

## China's Quiet Property Rights Revolution

by Douglas Wu

Privatization” is still a taboo word in the official Chinese media, but the emergence of a growing private sector has been one of the most dramatic phenomena in China since Deng Xiaoping instituted his economic reform two decades ago.

As more of China's state-owned enterprises become insolvent under pressure of increasing market competition, the private sector is becoming more important than ever before; it is providing goods and services, creating jobs, and generating government revenues. There is widespread consensus among economists in China and abroad that this process will continue, and that not even the Chinese Communist Party can reverse it.

The key to China's changing economy is the privatization that has been unfolding in the rural areas, partly because privatization originated in the countryside and partly because the problems associated with rural privatization are some of the greatest challenges that Chinese leaders face.

### Background: 1949 to 1966

Before the Communists took power in 1949, China was basically an agricultural society in which farmland was owned by the rich. The sale and purchase of farmland were permitted and protected by the Nationalist government, which was in power from 1911 to 1949. The land reform of 1949–51 deprived the landowners of their land and distributed it among the peasants—tenants who had little or no land of their own. At the same time, the landowners were politically ruined: they were declared to be the lowest social class in China; they

*Douglas Wu, a senior contract administrator for Globecomm Systems Inc., is a native Chinese who worked for a major Chinese financial institution for 16 years.*



Asian television stations film a press conference with Hong Kong central banker Joseph Yam and Richard Y. C. Wong, director of the Hong Kong Center for Economic Research, which cosponsored with Cato the conference “Globalization, the WTO, and Capital Flows: Hong Kong's Legacy, China's Future,” on September 4. (See page 3.)

lost all their political rights and were treated like prisoners on probation. The new regime intended thus to secure the support of peasants and to legitimize its ruthless crushing of any opposition.

That not only gave peasants land but also enhanced their social status. Before long, however, their euphoria was replaced by the new concern that some of them were becoming rich while others remained poor or became even poorer. Obsessed with the traditional Chinese belief that inequality was worse than destitution and convinced by Marxist doctrine that private ownership of the means of production was the root of all social evils, the government under Mao Ze-dong did away with land reform by forcing Chinese peasants to organize themselves into millions of production units (known as collectives) and to pool their land and other significant means of production. Every member of a collective became a part owner of the pool and as such was entitled to a share of the collective's harvests.

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## “Being a part owner of a collective didn’t arouse much enthusiasm in practical Chinese peasants, whose dream had always been to farm a piece of land they could call their own.”

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Under the new arrangement, individual peasants no longer possessed any means of production, and no collective member could do anything about his or her share of the pool, which was indivisible.

In the urban areas the Communist government assigned a job to every adult who was able to work and provided workers with all job-related benefits: salary, medical care, housing, and a pension at government-stipulated rates. But China was very poor and had a rural population of nearly 500 million, so the government assumed no such responsibility in the rural areas. To stick to its principle of “no private ownership of means of production” and to be realistic, the government threw the burden onto collectives and made it an unwritten law that each infant born to a member of a collective automatically became a member of the collective entitled to the benefits that the collective would provide. Whether the collective was able to provide any benefit at all, however, would depend on such factors as natural endowments, climate, and the efforts of the collective members.

By unwritten law, the government was not the owner of the collective and, therefore, had nothing to do with maintaining the income level of collective members. The government might reduce agricultural taxes to avoid starvation, but nothing more was to be expected in most cases.

Mao was pleased with the new arrangement, which some of his followers extolled as his “great contribution to the Marxist theory of public ownership.” According to orthodox Marxism, to eliminate private ownership of the means of production, the state must take responsibility for organizing production and looking after all the workers. Under the new arrangement, private ownership of the means of production was effectively eliminated, but the government had no direct responsibility for either production or peasants’ welfare.

Contrary to government propaganda, the new arrangement was unpopular in the countryside from day one. Being a part owner of a collective didn’t arouse much enthusiasm in practical Chinese peas-

ants, whose dream had always been to farm a piece of land they could call their own. The peasants also felt that the new arrangement had rendered them inferior to urban residents, whose welfare was provided for under the government budget while theirs was at the mercy of the weather or the quality of the land.

Nevertheless, the peasants did not offer any open opposition to the new arrangement. What they did instead, because every collective member got more or less the same share of the harvests, regardless of differences in individual contributions, was to shirk and to be very careful to do no more than others did. Consequently, agricultural productivity was low and the resultant food shortages haunted the government.

