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Revisiting China’s Economic History

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The current global geopolitical environment is marked by several transformative changes. While most parts of the world are still coping with the economic slowdown in the aftermath of the Covid-19 pandemic, many others are caught in the crossfires between Russia and the West sparked by the ongoing war in Ukraine. However, the moment for speculations and conjectures has come to an end as divisions between the East and the West have now become stark. A prominent reason for this division has been China’s economic growth threatening the West’s domination. At a time when the global geopolitical order stands at the cusp of change, it is important to understand how the Chinese economy was able to transform itself taking the country from the fringes to the centre. Towards this end, this piece attempts to trace the Chinese economic growth since the reform of 1978.

The year 1978 marks a clear separation between the erstwhile centrally planned Chinese economy and the present-day market-driven economy. Before 1978, China’s economy was characterised as poor, stagnant, centrally controlled, vastly inefficient, and relatively isolated from the global economy. The economic reforms of 1978 led by Deng Xiaoping worked wonders for the middle kingdom as they introduced sweeping changes to secure China’s economic growth. Until 1978, all the productive assets of the country were centrally planned and controlled by the state. This planning technique was borrowed by China from the Soviet Union. As there was an absence of a market economy, private enterprises and foreign-owned firms hardly existed leaving no scope for foreign direct investment (FDI) inflows. The government set production goals, controlled prices and allocated resources for most of the economy. In the 1950s, China collectivised individual household farms into large communes and undertook large-scale investments in physical and human capital to promote industrialisation. This policy could only achieve a moderate growth of 5.3 per cent on average.

After the reform of 1978, China encouraged the formation of rural enterprises and private businesses, liberalised foreign trade and investment through joint ventures, relaxed state control, invested in industrial production and education, instituted the household responsibility system in agriculture and established Town Village Enterprises (TVE) through which farmers could sell their surplus crops in an open market. The dual track system was also introduced where the Yuan represented its foreign trade currency and the Renminbi represented its domestic currency. It also followed a different pricing system for state-owned enterprises and private enterprises.

Deng Xiaoping's four pillars which ensured China's success in the economic sphere were – upholding Socialism; people's democratic dictatorship; leadership of the CCP; and the Maxis-Leninist-Maoist thought. Two years after the reforms, China's representation in international institutions started increasing – it became a member of the International Monetary Fund (IMF) and the World Bank. It also created four Special Economic Zones (SEZ) in Zhuhai, Xiamen, Shenzhen, and Shantou. The creation of these SEZs helped China to attract FDI inflows to a significant extent. Until 1978 China's annual growth was recorded at six per cent but after it introduced the new economic reforms, it recorded an average real growth of more than nine per cent with some years exceeding even thirteen per cent. In 1978 China's total imports and exports ranked 32nd globally contributing less than one per cent of global trade. One of the major advantages of these reforms was that they freed the enterprises from the regular interference of the state authorities. Hence, there was a decline in the output of state-owned enterprises from 56 per cent to 40 per cent from 1978-1992. During the same period, the output by collective enterprises rose from 42-50 per cent and that of private businesses and joint ventures rose from 2 to 10 per cent. The cumulative foreign direct investment which used to be insignificant before 1978 reached almost US$100 billion in 1994 and even the annual inflow increased from less than 1.1 per cent of total fixed investment in 1979 to 18 per cent in 1994. The profit incentives made available to factory owners and producers by the reform played a positive role in increasing and enhancing the private capital market as the businessmen invested more and more of their firms' revenues to improve business performance.

As a result of the economic reforms of 1978, China has now become one of the fastest developing countries and it figures at the very top in world trade. It is at present the world's second-largest economy after the US with a GDP of 17.7 trillion USD. Aside from making impressive strides in the economic sector, China is giving tough competition to the West in the field of Artificial Intelligence (AI) as well. China is also one of the biggest spenders when it comes to research and development (R&D).

While it is true that China's ideologies, political system and economic approach differ from the rest of the world, these differences should not come in the way of developing a wholesome understanding of the country. It is important for countries such as India to be aware of these differences as well as their growth trajectory.