China turns away from shock therapy, as threat of mass unrest grows

by Michael O. Billington

Two major "China Summit" conferences were held in Beijing during the week of May 11-15, featuring the top leadership of the Anglo-American financial structure to plan the next stage of their intended control of the Chinese economy. However, the conferences took place in the midst of a significant turn away from the free market reform process by a Beijing government faced with the mounting danger of mass unrest among the impoverished rural population and growing resistance to foreign efforts to dismantle the state sector industries.

The conferences—one sponsored by the *International Herald Tribune* (published overseas by the *Washington Post* and the *New York Times*) and the Chinese State commission for Restructuring the Economic System, and the other sponsored by the Ministry of Foreign Trade and Economic Cooperation (Moftec)—were treated to lectures from Henry Kissinger, deemed the Tai-pan of the new British colonial operations in China; Peter Sutherland, the director of the General Agreement on Tariffs and Trade (GATT); Ernest Stern, managing director of the World Bank; and executives of a variety of the multinationals which are sucking everything they can from the 200-million-strong unemployed being recycled through the trade zones in China. The conferences served as a public show of force to President Clinton, demanding that he renew Most Favored Nation status for China without conditions—which in fact Clinton did the following week. Also, all participants, including the faction of the Chinese leadership which attended the conferences, agreed that China must rapidly push through the free trade reforms required to achieve membership in GATT before the founding of the World Trade Organization (WTO) next year, so that China can be a founding member of this new U.N. free trade police force.

But the kind of shock therapy required to meet the wishes of these world financial leaders, who see China as the last source of loot for the cancerous growth of the financial bubble in the western banking system, is causing such severe internal hemorrhaging within China that Beijing is trying to apply emergency tourniquets to stop the bleeding. To the growing consternation of the London and New York China players gathered in Hongkong, the following measures have been adopted:

- strict controls on oil imports and distribution, which essentially reconstitute control over the oil market by the national oil monopoly;
- a freeze on trading in selected commodities and commodity futures, including oil, sugar, coal, food oils, and certain steel products;
- controls on the sale of state-owned assets by local governments without Beijing's approval;
- postponement of plans to sever all government controls over businesses in the Shenzhen Special Economic Zone, including state-owned firms;
- limits on profit margins permitted to foreign investments in power plants, set at a maximum of 12%, far below the average rate in previous deals;
- other measures similar to the 16-point "austerity policy" implemented last June by economic czar Zhu Rongji, intended to slow down the speculative binge in real estate and light industry. Those measures were essentially rescinded a few months later when Deng Xiaoping called for faster growth regardless of the consequences.

The *Asian Wall Street Journal*, in a story headlined "Market Lockup," complains that the new oil regulations "mark a sharp reversal from a two-year trend toward freer competition." Such protection of China's national industries is anathema to the free-traders at the *Journal*. "Unlike price controls imposed recently on sectors such as steel, coal, and grain products, intended to help consumers and state-run enterprises cope with inflation, the oil price controls appear to have one main beneficiary: the oil monopoly." Beijing both banned imports and raised the price on the oil produced domestically. Cheap imports had left the crucial domestic oil industry unable to sustain its operations, which also endangered a significant source of government revenue.

Although these measures represent a necessary turn away from the worst of the free trade reforms, they will not solve the fundamental problems facing China's state sector industries. Antiquated machinery and desperately inadequate infrastructure underlie the inefficiency of these state sector giants. The oil refineries, for instance, which are primarily in the north, have large stockpiles of oil, but the transportation bottlenecks in the country made it cheaper to import oil in the south than to use domestic sources from the north!

