

# Multiscale and Multimechanisms of Regional Inequality in China: implications for regional policy

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*Research on regional inequality in China has generated controversial findings. This paper reveals that the trend for the last four and a half decades shows no clear divergent, convergent, or inverted-U patterns. I argue that regional inequality in China is sensitive to geographical scale and influenced by multiple mechanisms, and that the global and domestic contexts for China's regional development have changed dramatically. In particular, China's triple transitions—decentralization, marketization, and globalization—have fundamentally changed the mechanisms underlying regional development. Changes require new thinking on regional development strategies in China, which should emphasize developing non-state sectors, fully utilizing human resources, enhancing geographical targeting, and reforming urban and regional planning institutions.*

## Introduction

Regional development, especially regional inequality, is an important area of academic enquiry and government policy. However, scholars have long disagreed over the trends and underlying forces of regional inequality, and debated over regional policy.<sup>1</sup> More recently, scholars have examined the effects of institutional change, globalization, agglomeration, and technology on regional development.<sup>2</sup> Empirical evidence also tends to be mixed. While regional inequality has declined in some countries, it has persisted or even increased in others. Rapidly changing global and domestic conditions have further intensified the debate on regional inequality and policy.

Scholars have also heatedly debated whether regional inequality declined in

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1. See G. Myrdal, *Economic Theory and Under-developed Regions* (London: Gerald Duckworth, 1957); G. H. Borts and J. L. Stein, *Economic Growth in a Free Market* (New York: Columbia University Press, 1964); J. G. Williamson, 'Regional inequality and the process of national development', *Economic Development and Cultural Change* 13(2), (1965), pp. 3–83; J. Friedmann, *Regional Development Policy* (Boston: MIT Press, 1966); W. Alonso, 'Five bell shapes in development', *Papers, Regional Science Association* 45, (1980), pp. 5–16.

2. See, for example, P. Krugman, *Geography and Trade* (Cambridge: MIT Press, 1991); R. J. Barro and X. Sala-i-Martin, *Economic Growth* (New York: McGraw-Hill, 1995); R. Lee and J. Wills, eds, *Geographies of Economies* (New York: Arnold, 1997).

former socialist countries, and more recently, whether regional inequality has widened since economic reforms.<sup>3</sup> They are widely concerned that economic reforms may have intensified income and regional inequalities. This concern has had tremendous impact in these countries, as it highlights the battle over development paths and power struggles among decision-makers. Regional inequality is an issue that reformers and hard-liners often use to justify their political agendas. It is an issue that is intertwined with economic growth, social stability, ethnic relations, and political unity. Regional inequality is also related to broad debates over equity and efficiency, the state and the market, the global and the local, and the rich and the poor.

In this paper, I examine changing patterns and mechanisms of regional inequality and discuss future regional policy in China. I first provide an overview of China's changing development policies and patterns of regional inequality. This is followed by an analysis of the changing domestic and global contexts of China's regional development. Finally, I discuss the implications of these changes to China's regional policy.

## China's development path and regional inequality: an overview

Regional inequality has been an important issue in China since the establishment of the People's Republic of China (PRC) in 1949, due largely to its role in the debates over the nature of socialism, central control and local autonomy, and resource allocation among regions. Influenced by Marx's socialist ideology and egalitarian ideas, Mao, during the First Five-Year Plan (FYP) period (1953–57), attempted to develop the interior region. Regional allocation of resources has since become an important part of China's national planning. Scholars generally agree that some effort was made to develop economically lagging regions, but they disagree over the extent and consequence of the effects.<sup>4</sup> I have argued that regional inequality in fact persisted during Mao's era, due largely to historical legacy, uneven geographic distribution of resources, the emphasis on industrialization and national defense, decentralization and policy changes, and political and social unrest.<sup>5</sup> These findings contrast sharply with the socialist ideology of equality, and challenge previous views which tend to over-simplify the complex mechanisms underlying regional development in China.

3. See, for example, I. S. Koropeckyj, 'Equalization of regional development in Socialist countries', *Economic Development and Cultural Change* 21(1), (1972), pp. 68–86; R. J. Fuchs and G. J. Demko, 'Geographic inequality under socialism', *Annals of the Association of American Geographers* 69(2), (1979), pp. 304–318; G. L. Ozornoy, 'Some issues of regional inequality in the USSR under Gorbachev', *Regional Studies* 25(5), (1991), pp. 381–393.

4. There are many studies on regional inequality under Mao, see N. R. Lardy, *Economic Growth and Distribution in China* (Cambridge: Cambridge University Press, 1978); S. Paine, 'Spatial aspects of Chinese development', *Journal of Development Studies* 17(2), (1981), pp. 132–195; T. Cannon, 'Regions: spatial inequality and regional policy', in T. Cannon and A. Jenkins, eds, *The Geography of Contemporary China* (New York: Routledge, 1990), pp. 28–60; T. P. Lyons, 'Interprovincial disparities in China', *Economic Development and Cultural Change* 39(3), (1991), pp. 471–506; Y. H. Wei and L. J. C. Ma, 'Changing patterns of spatial inequality in China', *Third World Planning Review* 18(2), (1996), pp. 177–191.

5. Y. H. Wei, 'Regional inequality of industrial output in China, 1952 to 1990', *Geografiska Annaler* B80(1), (1998), pp. 1–15; Y. H. D. Wei, *Regional Development in China: States, Globalization, and Inequality* (London: Routledge, 2000).

