being results of delayed liberalization or the somewhat closed nature of the market of a late-developing country. Regardless of the justification for any foreign demands for further liberalization of the Japanese market, the question of international competitiveness of manufacturing industries should be addressed from quite a different angle.

Finally, the Japanese experience of the CPC development is consciously related to the problems facing the present-day developing countries. A lively debate was going on both in Japan and in the developing countries as to the extent to which the country's successful experience of development is relevant and instructive to the Third World countries which may wish to follow in the footsteps of a late-developing country. The author's well-considered conclusion seems to be that to the extent that the conditions for successful CPC development are given, the Japanese experience is fully applicable to other developing countries. But the historical uniqueness of the international and domestic conditions Japan faced should be taken into full consideration. After all, a blind copying of Japan's procedures cannot provide any effective solution to the existing problems. An effective policy must be based on the objective analysis of the given conditions.

(Hiroshi Kitamura)

China: Macroeconomic Stability and Industrial Growth under Decentralized Socialism by World Bank, A World Bank Country Study, Washington, D.C., 1990, xxi+299 pp.

Since China's participation in the World Bank in 1980, the Bank's commitment to the development process of the country has been expanding rapidly. It has extended beyond financial or technological assistance to consultation to China's leaders and technocrats on the market-oriented economic reform.

The Bank surveys China's economy occasionally, and the findings are summarized as country economic reports. Among those issued in the 1980s, two comprehensive reports based on the surveys conducted in 1980, immediately after China joined the Bank, and in 1984 were most influential.[1] Some of the policy proposals affected the decisions of the China's leadership as revealed in a recent study.[2] The report I review below, though neither as voluminous nor as comprehensive as the preceding two,[3] presents a more clear-cut image of China's future development strategy.

The report consists of two parts. Part One deals mainly with issues related to macroeconomic stabilization. Part Two takes up problems in the supply side. I will focus on the policy proposals set forth in these two parts.

[1] World Bank, *China: Socialist Economic Development*, 3 vols. (Washington, D.C., 1983); idem, *China: Long-Term Development Issues and Options* (Baltimore, Md.: Johns Hopkins University Press, 1985).

[2] H. K. Jacobson and M. Oksenberg, *China's Participation in the IMF, the World Bank, and GATT: Toward a Global Economic Order* (Ann Arbor: University of Michigan Press, 1990). See also Vanessa Lide, "The World Bank in China: Getting Back on Track Is Slow Going," *China Business Review*, Vol. 18, No. 1 (January–February 1991).

[3] In particular, external trade is not detailed in the report.

As the performance of the austerity program implemented in 1990 revealed, short-term stabilization itself is a comparatively easy task in a country like present China where the central government still holds considerable power to control economic activities directly. However, exclusive and prolonged use of direct control may eventually destroy the growth potential of the economy, the report maintains. The report recommends a series of reforms of macroeconomic management, its system, and environment as prerequisites for growth with stability. The following is the concise summary of the recommendations.

Monetary policy (Chapter 2): monetary policy, as well as direct control on investment, is considered to be one of the most effective tools for short-term stabilization. The report stresses the need for the central government to be firmly committed to stable money supply, which was almost absent in the 1980s. To improve the effectiveness of monetary policy, the report calls for the development of inter-bank market and the integration of the segmented local financial markets into a single national market. The independence of the People's Bank of China should be enhanced not only formally but also virtually, with the support from the political and economic circles. The report does not recommend a fixed rule for monetary expansion as was advocated by monetarists. Monetary policy should be tailored to the evolution in real and financial sectors, the report insists. A combination of monetary policy with fiscal policy is also recommended.

Income policy (Chapter 2): income policy will effectively complement monetary policy. In the short run, administrative control or collection of surcharge tax on excessive payment of wages is useful. In the long run, reforms of enterprises, particularly that of ownership, are necessary to give managers enough responsibility and incentives to resist demands from workers.

Public finance (Chapter 3): given the low level of national debt, large private savings, and high GNP growth rate, the report considers that the size of the fiscal deficit is relatively limited. However, the report maintains that as long as the threat of inflation persists, a trend toward fiscal balance is desirable. The first step should involve cuts in expenditure, especially subsidies for food and the loss-making state enterprises. In the medium or long run, stabilization of the revenue should be a major concern. This could be achieved through comprehensive tax reform and normalization of central-local fiscal relation. The report recommends a non-discretionary tax system based on a few, broadly based taxes. Such measures may also contribute to prevent the local governments from imposing excess burden on enterprises. A limited recentralization of finance to provide the government with the resources necessary for investment in infrastructure is recommended as a longer-term approach.

