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Foreword

Zhang Weiying

It happened that I was honoured by UIE with the assignment of being executive editor in chief for the project of *Economics in China*, 2004. Like all my predecessors in previous editions, the task is to pick out, amongst the papers recommended by the members of Compiling Committee, what I think is rather representative in terms of both focus and level of domestic research that year. Of 41 papers stacked up high on the table, 17 came to pass, making their lucky way to the final print. A tricky business, I have to say. But what matters is how the Jesus I juggled them all out.

The sticks at hand are in three. One is the focus that is expected in line with some eye-popping issues bubbling up in the on-going reform. Two is the rigor as well as the norm (or standardisation) looked for in either academic or practical travails. And the last is the value inherent that would go a long way towards the build-up of knowledge and experience in the field. Little doubt, there are very much more than these 17 of the winning pack that live up to the par, only dropped in the last minute's consideration for the mere sake of space availa-

ble. Tough luck, as they are unwittingly rendered to team up with the group of also-rans. My apology all the same. It might yet be more comforting to know that the judgement exercised purely stays with me, not further beyond.

And that leaves us to those last ones standing, whose footholds, admittedly, scatter all over the place. In general, they spread over as wide the areas as that of regional disparity in both income and growth, the process of market integration, governmental behaviour and laws, rural economy and its labour markets, restructuring in both state-owned factories and banks, reform in the land ownership regime, and others. From here on out, I will make use of the remaining space to sketch out the story about each of our lucky survivors.

The one that heads the crowd in this edition is Dong Xian-an's paper, *Regional Income Disparity 1952—2002: Some Explanations*. Indeed, there is no secret that in recent years regional income disparity has been one of sizzling issues that gobble up bulk of the resources available to those sparkling brain-trusts in the country. No surprise, then, there are a slew of studies devoted to it, covering half century's development. What makes Dong's work superlative is that not only does it round them all up in one exquisite shot, but with anecdotal evidence and statistical justification retools the analyses in two of the popular hypotheses. One of them holds that the gradual shift in the scale as well as tightness of state control over both goods and factors markets would seriously impact on growth of regional economies. The other states that growth in

different provinces could possibly diverge if labour mobility is restricted under the circumstances of relatively free flow of goods and capital.

With elastic and restricted statistical devices, the author tested his growth model that takes in such explanatory variables as human and physical capital, composition of agricultural sector, income disparity between urban and rural households, industrial make-up, ownership structure, scale of local government, size of firms, household formation and so on. To no one's surprise, the model confirms that there exists significant positive-correlation between the growth of human capital and that of economy. As with the relationship between ownership structure and growth, the model predicts that for each percentage point of increase in public ownership, the growth would shrink by around 1.69%—1.9%. Similar result is also projected as to the scale of government, which says, for every 1% expansion in government size, the growth would suffer in a range of 0.04%—0.27%. The policy implication, then, for tackling income disparity could not be clearer: investment in human capital, smaller government, and lower proportion of state-owned economy.

Still on the subject is the paper written by Wang Xiaolu and Fan Gang, entitled *Changing Pattern of Growth Disparity in Different Areas and Factors at Work*. As the header goes, their work provides some explanation about the changing pattern of the disparity over the period of the 80's and the 90's of last century, taking into account the flow of labour, cap-

ital, and other resources, the role it plays, and the impact exerted as result of the shift in both market institutions and structure. The authors find that in both relative and absolute terms the hiatus between the eastern seaboard and the central-west inland has been broadening over the past two decades. The fundamental cause, however, is the difference in productivity, which has seen the profit-chasing capital of both home and abroad pouring into the east, fanning up market activities and tearing open growth rift.

Nonetheless, as Messrs Wang and Fan observed, over time the productivity of capital per se has been dwindling as the flux to the east continues. This trend, plus the heavy public work sustained in the west, would in the long run be conducive to the back-flow of the capital. Yet, that would again depend on some discernible uplifting of the regional total-factor productivity that has so far shown no sign of turnaround. One imperative suggested, however, is to improve regional investment environment that includes such measures as bettering the price system, raising the stake in the private sector, upping the level of governance in both firms and governments, revamping the R&D regime, quickening the pace of urbanisation, and so forth.

