education level had a positive effect on their health