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## The Evolution and Impact of China's Regional Policy: A Study of Regional Support Policy for Western China

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This article discusses the long journey of China's regions to prosperity and well-being. In this paper, we will consider various regions of China, both the most developed and the lagging. Investigating this at different time periods, taking into account the conditions in different regions, to get an idea of politics and its development over time. We evaluate the strengths and weaknesses of the regional policy of supporting the western regions of China, especially their impact on economic and social development in these regions. We show the path of change followed by the policy of regional support for the western regions.

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# Table of Contents

Introduction .....	3
<b>I. The First Wave of “GO WEST”: 1953–1962.....</b>	<b>4</b>
<b>II. The Second Wave of “GO WEST”: 1964–1975.....</b>	<b>4</b>
<b>III. Non-balanced Development Strategy: 1978–1991 .....</b>	<b>5</b>
<b>IV. Coordinated Development Strategy: 2000–2010.....</b>	<b>6</b>
References .....	9

# Introduction

Regional development has always been a fascinating subject, much like the question of a nation's rise and fall. There is a growing body of literature on regional development and regional policy since 1990s. Gradually, the key notions from Evolutionary Economics, such as historic events, selection, path-dependency, chance, innovation and increasing returns, gradually enter the research on economic geography and regional development. Nonetheless, from the perspective of Evolutionary Economics, there are still many questions relating to the Regional Support Policy (RSP), both in terms of decision-making process and its impact. In this paper, we will primarily focus on the following three questions: (1) What is the connection between RSP decision-making and the economic and political institutions at the time these policies were determined? (2) How does RSP respond and adapt to the changing economic, social and political environment? (3) What is the impact of RSP on regional economic and social development?

This paper also explores the possible links between Evolutionary Economics and regional policy change, through a study of regional policy for western China.<sup>1</sup> From the perspective of Evolutionary Economics, including historic events, path-dependency, innovation and institutional change, we enable a better understanding of the evolution and impact of China's regional policy on the western regions.

## **I. The First Wave of “GO WEST”: 1953–1962**

When the Communist Party of China (CPC) came to power in 1949, the Soviet Union was the one of the few countries that acknowledged the new Chinese government and established diplomatic relations with China. Devastated by decades of the anti-fascist war and the civil war, China’s economy and industry lagged far behind the Soviet Union and other industrial nations around the world. However, the new Chinese government led by CPC aimed to change this and set China on the path to becoming one of the world’s economic and political superpowers.

Following the lead of the Soviet Union, the new government of China adopted a highly centralized economic system and introduced her own ‘Five-year Plan’ in 1953, mainly aiming at the nationalization of private enterprises and the development of heavy industry. Hence, it became a priority for China to increase the production of steel, iron and coal, all of which are largely concentrated in the inland regions.<sup>2</sup> Moreover, the start of the Korean War and the threat of continuing conflict with the Kuomintang regime in Taiwan led to the “neutralization” of the Taiwan Strait by the US Navy. This led to the further isolation of China and stimulated a military build up in eastern regions. Hence, it was not possible for coastal regions of Eastern China to capitalize on their geographic advantage to establish business relations with foreign countries.

All of these political and economic constraints led to the decision of the Chinese government’s implementation of “Balanced Development Strategy (BDS)”, favoring development in inland China. Under this strategy, during the “1st Five-year Plan” (1953–1957) and the “2nd Five-year Plan” (1958–1962), the Chinese government introduced regional development policy to promote economic development in Western China and Central China. Western China was undergoing the first wave of the “GO WEST” campaign.

## **II. The Second Wave of “GO WEST”: 1964–1975**

In the late 1950s and early 1960s (the period of the 2nd Five-year Plan), both China’s internal and external situations deteriorated dramatically. The implementation of the adventurous policy of “the Great Leap Forward” greatly distorted individual incentives: both agriculture and industrial production suffered dramatic contraction, resulting in a great famine between 1959 and 1962. The 1st two Five-year Plans’ objectives were achieved only in part. China’s foreign relations also experienced substantial deterioration, mainly due to the increasing hostility between the Soviet Union and China and the US-led military intervention in the Vietnam War.

Facing these problems, Mao Zedong's government made it an urgent task to implement a large-scale relocation of industries to western China. This dramatic shift of the regional development policy came about after the special session of the CPC in August 1964. In this session, Mao proposed that factories, especially those military industrial firms in coastal regions, should be relocated to the western regions to protect them from potential military strikes. Following Mao's proposal, the CPC decided that most of the new projects should be allocated to the western regions and most of the capital should be invested on "third front construction", which primarily contributed to the economic development in Western China.

In the early 1960s, China's national defense followed the strategy of three fronts from the coast to the interior by CPC leaders (see Fig. 2). Third front construction led to a massive investment program started in 1964 in Western China, in particular Sichuan, Guizhou, Yunnan, Gansu, Qinghai, Ningxia, and a part of Shanxi. The objective of the program was to build a range of industrial bases in the remote areas of the western regions to prepare against the potential of war and famine (Naughton 1988).

### **III. Non-balanced Development Strategy: 1978–1991**

In the late 1970s China was in great need of foreign capital and production technologies in order to revitalize the Chinese economy and improve economic efficiency. The coastal regions, compared with the inland regions, have advantages in attracting foreign capital and technologies, due to their geographic location and large numbers of overseas Chinese from these regions.

In order to reconstruct the Chinese economy and restore the legitimacy of the CPC regime damaged by the poor economic performance and costly political movements, the CPC regime had no choice but to shift its focus from political ideology to economic development. This shift was endorsed by the de facto leader Deng in the late 1970s (Heberer and Schubert 2006; Holbig and Gilley 2010). The CPC leaders also realized that the excessive state control of economic activities was one of the major factors contributing to the low labor efficiency in agricultural and industrial production and looked to address this problem.