All of that seem just fine until one looks at the domestic market that, either by laws, regulations, or simply local xenophobic jitters (or, nicely put it “protectionism”) has long been a collection of separate, self-contained pieces. These scattered entities not only in their capacity stem the free-flow of almost

every moving objects in and out of the provincial fiefdoms, but to that effect, block any optimal allocation of resources and the realisation of regional comparative advantage. Indeed, much ado could come to little without an adequate level of market integration — one of essential attributes of a modern economy that entails unrestricted movement of labour, capital, and other resources as well as goods and services.

Fan Jianyong's empirical effort, *Trend of Market Integration, Regional Specialisation and Industrial Concentration — As well as Their Impact to Regional Disparity*, is one of those in the edition that dig into this buzz-raiser of economic chat-rooms in the country. Probing into the data covering the period of 1980—2001, What the author saw was that the level of regional specialisation and market integration had somehow lifted a notch or two (by and large concentrating on the coastal areas), though still hovering at a low level comparing to the international norm. To put it another way, the formation of regional advantage or specialisation was still in the early stage. And that may help explain the merry-go-east scurry of the manufacturing heavyweights, which in the wake of their haste split up the chasm lying in between.

That said, one of the ID-bearing symbols of the integration is the convergence of the factor productivity in different regions. *Flow of Production Factors between Provinces and Differences in Their Marginal Productivities*, the presentation of Gong Liutang and Xie Danyang, offers the first-ever empirical study on the subject. What they did is first to come

up with some individual production function for each of 28 provinces, and with them they worked out the changing pattern of productivity differentials in both labour and capital. Much to their surprise, the authors were struck by the fact that, while the differential in marginal revenue of capital was trending down over the period of 1970—1989 and levelling off thereafter, the labour's were moving in the opposite direction after 1993, even back as high the level as the 70's by the time of 1999.

That kind of finding on labour's is certainly running against ex-ante expectation as well as relevant international experience that says the differential in marginal labour productivities of different regions ought to be narrowing, or at least stabilising, along with expansion of an economy. One reasoning for that twist, as the authors suspected, is that it could be due to the upsurge of the flow in both labour and capital, especially the latter, as different provinces drawing up various kinds of preferential policies to entice inward investments got their ways.

While Messrs Fan, Gong and Xie come up with their anecdotal proofs to the woes of the market, others spare no time doing their duties as to root out the guilty parties involved. It doesn't have to take a sage to figure out which one would be first out and take the mother of all beatings — “local protectionism”, broadly deemed as the biggest drag on the stride of free trade and local specialisation. Though much blamed, notorious, and with all nasty stuff slapped on, to nail it down will one need proofs. And that is where Bai Zhongen et al fit in

with their piece of evidence, *Regional Protectionism and Degree of Industrial Concentration: Determinants and Trend*.

With the toil and moil, the authors have pulled off a huge database that contains both time series and cross-section information in 32 sectors of 29 provinces over the period of 13 year (i. e. 1985—1997). Moving across the time in the mist of the dripping figures, these number crunchers then pinned down what they think are the main culprits in stunting the growth of industrial clustering, which take the ordering of local protectionism, historical legacy, scale economies and external shock. As with the felony of all convicted — the protectionism, the verdict pronounces: the bigger share of state-owned economy does a sector have or the larger fiscal revenue does it contribute, the lower is it in industrial concentration; as local bosses have every incentive to keep it out of potential rivalries.

While there is no jarring opinion on the overall conviction, some writers would like to dispute on the pecking order of factors at play, particularly the external impact on the integration of domestic market. Li Jie and Sun Qunyan are two amongst them, who present their case with the argument, entitled *Impact of WTO Membership on Lessening Regional Protectionism: Reshaping the Beer Industry*, which exploits the notion of regional price disparity — one of the symptoms of segmented economy.

The authors make use of the monthly price index in beer market of 40 major cities in detecting the trend of price divergence for the tenuous leads. Three conclusions bear out from

their work. One is that over the time-span between Jan. 1997 to Mar. 2003, the overall picture was less encouraging, though improving. Two is that, if separating the trend at the cut-off point where the measures of reducing domestic trade barrier came into effect, the price-spread of the latter half had been narrowing, mostly around dual centres of Beijing and Qingdao. And the last one that tees up the point is that the WTO entry was noticeably the driving force behind those free-trade measures adopted by the central and local governments.

