China and its development model: a broad outline from a different perspective

Arturo Oropeza García
Professor and Researcher, Legal Research Institute at the National Autonomous University of Mexico

I. Abstract

China's economic success from 1978 to 2011 is truly surprising, for example the growth rate of its GDP (an average of 10% a year for thirty years, second place in the world in 2011, 14 times its GDP from 1978 to 2007). However, we could also add that China's economic history is very far from being over, and in the future it will continue surprising us with its innovations, which it will have to keep in mind if it wants to have a close idea of the most successful development strategy of recent decades.

II. Introduction

The reform in China is a great experiment that is not found in books.

DENG Xiaoping

Despite its success and widespread diffusion of its results, China's economic reform from 1978 onward is still a topic that is difficult for the Western world to interpret. From its inception, the creator of the model, Deng Xiaoping, warned that reforming modern China was a "great experiment" based on a broad outline and subject to trial and error. While Deng pointed this out in 1985, a trusting, overestimating Western world has not yet completely understood this unilateral declaration from the main author of Chinese success. From the beginning, it told the world that a new China was embarking on the adventure of traveling through unknown paths towards development despite the economic failure of its previous experience (the Maoist Period 1949-1976) and the urgent need to feed around 900 million people (1978), of which nearly thirty million had died of starvation just eighteen years before.

In the Western world, however, different development theories continue to compete between the prevalence of politics over economics and/or vice versa. In a never-ending search for predominance, analysis is frequently complicated, more than clarified, by forgetting that a healthy relationship between politics and economics is inherent to successful economic development. There have been many disputes within economic development theories regarding the different visions that have tried to be imposed throughout the 20th century in search of sustained development. This has occurred in spite of the fact that, as Douglass North points out, "…the similarity in the performance of the economies and the persistence of disparate economies throughout time has not been satisfactorily explained by the development economists, despite immense efforts carried out for 63 years. The simple fact is that the theory used is not up to the task." [1]

Despite the various formal economic development theories that have appeared since 1943 (Paul Rosenstein-Rodán), the new political group that began to re-think China's growth did not directly incorporate contemporary theories (Clark, Nurkse, Lewis, Rostov, etc.) when instrumenting their initial changes. China was well aware of its enormous economic limitations at the time: limited resources, overpopulation, widespread poverty, a lack of savings, an economy in arrears, ineffectual industry, a lack of infrastructure, limited external trade, an abundant but unqualified workforce, a lack of modern technology and a political crisis, among others. Its failure to fully adopt an earlier model (the Soviet model) led it to believe that reductionism was not the best way to attain successful development. As Oded Shenkar points out:

> *The first 27 years (1949-1976) of the communist phase will continue being object of discussion; although little by little the apologists from the period of Mao Zedong are decreasing. However, regarding the economy and politics, there are no absolutes, and although the general results from the period are negative and at times were chaotic, such as the famine that presented itself in the middle of the period, it can be said that within it some lessons were generated for the Chinese model that were greatly useful in its new boom, from 1978 onward. The first theory among them that can be highlighted is the one that detaches from the Great Leap Forward and the Cultural Revolution, which consisted of pointing out the fact that the forcing the ideology of the economy produces catastrophic results, that concrete results for development must be oriented toward this theory. At the very time that it was impossible to continue with the Russian model of investing and creating infrastructure in the whole territory in such a big country with so few resources, the advisable thing to do was to focus the effort on the areas with the greatest potential, in order to later disseminate the results, an experience that has been one of the most important points of*

the new development model, and finally, that the viability of the political project necessarily requires economic success[2].

Thus, talking about China's new development model is not an easy task. Its political environment from preceding years was imbued with intense nationalist sentiment. Its idiosyncrasy and its multilayered past intertwine and confuse observers with their various settings. Its political-economic platform derives from a centralized model and it has recently implemented a market economy. In view of their different natures, all these aspects continue to distort the opinion of a Western world accustomed to dichotomous economic models (Communism-Capitalism) and that as early as 1989 thought could be synthesized into a single model after the fall of the former Soviet Union. In an attempt to analyze certain qualities of the current Chinese development model, it is useful to follow Deng Xiaoping's advice and heed his warning: starting from the premise that it is a "great experiment" that has not been deciphered in important economic treaties. It is an experiment thought out and executed by a group of engineers and it must be seen as something outside familiar paradigms within the framework of the new global order.

The three sections of this paper are as follows: II. Economic Development as a State Priority; III. The Law as Leverage for Development and IV. Evaluation and Conclusion, in order to outline the new development model of the People's Republic of China.

III. Economic development as a state priority

Development by any means, without altering social stability.

DENG Xiaoping

In the political crisis of the late seventies, China's immediate challenge was to grow at any cost to meet the urgent demands of its people. The previous economic model had already failed and outside China, future growth wavered between the "success" of developed Western economies and an early prospect of globalization that was starting to outline a new order for international development. Thus, the starting point for the first reforms was clearly the need to implement an outward-oriented political-economic system. Deng used all the State's power to design a new development model that centered on increased foreign trade. For this purpose, pertinent parts of Taiwan's economic model were analyzed. It was noted that between 1960 and 1965 its GDP had grown an average of 9.5% while China was unable to go beyond 4.7%. Between 1965 and 1972, when the Chinese GDP rose only 1%, Taiwan's grew at a rate of 10.1%. Consequently, the Taiwanese example served as a starting point for the economic plan that Deng called "the four

modernizations" to attain "economic development by any means."[3] Various trade missions were sent to northern Mexico at that time to see the assembly plant model first-hand. These visits also played an important part in devising the new Chinese model.

