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Preliminary

**Ex Ante Determinants of Regime Transition:  
China, Vietnam, and Russia Compared**

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**1. Introduction**

Recently, I have been engaged in a study to explore the theme above, as one of the presently urgent tasks of international development policy. I consider the study useful at least to a certain extent for thinking about the experiences of Japan and East Asia's development in terms of the relevance to the studies of contemporary development issues, and about the role of regional study approach thereto.

Fig.1 (1) indicates broadly my idea which I have been holding in my study to explore the actual, ex ante processes of a specific socio-economic system transforming itself to another. It is shown as a causality map and in a stylized fashion: First, when a developing country of a specific economic regime encounters, after many years, the accumulation of economic issues to the extent that the economy cannot be sustained on the basis of the same regime ("institutional fatigue"), the leaders or the main group of people of the county are motivated to change the regime (Emergence of a change trigger). At this stage, however, it is unclear for them to foresee what are the final goal and the process to reach it (*a scenario of regime transition*), as a result of the efforts at these changes. Second, in these efforts, the government tasks to rely on exogenous models for regime transition as a guidance of exploration, and in order to ascertain their relevance, it also studies the socio-economic conditions of the own country (koku-jo). Third, the interaction between the exogenous model and koku-jo is repeated, to result in a trials and errors process for either a longer or a shorter period. A final outcome is the advent of the effective scenario for a new regime. Fourth, the implementation of this scenario may further produce a new series of economic issues, but they should be dealt with as second-generation issues.

One of these stylized causal relations, I bring out four links and name them, for convenience, as determinants: (1)Economic issues (trigger), (2) exogenous models, (3)Koku-jo and (4) scenario.

In Fig. 1 (2) is shown the ex post determinants of regime transition, which relate each other in the domain demonstrated in a quadrilateral. In the ordinary economic analysis, these determinants are used as variables. The variables with numbers ①~④ shown outside are

identical to those in Fig 1 (1), and thus indicate the relation between the ex ante and ex post determinants.

## 2. Concepts of regime transition and development

As preliminaries, these concepts might be discussed:

Fig. 2 illustrates one aspect of the concept: regime transition. It indicates that the transition of the economic regime from the centralized planning to the market economy takes place side by side with the changes in the instruments by which of the national income flow are realized in “three dimensions”: i.e. from the planners’ directives derived from physical planning to the decentralized markets. Numerical magnitudes of this change is shown in Tables 1 and 2 only in the dimension of income distributed: i.e. the shares of enterprise income and GDP among government, enterprises and private households that changed between 1978 (9) and 1988 (9) toward favouring the households (or workers).

Characteristics arising from the fact that the above transition is taking place in developing economies can be illustrated in a few ways. One: as Fig. 3 describes, the interrelationship between the government authorities and various economic entities in the national economy on the one hand, and the interrelationship among these economic entities themselves, on the other, were governed not only by the market-oriented one, but even after a series of reforms by the nonmarket, customary (and after even predatory) relations. Two: In the 1980s and early 90s, the economies of China and Vietnam were, although nominally designated as centrally planned, in fact comprising vast unplanned sectors. In China, I interpreted on the basis of my reviews of various survey reports that there were three broad sectors: (1) centrally planned (on the basis of “material-balancing method”), (2) nonplanned but regulated (by the party network) and (3) nonplanned and non-regulated (under ad hoc relations with cadres).<sup>1</sup> In Vietnam, a Swedish research group observed the large “spontaneous” sector existing side by side with the sector under the centralized control.<sup>2</sup> Three: In Vietnam (as well as in Laos and Cambodia) there is a vast domain where foreign currencies and gold are used as effective means of exchange and store of values, as recently revealed by the research done by the Watanabe group.<sup>3</sup>

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<sup>1</sup> Shigeru Ishikawa, “Resource allocation control in China,” *Keizai Kenkyu* (Economic Research), 31-4, Oct. 1980 (in Japanese).