Since the launch of reforms in the late 1970s, the central government has encouraged some regions to 'get rich first' and has emphasized coastal development, arguing that concentration and specialization are required for rapid growth and the diffusion from more developed regions would stimulate the prosperity of the whole country.<sup>6</sup> China's development policies during the 1980s and early 1990s, such as the open door policy and the coastal development strategy, favored and decentralized more decision-making power to some coastal areas.

Two decades of reforms have brought dramatic growth and change in China. However, China's reform process was marked by tensions between central and local governments, between plans and markets, and between the domestic and international political economies. Reforms have also been troubled by problems of corruption, dysfunctional state-owned enterprises (SOEs), rising income inequality, regional conflicts, and environmental degradation. Regional conflicts prompted many to consider regional inequality the root of China's regional problems and an important issue of government policy. The Ninth FYP (1996–2000) perceives polarization as a serious threat to China's prosperity, stability and unity, and places reducing regional inequality as a top policy priority. China's FYPs have never given such a high priority to regional inequality as the Ninth FYP does.<sup>7</sup>

Scholars once again disagree over whether regional inequality has intensified and what forces have contributed to the change of regional inequality in post-Mao China.<sup>8</sup> Some researchers maintain that economic reforms have stimulated the growth of coastal provinces and intensified regional inequality, while others argue that regional inequality has actually declined since the initiation of economic reforms, mainly due to diffusion, interregional resource transfer, and rural industrialization. The debate is also intense in Chinese literature.<sup>9</sup>

Four major findings can be summarized regarding regional inequality in China. First, regional inequality is sensitive to geographical scale, and multiscale seems an important feature of regional inequality in China. One major reason for the controversial findings of regional inequality is because of different geographical scales of observation and measurement. Interregional inequality across China's

6. State Council, *Zhonghua renmin gongheguo guomin jingji he shehui fazhan diqigewunian jihua 1986–1990* [The Seventh Five-Year Plan for National Economic and Social Developments in the People's Republic of China 1986–1990] (Beijing: People's Press, 1986).

7. Y. M. Wang *et al.*, eds, *Zhongguo quyu jingji zhengce yanjiu* [A Study of China's Regional Economic Policy] (Beijing: China Planning Press, 1998).

8. There also exist many studies on regional inequality in post-Mao China, see Lyons, 'Interprovincial disparities in China'; C. C. Fan, 'Of belts and ladders: state policy and uneven regional development in post-Mao China', *Annals of the Association of American Geographers* 85, (1995), pp. 421–449; X. B. Zhao, 'Spatial disparities and economic development in China, 1953–92', *Development and Change* 27, (1996), pp. 131–163; Wei and Ma, 'Changing patterns of spatial inequality in China'; D. L. Yang, *Beyond Beijing* (London: Routledge, 1997); J. Chen and B. M. Fleisher, 'Regional income inequality and economic growth in China', *Journal of Comparative Economics* 22, (1996), pp. 141–164; T. L. Jian, J. D. Sachs and A. M. Warner, 'Trends in regional inequality in China', *China Economic Review* 7(1), (1996), pp. 1–21; S. G. Wang and A. G. Hu, *The Political Economy of Uneven Development: The Case of China* (New York: M.E. Sharpe, 1999); Y. H. D. Wei, 'Regional inequality in China', *Progress in Human Geography* 23(1), (1999), pp. 48–58.

9. H. K. Wei, 'The change of regional income inequality in China', *Jingji yanjiu* [Economic Research] 4, (1992), pp. 61–65, 55; K. Z. Yang, *Maixiang kongjian yitihua* [Towards an Integrated Space] (Chengdu: Sichuan People's Press, 1993); D. D. Lu and V. Sit, eds, *Report on China's Regional Development, 1997* [1997 zhongguo quyu fazhan baogao] (Beijing: Commercial Affairs Press, 1997).

eastern, central, and western regions differs from interprovincial inequality. More specifically, interregional income inequality rose during both Mao's era and the reform period; interprovincial inequality, however, rose under Mao but declined during the reform period. Most theories of regional inequality are based on a highly simplified and conceptualized core-periphery structure. In empirical studies, scholars tend to measure regional inequality by using administrative units, which are the basis for statistics and government policy. This feature of measurement is inherent in regional inequality, but has not been carefully treated by scholars. In addition, different indicators and indexes of measurement can also lead to different findings.

Second, no single factor explains the change of regional inequality. Theoretical models, whether in neoclassical or neo-Marxist perspectives, often have strict assumptions, especially the free mobility of capital over space.<sup>10</sup> As I will elaborate in the next section, China in the reform period has experienced profound changes. While the role of the state is still important, the control and capacity of the central state have been declining. Meanwhile, as a consequence of global restructuring and China's economic reforms that emphasize decentralization, marketization, and globalization (open door policy), localities and global investors have emerged as important agents shaping uneven regional development in China. Therefore, foreign investors, the nation-state, and local forces all influence the process of regional development. Favorable state policy, concentration of foreign investment, and local factor endowments have contributed to the more rapid growth of coastal provinces, leading to the rise of interregional inequality. Meanwhile, traditional industrial bases, including Liaoning and to some extent the three centrally administrated municipalities (Shanghai, Beijing and Tianjin), recorded slower economic growth, especially during the 1980s. As a result, interprovincial inequality declined during the reform period. The notion of multimechanism captures the fundamental features of the Chinese transitional economy, and better explains the complexity of regional inequality in China.<sup>11</sup> Therefore, an investigation of the changing political economy, domestic and global contexts, and geography is necessary for a fuller understanding of regional inequality.