1. A Broad Outline of Deng Xiaoping's Economic Theories behind the Chinese Development Model

In the early stages of reform, Deng Xiaoping would say,

> *Once we are certain that something has to be done, we should dare to experiment, to break out, and to mark new paths with it. This is the important lesson that we should learn from Shenzhen. If we do not have a pioneering spirit, if we are afraid to take risks, if we do not have energy and direction, we cannot break out and mark a new path, a good path, or do something new… No one can be 100% sure from the beginning that what he is doing is right. I have never been so sure. Every year, the leaders should review what they have done, continue with the measures that have proven adequate, act immediately to change those that have proven wrong, and face up to new problems as soon as they are identified.*

Deng's own life (1904-1997) falls within one of the most chaotic eras of Chinese history. He lived through the end of the Empire (1912), as well as through various revolutionary movements (1912-1949) and the Japanese invasion (1931-1945). During the Maoist Period (1949-1976), he met with different movements, like the Cultural Revolution (CR, 1966-1976), which made him the target of strong political attacks from the more conservative groups.

After the triumph of the Revolution and confronted with different social challenges, Deng's discourse was marked by starting from the current situation in order to find new that would take China out of poverty, a course which clashed against the central power's triumph list and dogmatic discourse. In 1957, he pointed out that "Seeing everything through rose-colored glasses and too simplistically is manifest in our propaganda, idealizing the current situation of our country as if there were no longer any difficulties and we only need to enjoy the amenities." He added, "our main task from now on is building, which will be somewhat more difficult, or at least not easier, than the Revolution…"[4] In the face of the challenges of his time he spoke of "learning, of course, from all the advanced experiences of the world, learning how much

---

The new regime's objective was to attain China's economic development by means of modernization in four areas: agriculture, industry, national defense, and science and technology. Under the leadership of Deng Xiaoping, greater emphasis was placed on them to position China at the forefront of all world nations. JOHN KING FAIRBANK, CHINA: UNA NUEVA HISTORIA 486 (Andrés Bello, 1996).

they have advanced in different parts of the world, including the United States." Although in the fifties, he naturally put the Soviet Union in first place. He likewise recognized that "in China, many national capitalists opened their paths in the midst of arduous struggles, and they know more than we do about business management." This opinion, which grew out of building up a new framework for growth, led to his having multiple enemies and posed serious threats to him during President Mao's orthodox and distinctive "school of thought" for using his discourse and work in the Party to incite the country to follow the capitalist path.[5]

In spite of the opposition, he rose to power upon Mao's death. Deng then had the opportunity to put his ideas into practice, which basically stemmed from bringing together three factors: development, structural reforms and political stability. As to this, he pointed out, "the solution to all of China's problems depends on economic development," because "development is the absolute foundation and in order to achieve it, it is necessary to insist again and again on the reforms that make it possible." In 1985, he added, "all our reforms are aligned with a single objective, which is to remove the obstacles that limit or inhibit the development of productive forces, which, in turn, should be directed toward creating a technological basis for development." Deng's theory always regarded the link between reform and development as something perfectible with time and subject to trial and error; the reform to be applied should aim for the best possible development. Reforms are like permanent public policies that correct everything that does not contribute to development. However, he always maintained that these two premises would not be possible without the stability in the country brought about through social and political balance among its participants. On this topic, Deng Xiaoping declared, "If there is no stability, brought on by political disparities, it will be impossible for us to move toward social construction." [6]

This simple reform-development-stability trilogy forms the theoretical basis of Deng's development model. Its main challenge was to achieve a balance of the concepts in time, so that their combined effect would translate into benefits and improvements for the different social classes. Regarding this, Deng explained, "the basic expression of the superiority of our socialist system is found in the possibility that the productive forces of our society can grow rapidly, at rates never before seen in the old China, and gradually give us the satisfaction of the cultural and material improvement that our people need." [7]

While various reforms for economic and commercial growth were being built around this development strategy, the long-term vision of the project emerged: the knowledge of knowing what is desired and what is possible, and the certainty of knowing in which direction to go. In 1978, Deng Xiaoping said, "the essence of the reforms is to build the foundations for sustained development for the

next decade and the first fifty years of the next century." He devised a strategy with a view towards the future that he called "the three steps." "In this century, we will take two steps, which represent the solution to the problems of an adequate supply of food and clothing for our people. In the next century, we will spend another 30 or 50 years to achieve the goal of another step, which is to reach the level moderately developed countries of the world have."

Deng was a visionary with a great capacity not only to adapt to the new political period his country was entering after living practically walled in, but also to understand the great global transformation the world was experiencing in the late 1970s and to lead China to take advantage of this situation. In 1987, he said "currently, there are two models of productive development. Insofar as each one of them serves our purposes, we will make use of it. If socialism is useful to us, the measures will be socialist; if capitalism is useful to us, the measures will be capitalist." In an unusual approach, he pragmatically pointed out,

> *there are no fundamental contradictions between socialism and the market economy… The experience that we have gained throughout recent years has demonstrated to us that we could not develop productive forces in a rigid economic structure. It is for this reason that we have been implementing some useful capitalist measures. It is clear now that the correct approach for opening oneself to the world is combining a planned economy with a market economy, to which structural reforms are implemented.*[8]

This combination of concepts gave way to what we now know as "market socialism."

"Surely the affirmation that the market economy only exists in capitalist society, that there is only a capitalist market economy, is incorrect. Why can't socialism practice the market economy?"[9] This stance defined and revolutionized the paradigm of his central planning model and the theory of the capitalist model was met in the same way. After all was said and done, what stood out was the pragmatic and utilitarian intention of transforming economic models from ends to means. It did not matter whether the cat was black or white, Deng said paraphrasing an old Chinese proverb, what mattered was that it caught mice. He added, "there is no fundamental contradiction between socialism and a market economy, 'both are means.'" Even today, both (capitalist and socialist) theories continue to seek answers that clearly explain this new model, which has validated itself through the success of its results.

