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Characteristics of the Socialist Market Economic System Seen under the Impact of World Financial Crisis

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Abstract: The world financial and economic crisis caused by American sub-prime mortgage crisis has the following characteristics: violent influence; wide range; succession of financial crisis and economic crisis; powerful but invalid aid. The broad masses of the people suffered a great deal from such crisis. The reason why the Chinese economy could maintain a steady and fast growth under the impact of crisis is because that the market economic system of China is different from those of America and western countries, which has three characteristics: first, take the public ownership as the dominate part and the joint development of diversified forms of ownership as the basis; second, combine the national macro control with market mechanism; third, regard the solution of conflicts between strong social demand and lower productivity level. There is no intrinsic crisis but the capability to resist the financial crisis for socialist market economic system.

Facing the financial and economic crisis caused by American sub-prime mortgage crisis, the most serious one in the world over the past 70 years, the author observes that the

crisis occurred in the United States and major western countries instead of China though they are all under the condition of market economy; the mechanisms of crisis impact on western countries and China are different; the effects of countermeasures also vary from each other. The author believes that the analysis of causes of such phenomena should be made from the characteristics of socialist market economic system.

I. Characteristics of the World Financial Crisis

1. Violent Influence

In July 2007, the sub-prime mortgage crisis emerged in the United States, and in December of the same year, American economy started to slow down, and soon escalated into a financial crisis. On September 15th 2008, the US 4th largest investment bank Lehman Brothers with a history of 158 years bankrupted, it is the largest scale of business failure in the American history. The bankrupt declared by Lehman Brothers is a sign of outbreak of the world financial crisis. Its collapse foreshows a disaster of American finance industry. On the same day, Merrill Lynch, the US 3rd largest investment bank, was bought by the Bank of America. On the next day – Sep. 16th, the American government provided a loan of 85 billion U.S. dollars for the insurance magnate AIG (America International Group) to avoid bankrupt. Six days later, on Sep. 21st, the US 1st largest investment bank Goldman and the 2nd largest one Morgan Stanley were approved by the Federal Reserve to change into bank holding companies, plus the US 5th largest investment bank Bear Stearns that was purchased by JP Morgan half a year ago, namely in March 2008, out of the five US largest investment banks, one bankrupted, two were purchased and another two changed, all of them were shattered by the sub-prime mortgage crisis. Subsequently, on Sep. 24th, the US largest thrift institution Washington Mutual Inc. was sealed up and taken over by Federal Deposit Insurance Corporation. On Nov. 3rd, Wells Fargo US declared to purchase Wachovia Corp US. So far, within a short term of 50 days from the closedown of Lehman Brothers, the American finance industry lapsed into great crises rapidly and shook the world. On Dec. 5th 2008, Bush had to confess that: “our economy is in a recession. To a large extent, this is due to many serious problems in housing, credit and financial market.”

2. Wide Range

As a result of the integration of international finance market and the broad internationalization of financial institution, the financial storm transmitted rapidly from the Wall Street to the world over. Within two months, it has spread from America to major developed countries, then from developed countries to developing ones, and from the financial field to the real economy field, a severe chaos happened to the world economy. The stock market fell in the U.K., France, Germany, Italy, Switzerland, Japan and Australia

etc., and the price for crude oil, steel, iron ore, nonferrous metals also dropped sharply and the non-performing and bad debts increased obviously. Some banks have been purchased by the government as state-owned ones in the U.K. The Japanese stock fluctuated at the lowest point over the past 26 years.

3. Succession of Financial Crisis and Economic Crisis

The financial crisis spread rapidly towards the industrial economy, virtual economy and then promptly towards the real economy, forming a succession of financial crisis and economic crisis, which is another characteristic of the financial crisis.

With the transmission of financial crisis, it is estimated that in the U.K. the GDP 2009 will drop by 3.3% from the year earlier, the largest decline since 1949. Japan is experiencing the most serious financial crisis since the Second World War. Germany is also facing the worst economic downslide since 1940s. The French economy in 2009 is estimated to decline by 1.5-2% or more. The economy is dropping rapidly in Italy, Spain, the Netherlands, Belgium and Austria. Furthermore, some countries in Eastern Europe are affected by the financial storm too, including Russia, Ukraine and Hungary etc.; countries in Northern Europe like Finland, Sweden and Denmark etc. are stepping into a recession. Some other countries and regions in the North America, Europe and Asia that have plunged into a recessionary state include Canada, Ireland, New Zealand, Croatia, Estonia and Singapore etc.

