

# STARTING POINT:

## Thirty Years of Reform in China

*Chi Fulin*



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CHINA



Center for Strategic and International Studies

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# Preface

Ever since the Third Plenary Session of the 11th Central Committee of the Communist Party of China (CPC), which took place in December 1978, and which symbolizes the start of the era of reform, there have been nearly 30 years of reform in China. Nowadays, the reform has entered a new phase and is facing new challenges. On the one hand, the reform in marketization is facing difficult challenges. On the other hand, the need for sustainable development and the building of a harmonious society have introduced new requirements for reform.

The reform in the new phase is facing two growing conflicts: the first is the sharp conflict between rapid economic growth and unbalanced development and resource and environmental constraints; the second is the conflict between the rapid growth in public needs of the society and the lack of basic public products and insufficient public services. Given this situation, the process of reform in the new phase will need to make breakthroughs in the following three areas:

The first breakthrough must be in reform of the economic system with an aim to developing the market economy. The economic reforms of the past 30 years have been advancing to cover the field of resources, the monopoly industries, and the financial and taxation fields. The aim of reform is not only to get to the root of the resource and environmental problems but also to provide a fundamental political guarantee of fairness in the economic field.

The second requirement is to accelerate the reform of the social system, focusing on building a public service system. At the crucial stage of thoroughly regulating the interests of people, the reform in the public service system aiming at gradually equalizing access to basic public services is of great significance in solving people's problems and enabling most people to benefit from the fruits of reform.

The third breakthrough must be in the area of political restructuring with an aim to developing democracy. Together with the acceleration of the restructuring of the economy and society, various interest groups have

emerged in society. The interest appeal and social participation of various interest groups are the basis for reaching social equity and the general trend of social and economic development.

In the new stage of thorough reform and innovation, the reform in the economic system requires the imposition of regulations to maintain the boundary between the government and the market. The reform of the social system requires regularizing the boundary between the government and society and the political restructuring requires the imposition of regulations to restrain the powers of government. Therefore, the reform of the administrative system is the key to making progress and should be the emphasis of the reforms in this new stage.

Since the SAS crisis in 2003, my colleagues and I have been studying the restructuring of government. The actual requirement of the reform in the new stage makes the restructuring of government the key to administrative system reform. That is, the government must make the transition from a government focusing on economic construction to one focusing on public service. This book consolidates some of my academic papers and speeches from September 2005 to May 2007 and reflects my thinking about the related questions.

As the 30th anniversary of China's reforms approaches, from my perspective as a researcher on the subject of reform, I sincerely wish that the next phase of reforms will go better and more smoothly, and that this book can contribute to further research on the theory and practice of the reform in the new phase.

I would like to express my gratitude to my colleagues Fang Shuanxi, He Dongni, Long Xiaoling, Chen Suohua, Yang Rui, and Xiao Xiao for their support and help in editing this book.

During the editing process some words from the original papers were changed. Please forgive us if there is unavoidable repetition in some papers.

Chi Fulin  
May 25, 2007  
Haikou

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## *Introduction*

# **Toward Comprehensive System Innovation**

- *Comprehensive reform in 2006*
- *Targets and tasks in system innovation*
- *Accelerating reforms of the administrative management system in a scientific way*

The year 2006, the first year of the 11th Five-Year Plan period, witnessed achievements in reforms in many areas, particularly in the two areas of rural and financial reforms. “The Resolution on Major Issues Regarding the Building of a Harmonious Socialist Society,” adopted at the Sixth Plenary Session of the 16th Central Committee of the Communist Party of China (CPC), calls upon people “to pursue socialist market economic reforms, to adapt to the requirement for social development and to push forward reforms and innovation in economic, political, cultural and social systems.” This important Resolution symbolizes that China has entered a new period toward comprehensive system innovation for the goal of development in a scientific way.

### **I. Comprehensive Reform in 2006**

Since 2006, building system guarantees for development in a scientific way has been an overall requirement for overcoming the difficulties in the reforms. The central authorities have, therefore, repeatedly reiterated the importance of creating an environment for reform without any delay. The year 2006 saw a new situation for comprehensive reforms.

**1. The central authorities have emphasized the importance of “resolutely pursuing reforms.” It is of vital importance to push forward the reform in a comprehensive way**

In the past 30 years, China’s policies of opening up to the outside world have considerably emancipated and developed its productive forces. With the rapid economic growth in recent years, some new contradictions and problems have also become more obvious during the course of economic and social developments. For example, reforms in the ownership of state-owned assets, health care, housing and education have caused considerable concern and disputes within society. In the face of various doubts about reforms, the central authority’s clear-cut attitude was an important precondition for the achievements made in reforms in 2006 and played a very key role in building up motivation and confidence for reform, creating a favorable environment for comprehensive reforms.