<sup>2</sup> Stefan de Vylder, and Adam Eforde, *Vietnam: an Economy in Transition*, Swedish International Development Authority, Stockholm 1988.

<sup>3</sup> State Bank of Vietnam and JICA, *Dollarization and its Effect on Monetary and Foreign Exchange Rate Policy and the Development of Financial System in Vietnam, Lao PDR and Cambodia*, (Joint Research Project Workshop), July 5 2002, Hanoi.

### 3. Four ex ante determinants: China and Vietnam

#### (1) Economic issues (Triggers for transition)

These issues were described in policy decisions in the important party meetings of the two countries: China in 11-3 Central Committee Plenum, Nov. 1978 (Table 5 (1)), and in Vietnam in the 6th Party Congress, Dec. 1986 (Table 3). It is important to note that both these decisions by no means made clear their aim at transforming themselves from the planned regime to the market economy regime: No image of the scenario in our sense was not yet appearing. The issues in their mind were “economic crises” to be tided over urgently. The decisions stressed, rather the needs for restrengthening thereby “socialist reconstruction”.

The economic crises related in both countries to the immediate and forthcoming food shortages and fiscal (and international balance of account, too, in the Vietnam case) difficulties, but differed in their causes. In China, economic turmoil brought about by Cultural Revolution (1966-1969) and the disruption of economic management even under the planned economy by the so-called Gang of the Four. In Vietnam, the war against the U.S., the ensuing military expedition to Cambodia and the war against China caused large amount of financial expenditures. Entire national investment and even part of national consumption were financed by economic aid from the Soviet Union as well as COMMECON countries. But the amount of the aid came to diminish rapidly (Fig. 3).

Behind these immediate causes, there were in both countries longer-term difficulties caused by inefficient, bureaucratic management of the planned economy. The market economy and productive force formation were also in the primitive stage of development (Fig. 4).

#### (2) Exogenous models

There are two significant models commonly in China and Vietnam: one, the Comintern and Soviet models of socialist development and two, the World Bank (and IMF) model for marketization of the diligiste economy.

The Comintern model here refers to its These that the socialist revolution in the colonies (most post-WWII developing countries) should be preceded by the capitalist development, as their productivities were yet very primitive. This model applied to pre-WWII China resulting in a Mao Tzetung’s strategy of New Democracy. After accomplishment in Soviet Russia of rapid industrialization under the centralized, bureaucratic planning regime, it became the model to be applied to the socialist-oriented developing country. The concept of “Transition period” before the stage of socialism reaching the stage of Communism came to be stressed, side by side. After Stalin’s death (1953), the research for new regime of new economic management was becoming increasingly intense in the Eastern European countries, in particular, in Yugoslavia and Hungary. In Russia, it was only slow, but in 1965 there was Premier Kosygin’s reform of introducing profit and sales’ amount target in planning; in 1987

in Premier Gorbachev's Perestroika, the concept of "Commodity production and economy" (hence, "product market") was officially made acceptable, but not the concepts of the markets for the factors of production, in particular, for labor and capital. The concept of full-fledged market economy was allowed only in 1991 by Premier Yeltsin.

Because of the ideological collision with Russia and of Deng Xiaoping's pragmatism, China did not care about the Russian models officially. But in fact they cared about them after the 1980s, as shown shortly. In Vietnam, the Russian models have been taken seriously, but the difference between the transitional centralized model and the more recent reformist model in Russia introduced into the political leaders the policy-oriented conflicts between the conservative and reformist groups. The 6th Party Congress's decision (on the well-known Doi Moi Line) was said to be the compromise product between the two, although it officially admit the concept of "Commodity Economy" under the support of Premier Gorbachev.<sup>4</sup>