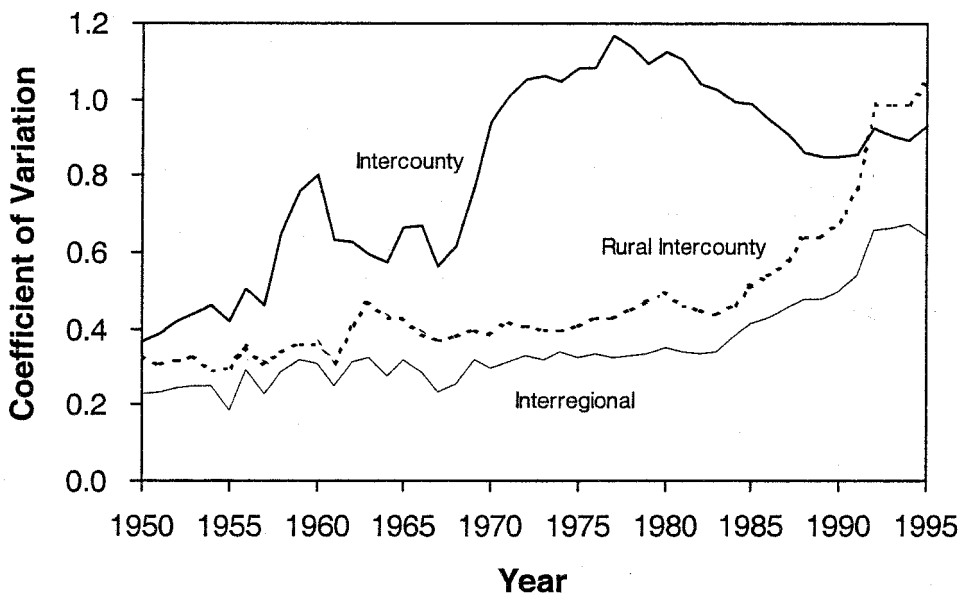
Third, regional inequality in China over the last five decades has not changed consistently, and shows no clear divergent, convergent, or inverted-U patterns. Corresponding to changing scales of observation and changing underlying mechanisms of regional inequality over time and space, patterns of regional inequality also change, rather than simply follow linear or cyclical paths. This irregularity is also consistent with empirical findings based on many other countries and regions. While theories of regional inequality tend to depict the patterns of change as convergent, divergent or cyclical patterns, the empirics of regional inequality, whether based on developed or developing countries, tend to show mixed patterns. Moreover, the short-term change of regional inequality, rather than the long-term change, is often more important to government policy and interregional relations.

Fourth, within a province, regional inequality also differs with geographical

10. Borts and Stein, *Economic Growth in a Free Market*; Williamson, 'Regional inequality and the process of national development'; N. Smith, *Uneven Development* (New York: Basil Blackwell, 1984).

11. Wei and Ma, 'Changing patterns of spatial inequality in China'; Wei, 'Regional inequality in China'.

scale. For example, while using a coefficient of variation of per capita gross value of industrial and agricultural output, Rozelle finds that rural intercounty inequality in Jiangsu increased between 1984 and 1989, but Fan, based on all county-level units, shows that intercounty inequality declined between 1982 and 1990.<sup>12</sup> Such difference is clearly related to different scales of observation, i.e. rural counties (counties and county-level cities) versus all county-level units (counties, county-level cities, and city districts). In fact, as Figure 1 shows, overall intercounty inequality (based on all county-level units) indeed declined during the post-Mao period, while rural intercounty inequality and interregional inequality across southern, central, and northern Jiangsu increased. These patterns of regional inequality in Jiangsu clearly point to the importance of geographic scale in the measurement of regional inequality. A further analysis reveals that the decline of intercounty inequality is very much related to the declining status of central cities which were favored by Mao's industrialization policy but have been growing slower than counties in Sunan. Moreover, the more rapid growth of Sunan's counties is not simply the result of central government policy, but also due to local efforts and factor endowments, and the infusion of foreign investment. Therefore, it can be argued that the interplay of three dominant forces—global forces, state policy, and local forces—is critical to the understanding of regional inequality in Jiangsu. In



**Figure 1.** Patterns of regional inequality in Jiangsu Province based on per capita gross value of industrial and agricultural output, 1950–1995. Comparable prices. *Source:* Jiangsu Statistical Bureau (JSB), *Jiangsu tongji nianjian* [*Jiangsu Statistics Yearbook*] (Beijing: Chinese Statistics Press, 1990–96); JSB, *Benxiang xiandaihua licheng* [*Pathways To Modernization*] (Nanjing: Jiangsu Statistical Bureau, 1994).

12. S. Rozelle, 'Rural industrialization and increasing inequality: emerging patterns in China's reforming economy', *Journal of Comparative Economics* 19, (1994), pp. 362–391; C. C. Fan, 'Development from above, below and outside', *Chinese Environment and Development* 6(1&2), (1995), pp. 85–116.

short, multiscale and multimechanism can also improve the understanding of the complexity of regional inequality within provinces in China.

The above analysis indicates that regional inequality is multifaceted and is more complicated than often assumed. While regional inequality may decline at one geographical scale, an analysis of alternative scales may reveal contradictory trends. Moreover, underlying forces of regional development also differ from country to country and from region to region. The issue of regional inequality is often intertwined with ethnic conflicts, trade disputes, migration, resource flow, and many other issues. Therefore, policies towards regional development and regional integration must consider the complexity of regions and the multiscale nature of regional inequality.