Two other, very different conferences

Kissinger's friends at the World Bank have used the fact of this inefficiency to demand the implementation of the "shock therapy" methods used in eastern Europe—simply shutting down much of the state sector entirely. There is resistance to this in Beijing, which is not blind to the unfolding disaster in Russia, Poland, the Balkans, etc., caused by shock therapy imposed by the International Monetary Fund (IMF). Vice Premier Zhu Rongji, who has been put in charge of the economy and was made acting prime minister during Li Peng's recent trip to Central Asia, was notably absent from the two "China Summit" conferences. Zhu was instead addressing two very different conferences held in Wuhan, the capital of Hubei Province, and Zhengzhou, the capital of Henan Province, both in central China. His message, as reported by the official *China Daily,* was that "reforming farm policies and efficiently running state enterprises are the keys to developing a good economy and stabilizing society." He directed "officials at all levels" to "emphasize their economic work on agriculture and running state enterprises. This is the key to handling the relations between reform, development, and stability."

In a similar vein, Qiao Shi, the ex-chief of security who now heads the National People's Congress, called for a mobilization of the surplus rural labor to build roads and water conservancy facilities. He also said the key to improving the state sector industries lies in the application of "sophisticated technologies."

Such emphasis on government support for industry, agriculture, and large-scale public works projects in infrastructure is far from the free market prescriptions of the Kissinger gang.

In keeping with this turn in policy, the government has carried out an aggressive domestic bond sale program this year, the first in several years except for a small offering last year. A record $11.5 billion in state bonds have been assigned to local banks across the country. This fund is intended to fill the growing federal deficit which has reached drastic proportions due primarily to losses accrued by over one-third of the state sector industries and resistance to central taxes in the provinces, which would rather spend the money in the speculative markets locally. Guangdong Province, the center of the China bubble in the south, has failed to meet the schedule on the state bonds, bringing stern orders from Beijing to restrict "indiscriminate fundraising" for local investment schemes, in order to "ensure the fulfillment of the task of issuing treasury bonds as scheduled across the province."

The additional funds in Beijing are crucial if Beijing is to back up Zhu's orders to support agriculture and the state sector industries. Over the past years, peasant income has been squeezed by the rising cost of farm inputs and general inflation, coupled with stagnant farm income. Peasants have often been paid in scrip due to the lack of cash in government coffers, which, together with the mass unemployment (approximately *200 million*) in the countryside, has led to thousands of local demonstrations and riots across the country (see accompanying article). A similar increase in labor actions in industry, protesting the layoffs and industry closings, has Beijing even more worried. The threat of a Polish-style Solidarnosc movement is one that deeply haunts the Communist Party, as evidenced by the continuing ruthless repression of every new occurrence of independent labor organizing, despite the international pressure around human rights violations. The government announced on May 5 a group of new "offenses against Public Order" which include penalties for membership in "unregistered organizations" or secret societies, and "distorting facts, spreading rumors, or otherwise disrupting public order." Besides such outright repression, however, the current economic policy turn indicates an effort to at least slow down the deadly bloodletting against the population.

'Development Banks'

Another step in the same direction was the launching of the State Development Bank (SDB) in mid-April. The SDB is one of three "development" banks announced in January, although the other two (an agricultural bank and an export-import bank) are yet to be established. These banks, modeled on the Japanese Ministry of International Trade and Industry (MITI), are intended to funnel state revenues into targeted development projects in state sector industry and agriculture, while the commercial banks are allowed to function with less state regulation. The SDB is raising another $7.5 billion in domestic bond sales, which, like the $11.5 Treasury bills, have been assigned to banks around the country under a quota system set by the People's Bank of China (the central bank). Besides garnering the funds desperately needed in Beijing, the two massive bond sales are intended to dampen the virtually uncontrolled speculative binge in real estate and low-skilled process industries in the provinces.

There are signs that the massive foreign investment of the past three years may be drying up. The "rush is over" for Taiwan investment in the mainland, according to the *Asian Wall Street Journal,* partially due to the fact that much of Taiwan's low-skilled process industries have already moved to the mainland, and Taiwan will not allow the more advanced industries to follow suit, due to political concerns. But it is also due to the fear of a breakdown and social chaos in the mainland, and the potential bursting of the speculative bubble.