On the topic of structural reforms, Deng indicated in the eighties that "without development, reforms don't mean anything." To that, he added, "to reform was to remove the production relationships and the superstructures that weren't driving the development of productive forces."[10] Reform-

development, development-reform, this new learning curve drew from successful experiences in the world, a learning process that compared the challenge to crossing an unknown river leading to development that would benefit the people. Therefore, "one should proceed with caution, feeling the stones." To do this, every reform and every development had to comply with three objectives (the three "favorables") to be considered viable and thus be approved. The criterion focused on a*) whether* it promotes the growth of productive forces, *b)* whether it increased the strength of the Socialist State, and *c)* whether it raised people's living standards. A clear understanding of a globalization in its initial stages more than a quarter of a century ago and the implementation of a winning strategy to participate in it contrasts with the lack of direction a number of economies present today.

2. *A General Outline of the Economic Model*

The combination of public policies the new Chinese model adopted, regardless of their origin, has led to a pragmatism that breaks with traditional methods of analysis and enhances China's economic results. After the fall of the Berlin Wall, the West consolidated its idea of a victorious free market model that was positioned well above the central planning strategy implemented by the former Soviet Union, which had clearly demonstrated its incompetence when compared to its Western counterparts. In the face of failure, both China (1978) and the former Soviet Union (1989) opened their borders and emerged into the world. The most foreseeable conclusion was that they had to put the neoliberal model into practice and wait their turn in a predetermined economic order. With the difference of only a decade, Russia followed a shock therapy strategy using the IMF model and established an open privatization plan (*laissez faire*) that was abruptly carried out under the 500-Day Program. It resulted in the massive closing of businesses and the loss of an important number of strategic State assets. This model instigated the full opening of its market and the free exchange of its currency, which brought about enormous debt and a financial crisis that entailed the loss of 4.2 times its gross national product (GNP) between 1992 and 1996. This strategy also led to a drop in income for 60% of the population while levels of extreme poverty rose to 40%. Moreover, only 10% of the population had access to higher levels of wealth and the development of Russian economy was thrown back twenty years.[11] In contrast, the gradual progression, selective openness and comprehensive strategy the Chinese State implemented in its economic development model produced completely different results.

One aspect stands out from among the different paths of learning gathered from the new Chinese development model: its caution in not impetuously giving over to the offer of free market models, as Russia and most Latin American countries have done. In addition to "feeling the stones of the new river,"

there is the wisdom of putting national interest and reality ahead of the different strategies being implemented without deterring them from inventing new, unproven formulas in the midst of a new free market dogmatism that worshipped the invisible hand of development. Some authors point out that, "it is precisely the success of the Asian nations that allows current free market theorists, especially civil servants in the World Bank and the International Monetary Fund, to highlight the goodness of the free market, and, given its importance in the adjustment and stabilization programs, brings about the resurgence of the neoclassic paradigm."[12] As far as China is concerned, this idea is not wedded to a socialist market model that benefits from all kinds of strategies, regardless of their origin. The only requirement is that they contribute to its development.

At the 15th Congress of the Chinese Communist Party (CCP), China defined its model as follows:

to build a socialist economy with Chinese characteristics means developing the market economy under conditions of socialism and constantly emancipating and developing productive forces. We should maintain and improve distribution models based on the dominant work, allowing certain people and certain areas to be prosperous in the beginning so that they can later help others and thus achieve prosperity step by step. [13]

The new Chinese model is defined, first of all, by its awareness of historic change: that of facing a decision that if it succeeds, it would require its people's effort for around 100 years. It was also conceived as a gradual transition from an illiterate rural country to an industrialized one with high levels in science, technology, education and culture. It would merge its economic future with the favorable aspects of a market economy. It was seen as a historical period in which the free market would not affect its strong socialist system upon which they would build a socialist regime with Chinese characteristics, a socialist economic system and a socialist democratic political system. This last point is the most difficult for Western observers to understand since they forget that throughout the different stages of China's economic development, the State has never stopped taking direct responsibility for the different policies made and this is seen at every step of its burgeoning private sector's contact with Western economy. China never accepted the simplistic concept of the "invisible hand of the market," but has opposed the "visible hand of the State" since its opening. This reflects its commitment and direct responsibility over the success of its sectors, businesses and businesspeople, and is one of the distinctive fundamental elements of the Chinese model.

3. *Instrumenting a Selective Opening Policy*

Development requires getting rid of all the notions that hinder it; changing all the practices and regulations that prevent it, and liberating itself from economic burdens.

JIANG Zemin

The biggest challenge in 1978 was development by any means and at any cost. The direct struggle among internal forces over the opening and the corresponding adjustments were not yet settled and the open door policy had to be handled progressively. Above all, as Deng Xiaoping used to say, it was still necessary to decide on which front the fight would take place against the "flies" entering the open windows of the foreign market, without losing sight of the fact that the name of the game was development, development and more development. China bore in mind the teachings of Sun Tzu to face this challenge: an army that wants to fight a battle throughout an entire territory is doomed to failure; it cannot be strong in everything. Therefore, they launched a policy for each geographic region (Pacific, Central and Western) and decided to allocate greater emphasis and resources to the first region due to its attributes with respect to the Western market. The strategy also enlarged its focus and defined the priority sectors that would receive State support. Thus, the Chinese again adopted the words of Sun Tzu in that, "the place of battle must not be made known to the enemy. If it is not known, then the enemy must prepare to defend many places. If he prepares to defend many places, then the forces will be few in number."[14] In an initial attempt to give a hierarchical structure to the sectors, Deng started from a broad idea called the "Four Modernizations," which included: liberalizing agriculture, attracting foreign investment, implementing an aggressive export policy and creating special zones. Subsequently, in1981, priority sectors were established under the National Program of Science and Technology: agriculture, energy, new materials, computer science, space technology, genetic engineering, physical engineering and laser technology.