The government tried to inject a spirit of collectivism into the peasants’ minds, without much success. To diminish the threat that starving peasants might rebel—almost the exclusive cause of political upheavals in China’s 5,000-year history—the government reluctantly agreed that a small piece of the collective land could be used by each farming household to plant crops of its own choice and that the harvest from that land could be retained by the household. (Those small pieces of land became known as private reserved land.)

To justify its policy change, the government emphasized that the private land could not be more than a small fraction of the collective land and that peasants should not be allowed to farm their private land until they had finished their daily work for the collective. Despite those restrictions, the new policy brought wealth and life to China’s countryside. The enthusiasm with which Chinese peasants worked their private land and the resultant high productivity were in such sharp contrast with what was happening on the collective land that the official Chinese media frequently complained that, “if we fail to do a good job of educating peasants properly so as to free them from selfishness and narrow-mindedness, capitalism will prevail in China.”

Although the private reserved land policy saved Chinese peasants from starvation after 1963, most of the country’s farmland was still in collective hands, and the time peasants were permitted to work on their

private land was very limited. Meanwhile, the government’s persistent efforts to re-educate peasants failed to show positive results. Consequently, the low productivity of the agricultural sector remained a big headache for the government at a time when the population was doubling. There seemed never to be enough to eat, so food had to be rationed again and again in urban areas. Despite the fact that people had been working hard under Communist rule for nearly 30 years, their standard of living had not improved much.

At last, complaints against the government policy were voiced, disenchantment with Mao’s ideology grew, and people began to dream of better lives, not just empty promises. Mao perceived all such developments as evidence that some of his fellow Communist leaders were trying to undo his accomplishments. He couldn’t tolerate such subversive efforts. The Cultural Revolution was instituted in 1966 with a view to sweeping away all that was in Mao’s way.

### **Cultural Revolution and Economic Reform**

The Cultural Revolution dominated China for 10 years, during which millions of

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## “Deng and his followers were pretty sure that Chinese peasants would be able to create economic wonders if and only if they were given back what had belonged to them and allowed to farm their own land.”

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Chinese families were plunged into tragedy and the economy was pushed to the verge of collapse. The actual effects of that catastrophe were to tear to pieces Mao's mystique (which had been the pillar of his rule), to expose fully the fatal diseases inherent in China's Soviet-style social and economic structures, and to lead the Chinese to seek different solutions to their problems.

Mao's death in 1976 presented China with a chance to break with its past. The Chinese elite led by Deng seized that chance, terminated the Cultural Revolution immediately, and after about a year launched “economic reform,” the original aim of which was to raise the people's living standards by liberating the economy from the fetters of the Soviet model and by introducing market mechanisms to solve some of China's economic problems.

The economic reform started in the countryside, the chronic low productivity of which made it increasingly difficult for China to feed its 1 billion people. Thanks to the experience with the private reserved land, Deng and his followers were pretty sure that Chinese peasants would be able to create economic wonders if and only if they were given back what had belonged to them and allowed to farm their own land. The leaders knew that the reform would not cause any loss to or require any new investments from the government, as the government was not the owner of the collectives. The solution was simple and straightforward. But before anything could be done to implement it, the reformists, while insisting that the system of collective land ownership was not being dismantled, had to develop a “socialist” theory by which peasants could effectively reclaim their land. In the years right after the Cultural Revolution, although most people were convinced of the inefficiency of the state sector, their support for “socialist” ideals was not diminished. Their fear of private ownership was deep-rooted. Without justification by a theory that sounded definitely “socialist,” any reform would be viewed as an attempt to deviate from the right path and thus could not succeed.

Fortunately, there existed in the West the practice of leasing, which the reformists found readily usable. They lost no time in transforming it into a set of policies (later known as the household responsibility system) aimed at launching the Chinese countryside into a new production system that would solve the problem of food shortage once and for all. Under the household responsibility system,

- the collective remained the owner of the collective land and other means of production used by collective members; therefore, the system was still “socialist”;
- if so desired by collective members, however, the collective land and other means of production could be leased to any household in the collective;
- the quantity of the object to be leased to each household could not exceed the quantity that the lessee had contributed to the collective at the time of its formation almost 30 years earlier;
- the terms of leases might be as long as 50 years;
- during the term of a lease, the lessee did not need to pay any rent to the collective but had to pay taxes to the government in proportion to the quantity of the object leased; and
- the object so leased could be re-leased among collective members during the term of the original lease, subject to the consent of the collective.