The latter is definitely the cause of the dramatic declines in the Hongkong stock market since January—a fall of 25%, almost entirely due to China-based stock issues—as well as the collapse of the new domestic stock markets in Shanghai and Shenzhen. Several major private investors, notably Hongkong builder Gordon Wu, have cut back drastically on their plans for major power and transportation projects in the mainland. The World Bank and the Asian Development Bank, in the meantime, have both announced a cutback in infrastructure loans, claiming that the private sector is providing adequate financial support for infrastructure.

Ironically, the largest slice of the projected foreign investment in infrastructure is coming from the world's leading derivatives speculator, George Soros, who has set up funds with both GE Capital and the Hongkong-based Peregrine Investments totalling $3.5 billion, according to the *Financial Times,* with China the primary target. As the global derivatives bubble collapses over the coming period—perhaps in the coming months—these sources will disappear.

Opportunity awaits

The battle for power in China after the death of Deng (an occurrence which must be considered just as inevitable as the crash of the global derivatives bubble), or perhaps even before Deng's death, will provide an opportunity for a dramatic transformation of the past 45 years of recurring economic disasters under Communist Party rule—provided there are those with the commitment and basic economic intelligence to meet that challenge. The publication in *Strategy and Management,* the journal of the Chinese Academy of Social Sciences, of the proposal by *EIR* founder Lyndon LaRouche and his associate Dr. Jonathan Tennenbaum, demonstrates the existence of at least some motion in that direction. The LaRouche program, featured in *EIR* on Feb. 11, 1994, is based on the construction of 1,000 new nuclear-powered cities over the next century, built along a series of "development corridors" cutting into the interior and connecting with several new "Silk Routes" to Central Asia, Africa, and Europe. This approach would allow the use of the high concentration of people and land use to increase per capita and per kilometer use of energy, water, transportation facilities, etc., and build the infrastructure necessary for these cities and for modern agriculture.

Along similar lines, an interview granted to *EIR* by Hui Yongzhen, vice minister of the State Science and Technology Commission of China (see *EIR,* May 27, 1994), expresses a serious approach to the necessity of developing the entire Eurasian landmass as the minimum approach to assure peace and development. It is these tendencies which must overcome the still-dormant view of the Chinese leadership that the capital needed for development must be extracted from coolie labor in primitive agriculture and low-skilled sweatshops.

If this latter policy is continued much longer, yet another holocaust awaits China's 1.2 billion people.

P.R.C. never stopped looting its peasants

by Michael O. Billington

Faced with a severe agricultural crisis, including thousands of peasant demonstrations and riots across the country as well as mounting production problems, the People's Republic of China (P.R.C.) Ministry of Agriculture Rural Economic Research Center released in January a stark analysis of the causes behind the crisis. (A translation of the report was published in the May 13 Foreign Broadcast Intelligence Service of the U.S. State Department.) The report is as notable for its honest admission of the systematic looting of the agricultural sector since the early days of Maoist rule through to today, as it is for a lack of any competent conception of how to solve the problem. In particular, there is absolutely no mention of the question of the mechanization of agriculture, nor of the horrible state of water and transportation infrastructure.

The report lists the problems affecting peasant income as follows: "the continuous deterioration of trading conditions for agriculture, the issue of IOUs for the purchase of farm products, the outflow of agricultural funds [the diversion of agriculture funds to speculation in real estate, etc.], the holding up of farmlands by development zones, and the added burden on peasants [extra taxes, levies, etc. by local government]." The result is that a rapid deterioration of farm income has reduced the ratio between the peasantry's per capita income and that of urban residents back to the pre-reform level of 1978, following the dark days of the Cultural Revolution.

Production growth, which fell significantly in the mid-1980s, recovered somewhat between 1989 and 1992, but only enough to sustain zero-growth in output per capita. The report provides the data shown in **Table 1,** which show the dramatic growth in farm output *and* income between 1979 and 1984, when the commune system was abolished and agricultural investments increased rapidly. However, in 1984, as the free trade reform policies were first being implemented as part of the deal with the British over the eventual return of Hongkong, the government intentionally cut agricultural investments, de-emphasized tractor production, and began to look the other way when peasants broke the residency laws, eventually flooding into the coastal cities in search of work in the export zones. The report points out that peasant income growth did not fall further than 5% in this