4. Powerful but Invalid Aid

In order to deal with the financial crisis and prevent economy from a further recession, the United States and other countries in the world, with the power of government, have announced vigorous economic bailout programs respectively in succession, taking economy stimulating measures in many ways. On Oct. 3rd 2008, the American president Bush signed a bailout bill amounting to 700 billion U.S. dollars, but just within a week later from Oct. 5-11 the share price plummeted by at least 20%, the biggest percentage drop since more than 20 years ago. On Feb. 17th 2009, new U.S. president Obama signed another economic stimulus package with a total amount of 787 billion U.S. dollars. The British government launched the first round of financial bailout program in October 2008. Under the circumstance of failure, the British government announced the second round of financial bailout program in January 2009. In addition to offering guarantees for distressed assets of major financial institutions, it is intended to nationalize some large banks. The German government declared in Oct. 2008 to allocate a fund of 480 billion Euros for financial crisis, but the effect was limited. In Jan. 2009 the German government launched the second economic stimulus package, planning to invest 50 billion Euros in total in two year that will be mainly used for infrastructure construction. The French president Sarkozy announced a

bailout program amounting to 360 billion Euros totally in Oct. 2008, as well as an economic stimulus package with a total amount of 26 billion Euros, but the French economy is still going to slide down in 2009. The Japanese government launched a large-scale new economic stimulus package on Feb. 15th 2009, with the total amount reached at 1 trillion U.S. dollars. In Dec. 2008 India declared an economic revival program of 60 billion U.S. dollars in Dec. 2008, but no actual effect has been observed.

Coping with crisis through international cooperation is a kind of new operation mode under current situation of economic globalization. To deal with the world financial crisis, besides those bailout and economic stimulus measures respectively taken by different countries, they also managed to “spend the winter together” in an active and cooperative way. After the outbreak of financial crisis, finance ministers of the G7 and the chairman of Europe Group held a special meeting, and released a wide range of 5-Point Action Plan on Oct. 10th 2008. European leaders gathered in Paris on Oct. 12th 2008, and drafted a Collective Action Plan to rescue the banks in bad situation. However, all these failed to prevent the stock market from continuous downslide. On Nov. 15th 2008, leaders from the 20-country group, with 80% of the global economic aggregate and both developed and emerging countries involved, held the “Financial Market and Global Economy Summit” in Washington, where an agreement was reached on strengthening the cooperation of international society, coping with the financial crisis together and supporting the economic growth, and they also appealed to change the world financial system in order to prevent from reoccurrence of similar crises. This summit has positive effects on agreeing to an intention of cooperation among all present countries, but has no effect on saving the financial market. In April 2009, a summit of the G20 leaders will be held in London, England, to further discuss about effective measures for financial crisis. It is difficult for people to estimate what outcomes will be resulted in.

Though the aforesaid a series of bailout measures were taken timely and powerfully, no obvious effect has been observed. Till the middle of Feb. 2009, another 13 banks went to bankrupt in America. The Federal Deposit Insurance Company forecasted that about 100 American banks would be closed in 2009. The World Bank estimated that in 2009, the world economy would show the first negative growth since the Second World. The global trade would fall to the lowest point over the past 80 years. 129 countries would face a financial gap of 270-700 billion U.S. dollars. It remains to observe continuously when the world financial crisis will close. Russian *Red Star Newspaper* published a signed paper in March 11th, which put forwards “The Second Wave of Financial Tsunami Threatens.”

II. Consequences of World Financial Crisis.

The financial crisis is not only of violent influence, wide range and difficult salvation,

but also has resulted in serious economic and social consequences, which are mainly revealed in: the stock market kept on declining; the housing market depressed for a long term; the price of commodities decreased generally; the economy declined obviously; many workers lost jobs, broad labors lived in trouble. Asian Development Bank claimed in a report dated on March 9th 2009 that “the shrinkage of global financial assets might have exceeded 50 trillion U.S. dollars, equivalent to the annual output in global economy.” It also released that “excluding Japan, the financial assets lost 9.6 trillion U.S. dollars in value last year in Asia, a little bit higher than the annual GDP of Asia.” At the end of 2008, the household wealth shrank 11.2 trillion U.S. dollars in America. From the second half of 2007 to the end of 2008, the net value of household wealth in America has dropped by about 20%.