**2. Progress made in the reforms and new breakthroughs in a number of key areas and links achieved in 2006**

In order to objectively evaluate the progress of reform, China (Hainan) Institute for Reform and Development designed a “Questionnaire on China’s Reforms in 2006” to solicit opinions from experts and specialists in different areas. A total of 356 questionnaires were returned. The survey shows that 8.36 percent of those questioned held the view that major breakthroughs had been made in 2006; 76.21 percent of those believed that, generally speaking, progress had been made in 2006.

***(1) Rural reforms created a stable situation which had rarely been seen for many years***

The rural reform in 2006 gathered the most attention. The survey conducted by China (Hainan) Institute for Reform and Development on the reforms in 2006 indicates that 25 percent of the experts interviewed believed that major breakthroughs had been made in the area of rural reform; 63.22 percent of those thought that progress had been made, bringing the total to 88.22 percent. Compared with several years ago, visible achievements in the area of rural reforms had been made in the following areas:

Firstly, the 19th Session of the Standing Committee of the 10th National People’s Congress abolished “The Regulations on the Agricultural

Tax of the People's Republic of China." From January 1, 2006, Chinese farmers bid farewell to the practice of paying agricultural tax. The document issued at the beginning of 2006 entitled "Opinions of the Central Committee of the Communist Party of China and the State Council on Building Up New Socialist Rural Areas" marked a new round of profound changes which were to take place in rural China.

Secondly, the conference on the comprehensive rural reforms in the whole country marked the establishment of principles and guidelines for rural reforms in the new phase: to center on the reform in the superstructure in rural areas, to promote comprehensive rural reforms and solve the complicated problems of contradictions between the superstructure and economic basis in rural areas. In many places, remarkable progress was made in township fiscal revenue and payments supervised by county governments. Visible results had been obtained in the rural compulsory education system by sorting out the responsibilities of governments at different levels, securing sources of funding for education for rural compulsory education and relieving students of their burdens. The promulgation of "The Law on Compulsory Education" has guaranteed funding for compulsory education, which means that the restructuring of compulsory rural education has entered a new period of system regularization and standardization. About 40 percent of the counties and prefectures in the entire country have entered into a new system of cooperative health care. The amount of RMB 4.73 billion from the central treasury was earmarked for this purpose, over seven times more than the figure in the previous year. The Rural Working Conference held by the central authorities at the end of 2006 announced that in the year 2007, students would be exempted from all miscellaneous tuitions fees during the compulsory rural education stage, and the new rural cooperative health care arrangement should cover over 80 percent of the counties (cities and prefectures) in the country.

Thirdly, at the Rural Working Conference at the end of 2006, the central authorities explicitly promoted the following: the need to actively explore the development of a social security system to cover both urban and rural areas and to establish a minimum standard of living in rural areas in the whole country. The central government requested that administrations at different levels should, in accordance with the local level of economic development

and fiscal ability, define the targets and standards for poverty stricken people, encourage the areas with established systems to make improvements, support those areas without existing systems in setting up systems, and allocate subsidies from the central treasury to poverty stricken areas. This constitutes major progress compared with the system of rural minimum living security where conditions permitted, called for at the Fifth Plenary Session of the 16th CPC Central Committee held from October 8 to 11, 2005.

***(2) Substantial achievements have been made in the sphere of financial reform***

The survey on the reforms of 2006 made by China (Hainan) Institute for Reform and Development proved that 13.08 percent of the experts questioned held the view that major breakthroughs had been made in financial reform in 2006. This percentage point is next to the rural reform in the evaluation of a single reform item. Among the experts, 60.76 percent of them believed that the year 2006 saw progress in financial reform. The two figures come to a total of 73.84 percent. The achievements in the financial reform in 2006 covered the banking, securities and insurance areas, where some fundamental reform measures had been implemented.

Firstly, substantial steps had been taken in the reform of the shareholding system of state-owned banks. After the Bank of Communications, China Construction Bank and Bank of China were listed in the Hong Kong Stock Exchange and the Bank of China was listed in the A-share market on the mainland, the Industrial and Commercial Bank of China was listed simultaneously in both A-share and H-share markets and investment in the banking shares of the Chinese banks became hot items in the capital market. The banks mentioned above have made achievements in ownership, corporate governance, internal control, strategic cooperation and quality improvement of the staff, creating a good image of modern commercial banks.

Secondly, reform on the division of stock rights went smoothly. By the end of 2006, about 1,300 companies listed in Shanghai and Shenzhen completed reforms in this regard or had started the reforms. The values of shares that had been reformed took up over 97 percent of the total market value.<sup>1</sup> The time

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<sup>①</sup> Ba Shusong, "Review of 2006 and Looking Forward to 2007 in China's Financial Reform," *Ping'an Securities*, January 10, 2007.

has come when all the shares can be circulated, effectively reducing risks in the securities market where the situation has obviously taken a turn for the better.

Thirdly, the reform on the RMB exchange rate has continued in the direction of a market economy. Since the reform on the exchange rate in 2005 was initiated to develop a mechanism, new financial products were available and related policies were issued to create a combination of a balanced market value and adjustments of market mechanism so that pressure on RMB revaluation has been relieved, elasticity of the exchange rate has been constantly strengthened and revaluation has been stabilized.