This focus on developing fields of priority economic action is very different from Latin America's strategy in general, and the Mexican one in particular. These countries opened their economies and trade in all aspects of their economic chains, losing strength and the concentration of resources in the process. When deciding the battles to be fought, competitive advantage can be gained by concentrating financial, material and human resources in the fields of development selected as the frontrunners of the global competition, keeping in mind that opening all sectors in haste weakens public and private lines of support and disperses State resources and attention. One example of this is the Chinese automotive industry. Designated a priority sector, this industry drew on the State's strengths (subsidies, research, development, education, raw materials, costs, etc.) to become a winning sector, taking it from 200 thousand units in 1995 to over 5 million in 2004 and nearly 10 million by 2010 (CSM WorldWide). This growth logically

led to increased vehicle sales (sales increased 75% from 2002 to 2003) and greater growth in its supply chains (in recent years, the demand for steel has grown an average of 20% a year). This policy of preferences has also led to an industrial integration of 70% in the automotive sector; that is, only 30% of foreign supplies is required to produce vehicles. This level of integration is higher in other sectors, such as the electronics, textile and shoe industries, which have gone from 90% to 100%.

By establishing development as the State's comprehensive policy, geographic areas as the wise choice for managing its opening and globalization, and a hierarchical structure of sectors as clear objectives for national growth, Chinese development has gained strategic advantage.

4. *The Creation of Special Economic Zones*

The birth of Special Economic Areas (SEAs) is the most important event within the opening policy and China's reform and the most evident sign of its change toward the outside world. Through the last shining fifteen years, an enormous amount of information derived from the SEAs, which have been considered a miracle by their great number of observers, has been accumulated.

CHI Fulin

In the late seventies, the Chinese model created different kinds of territories or privileged economic areas to concentrate public support in strategic points of its territory while providing them with a differential competitive value that could be identified by foreign investment without being tainted by the huge social, economic and productive inequality in the rest of the country. Therefore, it launched a regional development policy that established Special Economic Zones (SEZs) with the highest concentrations of foreign investment. SEZs included: Economic and Technological Development Zones (ETDZ), Free Trade Zones (FTZ), High-Tech Industry Development Zones, Border Economic Cooperation Zones and Export Processing Zones (EPZ). These international competition zones-regions continue to grant all kinds of facilities and support for the entry and exit of products, especially for technology-oriented ones.

From 1978 to 1985, the first five SEZs were set up in the provinces of Guangdong (Shenzhen, Zhuhai, and Shantou), Fujian (Xiamen), and Hainan. By offering a wide range of public stimuli, new undertakings were encouraged in these areas. An extensive promotional campaign targeting foreign entrepreneurs was carried out so they could form joint ventures with Chinese businesses. In this same period, another six Priority Investment Areas were opened and Economic and Technological Development Zones were established in fourteen cities on the eastern coast. With this policy of focusing and concentrating resources, three "Development Triangles" were instituted to accelerate economic growth in the Pearl River Delta. In the 7th Five-Year Plan (1985-1990), the decision was made to enlarge the SEZs and the ETDZs in the coastal region. The 8th Five-Year Plan (1990-1995), devised the modernization of the famous Pudong

(Shanghai) District, which received SEZ treatment, boosting its development with the creation of 15 duty-free areas, 54 Economic and Technological Development Zones, and 53 High and New Technology Industry Development Zones. The support policy for capitals and provinces in the interior was expanded at this time to implement a strategy to gradually incorporate the central area into the thriving development of the Pacific coast, which would continue to remain under the special support public policy. Most notably, this special support policy to attract foreign capital was expanded to include the area of the three gorges (Chengdu and Chongqing). Given the success of this strategy, the 10th Five-Year Plan determined the opening of the central and eastern zones (Tibet, Hubei and Mongolia) to FDI. Fishing villages on the east coast and marginalized agricultural towns in the central part of the country have been transformed into global production and technological research cities, in ten to twenty years.

This policy of focusing resources and forming value chains, along with segmenting geographic areas, defining priority sectors and creating special economic areas, has yielded a high level of competitiveness from Chinese producers, who have easily surpassed those from other countries. This concentration of strategic assets can be clearly appreciated in cities like Shang Yang and Nanchong which manufacture around 8 billion pairs of socks a year; Xiamen, 225 million pairs of jeans; and Suzhou, 300 million of ties. On the other hand, businesses like Hon Hai Precision Industry Co., the main contract exporting company of electronic appliances in the world, are true manufacturing units with nearly 500,000 employees.

The idea of a countrywide boom in such a large territory with an overwhelming marginal population would have led to the failure of any development plan opted for “all together, at the same time” growth. Criticism of the Chinese model’s privileging certain areas at the expense of others overlook this. This development model, which begun on the East Coast for its geographic location and facilities for exporting, has extended over time to the central and western areas. In view of its success, migration from rural areas to urban areas has become a permanent labor phenomenon with the more than 300 million jobs the model had created by 2006. For Deng Xiaoping, economic advancement would be progressive and the wealth and development in the Eastern-Pacific area would spill over to the central and western areas, representing one of today’s greatest challenges to China’s political-economic stability. To guarantee the institutionalization of this policy, the “Law on the Promotion of Development in the Western Area” was passed for the 11th Five-Year Plan of the National People’s Congress. These 50- and 100-year regional government investment strategies have already started by prioritizing 50% of the industrial value of state-owned businesses in 2002 (20% more than in the Eastern Zone), and 53% of their fixed-asset investment for that same year (14% more than in the East). A specialized financial policy for the area (banking, loans, development funds, etc.) has been added, as well as more aggressive social policies. [15]

With China's entry into the World Trade Organization (WTO) in 2001, preferential treatment to the different kinds of strategic zones has been losing the impact given to the first SEZs. Even then, China continues granting SEZs preferential treatment in its public policy, especially seen in the different facilities given to central and western provinces. In an atmosphere of free competition, these facilities rival in their offering of qualified personnel, technical innovation, and a business environment, among others.