Broad labors suffered most under the impact of world financial crisis. The *St. Paul Declaration*, which was passed on the 10th International Conference of the Communist Party and Workers’ Party held in St. Paul on Nov. 21st 2008, claims that “in this large-scale economic crisis, workers and the masses of people became the victims, when the public resources amounting to a hundred millions of U.S. dollars were used to rescue those monopoly capitalists, high-ranking finance businessmen and speculators – the originator of crises, workers, small farmers, middle-class persons and all the people merely making ends meet were difficult to breathe under the heavy pressure of monopoly stratum, suffering from hunger and poverty___”. According to the statistics made by American estate tracking companies, that nowadays in America, the number of house properties having been withdrawn by banks has reached 820,000, making a new record, which is much more than the number of 224,000 at the end of 2006. It is obvious that the households in such 820,000 houses were drummed out for they couldn’t afford for the repayment of bank loans. In 2009, the unemployment rate will reach at 10% in America. Recently, Brezinski, an American famous scholar of international relationship and geo-strategist pointed out, that the financial crisis might cause social disturbances in the United States. As a result of the financial crisis, he said, “hundreds of jobless people” came out lately in America, lots of common Americans thus would “suffer from a serious problems of material requisite”, and then a social disturbance was going to be triggered. He said that in 1907 when American banks were in crisis, street clashes between different social stratum had occurred, “it is impossible to rule out the reoccurrence of such situation at present.”

III. The Chinese Economy Could Develop Steadily and Rapidly under the Raid of Financial Storm

Premier Wen Jiabao said in Davos Forum on Jan. 28th 2009: “frankly speaking, this crisis has also brought a major impact to the Chinese economy, we are facing severe

challenges, which mainly include: obvious shrinkage of external demands, superfluous capacity in some industries, difficult production and operation for enterprises, and increased number of jobless people in cities and towns, the pressure of declined economic growth increases obviously.” Although the Chinese economy has encountered severe challenges unprecedented, in general, the difficulties we met are still problems existing in the ongoing progress, the fundamentals and long-term tendency of our economy growth remains unchanged. Among major economies in the world, China was less seriously impacted by the world financial crisis, especially the Chinese financial system maintained a steady operation, and the Chinese economy kept a tendency of continuous growth. Specifically the following aspects are shown:

1. Continuous fast economic growth.

In 2008 the Chinese GDP reached RMB 3006.70 billion , increasing by 9% from the year earlier, and the contribution rate to world economic growth has exceeded 20%. The economic aggregate of China has surpassed Germany, is only next to America and Japan, ranked the third in the world. In spite that the Chinese economic growth declined 6/8% in the 4th quarter of 2008, which never came forth in recent years, the quarterly speed of increase is still the fastest one compared with many countries in the world.

2. Food harvest.

Food is a strategic product to ensure a steady economy and society. At the beginning of 2008, though the southern China suffered from a disaster of low-temperature frost, grains still maintained an increase in production for 5 consecutive years; the total yield reached 528.50 million tons in 2008, 5.4% up.

3. Income increased and life improved for urban and rural residents.

In 2008, the per capita disposable income for cities and towns reached at RMB 15781, increasing by 8.4% actually; the per capita disposable income for rural residents reached at RMB 4761, increasing by 8% actually. The Engel coefficient is 37.9 for urban residents and 43.7 for rural ones, both are better than last year. The consumer price fell back from 8.7% in Feb. 2008 to 1.2% in Dec.; thereby the life of inhabitants was materially benefited.

Though a large number of migrant workers returning home appeared in China under the impact of world financial crisis, thanks to the re-employment project actively promoted by the government, until the end of 2008 the registered urban and rural rate of unemployment was 4.2%, only up 0.2% compared with last year.