Fourthly, "Opinions on Reform and Development of the Insurance Industry" promulgated by the State Council in June 2006 clearly indicated that a social security system with different levels should be built up, that individual and group pension business, responsibility insurance and expanding insurance service areas should be actively developed, mapping out a basic framework for the reform of the insurance industry. In October 2006, China Insurance and Supervision Regulation Commission formally issued "The Guidelines for the Development of China's Insurance Industry in the 11th Five-Year Plan Period." This marked the fact that blueprints had been established for the reform of China's insurance industry, introducing a new orbit for speedy development.

### ***(3) Starting reforms in a comprehensive way in the social sectors with public services as the focus***

Compared with the past 28 years, the year 2006 witnessed visible progress in the reform of the social sectors. In the past, social stability was the precondition for reform and development. Now the building up of a harmonious society is one of the basic goals for the reforms in the new period.

Firstly, the reform of the income distribution system has commenced. Faced with the widening gap of income distribution, the Political Bureau of the CPC Central Committee held a meeting on May 26, 2006, and put forward systematic ideas on reforming the income distribution. Since July 1, over-all reforms of the income distribution system have started from the regularization of the income distributions for civil servants.

Secondly, major goals for reforms of the medical and health system had been set. Headed by the National Development and Reform Commission and Ministry of Health, a coordination group for reforms was formally

set up with participants from 11 ministries and commissions to table an agenda for new medical and health reforms. Hu Jintao, General Secretary of the CPC, reiterated that the public welfare nature of the health sector should be maintained to serve the public interest and that a basic health care system covering both urban and rural residents should be established to provide them with safe, effective, convenient and inexpensive public health and basic medical care services. This indicates that substantial reforms of China's medical and health systems have entered a new phase.

Thirdly, major steps have been taken toward a public fiscal system in the fiscal system reform. "The Resolutions" adopted at the Sixth Plenary Session of the 16th CPC Central Committee outlined the major tasks for building up systems and guaranteeing social fairness and justice, "to improve the public fiscal system and gradually achieve equality of basic public services." The goal for reforms of the fiscal system is more clearly defined: the focus should be placed on the equality of basic public services and increase of input in social undertakings. In 2006, additional fiscal payments were made for rural areas, agriculture and farmers, and for the development of social undertakings, preliminarily demonstrating the welfare nature of the fiscal system. In 2006, reforms in the categorization of governmental fiscal revenue and payments were also conducted. They have been the most important changes to the fiscal statistics systems since the founding of the People's Republic of China. This reform helped to reflect the sizes of governmental revenue and expenditure and major governmental functions in a complete and explicit way, to strengthen control over fiscal payments and budget transparency to prevent and control corruption from its very source.

### **3. The overall situation in 2006 showed that expected results had not been obtained in the reforms in some important sectors, underscoring that the reform is a fairly difficult endeavor**

#### ***(1) Reforms in the state-owned monopoly industries are moving at a slow pace***

The survey for the reform in 2006 conducted by China (Hainan) Institute for Reform and Development showed that 49.13 percent of the experts questioned believed that there was almost no progress in the reforms of the

state-owned enterprises. Although the reform of the monopoly sectors was one of the key reform tasks at the time, progress was slow in this area in 2006, resulting in low ratings from the experts: 66.28 percent of the experts held the view that there was no progress; 10.95 percent of the experts even believed that there had been negative progress. Now the reforms in the state-owned monopoly sectors have become a focal issue and a headache.

*(2) No major progress seen in the marketization of major elements*

For instance, the absence of marketization of land is still a key factor causing disputes in land acquisitions. The investigations conducted by a study group of the Development and Research Center of the State Council have shown that 40 percent of the farmers' complaints were triggered by land acquisition, 26 percent by changes concerning contracted land. Furthermore, the marketization processes of labor forces and technologies are still not satisfactory.

*(3) The reform of the governmental administrative management system, listed as a key area, saw no major efforts in 2006*

In the guidelines for the 11th Five-Year Plan adopted by the National People's Congress in March 2006, the governmental administrative management system was listed as a key sector in need of reform. The Working Conference on Economic Restructuring held soon after also pointed out that major and immediate efforts should be made to promote reform of the governmental administrative management system. The survey on the reforms in 2006 conducted by China (Hainan) Institute for Reform and Development proved that 52.3 percent of the experts believed that almost no progress had been made in the reform of the administrative management system in 2006. Take the investment system as an example. The State Council promulgated in 2004 "The Decision on the Reform of the Investment System," but 62.49 percent of the experts believed that there was no substantial progress in this area of reform in 2006.

**4. The resolution on building up a harmonious socialist society adopted at the Sixth Plenary Session of the 16th CPC Central Committee marked a new phase of reforms on comprehensive system innovation**

The adoption of the resolution on building up a harmonious socialist