On the other hand, international pressure and the institutional commitments signed in this century have made China's latitude with SEZs more difficult. However, China will clearly not stop using this strategy although with some adjustments along the way. As Jiang Zemin pointed out, "SEZs should be developed during the entire course of the construction of modern socialism,"[16] that is, for at least 100 years. Chi Fulin, one of the main economists and ideologists behind the Chinese model, has also stated that the experience gained from SEZs will be of great help and exemplary importance in future reforms to the model, which are quickly turning toward a market economy. However, he adds, it will be necessary and even obligatory for the SEZ economic policy to continue as intact as possible.[17] The dynamic changes in the Chinese economy unravel within this frame of reference: compliance with international commitments (WTO) and internal advancement toward Rule of Law on one hand, and the challenge of upholding an economic model that has maintained and privileged direct State participation in different economic stages and processes for 30 years on the other. This has given it an edge over competition from other countries, such as those in Latin America that began their extreme withdrawal from State models in 1980. In this Statemarket challenge, despite China's important legal advancement in economic development, direct State participation in economic processes does not entirely disappear. On the contrary, it continues to steer the model toward the center and west of the country by sustaining SEZs and special policies that motivate and support sustainability in the eastern area and new development in the center and west. Company classifications ("encouraged," "restricted" and "to be eliminated") are still in effect to determine the financial and tax support that allow them to develop and compete internationally. The State continues to hold direct shareholdings in "strategic industrial" sectors (military industry, power generation, petroleum, telecommunications, etc.) and in so-called "basic industry" areas (machinery, automotive, technology, etc.). It also has reduced and slowly "corporatized" their participation in state-owned enterprises (SOEs), or maintained certain prices under State control (approximately 4%), or continued to keep the price of utilities (water, electricity, gas, etc.) below normal to support local or strategic businesses. Furthermore, it has sustained tax rates and development policies for companies in certain geographic regions or sectors that are still considered of national importance, such as those in

research and development.[18] These are only some examples of a China that advances in compliance with its international relations and another China that continues to privilege growth strategies that give added value to economic development, though not entirely in line with global business regulations.

One of the main virtues of the Chinese model is that it changes at all times. Its flexibility and ability to adapt to new challenges place it at the forefront of the world economic scene. The 1980 Chinese model, weighed down with cheap manufacturing, is very different from the model of the 1990s with its intense electronics and technology exports. The 21st century model already shows a very solid outline, both in the strength of its exports and in the emergence of an internal market that did not exist in 1980.

Priorities have also undergone changes. The model has now shifted its strategy toward the center and west of the country, combining new and old formulas aimed at giving China more stable and homogenous growth. Both the new Corporate Income Tax Law (2008) and the Contract Labor Law (2008) have further strengthened workers' regulations. Both regulations form part of an economic development reorientation strategy, since the eastern area has started to reach the same levels of tax and work environments as the Western market. By discontinuing some of the attractive tax and labor benefits from the eastern area, companies and investments are encouraged to move to the central and western areas of the country, which are a waiting to take part in China's economic success. This is a significant change since, for example, nearly 80% of the manufacturing companies located in the Pearl River Delta are based on a low-cost business model. With these measures, companies will either survive with low profits, shut down or move to more advantageous areas with cheap labor, as they did 30 years ago in the same Delta region. As to this, the vice-president of the Taiwan Business Association in Dongguan pointed out, "no one wants to leave, but we are forced to move due to the vertiginous growth of costs."[19] In spreading out businesses as a result of the adjustments made to the model's inherent strategy (along with a devaluating exchange rate, international pressure from the WTO and the very success of Chinese trade), the Federation of Hong Kong Industries, one of the main participants in the area, estimates that 37% of its 80,000 companies have planned to move some or part of their operations outside the Delta. The Asian Footwear Association says that about 50% of its manufacturing centers will move to interior provinces while 25% have chosen another Asian country and the remaining 25% will wait and see. Authorities anticipate that technology manufacturing plants in the eastern area will prompt the sustainability of cleaner and more advanced industries in the fields of technology or research and development. Bearing in mind the experience and success attained in the Pacific, they expect to reproduce the 1980 and 1990 models in the central and western parts of the country with provisions for investments and more relaxed regulations.

Given its enormous success in China, this policy of preferential customs duties, meticulously applied in the 20th century and selectively applied in the 21st century, has brought about changes in global public tax policies and has even put pressure on tax application strategies in some European countries, which in recent years have seen the advantage of lowering income tax rates to maintain a level of competitiveness to in turn attract international capital. For example, in May 2004, France and Germany decided to reduce their corporate taxes to stimulate employment. In Mexico, global competition has compelled it to implement an income tax reduction policy, which went from 35% in 2000 to 28% in 2008. However, both in Europe and in Mexico, the measures applied correspond to a general economic inertia that makes no distinction between sectors, products or regions, as the Chinese model does. In consequence, the effectiveness of the measure decreases its application levels, its focus and its precision.

Since 2001, China has suffered international pressure to stop applying this kind of special support, commonly known as "tax dumping." Although China passed a new Corporate Income Tax Law in 2008 that already considers to progressively homologate company rates by 25%, this same law still includes a series of special discounts, such as 20% of applicable tax for small businesses with low profits, 15% for high-tech businesses, tax exemption for environmental protection businesses and "lower duties in general," which is completely discretional for venture capital businesses in State-motivated investments. Businesses with agricultural projects or in the central and western areas will continue to receive preferential customs duties for both income tax and sales tax, which may be fully extended in these cases (17%) (Annual sales tax evasion in China is estimated at 45% of the total collectible amount). [20]

The current strategy of raising China's Foreign Direct Investment (FDI) is not the same as the one instrumented in the two previous decades. The National Commission for Development and Reform and the 11th Five-Year Plan 2006-2010 have pointed out that the priorities have changed from quantity to quality, giving precedence to high technology, research and development and high added-value sectors, which are advised not to resort to intellectual property rights arguments to frustrate China's pursuit of innovation; that is, that they be willing to share technology. Services within strategic and national security sectors have been opened up to FDI, closely watching the impact wholly foreign-owned enterprises (WFOE) might have on China's economic security and particularly on its industry. [21]

Investments in China's central, western and northeastern regions are encouraged and an expected 80% of the new FDI is destined to these areas. Foreign investments with low technological content, high natural resource consumption or highly contaminating activities are prohibited.[22] In summary, China has gone from giving many facilities in the 1980s and 1990s in the early days of FDI in China (1978, scant FDI records) to a selection program that limits or prohibits unwanted investment and is moving toward a new

elitist FDI centered on technological value and the region where it will be used. Despite these limitations, the amounts obtained have not decreased with 75 billion dollars recorded for 2007 (World Bank). The recent legal changes in the eastern area, along with new FDI criteria for entry into China, come together in a clear strategic line, demonstrating that after 30 years the "Deng" model with Chinese characteristics is still applied.