4. Abundant funds.

Since the Chinese financial system maintained steadily under the impact of world financial storm, plus the state is rich in financial resources, China possesses abundant funds enviable. At the end of 2008, the balance of China's M2 - the broad measure of money supply was RMB 47.5 trillion, up 17.8% compared with the end of last year; the narrowly defined money supply (M_1) was RMB 16.6 trillion, increasing by 9.1%; the balance of M0, the currency outside bank, was RMB 3.4 trillion, up 12.7%. The balance held on deposits of home currency and foreign currencies was RMB 47.8 trillion for all financial institutions, up 19.3% compared with last year; the balance of loans, including both home currency and foreign currencies, was RMB 32.0 trillion for all financial institutions, up 17.9% compared with last year. The amount of deposits is RMB 16 trillion higher than that of loans, equivalent to more than half of annual GDP, plus nearly 2 trillion U.S. dollars for foreign exchange reserve, which is 3 times of the balance of total foreign loans, so we are ensured to be sufficient in debt paying ability and investment ability.

Of course, we have also recognized clearly, that at present the world financial crisis is far from the bottom, the impact of crisis on China may become more serious, therefore we should prepare for a long-term crisis. However, since China is powerful in economic strength, has a huge space of development for domestic market, and the reform and opening outside helps to release forceful power of economic development, all these enable us to possess a stronger capability to resist risks. Therefore, no matter what ups and downs will appear in specific progress, China is always confident to get rid of the crisis earlier, to reduce economic losses to the minimum, to maintain a steady and fast growth of Chinese economy even under the situation of world financial crisis, and will try its best endeavors to make 2009 GDP increased by about 8% and Chinese economy revived the first one in the world.

Where is the guarantee for all mentioned above? Rather than any other aspects, it mainly lies in the advantage of Chinese market economic system and mechanism. Different from western one, the Chinese economic system has Chinese characteristics, namely the socialist market economic system.

IV. Features and Advantages of Chinese Socialist Market Economic System

The Chinese socialist market economic system is as same as the western one in the flowing aspects: bring the market role on resources allocation into active play, force the economic activities to abide by the requirements of value rule, adapt to the change of relation between supply and demand, pass the function of price leverage and competitive mechanism, realize the effect of selecting superiors and discarding bad ones, but they have a principle distinction in fundamentals. The characteristics of Chinese socialist market

economic system are mainly shown in the following:

1. The Chinese socialist market economic system is combined with socialist fundamental economic regime. That is to say, it is established on the basis that takes the public ownership as the dominate part and seeks the joint development of diversified forms of ownership. Up to 2005, although the number of the state-owned and state-owned holding enterprises in China accounted for only 11% of the total number of nationwide industrial enterprises, the gained profits and tax payments respectively accounted for 44.9% and 56.7%. In 2005, the tax payment of national enterprises accounted for nearly 1/5 of the national tax revenue.

The state-owned economy not only has a certain share in quantity, but the most important point is that it has occupied all the key departments in relation to the national economy and the people's livelihood, such as railway, mining, banking, aviation and high-tech fields. It is obvious that the state-owned economy controls the life lines of Chinese national economy.

The whole public economy, the state-owned economy plus the collective one, has dominated in the Chinese national economy.

2. The Chinese socialist market economic system is a kind of economic pattern that regards national macro-control as the precondition, and combines macro-control with market allocation. It is pointed out on the 14th National People's Congress of the Communist Party of China: "The socialist market economic system we are going to establish is a kind of economic system enabling the market to serve as the basic means of regulating the allocation of resources under the macro-control of socialist state." Such system is obviously of "power-power association and complementary advantages", combining the government advantages with the market ones under the common goal of accelerating a harmonious and rapid growth of economy. It may compensate not only the defects of market failure, but also the defects of ineffective government activities. For example, facing the impact of world financial crisis, in order to compensate the deficiency of market regulation, the central government launched decidedly ten measures to expand domestic demand and spur economic growth on Nov. 5th 2008, totally RMB 4 trillion will be invested by the end of 2010, where the central government will invest RMB 1180 billion. At the beginning of 2009, the central government launched and requested to carefully implement the adjustment and revival programs for key industries including automobile, steel, shipbuilding, petrochemical, light industry, textile, non-ferrous metals, equipment manufacturing, electronic information, modern logistics and so on. " The implementation of adjustment and revival programs for ten major industrial fields will effectively ease the impact of world financial crisis, and effectively solve those deep-rooted conflicts existed in domestic industries, such as excessive productive capacity, low degree of industrial

concentration, lack of core and key technologies, weak market competitiveness etc.