Investment (Chapter 4): to curb sharp and unrestrained surge of investment, "hardening" of budget-constraint of enterprises—and local governments, to a lesser extent—is required. Enterprises must face prices—interest rates, above all—which reflect scarcity. The report intently warns against the investment drive from the local governments.

Saving (Chapter 5): the upward trend of the household saving rate in the latter half of the 1980s contributed to the resource equilibrium during this period. Recent high saving rate may, nevertheless, include an element of involuntary saving induced by the shortage of preferred consumer goods. Thus the report warns against the liberalization of consumer prices in the presence of excess demand. It is suggested that expected return on financial assets should be raised. This measure, coupled with the reforms of urban housing and labor market, which enhance the propensity to save for city dwellers would keep the household saving rate at a high level.

Policy proposals presented in Part Two are classified into three categories: reforms of state enterprises and their economic environment; regional development and national market integration; and industrial policy.

Reforms of state enterprises and their economic environment (Chapters 6 and 7): in spite of the reforms implemented in the 1980s, most of the state enterprises still remain inefficient. For the lifetime employment system to work as an effective incentive mechanism as it does in Japan, the report advocates a closer link between a firm's profit and reward to workers. As a long-term approach, liberalization of the labor market combined with housing reform is recommended. Above all, state enterprises must acquire the full characteristics of autonomous economic entities and the influence of superiors must be restricted legally. These reforms will not work without price reform.

Regional development and national market integration (Chapters 6 and 8): to alleviate the widening gap in growth rates among provinces, the report recommends the liberalization of the flow of goods and factors. This measure necessitates (a) the coordination of industrial policies between provinces and dismantling of administrative barriers that hinder the flow of goods and factors, (b) a market-led integration of enterprises into large firms that can operate nationwide, and (c) the development of marketing and transportation infrastructures.

Industrial policy (Chapter 9): market principles do not function in a vacuum, but in the framework which prevents malfunction of the mechanism. And this framework, which China definitely lacks at present, has to be created and maintained principally by the government. Industrial policy discussed in the last chapter consists of three aspects: development of the legal system, especially laws that define property rights and contract relations; regulations such as anti-trust legislation; and the government's role as a coordinator of industrial structure. As for the third aspect, the report assigns a more positive role to the government than what had been contended by the neoclassical persuasion of economics. It states that

> China is now entering a stage when decentralized decision-making, increasingly influenced by market forces, will decide the course taken by the economy. This is the moment when a framework of rules on industrial strategy providing guidance for the long haul could usefully fill the vacuum left by the attenuation of central planning. Embryonic market...are inefficient at transmitting signals that can guide long-run decisions. (p. 225)

The policy proposals presented in the report are summed up as "macroeconomic policies juxtaposed with long-run development plan for the production sector." While the basic line is placed upon the development of the market mechanism and its necessary framework, the report suggests the applicability to China of the East Asian model of development, where the government intervenes in the market mechanism to reshape the industrial structure from the viewpoint of long-term national interest.[4]

This tenet of the report seems to provide a far better guidance for China's economic development strategy than the ultra-economic liberalism which prevailed in the 1970s and the 1980s. However, some aspects remain vague.

[4] *World Development Report* of 1987 issue touched upon the debate around industrial policy (p. 71, Box 4.4). There the importance of "the government's role as a coordinator and information clearinghouse" was suggested.

(1) Even moderate measures for a government to affect decisions of economic agents (affecting resource allocation) such as those mentioned in the report can provide substantial opportunities of rent-seeking. For a successful industrial policy, a government need not to be (and can never be, evidently) perfectly "honest" or "fair." But there should be certain socioeconomic conditions precluding the government's excess intervention which could involve the government in the network of vested interests thus providing wide opportunities for rent-seeking. Whether and to what extent these conditions can be met in China is quite uncertain. Industrial policy, therefore, may be associated with insurmountable side-effects in China.

(2) As is suggested in the report, under the fiscal decentralization, policy coordination between the central and local governments has become increasingly difficult. But the report does not give a clear-cut plan for the central government on how to implement a nationwide industrial policy in this era of economic separatism. Recent evolution of the central-local relations suggests that recentralization aimed at restoring the central government's control on the economy is neither probable nor desirable. Thus, the central government must accept the near-independence, in terms of economic policies, of provinces as given and design an industrial policy in taking the behavioral patterns of provincial authorities into consideration. The role which the central government will play in the future development process may be a more modest one than envisaged in the report.

(Ken'ichi Imai)