5. *Long-Term Vision*

China already knows what it wants for the year 2020 and has a plan to achieve it. According to its Economic Development Plan for 2020, its goals are to quadruple its GDP, grow at an annual rate of 7% and reach a GDP per capita of US$4,000 to US$5,000 for roughly 1.5 billion people. It foresees 50% of its exports being made up of high tech goods. Finally, it contemplates implementing an internationalization program to position 50 transnational companies, 500 medium-sized companies and 5,000 SMEs in the world market by the year 2015. In 1953, China began its long-term programs with its 1st Five-Year Plan, drawn up under the guidance of the then Soviet Union and privileging heavy industry and the agricultural sector. To date, China has continued to plan ahead, as evidenced by its 11th Five-Year Program (2006-2010), which stresses the importance and responsibility of civil servants. This program will be evaluated not only on the country's success in economic growth, but also on the progress made in social development, education, environmental protection and job creation. This general and systematic policy of working towards long term goals is enhanced by special plans for specific topics, such as technology, income distribution, poverty reduction, etc., based on the State's development strategy. China has reached the point of planning 50 or 100 years into the future, as in the case of development in the western area. [23]

The use of time and space is an intrinsic part of Asian culture in general, and to China in particular. Incorporating these variants into the development model and its business strategy has given China a competitive advantage over most developing economies. Most Latin American countries —Mexico included— do not have an economic objective for 2020, just as they lack clear strategies or specific plans to achieve it. There is still a notable absence of planning that lays down a public and private policy derived from each country's strengths and aptitudes that could be successful within the framework of global competition. The only discernible route taken into consideration is generally found in the commitments established at the Millennium Summit for 2015. During this summit, goals to reach for certain rates of human development and social improvement were set. To date, China is the only country that has attained them. In Mexico, however, the political power struggle (executive vs. legislative) along with short-term out-dated government criteria have brought development expectations to an immediacy that is not

compatible with a policy for a project that evolves, like that needed in the technology sector, for example. China already knows which technological products it will incorporate next into its export platform, just as it has already defined what will be produced in given regions or areas of the country and when it should be achieved. Comprehensive long-term vision is a lesson that could be of great use in Latin American public policy.

6. *State-Owned Enterprises*

In 1980, state-owned enterprises (SOEs) made up approximately 99% of China's productive sector, a logical result of a central government. Under its various connotations, this sector had lessened its participation in enterprises to 8% by 2007. Given that it provided 18 million jobs in 2006 its strategic importance in the industrial sector is far from diminishing.[24] This important diminution of State ownership, especially in the last two decades, was the result of adopting the new economic model, which coincided with the arrival of foreign capital that gradually replaced state-owned companies. At the same time, the State privatized its public companies locally, mostly from 1990 to 2000, by offering executives and workers from medium and small enterprises the facility to acquire these companies.

The strategy the Chinese State implemented has followed a gradualist policy since its inception. Hence, it has privileged privatization, activities that produce increased exports or yield an apprenticeship in technology or some other area that gives added value over non-strategic sectors. Within this process, the State always assumed the role of referee for the different interests involved and balanced out privatization, foreign investment, strategic sectors and the strength of the development model. In contrast, there was no gradualism in Latin America and Mexico. On the contrary, most Latin American countries established a competition to see who could liquidate their public assets first. The different results of the two strategies are obvious. China emerges as a modern State with considerable economic power and large public enterprises, in addition to a private sector that has been converted into the basic force behind exports, technological change and the implementation of best management practices. In other words, by privatizing and opening up to trade, China consolidated a growth strategy that has positioned it today as one of the most successful countries, setting the pace and new paradigms for the entire world.

Latin America in general displays weak states in terms of its industrial chain, having lost important public assets whose proceeds were used for dead-end developmentalism or an increase in current spending. Between 1990 and 2000, most Latin American countries handled their privatization processes anarchically, without any strategic orientation that would allow them to select the goods to be privatized beforehand based on a long-term development plan that would strengthen their economic model.

Although there are a few exceptions like the oil and electric industry in Mexico, the sale of public assets, which included industrial, banking, services, or electric industry companies, transpired under a formula of international demand and not a systematic offer from the State (a process that was not exempt from acts of corruption). Unlike China, State privatization in Latin America did not promote the political or economic growth of the participants. On the contrary, because of its deficient implementation, Latin American nations are now less able to fulfill the task of promoting economic growth, social development and the preservation of public order.

Privatizing millions of enterprises or going from a central planning economy to a mixed market economy has not been easy for China. The State has confronted many problems and contradictions during the process of implementing "Market Socialism" without any historical reference at all. Which enterprises are non-strategic? How can national interest be safeguarded? How are the resulting monopolies to be administrated? How can corruption be prevented? How can a SOE legally be on the same level as a private enterprise? How can local SOEs be transformed without resistance from the provinces?