The World Bank model is well-known. I have only shown Table 4, which indicates the places of the World Bank's marketization model under the name of SAL conditionality and the PRSP where the first priority goal of aid has been shifted from growth promotion to poverty reduction.<sup>5</sup> For China, the model did not play a significant role as conditionality. China's international balance of payment performed well, so that it need not request SAL. But Chinese government seems to have received significant but...friendly assistance for learning how to introduce and manage the market-oriented economy. The relationship between the Chinese leaders (in particular Premier Zhao Ziyang) and the World Bank resident mission in China (in particular Edwin Lim) was also intimate and flexible until the end of the Zhao period. For Vietnam, the World Bank first (1989-92) reported to have maintained active dialogues with it. Between 1994 and 97 it provided SAC (Structural Adjustment Credit) to Vietnam; the negotiations for SAC 11 started in 1998 but not been finalized until 2001. It appeared that as Vietnam government became familiarized more and more to new economic management, the conditionality imposed upon them came to become unhappy.<sup>6</sup>

### (3) Scenario of the regime transition

As for determinants (3) and (4), the order of presentation is reversed for its convenience of easier description: This sub-section will describe what are the scenario finally identified and why it is considered the final one; then, in the next sub-section the process of "trials and errors" in which that scenario is reached after the repeated interactions between the exogenous models and studied Koku-jo.

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<sup>4</sup> Motoo Furuta, "Inner-Party Controversy in the period of Formation of Doi Moi Line," in M. Shiraishi and I. Takeuchi eds., *New Development of Doi Moi Line in Vietnam*, IDE, 1999.

<sup>5</sup> S. Ishikawa, "Growth Promotion versus Poverty Reduction: World Bank Rethinking of Aid Policy and Implications for Developing Countries," *GRIPS Discussion Papers*, No.3, August 2002.

<sup>6</sup> S. Ishikawa (1999), source of Table 3.

The scenario thus identified is shown for China in the Decision on the “Socialist Market Economy” of the 14-3 Central Committee Plenum in November 1993 (Table 5 (1)). (To this Table is added the decision on “Socialist Commodity Economy” of the 12-3 C. C. Plenum in October 1984, which was considered as the mid-point landmark of the trials and errors process toward the 1993 decision (Table 5 (2)), as well as the Communiqué of the 11-3 C. C. Plenum in December 1978. The latter constituted, as discussed earlier, the regime transition “trigger” (Table 5 (3)).

In connection with the Russian models, the 1978 decision only expressed the leader’s desire to get out of the traditional, centralized physical planning model; the 1984 decision was the decision to introduce the product market, but not the factor markets. Therefore, the resources are not allowed to be allocated beyond the boundary of each individual enterprise, but only inside each individual enterprise. The 1993 decision finally allowed the resource allocation even among the enterprises. On the other hand, the 1993 reform seems to have included most items in the marketization agenda of the World Bank model. However, for most of the period in the 1980s, the World Bank did not have the self-confidence on the applicability of its own SAL model to China which was under very different initial conditions from other developing countries.<sup>7</sup>

As for Vietnam, the final scenario seems to have been identified in the decision of the 9th Party Congress (June 2001), and as a much cruder form, already in the decision of the 8th Party Congress (June 1996) as shown in Table 6. This decision compares to the Chinese decision in 1993 in that the market economy is allowed in the factor markets as well, although it emphasizes that the labor and capital markets are yet nonexistent or primitive.<sup>8</sup> The Vietnam scenario appears to have been influenced at least in the form of presentation, as shown in Table 5.

Next, I have to make explicit some of the conditions to be judged as having been met when we evaluate that the above scenario is finalized. The trials and errors process in the next sub-section is in fact the one through which these conditions were sought after.

- a) Ideological admittance of both the product markets and the labour and capital markets.
- b) Identification of the steps to raise and foster each of the product and factor markets, as well as the full-fledged enterprises.
- c) Capacity-building for bringing about stability and development of the macro-economy, including the establishment and operation of the national and local governments’ fiscal system and the banking and other financial architecture.
- d) Articulation of the industrial policy in necessary details: agriculture, vital branches of

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<sup>7</sup> World Bank, *China: Long-term Development Issues and Options*, The Johns Hopkins Univ. Press 1985, Summary and Conclusions, esp. pp. 13-16.