### **Changing mechanisms of regional development: China's triple transitions**

China's economic reforms have fundamentally changed the mechanisms underlying regional inequality. A burgeoning literature has attempted to explore the nature of economic transition in China. Oi conceptualizes China's economic transition as a process of decentralization, during which local states have taken control of economic development, giving rise to local state corporatism, while Nee's market transition theory emphasizes the infusion of market mechanisms as fundamental to the change of income distribution in rural China.<sup>13</sup> I synthesize that China's economic transition can be best understood as the triple processes of decentralization, marketization, and globalization. These triple transitions have fundamentally changed the mechanisms underlying regional development and policy in China.

Shortly after the founding of the PRC in 1949, China formulated a centralized system of finance, investment, and administration in order to take control over the economy and to launch the Soviet model of socialist industrialization. While during certain periods China decentralized its economic systems, Mao's system was essentially centralized. Post-Mao economic reforms have brought dramatic changes to the level of central control and the role of the state. Decentralization, in an attempt to reduce the central control of decision-making and to provide more incentives to regions, is an important part of reforms. Consequently, reforms have given local authorities considerable power in decision-making and resource allocation. Although the state remains important, the control and capacity of the central state have declined, which can be shown by an analysis of China's fiscal and investment systems.

During much of Mao's period, China's fiscal system was characterized by centralized revenue collection and interregional resource transfer, giving little autonomy to the regions.<sup>14</sup> Through the introduction of contracting systems, fiscal

13. J. C. Oi, 'Fiscal reform and the economic foundations of local state corporatism in China', *World Politics* 45(1), (1992), pp. 99–126; V. Nee, 'A theory of market transition', *American Sociological Review* 54, (1989), pp. 267–282.

14. For China's central–local fiscal relations, see, for example, D. S. G. Goodman, 'Political perspectives', in D. S. G. Goodman, ed., *China's Regional Development* (London: Routledge, 1989), pp. 20–37; M. Oksenberg and J. Tong, 'The evolution of central–provincial fiscal relations in China, 1971–1994: the formal system', *China Quarterly*

decentralization has reduced the fiscal control of the central government, and local governments have received greater power in revenue collection and local spending. Local revenue retention rates rose steadily in all of the provinces. The tax assignment system was implemented in 1994, and has more clearly specified fiscal responsibilities of the central and local governments. Viewing the reform period as a whole, fiscal reform has given regions much fiscal authority and incentives. Although the central government retains certain levels of fiscal control, fiscal reform has contributed to the increasing revenue shared by regions and the growth of local spending.

Investment reforms have increased the control of local governments over capital resources and financial institutions.<sup>15</sup> The project approval process has been largely decentralized to the local governments that are managing more investment projects than the center. The central government instead focuses on large-scale projects and priority sectors such as energy and infrastructure. For example, in 1997 the central government administered only 129 key-point (*zhongdian*) construction projects. Decentralization has also conveyed local governments considerable power in enterprise management. As a result, the central government is no longer monopolizing the investment allocation process, and local governments have used their increased power to mobilize resources for investing in more profitable sectors. Moreover, reforms have encouraged the use of multiple sources of capital for investment, such as private savings and foreign investment; most of these funds are beyond central control.

Local governments, especially township and village governments, are acting very much as entrepreneurs whose motives derive from a desire to maximize income and power. The interdependence between local governments and enterprises stimulates the bargaining effort of local governments who have actively initiated policies to stimulate local economic growth. However, the tension of central control and local autonomy has persisted in China, and waves of decentralization tend to be followed by attempts at recentralization by the central government. Moreover, decentralization alone does not characterize the process of China's economic reform; marketization is another major theme of reforms and has become especially important during the 1990s.

The relaxed state control and the growth of market mechanisms in economic development can be demonstrated in many aspects. Firstly, the control of state budget over the economy has declined, as evidenced by the decrease in the ratio

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Footnote 14 continued

125, (1991), pp. 1–32; C. P. W. Wong, 'Central–local relations in an era of fiscal decline: the paradox of fiscal decentralization in post-Mao China', *China Quarterly* 128, (1991), pp. 691–715; Y. H. Wei, 'Fiscal systems and uneven regional development in China, 1978–1991', *Geoforum* 27(3), (1996), pp. 329–344; A. Wedeman, 'Agency and fiscal dependence in central–provincial relations in China', *Journal of Contemporary China* 8(20), (1999), pp. 103–122.

15. The work on regional investment in China is very limited, see, however, B. Naughton, 'The third front', *China Quarterly* 155, (1988), pp. 351–386; Q. S. Zhou, 'Capital construction investment and its regional distribution in China', *International Journal of Urban and Regional Research* 17(2), (1993), pp. 159–177; Y. S. Huang, *Inflation and Investment Controls in China* (Cambridge: Cambridge University Press, 1996); L. J. C. Ma and Y. H. Wei, 'Determinants of state investment in China', *Tijdschrift voor Economische en Sociale Geografie [Journal of Economic and Social Geography]* 88(3), (1997), pp. 211–225; Y. H. D. Wei, 'Fiscal reforms, investment, and regional development in Jiangsu province', *Issues & Studies* 36(2), (2000), pp. 73–98.