Today, the process is far along, but it is a long way off from the finish line. To begin with, a countless number of company categories still exist in China. However, according to Ministry of Industry and Commerce statistics, in 2006, there were already close to 5 million private enterprises in the various categories employing 52 million people, which represents 57% of the companies in the country. Despite the importance of privatizing, the Chinese strategy clearly indicates that progress made in the market economy or in the privatization of its assets is secondary to national economic interest. For example, the 2007 assessment report on the reforms carried out by China indicates that, "…experience has shown that in the context of economic globalization, a passive resistance to foreign investments turns out to be counter-productive…" adding that, "in the current situation, the excessive relaxation as far as an irrational placement of the State's assets in the productive sectors should be halted,"[25] to such a degree that, even with privatization, State-owned enterprises continue to have very strong participation in strategic sectors, such as gas and oil, where the State controls almost 100% of the area, 100% of the basic telecommunications services, 55% of electric energy generation, 82% of civil aviation, 89% of water, 50% of automotive production, 60% of the steel industry, 70% of the hydroelectric industry, etc. At the same time, SOEs have increased productivity over time, quickly adapting to more intense free market competition, drastically increasing its annual profits from 1.46 trillion Yuan in 1998, to 19.50 trillion Yuan in 2006. [26]

7. *Industrial Policy*

> *The strategy of low prices on finished industrial products within the Chinese domestic market inevitably has been spread to the international market. This can provoke phenomena associated with the current industrialization stage in China, such as antidumping lawsuits, a large-scale trade surplus, reevaluation pressures for the RMB (Ren Min Bi, currency of the People's Republic of China), as well as a hollowing out of the industry in some developed countries and neighboring countries as a result of the industrial transference. Fundamentally, these phenomena turn out to be imbalances in the economic trade relations, caused by the irrationality of the world economic order. They are also manifestations of the competitiveness of the Chinese finished industrial products, which have been moderated by the market competition between the 'good and the cheap.'*[27]

In 1978, internal credit in China's State banking sector represented 51% of the GDP. In 1985, it rose to 67%; in 1990, to 87%; and to more than 100% in 2000. Although the significant increase in these flows put an end to most of the corruption that had arisen from granting loans arbitrarily and fraudulently, its main aim was to transform an obese, inefficient industrial sector. The goal was fully reached when its participation in the economy rose from 40% to 50% over a period of twenty years. However, what was more important was the financial facilitation of the cost of its learning period, and later that of its industrial reconversion period and the development of a modern, efficient platform of goods and capital that today sustains the priority sectors. Such is the case of the automotive sector, in which 50% of the machines and numerical control instruments used in these factories are already produced by Chinese companies. In addition to preferential, there was also a tariff subsidy and duty-free benefit strategy that opened up machinery and capital goods imports exempt from any payment whatsoever to cover part of the learning stage. To date, the machinery for high technology sectors or priority sectors are still exempt from import tariffs or restraints. Moreover, strategic industrial lines were backed by monopoly policies in the internal market and access to international financial markets were established. SOEs were given priority treatment in the metallurgic, transportation equipment and chemical industry sectors, as was foreign investment in textile and manufacturing, electronics and telecommunications exports with the opening of the market.

When one speaks of the "world factory," one thinks of the 30 or 50 cents on the dollar per hour paid to the Chinese workforce. Although this cost is a strength (both for China and all developing economies), a comprehensive public strategy that transforms a weak manufacturing position into an internationally competitive productive activity is required to make it possible for this workforce to give added value. This change can be clearly seen in the composition of the Chinese industrial sector, in which manufacturing-assembly lines went from representing 90% of it in 1978 to 70% in 2002, despite a significant increase in the industrial sector's GDP for the same period. Just as in-bond assembly and the agricultural sector lived

through the Asian development boom, the trade surplus generated by mature 100% Chinese manufacturing branches, such as the textile and clothing, toy, sports, footwear and furniture industries currently provides for the new technological sectors that have yet to generate surplus balances, such as electronic, medical-surgical, electrical material and photographic equipment sectors, etc., or lack supplies like fuels, minerals or steel. [28]

Industrial policies in China and Latin America (including Mexico) have followed different patterns. With mercantilist pragmatism, the Chinese model first focused on opening by exporting manufactured goods made by its ample workforce and then went on to flexible specialization with strong state investment. This led to setting up labor intensive industries such as textiles, clothing and electronics, and later moving on to heavy industries (steel, petrochemistry, vehicles, aeronautics) and now to high technology. This process was accompanied by a strong boost to infrastructure for development and important resources in innovation and technological development with high rates of internal savings and investment. This model followed a gradual and progressive path that made it possible for them to learn from their own experiences.

The Latin American industrial model, however, came about with an almost complete trade opening without possessing the experience to administrate it properly, and with an extreme lack of State involvement. This left the national production chain at the mercy of free market forces. Jin Bei points out that "[t]he most powerful driver of the market economy is competition, which generates efficiency, promotes growth, and creates well-being." However, he adds,

> *this market mechanism does not intrinsically have the ability to reach balance, security, and automatic innovation, and it is not in itself a mechanism that distributes the fruits of industrialization to all its participants. On the contrary, the competition of an imperfect market will always generate great disparities, even chaos, crisis, and polarization, creating an undesirable situation that is contrary to the accepted human values and that goes against long-term national interest and its basic values…*

Which is why, "[i]n summary, the industrial development strategy of a country will always be based on rational and national factors that include factors such as nationalism, ethics, and many other cultural values."[29] National interest is precisely what some Latin American countries have lost on their way to the free market. It is also marks the big difference with the Chinese model, which is based on the basic principle of regarding national interest as a priority. Therefore, China has always been on the side of its companies and

industrial projects in both its internal market where it has successfully increased the production of products selected every five years and in its external market where its participation in world exports was only 0.8%, in 1980 but reached 5.3% by 2001 to be surpassed in 2007 with 6%.

Fig. 1 INDUSTRIAL GROWTH (1978-2006)

Industrial Product	*1978 Production*	*2006 Production*	*Industrial Product*	*1978 Production*	*2006 Production*
Automobiles	0	3.8 million	Chemical Fibers	280 thousand tons.	20.7 million tons.
Washers	0.04	35.6 million	Beer	400 thousand liters	35 million liters
Refrigerators	2.8	35.3 million	Water Energy (100 million KHW)	4.4 million	43.5 million
Air Conditioners	0.02	68.4 million	Paper	4.3 million tons.	68.6 million tons.
Cellular Phones	0.0	480 million	Sulfuric Acid	6.6 million tons.	50.3 million tons.
Micro computers	0.0	933 million	Chemical Fertilizers	8.6 million tons.	53.4 million tons.
Clothing	1.1	5.9 million	Ethylene	380 thousand tons.	9.4 million tons.

