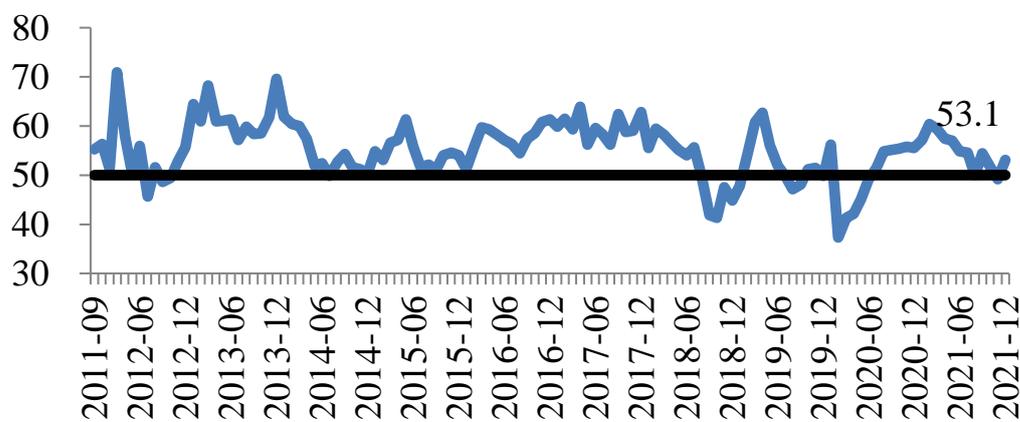


Commentary on the December 2021 CKGSB Business Conditions Index

Professor Li Wei

In December 2021, the CKGSB Business Conditions Index (BCI) experienced somewhat of a rebound, rising from 49.2 to 53.1, and breaking through the confidence threshold of 50.0 (Figure 1). Company operations are in a better place than the month before.

Figure 1 Business Conditions Index (BCI)



Source: CKGSB Case Center and Center for Economic Research

In the third quarter of 2021, the national GDP growth rate was down to 4.9%, and with further weakness in areas such as real estate, shows that the Chinese economy was continuing to slow. Some market views suggest that economic stabilization will not be realized until roughly the second quarter of 2022. In order to support the economy through the bottom, policymakers are making a major turn, cutting the cash reserve ratio and cutting interest rates again. These measures will help, but they are not enough, because our current approach to promoting economic growth focuses mainly on stimulating aggregate demand. Really sustainable high-quality economic growth comes more from structural reforms. Structural reform involves measures that allow for new economic growth without increasing capital and labor inputs. Structural reform often refers to institutional change and the resulting reallocation of resources, in which more efficient sectors receive more resources and therefore get more out.

A key characteristic of structural reform is that it isn't easy. It involves the redistribution of benefits, which is not good for those with vested interests. On a recent visit to Nantong in Jiangsu, Huanbei township, I learned about property rights reforms at the local township enterprises which illustrates what structural reform really entails. At the end of 1992, the 22 rural enterprises in the township had fixed assets worth 11 million yuan combined, accumulated losses of 12 million yuan, and total liabilities of more than 20 million yuan. That year, they produced 27.14 million yuan-worth of goods and made a loss of more than 1.5 million yuan. Only one company made a profit, two broke even, and the rest lost money. Funding from the township credit cooperatives accounted for more than 85%

of total loans, which also puts the township finances in a tricky situation. With a cumulative deficit of 680,000 yuan, it was difficult for government agencies to operate normally. Some local authorities had trouble paying wages. From a financial point of view, these small and medium-sized local state-owned enterprises were in badly need of reforms.

The local government took certain measures, like choosing a factory manager, implementing collective contracting, and risk mortgage contracting for all employees, but none of them worked, and the company remained unprofitable. This was also the year in which Deng Xiaoping delivered his Southern Tour speeches, “The reason people hesitate to carry out the reform and the open policy and dare not break new ground is, in essence, that they're afraid it would mean introducing too many elements of capitalism and, indeed, taking the capitalist road. The crux of the matter is whether the road is capitalist or socialist. The chief criterion for making that judgement should be whether it promotes the growth of the productive forces in a socialist society, increases the overall strength of the socialist state and raises living standards.”

Right from the very beginning of property rights reform, there was huge controversy. Some believed that collective property should be transferred to the individual. But this elicited debates about private ownership and the power of the government. Some people also thought that reforms would inevitably disturb the status quo. However, the situation in Huanbei Township was very serious, and it seemed impossible to change its fate. Therefore, the local government did not back down when people raised such concerns. They actively prepared and pushed forward with reforms.

First, the local government adopted its reforms by selected two enterprises for the pilot, then rolling out the reform when the pilot was successful. Second, there were a lot of issues in the process of enterprise restructuring. One of the issues centered around what to do with the laid-off workers. The local government adopted a “redemption” policy, using more than 2 million yuan it obtained from auctioning off business assets as capital on which interest was generated. More than 200,000 yuan was accrued in annual interest payments, which was earmarked for subsidizing the laid off workers.

After the reform of property rights, the enterprises in Huanbei township regained their vitality, and their operating efficiency increased significantly. After the reform, these small state-owned enterprises created more benefits less burdened by people, which is a typical form of structural reform. From this case, we can highlight a few points. First, structural reform is often adopted when there is no way out, because it is too difficult, so it is not impossible, and not everyone will adopt this method; third, the risk of failure of structural reform is very high. Even if careful preparations are made, there may be omissions. Just like Huanbei township’s “redemption” policy for laid-off workers, if this had not been taken into account, there would likely have been problems; Experiments in the township proved that structural reform is feasible as long as there is firm determination and sufficient courage, coupled with certain patience and careful thinking. Once successful, it will bring tangible benefits.

China has, until now, been a developing country, and with much reform left to go, can still claim

the mantle to some extent. There is indeed a lot of “low hanging fruit” left to pick. As long as China makes up its minds to change, the Chinese economy’s road to high-quality growth is something we can all look forward to.

This is a commentary on the CKGSB BCI report for December 2021 to which you are welcome to refer for detailed statistics. Do not hesitate to contact the BCI team by email for the accompanying BCI data report.

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