**Table 1.** Sources of finance for fixed asset investment (%), 1981–95

Year	State budget	Domestic credits	Foreign investment	Enterprise funds	Other
1981	28.1	12.7	3.8		
1985	16.0	20.1	3.6		
1990	8.7	19.6	6.3	52.4	13.1
1995	3.1	21.0	11.5	53.2	13.8

Source: State Statistical Bureau, *Zhongguo tongji nianjian* [Statistical Yearbook of China] (Beijing: China Statistics Press, 1991, 1996).

of budget revenue to national income from 37.2% in 1978 to 21.8% in 1991.<sup>16</sup> The control over local expenditures has also been reduced, and enterprises and individuals have obtained considerable fiscal authority. Secondly, state control over investment has steadily declined, while proportions and absolute sizes of investment controlled by localities have increased. Budgetary investment as a percentage of total investment declined dramatically from 77.7% in 1978 to only 6.6% in 1995.<sup>17</sup> As shown in Table 1, state budgetary investment as a source of finance for fixed asset investment declined from 28.1% in 1981 to 3.1% in 1995. In 1997, enterprise funds and domestic credits provided 55.6 and 18.3% of fixed asset investment, respectively, followed by foreign investment (11%). These investments are controlled less by the central and local governments. Thirdly, price reform has dramatically reduced state control over prices. A two-track price system was created in the early and mid-1980s, but market prices have eventually taken control. From the late 1970s to 1994, the share of industrial output subject to the plan fell from 95 to 4%.<sup>18</sup> Lastly, shares of output and labor absorption by SOEs have

**Table 2.** Gross industrial output by ownership, 1952–95

Year	Volume (billion Yuan)				Proportion (%)			
	State	Collective	Individual	Other	State	Collective	Individual	Other
1952	14	1	7	12	41.2	2.9	20.6	35.3
1965	126	14	0	0	90.0	10.0	0	0
1978	329	95	0	0	77.6	22.4	0	0
1985	630	312	18	12	64.8	32.1	1.9	1.2
1990	1,306	852	129	105	54.6	35.6	5.4	4.4
1995								
China	3,122	3,362	1,182	1,523	34.0	36.6	12.9	16.6
Zhejiang	114	373	226	96	14.1	46.1	27.9	11.9
Jiangsu	250	709	52	170	21.1	60.0	4.4	14.4

Source: Same as Table 1.

16. Ministry of Finance, *Zhongguo caizheng tongji (1950–1991)* [China Finance Statistics (1950–1991)] (Beijing: Social Press, 1992).

17. State Statistical Bureau, *Zhongguo guding zichan touzi tongji nianjian 1950–1995* [Statistical Yearbook of Fixed Asset Investment in China] (Beijing: China Statistics Press, 1997).

18. J. H. Chen, ed., *1995 nian zhongguo guomin jingji he shehui fazhan baogao* [1995 China National Economic and Social Development Report] (Beijing: China Planning Press, 1995).



declined dramatically. As shown in Table 2, the share of output produced by SOEs declined from 77.6% in 1978 to 34% in 1995. Multiple forms of ownership have emerged in China, including state, collective, private/individual, share holding, foreign, and joint ownership forms. Non-state sectors have grown more rapidly and are exerting great influence on the Chinese economy.

The reform of China's planning system has been critical in the changing role of plan and markets. In the early and mid-1980s, Soviet-style mandatory planning was gradually discarded in favor of guidance planning to establish a planned socialist commodity economy. A two-track price system (state-fixed prices vs. market prices) was created to introduce the market mechanism gradually. In 1987, the policy was coined as 'the state regulates the market, and the market guides the enterprises'. This policy was changed in 1992 so as 'to develop socialist market economy'. Consequently, many bureaucratic coordination organs and vertical control instruments have been removed. The state has become more flexible, entrepreneurial, legalistic, and technocratic than its predecessor.<sup>19</sup> The state has been changing from one of planning and directing economic resources directly to one where the state manages the policies, which adjust the resources and markets. The state is exerting much less control over the economy than in Mao's era, and is no longer monopolizing economic development in China. Indeed, many scholars have been very concerned that the state has lost its control over the Chinese economy, but the process of China's economic reform is not simply removing state control; the state still actively initiates macro policies that are critical to economic and regional development. In addition, the processes of decentralization and marketization are accompanied by another process, the globalization of economic activities.

China has dramatically restructured Mao's policy of self-reliance and favored opening up its domestic economy to the outside world. To encourage foreign investment, the Joint Venture Law permitting foreign direct investment (FDI) in China was introduced in 1979, followed by the establishment of four special economic zones (SEZs) of Shenzhen, Zhuhai, Shantou, and Xiamen in 1980. Various state incentives were granted to the SEZs to attract FDI, such as tax and duty exemptions, flexible labor policies, and infrastructure improvement. China's open areas were extended consecutively from SEZs to 14 open coastal cities (OCCs) in 1984, and three delta areas (Zhujiang, Minjiang, and Changjiang deltas) in 1985 and 1986. A series of laws and incentive policies were introduced in the mid- and late-1980s to encourage foreign investment and trade. In 1988, Hainan Island was separated from Guangdong and was designated as China's largest special economic zone. In the early 1990s, the center emphasized opening up Shanghai's Pudong district. The government has gradually improved China's foreign relations, especially with investors from Taiwan, South Korea and Singapore.