Fig. 2 INDUSTRIAL GROWTH (1978-2006)
(continuation...)

Industrial Product	*1978 Production*	*2006 Production*	*Industrial Product*	*1978 Production*	*2006 Production*
Color TV	0.38	83 million	Cement	65.2 million tons	1236.7 million tons
Tractors	110 thousand units	190 thousand units	Crude Iron	31.7 million tons	419.1 million tons
Motor Vehicles	140 thousand units	7.2 million	Pig Iron	34.7 million tons	412.4 million tons

SOURCE: CHINA STATISTICS YEARBOOK 2007.

In the last 30 years, China has never stopped its industrial process nor has it allowed it to eliminate its weak and inefficient industry of 1978 in the interests of a "free market." On the contrary, by using the free market, it has established continuous improvement and strengthened the greater part of its manufacturing sector. As Meza Lora points out,

> *the convergence of the market and the State in the industrial sector in China is an expression of an unquestionable fact: recognition that the rules of the game should be governed by the market and the necessary State intervention given the weakness of this Institution. A socialist market economy with Chinese characteristics does not assume the antagonism between the State and the market. On the contrary, it understands that the market and the State can play a complementary role in industrial coordination activities. If the market is deficient in solving coordination problems, an explicit industrial policy is justified as a coordination mechanism ex ante that does not come from the market.* [30]

Within this general framework of joint State-market work, the following actions that the Chinese government has implemented in its industrial policy stand out:

- Direct investment in infrastructure projects; financial and budgetary assistance in projects from regions lagging behind.
- Administrative intervention from the central authority in its enterprises to conclude and establish joint ventures, mergers, etc.
- Price control over basic supplies (for example, energy and water supply).
- Direct and long-term financing for key companies; preferential capital allocation to companies by way of the capital market, especially for new companies or those seeking to increase their technological development.
- Tariffs and duty-free measures, import quotas, licenses and local restraints on imports.
- The prohibition for foreign companies to distribute products not produced in China or for controlling their own distribution networks.
- Low interest rates in State banks and selective loans to different industries.
- Tax incentives to companies oriented toward industry.
- Reduced tax rates for high-tech companies in the field of industrial technological development.
- Zero taxes for companies of "urgent need for the State" (fixed capital investments for agriculture, water conservation, transportation, postal service, telecommunications, certain medical projects and machinery and electronics, etc.).

- State enactment of a Direct Foreign Investment Guide that specifies the projects that are encouraged, allowed, restricted and prohibited, etc. [31]

IV. Bibliography

[1] González García, J. (2006). *Perfiles recientes del desarrollo económico de China*. Mexico: Universidad de Colima-UAM.

[2] Deng Xiaoping (1994). *Selected Works*, Vol. I. & Vol. III.

[3] Deng Long (2002). *Deng Xiaoping & the Cultural Revolution*. Beijing: Foreign Languages Press.

[4] Wang Mengkui (2003). *China's Economic Transformation over 20 years*. Beijing: Foreign Languages Press.

[5] DENG LONG, DENG XIAOPING AND THE CULTURAL REVOLUTION 35 (Foreign Languages Press, Beijing, 2002).

[6] *Id.*

[7] *Id.*

[8] *Id.* at 40.

[9] DENG XIAOPING, SELECTED WORKS, Vol. II, 266 (2nd ed. 1995).

[10] Mengkui, *supra* note 8, at 38

.

[11] *Id.* at 19.

[13] Mengkui, *supra* note 8, at 23.

[14] SUN TZU, EL ARTE DE LA GUERRA 52 (Mercado, 1999).

[15] CHI FULIN, THE THRESHOLD 178 (Foreign Languages Press, Beijing, 2006).

[16] GAO SHANGYUAN & CHI FULIN, NEW PROGRESS IN CHINA'S SPECIAL ECONOMIC ZONES 9, 41 (Foreign Languages Press, Beijing, 1997).

[17] CHI FULIN, PRESSING TASKS OF CHINA'S ECONOMIC TRANSITION 261 (Foreign Languages Press, Beijing, 1996).

[18] United States International Trade Commission: China Description of Selected Government Practices and Policies Affecting Decision-Making in the Economy, 2007.

[19] Interchina Insight, *¿Dónde estará el próximo Dongguan?* 3, March 2008, available at: *www.interchinaconsulting.com*.

[20] United States International Trade Commission *supra* note 21, at 67-69.

[21] Interchina Insight, *La actitud china hacia la inversión extranjera está cambiando*, November 2006, available at: *www.interchinaconsulting.com*

[22] *Id.*

[23] ARTURO OROPEZA GARCÍA, CHINA ENTRE EL RETO Y LA OPORTUNIDAD 290 (IIJ-UNAM, 2006).

[24] CHINA STATISTICAL YEAR BOOK 520 (2007).

[25] 2007 EVALUATION REPORT ON CHINA'S REFORM 83 (Chi Fulin ed., Foreign Languages Press, Beijing, 2007).

[26] Jin Bei & Li Gang, *Chinese Industrial Enterprises*, *in* CHINA ECONOMIST 55 (2008).

[27] JIN BEI, THE INDUSTRIAL COMPETITIVENESS OF CHINESE INDUSTRY 32 (Foreign Languages Press, Beijing, 2007).

[28] Oropeza, *supra* note 26, at 308.

[29] JIN BEI, THE INDUSTRIAL COMPETITIVENESS OF CHINESE INDUSTRY 155 (Foreign Languages Press, Beijing, 2007).

[30] José Salvador Meza Lora, El Rol De Las Instituciones Con Las Grandes Transformaciones Del Sector Industrial En China Durante La Reforma Económica 285 (Porrúa, 2006).

[31] *Id.* at 229.