So much for the integration, before getting dizzy, it seems a good idea to take a bit of shift, turning to some agricultural matters. Now that the economic activities are undergoing a major changeover from the ancestral paddy-land practice to the modern-day urban mass-production, the drudges that are left behind on the land of yore will more than ever deserve public interests. This book also takes in 4 papers that have gone all the way to meet their unremitting grievances head on.

Since the mid 80's of last century, the state has here and there fashioned a swathe of measures purporting to alleviate widespread poverty in rural areas. One of them is the project trained on those penny-strapped counties in the hope of affording some much-craved relief to the low-income rural households. The success of it will inevitably be hinged on the targets so chosen that the finite resources could possibly produce the maximum outcome. *Project Targeting in Rural Poverty Alleviation*, a study carried out by Yue Ximing and Li Shi, is one of the efforts

that see to the process with gripping intensity.

With the data available from State Bureau of Statistics, the authors took stock of the following two facets of the matter: one is the target accuracy as to those counties chosen by the state; the other is the distribution pattern that links up the provinces, the counties and the households concerned. The upshot that their observation has come to is that there was some discernable improvement nationwide in the process of selection in 2001 compared to that in 1993, as there exhibited significant negative correlation between counties selected and the average net earning of the households concerned. Yet, up an echelon or two at the provincial level, such a correlation started blurring out. Worse still, there was no clear statistical evidence indicating that the poor had received more support financially than other groups.

In another study, *Rural Industrialisation and the Role of Human Capital*, the authors, Chen Yuyu and Xing Chunbing, look at the role of education in the play-out of alleviating game with the effort made in detecting the relationship between the levels of wages, labour employability and the length of education. They noticed that, while the average level of wages was rather independent of the length of education, the labour employability was nonetheless positively related to it. Specifically, the likelihood of being employed increases by a range of 2.3%—3.2% with every one additional year of education. And that may translate into the increase in the average level of household incomes by 1.2%. Better yet, the level of

education is also related to the kind of compensation received; higher the level of education, higher the chance to obtain it at risk-free time rate as oppose to piece related one.

While the level of education affects the employment and the average household income in the rural markets, what about the state of heath? Wei Zhong with his study, *The Role of Health in Non-farm Employment and Wage Determination*, gives it a go with the similar working technique, but using the data from 1993 *China Nutritional Survey*. As much expected, the parallel conclusion has been generated; while the state of health does not affect much of the average wage level, it does lift up the probability of employment, and thus translate into an increase in the average level of household earnings.

Staying on with the topic of rural health is the presentation of Gao Mengtao and Yao Yang, *Sex, Life Cycle and Investment in Health within a Family — An Empirical Evidence of Examining of Farmers in China*. Admittedly, there is no shortage of similar studies abroad concerning the investment in family health. Yet, most of them fall short of the comparative advantage enjoyed by different members of a family, especially by difference sexes, in the non-market activities. Plug it in together with the factor of life cycle, the model that draws on the health data of rural households obtained from 8 provinces, has patched up the hole left by their overseas colleagues. As a bonus, the study stumbles upon something new that says female members in the period of childbearing and infant caring should reign supreme in the scheme of

family health investment.

Now, turning to those ever-lasting stories of the state-owned something. For all their eternal quality, the fervency received has somehow started tailing off, as those countless nagging talk-shops have at length guzzled up all the words that domestic economists care to produce. Little it seems needed except politician's stomach. Yet, amongst the precious few, the glumness has a glossy sheen to it. *Welfare Burdens, Moral Hazard and Sofe Budget Constraint*, the paper co-authored by Lin Yifu and Li Zhibin, is one of the few that remain as the rare beholders of the state-owned beauties.

The paper represents Prof. Lin's long-held view that the low efficiency in the state-owned firms has nothing to do with their ownership structures, but is by and large the result of policy-induced welfare burdens that inevitably leaves a bend in the budgetary discipline. Under the circumstances of asymmetric information, goes the argument, managers of firms, be it public or private, would have every incentive to slack off their budget constraints as market pressure mounts. Yet, the obligation of public welfare is just there to provide a much-hankered lifeline for those head-scratching execs plotting their escape with the desperation of Showshank lifers — the “hidden action” broadly known in the trade. Little doubt, asserts the professor, reliance on the markets for the end of redistribution is always the second-best arrangement as it unavoidably alters the behaviour of firms.