Facilitated by globalization of capital, China's economic reforms and favorable

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19. J. Howell, 'The impact of the open door policy on the Chinese state', in G. White, ed., *The Chinese State in the Era of Economic Reform* (Armonk, NY: M.E. Sharpe, 1991), pp. 119–146; World Bank, *China: Reform and the Role of the Plan in the 1990s* (Washington, DC: World Bank, 1992).

investment conditions have attracted the interest of foreign investors. FDI in China increased dramatically from US\$4.4 billion in 1991 to US\$45.2 billion in 1997. Rapid economic growth, foreign investment, efforts of local governments, and ties to the international markets have also contributed to the growth of international trade. Export increased from US\$9.8 billion in 1978 to US\$183 billion in 1997, and in 1997 import reached US\$142 billion.

In much of the reform period, foreign investment was less significant. During the 1980s, FDI as a source of financing often accounted for less than 6% of fixed asset investment, such as 3.6% in 1985, but in the 1990s, foreign investment and trade have become important components of the Chinese economy. In 1995, FDI in China accounted for 11.5% of fixed asset investment, and the ratio of export to GDP was 21.5%. Although some restriction policies towards FDI were introduced in the mid- and late-1990s, China is much more integrated into the global economy. Foreign investment is particularly important in technological improvement, and is unevenly distributed among the provinces. China's coastal provinces have generally attracted 90% of FDI, and even in 1995, the central and western regions as a whole still only attracted 12.3% of the total.<sup>20</sup>

The above analysis shows that China has experienced dramatic restructuring. The macro context for regional development and policy has changed rapidly. While the direction for future development remains debatable, it can be assured that China is no longer the same as traditional state socialism. While the Chinese government has not been willing to adopt the term 'capitalism' to describe the nature of China, the analysis of this section has shown that the control and capacity of the central state have declined dramatically, and local and global forces have emerged as important forces underlying economic and regional development. Since the mid-1990s, the development of regions, such as Sunan, has been heavily influenced by globalization and marketization/privatization, as well as by the role of the local states. The wealth of regions relies not only on local states, but also on central government policy, local factor endowments and non-state agents, and foreign investment and trade. Again, it is the multiple mechanisms of global forces, the central state, and local states and factors that are shaping regional inequality. As I will elaborate in the following section, China's triple transitions also suggest that the orthodox regional policy will be less effective in dealing with regional development issues.

### **Regional policy in China: towards the twenty-first century**

Since the 1990s, the central government of China has been increasingly concerned with the rise in the coastal–interior inequality, weak diffusion effects, and regional conflicts. In fact, the central government has never totally ignored the issue of regional inequality and interior development. Even during the 1980s when development policy was biased towards the coastal region, some measures were still taken to reduce poverty and the coastal–interior divide. Special funds, preferential bank

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20. State Statistical Bureau, *Zhongguo tongji nianjian* [Statistical Yearbook of China] (Beijing: China Statistics Press, 1996).

loans and tax exemptions have been continuously granted to the interior. The government encouraged the coastal provinces to make compensation agreements on energy and raw materials with the interior provinces. Economic reforms and open door policy have been gradually extended to the interior areas. With the increasing revenue as a result of income growth and tax reforms, state investment in the interior region has increased since the mid-1990s, especially for the improvement of education, infrastructure, energy and raw materials. The central government has urged coastal enterprises and foreign investors to provide capital and management skills to improve the conditions of the interior. The interior has also experienced some growth in export and foreign investment.

However, as I have shown in the above section, the macro context for China's regional development has changed dramatically. Economic reforms have brought profound changes to the roles of the state, regions, and global forces. While the state remains important, the control of the central state over the Chinese economy has declined. The central government no longer monopolizes the resource allocation process and has become less capable of committing a large share of total investment for interior development. Moreover, the central state could never ignore the development of the coastal provinces, which are the major tax contributors to the state coffers and can more effectively participate in the international division of labor. This is evidenced by the vigorous development of Shanghai's Pudong district and the drive to build Shanghai into a global city. Meanwhile, as a result of decentralization, marketization and globalization, local and global forces have emerged as important forces underlying economic and regional development. Foreign investment tends to concentrate on China's coastal provinces and well-developed regions, and always favors some regions over others.

The changing global environment, as well as the changing domestic context, has important implications for China's regional development policy. First, globalization has become a major trend of the world economy and the world is changing more rapidly.<sup>21</sup> While scholars are debating over the nature and consequence of globalization, our economies have become more integrated, and the competition among countries and regions has become more intense. Multinational enterprises (MNEs) have risen as major players in the global economy, challenging the control of nation-states. Capital and labor have also become more mobile, and government control over factor mobility has become more difficult. Foreign investment and trade will continue to serve as important factors of regional development in China. Firms and regions in China have to adapt to the globalizing economy and to participate in global competition and the international division of labor. Traditional ways of vertical control and state dominance under state socialism, paying little attention to the global environment and local context, have become ineffective in territorial administration.

Second, the process of globalization is accompanied by regionalization, either at supra- or subnational scales. The former includes the establishment of regional trading blocs, such as the North American Free Trade Area (NAFTA), the European Union (EU), and Asia-Pacific Economic Co-Prosperity forum (APEC).

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21. P. Dicken, *Global Shift* (New York: Guilford Press, 1998).

The latter refers to the emergence of new clusters, metropolitan regions, and border trading blocs. The dynamics and complexity of the global economy stimulate the emergence of alliance capitalism and networked regions. Governance in developed societies has been changed from managerialism to developmentalism/entrepreneurialism and public-private partnership. Regions have to exploit their competitive edges and fully take advantage of their region-specific conditions. With increasing power from decentralization, regions also tend to seek fair treatment from their higher-level governments. Moreover, local states and firms have to collaborate more actively and purposefully with each other. The attitude of governments toward firms, especially in China, must be changed from principle-agent relationships to partners in order to achieve the goal of regional development. Local initiatives using local resources and regional networks to promote economic development will become even more important, and should serve as a major component of regional policy.

