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a weekly chronicle of the Chinese economy

- The *communiqué* emanating from the 3rd Plenum of the 18th Central Committee of the Chinese Communist Party states that the market has been upgraded from playing a “basic” role in the allocation of resources to a “decisive” one. **Phat Dragon’s** multiple previews of the Plenum highlighted that China’s present unbalanced economic structure is symptomatic of distorted markets for the factors of production, and that reducing these distortions (price and non-price) would go a long way towards ensuring the sustainability of the country’s long run growth path. With this single statement, the leadership has signalled that the market is the new arbiter of resource allocation. Further, by investing substantial political capital in a new leading group to steer the “*comprehensive deepening of reforms*”, while sending explicit instructions that “*the entire Party must unite their thoughts and actions around the Centre’s major policies and deployments on comprehensively deepening reform*”, cadres at all levels cannot be confused about the resolve of the leadership to execute on their vows. A lack of clarity on this point can effectively neuter a reform program before it begins. Here we have both clarity and a voyage that is already in mid passage.

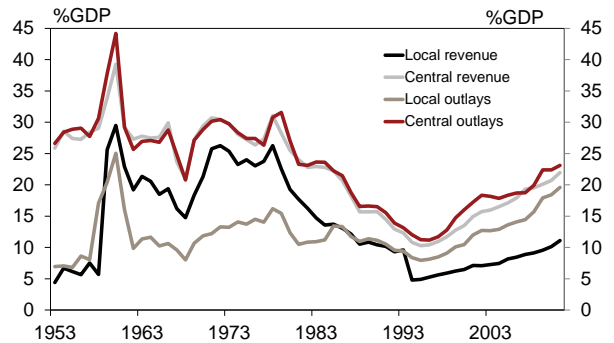
- Exactly what is the content of this program? **Phat Dragon’s** interpretation is that the agenda is marketisation writ large, with price signals moving to the centre of decision making; the rise of ‘black and white’ law to displace the present murk; transparency of governance with a clear separation between administration and policy on the one hand and the commercial activities of state firms and agencies on the other; modernisation of the fiscal and financial systems, with rising international engagement and lower entry barriers; removing disadvantages faced by the private sector (as opposed to the dismantling of the advantages enjoyed by state firms) and internal migrants; enhancing property rights of rural residents; moving forward on the enhancement of the soft infrastructure of the society (social security, education and health access and quality of provision); while optimising urbanisation away from the coast and in small and medium sized agglomerations (noting that President Xi chose the landlocked province of Hunan for his pre-Plenum tour). An increased emphasis on environmental amenity comes through vividly.

- This agenda is not the sort that breeds overnight deliverables - hence the leadership citing 2020 as the moment when they will seek to be judged. **Phat Dragon** refers readers to two official quotations from other fora, which help to explicate the Plenum outcome: “*the impetus for sustained development lies in deepening reform, urging targeted policies to cure not only ‘symptoms’ but deeply-rooted problems.*” And “*deepening the reform is a systematic project that is arduous and complicated and concerns the reallocation of various interests. There is no way to accomplish it overnight.*”

- What the *communiqué* does not do is present a catalogue of specific measures or divulge information on pace and sequencing. Those with a granular interest in financial deregulation will find the document underwhelming. On this point, it must be remembered that the *communiqué* is a Party document, not a Budget or a Monetary Policy Statement and the text itself is accordingly at times vague, oblique, circular, cryptic, obtuse and meandering. It is essentially a statement of principles not a menu of action, an expression of the leadership’s will and general intent. Even so, **Phat Dragon** is aware that a major domestic and international information harvesting mission is underway in the financial reform arena,

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### Revenues & outlays by level of government



(having contributed to it) the progeny of which should manifest in due course. The *communiqué* does state that “scientific financial and fiscal structures are an institutional guarantee to optimize resource allocation”. More poetically, Premier Li has styled financial reform as a chess piece, the strategic deployment of which is vital to China’s prospects in the grand development game. Clearly financial reform is seen as a vital tool in the marketisation of aggregate resource allocation. Ergo, the financial system itself must be marketised. As China edges its way across this particular river, the next foothold is surely the deregulation of deposit interest rates, with a flurry of private bank license approvals following not too far behind. Greater regulatory coordination will also emerge. On financial openness, the CNY’s daily trading band should be widened again soon, with the Shanghai Free Trade Zone playing host to a range of experiments across the internationalization space.

- Regarding SOEs, the predictable tactic is to work towards a level playing field in pricing, access and entry, which will gradually erode their privileged market position and dissipate the rents presently being accrued at the expense of households and private firms - and to an extent the government itself. The State Council income distribution roadmap was more precise in its calls for SOE dividend payout increases, while senior SASAC officials (the custodian of the government’s stakes in national SOEs) were reasonably forthcoming with proposals in the lead up, which raised expectations among the commentariat that something more substantive would arise from the Plenum.
- And finally, here are some of **Phat Dragon’s** favourite quotes from the floridly worded *communiqué* [note that these are unofficial translations that may prove unreliable]. “*Let power be wielded in the sunlight*”; “*not marching the old road of closedness and fossilization, not marching the evil road of changing banners and allegiances*”; “*the construction of a beautiful China in deepening ecological civilization structure reform*”; “*let all sources for the creation of social wealth fully gush out*”; and one for the true bureaucrats out there “*... moving forward with the institutionalization, standardization and proceduralization of ...*”.
- Stats of the week:** The *communiqué* used the word “reform” 54 times, “market” 22 times, “ecological” 11 times, “accelerating” 17 times, “governance” 14 times, “public” 12 times, “law” 8 times, “non-public” “free” “ownership” and “financial” 4 times each, “fiscal” 3 times and “transparent” twice.

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