<sup>8</sup> Communist Party of Vietnam, *9th national Congress Documents*, the GIOI Publishers, Hanoi, 2001, p. 44.

manufacturing and other industry and infrastructure included.

- e) Conditions relating to “globalization”.
- f) Establishment of social service sectors.
- g) Administrative modernization

##### 5. Koku-jo and the trials and errors process

This process of trials and errors was a long and difficult one for China; it took altogether fifteen years finally to arrive at the point of identifying the effective scenario. There were no exogenous model that fitted fairly well to the initial conditions similar to China and which was also considered useful to rely on in confronting at least some issues arising in China. In Vietnam, the process was shorter: 10 to 15 years. As compared to China, timing of the “trigger year” was nearly ten years later; hence more potential exogenous models were available. And, China's reform effort itself also played a role of one of the models, as between China and Vietnam, there were many similarities in the initial conditions and issues.

It is for these reasons that the cases of trials and errors are many in China, relating almost all items to the above conditions. In these cases, the policies and measures, which constituted the components of the final scenario were made available only by way of such trials and errors. I can indicate only one exceptional case to those with certainty - that is relating to item (e), namely the decisions to establish Special Economic Zones in the provinces of Southern China as early as 1978 and 79. They were followed in later years by a series of outward-looking policies for foreign trade and FDI. However, for Vietnam, the cases were a few in number and mostly implicit. It is possible for me by now only to show a few cases.

With regard to the cases for China, I would only refer to those which I was able to detect in my review studies in the 1980s and in which the government attempted to introduce the market simply by means of issuing laws and regulations but could not attain success (Table 7). They cover many cases in agriculture and modern urban industries, which emerged in the earlier stages of trials and errors when the government did not yet recognize that the effective market economy required not only the regular market exchange rules, but also the rules prohibiting opportunistic and unlawful activities of the participants. It required even what is now well-known under the name of “social capital”. It must also accompany the accumulation of productive forces to the extent that is suitable to the intended level of the market development.

As for Vietnam, probably the most explicit case of trials and errors is that related to the above referred controversies that occurred in 1985 and 86 between the conservative and reformist groups within the party leadership. The former group argued that the product market liberalization would allow the private merchants dominate the commodity circulation thus

destroying socialist construction, whereas the latter considered that the bureaucratic, and subsidy-based planning economy would suppress the productive forces and thus aggravate the economic crises further. The Doi Moi strategy was a product of compromise between the two. The cases of trials and errors can be detected in the areas of rural credit cooperation and private joint-stock banks, as well.

#### 6. Russian experience - Disastrous trials and errors

Finally, a few words on the Russian experience - which is in short the case of disastrous trials and errors:

Trigger: Breakup of Council of Mutual Economic Assistance and the Soviet Union (Dec. 1991). Crises of the macro-economy caused by large fiscal deficit, price spiral and rapidly diminishing industrial output in the first half of 1992. Starting from these events as background, President Yeltsin took up an Enhanced Economic Reform Program in June 1992, which followed fully the IMF program of a nearly complete set of liberalization, stabilization and privatisation.

Exogenous model: The IMF program was accepted in exchange for IMF's provision of US\$ 24 billion credit to Russia. "Western advisers marched in with their sure fire recipes for a quick transition to a market economy." (J. E. Stiglitz's words)

Scenario: Yeltsin's goal was seemingly the establishment of the market economy of the western capitalist countries, regardless of the answer to the question whether he took into consideration Russia's Koku-jo in order to modify that goal. The process toward it was indeed misconceived.

Trials and errors: most conspicuous indications of this process are the movement of CPI and GDP as shown in Fig.5.

(to be ended)