The third trend is the coming of the information age. Flexible production and rapid technological change have become norms for today's economy. New initiatives promote entrepreneurship, international cooperation, and the triple alliance among firms, universities, and governments in research and development. Technology enhancement and human capital development should also be part of regional development policies. Rapid technological change has placed a heavy burden on developing countries and poor regions, as those countries and regions lack resources to lead the technological revolution. These changes have intensified competition among nations, regions, and firms. These broad changes, as well as domestic restructuring, require new strategies of regional development in China.

### *Facilitating the development of non-state sectors*

While some scholars have argued for increasing fiscal transfers to reduce regional inequality in China, regional policy in developed countries no longer emphasizes redistribution, although interregional budget transfer had been heavily used for industrialization, infrastructure development and resource exploration.<sup>22</sup> China's regional policy should not emphasize interregional fiscal transfers, as regional policies centered on the welfare system and interregional fiscal transfers simply do not work well. Moreover, the central government is no longer monopolizing the Chinese economy, and China has become part of the global economy. State support for interior development is limited, and the state is no longer functioning as the dominant force driving regional development. As I have argued previously, state policies, local forces and global change have become the three major mechanisms driving China's regional development. China's central and local governments are becoming global citizens, and sound policy making must consider the changing global environment and the global community. Domestic and global changes have

22. J. Taylor and C. Wren, 'UK regional policy: an evaluation', *Regional Studies* 31(9), (1997), pp. 835-848; D. Maillat, 'Innovation milieus and new generations of regional policies', *Entrepreneurship and Regional Development* 10, (1998), pp. 1-16.

also intensified the competition among regions and stimulated the efforts of local governments in improving local development.

China's SOEs have been in trouble for years, and previous reforms have failed to revitalize SOEs and to solve the problems of state ownership. However, in many interior provinces, SOEs are still the backbones of the economies and state banks still tend to favor SOEs in providing loans. While the State Council and State Planning Commission had attempted to promote the development of township and village enterprises (TVEs) as engines for interior development, the evidence suggests that no significant progress has been achieved.<sup>23</sup> While I am not rejecting the continued reform and development of SOEs and TVEs, the governments must make more efforts to facilitate the development of shareholding companies, foreign invested enterprises, and the private sector by initiating further reforms and providing more favorable policies to these sectors.

The use of non-government funds in industrial and infrastructure improvement, especially foreign and private investments, needs to be expanded dramatically. Shareholding companies have the potential to become the backbones of the economies in both coastal and interior China. In addition, foreign capital and foreign invested enterprises are important in the development of both rich and poor regions. Moreover, international evidence suggests that small enterprises tend to generate more jobs than large companies, although the latter is better positioned in regional and global competition and has advantages in economies of scale and agglomeration. Small enterprises also have some advantages in market penetration and flexible production, and should be encouraged in development policies.

### *Improving 'soft' infrastructure: human resources*

More efforts should be made to improve the 'soft' infrastructure. The improvement of 'hard' infrastructure, such as transportation, is certainly important in China, but the soft infrastructure is equally important, especially in human capital and networking development. Intangible factors have been widely concerned by regional policy, and developing interregional networks and partnerships has also become an important component of regional development strategy.<sup>24</sup>

Cheap labor is a major advantage of the interior provinces. While coastal China has attracted migrant workers from the interior by providing more job opportunities, higher wages, and better living conditions, the interior region still has a large labor force pool which is attractive to foreign companies and coastal enterprises.<sup>25</sup> Cheap production costs have been successfully promoted by the United States' South in attracting investment from the North, and can also be promoted as a major advantage to attract investment by interior China. In addition, interior China has

23. D. L. Yang and H. K. Wei, 'Rural enterprise development and regional policy in China', *Asian Perspective* 20(1), (1996), pp. 71–94.

24. S. Holland, 'New dimensions to regional theory and policy in the European Union', in W. Blaas, ed., *A New Perspective for European Spatial Development Policies* (Brookfield: Ashgate, 1998), pp. 86–101.

25. There is a huge literature on migration in China, for example, Y. H. Wei, 'Interregional migration in transitional socialist countries: the case of China', *GeoJournal* 41(3), 1997, pp. 205–214; D. J. Solinger, *Contesting Citizenship in Urban China* (Stanford: Stanford University Press, 1999).

some advantages in education and technology development, especially in cities like Wuhan. Regions must fully utilize human resources, at the same time enhancing human capital development should be emphasized in regional development.

In addition, the Chinese government has encouraged the development of inter-regional cooperation, in an attempt to promote interior development. At the same time, factor mobility is still highly constrained by such regulations as the household registration system, urbanization policies, and monetary policies. Moreover, co-operative relationships should be developed between large cities and their surrounding counties, especially in fiscal and monetary policies. For example, the current 'city-leading county' (*shi dai xian*) system does not promote fair economic relationships between cities and counties, and is sometimes described by counties as 'cities exploiting counties' (*shi gua xian*). Reforming local public finance and interregional relations has become an urgent task in the regional development of China. Such reforms cannot be carried out by the Ministry of Finance only, but have to be in alliance with planning and resource management agencies.