Taking a slight turn to the banking sector, there we have

two field studies handy. The first one is Zhang Jie's *Re-capitalising and Reform in State-own Banks — A Perspective of Political Economics*, which tries to read into the intention and the fallout of fiscal re-capitalisation in the sector's reform. The study has produced quite an observation of some time-honoured practice repeatedly tried out by those bureau-geeks in charge of the reform. In a nutshell, it is no more than a glossing-over makeshift that invariably shines up to the external pressures. The authors argues that mere fiddling with a few technical parameters that may appear to have measured up to the international standards won't make a dent in the chronic ill of the system. Specifically, the shake-up in the fashion of reducing the share of public ownership in the sector alone would not go anywhere in the absence of economy-wide restructuring. The process of the reform, insists the author, should lie over the long haul in an evolving manner.

Indeed, there is no secret that the domestic banking system is creaky under the heavy loads of bad loans and bedevilled by the trouble of low efficiency. The consensus on the gloomy nature of the sector boils down to the ownership structure and the state of soft budget. Yao Shujie, Feng Genfu and Jiang Chunxia, then, decided to have a dig at the issue, resulting in their field report, *The Issue of Efficiency in China's Banking*, which sampled 22 domestic banks over the period of 5 years between 1995—2001. Not surprisingly, their finding has chimed with the conventional wisdom. In particular, as the reading reveals, the banks without the sloppiness in their

budgets more often than not outperforms those that are grossly coddled with cash-feed by the powers that be. As well, the efficiency level of the non-state-owned is on average higher than that of the state-owned by a range of 11%—18%.

And that at length brings to an end the long-running stories of the state-owned affairs. Time to move on to some legal matters as well as that concerning governmental behaviour. Admittedly, recent years have seen the academic economics be all the sign of overgrown species, not just being exuberant on its own turf, but crawling out onto once deemed arid patches, and in time with the fruits of all colours decking out the landscape. Sauntering down a trail, your editor cannot but stretch out, making it three for the book's collection.

The first one, *Enforcement of Third Party Rights in the Formal Contract and Optimal Arrangement*, is a co-work done by Yang Ruilong and Lu Zhoulai, where the authors try to figure out the likely sources of wide-spread wage dispute in the domestic bricks and mortar trade. The study put much of its stock in the ideas of contract theoreticians as it wrestled with the reality of unpaid services that long piques our rural folks. In the eyes of the authors, the perpetual wrangling over the pay does not rest with much-rapped tatty deals made in words between the toilers and their bosses. It does, in truth, have much to do with the formal agreements drawn up between project owners and the developers as well as that between the developers and their subcontractors.

All the same, the failure to honour such a verbal deal,

however shabby, would be more than enough to persuade those folks into some plan B solution, to wit, law of jungle in the streetwise manner as they take the matter into their own hands. What then? Instability ensues. That said, the knot of tangling up comes in two. One is the unenforceable nature of formal contracts, thanks to the fact that those bureaus in charge outwit the system by making a smart, but otherwise devious use of their third party rights in the rent-seeking pursuit. Two is that the judicial power gets tampered as vested interests start to throw in their weights. There, it becomes all too obvious, reckoned by Messrs Yang and Lu, that in a practical world of conflict interests, the knack of shoring up the third party rights lies in the need of striking a balance. And that gives rise to some optimal arrangement in the contract regime.

Next comes our story of governmental behaviour. For some years now, the nation has been revelling in much of the hoopla of political melodrama that has seen the ruling sort have at last brought in an alien species, called “democracy”, in some unlikely areas of countryside. The news carried by the state-express of media bandwagon travelled wide and far. Yet, for those in of touch, it is little more than a morphing type — a laughingstock at best. On one hand, we have those much-touted ballot boxes fixated by law in the rural habitats, purporting presumably to bring about some balances and checks to the local fiefdoms where the lords would be expectedly more sympathetic to their subjects, not least in those open-ended ta-