It is proven above that the socialist market economic system has the advantages of combining “invisible hands” with “visible hands” and effectively adjusting and controlling the operation and development of economy.

3. The Chinese socialist market economic system takes the effective solution of social major conflict between increasing demand of people on material and culture and the out-of-date social production as its task. Influenced by the neoliberalism, the development of market economy in western countries is free, autonomous and without definite objectives, which inevitably has a high degree of blindness. While the Chinese market economy develops in a different way, it spurs the economic and social development through solving those major conflicts revealed in the process of such development. The major social conflict existing at the primary stage of socialism is “the conflict between increasing demand of people on material and culture and the out-of-date social production”, while expanding market economy is the basic means to solve this conflict. The solution of this conflict will lead to building up an overall well-off society, realizing modernization in China and completing the historical task of the primary stage of socialism.

The features of socialist market economic system mentioned above also enable it great advantages:

First, the socialist market economy is a kind of market economy that pays attention to equity. Under the condition that takes the public ownership as the dominated part and regards the performance-based distribution as the main form of distribution, the society pays attention to the efficiency, but pays more attention to the equity. In the case of serious polarization, the government shall adjust it by consciousness. For example, the *2009 Program for Chinese National Economy and Social Development* highlights to “intensify the improvement of people’s livelihood, concentrate on solving hot and difficult problems related to the people’s interests, and implement a more energetic employment policy”. In particular, a financial fund amounting to RMB 43 billion was specially arranged to help with poor householders.

Second, the socialist market economic system benefits to bring the leading effects of government into play.

Different from those western countries following the neoliberalism, the government of socialist countries has a function of organizing the development of economic society. Under the circumstance of market economy, though the market could play a fundamental role in resources allocation, the government still take non-replaceable leading effects in formulating development program, industrial policy, distributive policy, regional policy, financial policy, monetary policy and foreign trade and economic policy etc. besides directly control the life lines of national economy. Especially, the Chinese government has

a real power in disposing and dispatching financial resources, which is decisive to regulate and control the overall situation of national economy's operation and development.

Third, the socialist market economy is running and developing under a planned regulation and control.

It appears to those neo-libertarians that under the condition of market economy, the planned operation and development of national economy seem inconceivable and harmful. The word "planning" is nearly a derogatory term for them. Certainly it is incorrect. In the opinion of Marxism, the planned development of national economy is an inherent demand of large-scale socialized production, which is not only necessary but also practical. The planned development of national economy is a kind of demonstration of social advancement and civilization. However, limited to the development level of social economy, the developed degree of science and technology, and the capability of management, the requirements for a real planned economy cannot be reached. Nevertheless, since the socialist market economy has the aforesaid features and advantages, the Chinese socialist market economy may execute a planned regulation and control in the goal of development, rate of growth, economics of scale, keystones of strategy, balance of regions and improvement of the people's livelihood etc., also the practice of the Chinese economic expansion has proved its feasibility and advantages.

As has been said, it can be confirmed that the socialist market economic system is a kind of new economic system that takes the public ownership as the main form and the joint development of diversified forms of ownership as the basis, combines macro-control and regulation by the state and resources allocation by the market, and regards the solution of social major conflict between increasing demand of people on material and culture and the out-of-date social production as its target. This system has advantages like equity, controllability and government dominated etc. Gathering all these features and advantages, it appears that the socialist market economy is a kind of economy without inherent crisis. It possesses not only the inherent capability to resist crisis, but also the internal power to maintain a steady and fast growth. It is the best evidence that nowadays the Chinese economy could grow steadily and fast even under the impact of world financial impact. Though the growth of Chinese economy is currently shown a downslide, as well as jobless workers and so on, it is a result of the transmission of foreign economic crisis rather than a product of conflicts inherent to the Chinese economy.

It is observed that the socialist market economic system that has just set up is not perfect enough, which can not only be found in the insufficient and unskilled exercise of market system, but also in the insufficient understanding and exertion of the advantages of socialist system. However, we believe that through further optimization, the socialist market economic system, especially after the practice of withstand financial storm, will become more mature and advanced, and the capability of which for crisis will become much stronger.

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