Under Deng's leadership, China began to reform its economic system and implement the opening-up policy (i.e. Reform and Opening-up). The core of Deng's reform was known as "decentralization and interest concessions", which meant that governments would give

households, firms and local governments some degree of autonomy. Deng's reform primarily focused on institutional rearrangements and the introduction of appropriate incentive mechanisms.

In the late 1970s, facing a dire economic environment, large numbers of residents in Guangdong Province fled from their hometowns to overseas areas or countries, including Hong Kong, Macao and southeast Asian countries.<sup>5</sup> In order to stop the illegal emigration of local residents and revitalize the local economy, Xi Zhongxiong and other leaders of Guangdong at the time, proposed the introduction of Special Economic Zones (SEZs). SEZs would be entitled to a new economic management system with more economic freedom and more conducive to business and economic activities than that in the rest of mainland China.

The proposal to introduce SEZs was supported by the CPC leaders Zhao Ziyang and Deng Xiaoping. In 1980, the central government established special economic zones in Shenzhen, Shantou and Zhuhai in Guangdong Province, and Xiamen in Fujian Province. All these cities achieved tremendous success in establishing foreign business relations and promoting local economic development from the early 1980s onwards (Graham and Wada 2001).

After a comprehensive assessment of the reform achievements and issues in the 1980s, Deng Xiaoping and his allies launched a campaign to transform the planned economy into a market-oriented system in 1992.

#### **IV. Coordinated Development Strategy: 2000–2010**

Relying on relative advantages on the level of economic development, the eastern regions were able to capitalize on economic disparities to the detriment of the western regions. Attracted by more job opportunities, higher wage levels and better living conditions, large numbers of workers left their hometowns in the western regions, and migrated into the towns and cities of the eastern regions, especially into the coastal cities in the 1990s. As a result, the development of the western regions was hindered by a severe and continuous lack of labor. Furthermore, large amounts of various raw materials, such as coal, iron ore and logs, were transferred away from the western regions into the eastern regions at rather low prices, whereas the industrial products from the eastern regions were sold into the western regions at profitable prices (Xiao et al. 2010).

Facing these economic disadvantages and the overwhelming competition from the eastern regions, the local governments in the western regions adopted many protectionist measures (Bai

et al. 2004). As a result, economic conflicts between different regions rose steadily during 1990s. Moreover, there is an obvious trend of resemblance in industrial structure, disregard of great differences in economic, social and natural conditions in different regions (He et al. 2008). This led to a sharp increase in transaction costs for cross-region economic activities and a tremendous loss of overall economic efficiency.

In 1994, China government embarked on the reform of the tax sharing system between the central government and the local governments, through which the central government gradually strengthened its fiscal capacity. China's central government realized it was time to take practical measures to accelerate the development of the lagging regions, and to reduce the regional disparities and tackle the problems resulting from those disparities. In 1999, the Chinese government launched the third wave of the "Go West" campaign, known as WDS. This led to the implementation of some concrete policy measures by the Chinese State Council in October 2000, so as to promote the economic development in Western China. By 2010, WDS had been in effect for 10 years. In June 2010, the CPC Central Committee and the State Council announced a new policy guideline, which adjusted and intensified policy measures and extended the key preferential policy for 10 more years. We will explain WDS in more detail in the following two sections.

## **V. Conclusion**

In this issue, we discuss regional policy changes with a focus on China's Western Development Strategy (WDS), from the perspective of evolutionary economics. Some of the key concepts of evolutionary economics may help explain the factors and logic underlying the evolution of China's regional policy.

First, the institutional changes and the regional policy adjustment almost occur simultaneously in China, indicating that the Chinese political and economic system deeply affects its regional policy for Western China. It is worth noting that political events and movements play a decisive



role in RSP for Western China, breaking up the path dependent trajectories of economic development in western regions. Our examples include the Great-leap-forward, the Sino-Soviet Confrontation, the Cultural Revolution and the Reform and Opening-up strategy.

Second, given the highly centralized regime in China, in which supreme power is held by the central government. The central government and CPC leaders design the blueprints for national economic development and decide which regions are entitled to RSP in different periods, based on their assessment of: (a) the political, economic and social situations, (b) the evaluation of the previous RSP, and (c) various objectives that may be achieved with the implementation of new RSP. The evolution of RSP is a process of trial-and-error, learning and adapting to changes in the political, economic and social situations.

Third, RSP can play a decisive role in the development of the regional economy and national economy. When these policy measures were based on excessive political and military objectives, instead of economic conditions and considerations, these measures would be rather inefficient in promoting regional economic development, while their negative impact could be destructive and long-lasting. On the contrary, RSP based on regional economic and geographic conditions and advantages, tend to have a stronger and longer positive impact on the development of regional economy. For example, the central government granted the Kashi area privileging RSP equivalent to policy privileges given to Shenzhen in Guangdong province, after a 2009 incident in Xinjiang Autonomous Region, known as the “the ‘July-5th Incident’”. This policy was implemented in order to address the discontent of the native Uyghur people and to quickly stabilize the local political and social situation. Nevertheless, without the necessary economic, geographic and social conditions in this area, it is unlikely that this regional support will achieve its objectives, or successfully change the economic and social development trajectory.

Fourth, the local governments play a critical role in determining RSP. In order to obtain desirable RSP, the local governments mobilize various resources and resort to all available channels to influence the central government.

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