### *Enhancing geographical targeting*

A fundamental feature of the space economy is geographical unevenness. Geographical targeting has long been used as an important approach to urban and regional development, and continues to be widely used in both developed and developing countries.<sup>26</sup> More efforts should be made to use enterprise zones to promote the development of poverty stricken areas in China. In China, numerous development zones (or industrial districts) have been promoted for economic development, including special economic zones (SEZs), the high-tech zones, and enterprise zones. Unlike the United States, where the Empowerment Zones and Enterprise Communities (EZ/EC) program is a key step in rebuilding America's inner cities and rural heartland, many of the development zones in China are located in the coastal region. One of the major purposes of the EZ/EC is to create a better business environment and to promote local entrepreneurialism. However, development districts in Chinese cities tend to have few linkages with the cities, and contribute little to the improvement of the regional development environment and to the role as incubators of innovation.

Some regions, such as Wenzhou of Zhejiang province, have never received any strong support from the central and provincial governments, yet show tremendous dynamics in economic growth. While after the mid-1990s the emphasis of regional policy shifted to the interior region, the central government should also pay some attention to the development of the coastal areas that are better positioned in global competition and are the major tax contributors to the state coffers. Problems of intraprovincial inequality in coastal China remain serious and should receive more attention from the central government. Numerous TVEs and private enterprises have contributed significantly to the rapid growth of the Chinese economy and provided jobs for millions of rural workers, but these enterprises are not ready to

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26. D. Bigman and H. Fofack, eds, *Geographical Targeting for Poverty Alleviation* (Washington, DC: The World Bank, 2000).

compete at the global level and are ill-prepared for the information age. Traditional cities in coastal China also require proper policies for successful economic and spatial restructuring.

### *Reforming urban and regional planning institutions*

Institutional reform is especially important to the poor regions that have inferior environments for economic development. More efforts should be made along lines that improve the transparency and fairness of government policy and encourage people's participation in the decision-making process. Strengthening urban and regional planning and management in China is needed. *Europe 2000 +* stressed the need for spatial planning and increased cooperation in spatial planning issues.<sup>27</sup> Chinese urban and regional planning was interrupted for many years, particularly during the Cultural Revolution when urban planning departments were even eliminated.

In 1998, China initiated a radical reform of its central government. The original 40 components of the State Council were reduced to 29, and the number of central government officials was cut as well. Territory planning, which was under the administration of the State Planning Commission (SPC), has been transferred to the newly established Ministry of Territory and Resources (MTR). SPC, which has been renamed State Development Planning Commission (SDPC), is no longer in charge of territory/regional planning, but MTR lacks the power to administer comprehensive regional planning. SDPC, Ministry of Construction, and MTR all deal with regional development and planning issues, but are not well coordinated with each other. Further institutional reforms are needed to promote regional development in China.

Although great improvements have been made since the late 1970s through the increase of personnel, funding, and decision power, the current urban planning approach in China still partially follows the Soviet mode, emphasizing project allocation and urban design. Planning is often isolated from development strategies, planning implementation, and urban and regional management, and has to be remedied constantly. Planning has not been effective in providing guidance for urban/regional development and growth management. Poor coordination exists among different ministries, departments, bureaus, and their branches. A more fundamental problem is that many of the planners are trained as technocrats, and they have to work harder to deal with issues in development strategies, resource management, environmental protection, citizen participation, regulatory framework, and implementation mechanisms—issues critical to contemporary urban and regional planning. While China's economic system has experienced dramatic changes, China's urban and regional planning system still needs radical restructuring, especially during the process of rapid transition from state socialism. Reform

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27. Commission for European Communities, *Europe 2000 + : Cooperation for European Territorial Development* (Luxembourg: Commission of the European Communities, 1994).

of the planning system and the improvement of territory management remain urgent issues in China.

While the government is needed to improve infrastructure and human capital, nonprofit organizations, non-state enterprises and individuals should more actively engage in the regional development process, but unlike Western societies, where non-governmental organizations (NGOs) are important participants and decision makers of regional development processes, non-state enterprises and agents are largely excluded from decision-making in China. As I have argued previously, non-state enterprises and agents have emerged as major components of the Chinese economy, and must be given more roles to play in the development process.

## Conclusion

The issue of regional inequality in China has attracted considerable scholarly attention. This paper has shown that patterns of regional inequality relate to geographical scale, and an analysis of multiple mechanisms can improve the understanding of the change of regional inequality. Rather than neoclassical or radical theories of regional inequality which emphasize free mobility of capital, this paper argues that it is multiple mechanisms, including state policy, global forces, and local states and agents that determine uneven regional development in China. Such arguments are based on the dramatic changes taking place in China, i.e. the control of the central government has declined, while the roles of regions/localities and global forces in regional development have become more important. While what will eventually emerge remains debatable, the global and domestic contexts for China's regional development have changed dramatically.

Globalization of the economy is fueling competition among countries and regions, and competition among China's regions has become more intense. The future of China's regions has become uncertain in the globalization and information era. Changes require new thinking on regional development strategies and policies in China. While considerable efforts have been made in promoting regional cooperation and integrated regional development, problems still exist. More efforts should be made to improve current regional development policies in China. As the issue of regional inequality is complex, and multiple mechanisms have contributed to uneven development across regions, we should neither over-emphasize, nor de-emphasize, the role of the state in regional development as advocated by disciplinary exclusionists and theoretical extremists. I expect China's regions will continue to be fragmented and the coastal-interior inequality will tend to persist into the future. Regional inequality will remain an important issue facing researchers and the Chinese government, and constant monitoring and research are required.