The household responsibility system spread through the countryside almost overnight. The peasants seized their chance with such vigor that soon all the collective belongings fell into private hands and the collectives existed in name only. That unexpected development embarrassed the reformists for a while but was soon forgotten because “economic wonders” were appearing in the countryside. Virtually free from any interference from either the collective or the government, the Chinese peasants devoted their hearts and souls to the land under their control and made every effort to provide whatever consumers were demanding. Very soon, bumper harvests

led to flourishing peasants' markets, where nearly every kind of food that can be grown in China was in abundant supply. Food shortage became a problem of the past, and the government found itself called upon to address a new issue: food oversupply.

The whole nation benefited so much from what the peasants were doing that the virtual disappearance of the collectives aroused little political opposition. Deng drew some important insights from that. In later years, whenever he intended to introduce a new “reform policy” that might give rise to a new ideological battle in the Communist Party, Deng would launch the policy first and let it become popular with ordinary folks before his opponents could block the policy.

With increasing productivity, greater purchasing power, and accumulated capital, some of the peasants gave up farming and started their own industrial enterprises (known as township enterprises). By the early 1980s, thanks to the success of the economic reform, the official attitude toward private ownership of the means of production had changed substantially. As a result, the township enterprises were granted formal status as part of a legitimate private sector, the existence and growth of which, according to the official line, are not ideal but are necessary to the country's efforts to “lift itself to a higher level of a truly socialist society.”

The past two decades have seen great changes in China's countryside: virtually all means of production have been shifted from the state to the private sector, and efficient markets for agricultural products and equipment have been created. Given that some 80 percent of China's population live in the rural areas, nearly all the rural economy is effectively in private hands, and most of the working adults in the countryside are employed by the private sector, it is difficult to accept the official claim that “socialism” is still dominating China's countryside.

Under the household responsibility system, peasants were permitted to re-lease their land to others. As a result, a market for farmland has been in active operation since the early 1980s. However, it is a market for which the government has failed to

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provide any clear guidance. More often than not, there is no written contract for land re-leasing. Even if there is one, it is not legally enforceable, because, in accordance with the official rule, any land re-leasing must have the prior consent of the collective, which is long gone in most cases. Nevertheless, the government is unwilling to officially admit this fact, as such admission would be equivalent to saying that China’s countryside is no longer “socialist.” However, the government has neither the intention nor the resources to change the status quo, so peasants are the de facto owners of the land under their control and, as such, are buying and selling land as they wish. One can anticipate that the peasants will feel frustrated when they have problems involving their re-released land and cannot go to the government for justice.

### The Present Challenge

Although the Chinese government has been fully convinced of the effectiveness of privatization in solving the country’s economic problems and has implemented privatization bit by bit whenever politically feasible, it still has great difficulties in officially accepting it. There are two main reasons for this dilemma. First, nobody doubts that China has gone a long way in transforming itself into a market economy. But people still fear the social conflict that Karl Marx warned would be the result of private ownership of the means of production. Under such circumstances, any open advocacy of privatization is likely to be very unpopular with the majority of the population until they have been fully convinced in theory that Marx’s analysis is outdated and that privatization, if properly structured and implemented, can bring economic benefits to most people without causing social conflict.

The second (and perhaps more important) reason is that, if the government lifted the taboo on privatization now, it might well encourage people to demand an end to the one-party system, which is far easier than privatization to justify under orthodox Marxist theory. So, any official pronouncement about privatization would be likely to lead to a review of the mandate to rule, something the Chinese leaders are

not yet ready to face.

What has happened in China’s countryside during the past two decades can be characterized as de facto privatization, in the sense that the process has resulted in virtually all of the means of production of the agricultural sector being transferred to private hands.

At the same time, it is definitely different from the privatization we have seen in other countries. Although the transfer has involved nearly 1 billion people, it has not caused any changes in the government’s financial accounts. (Under the new arrange-

ment, the government did not acquire either the collectives or any of their property. As a result, when the peasants reclaimed what had belonged to them, the government did not lose anything.) Indeed, privatization cost the government nothing and brought it large tax revenues.

The Chinese peasants still have a long way to go before they have proper legislation and institutions for protecting their legitimate property rights. Nevertheless, what has taken place in China’s countryside is one of the largest and most successful privatizations the world has witnessed. ■

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