

Appendix: Government Regulations and Protectionism

Central government regulations

If the central government is interested in rapid economic growth (as seems to be the unifying theme of China's various leaders in the reform period), then it will want to act against local protectionism and promote a domestic free trade zone. A State Council (SC) circular of 10 April 1982 states: "regional or departmental (trade) blockades ... are extremely harmful to China's economy in total." But even though the central government clearly recognizes the negative effects of trade barriers, it only saw the need to act three times in the reform period, in 1982, 1990, and 2001.¹

The 1982 circular constitutes a brief, general admonition, of the type of which the SC issues many, on different topics, each year.

The SC clarified that as long as enterprises fulfilled the plan, they now had the authority to sell their above-plan output anywhere they wanted across the country; local governments and central government departments were not to interfere in the distribution of the above-plan output. But *central* government departments in planning industrial production were also asked to, if quality and price were the same, meet local demand with *local* production; this appears a move away from excessive interregional trade between centrally controlled enterprises and thereby a reduction in inter-provincial trade that would have nothing to do with trade barriers. Minority areas and underdeveloped areas were explicitly given the right to, for an unspecified but supposedly fixed period of time (*zai yiding shiqi nei*) "appropriately" (*shidang*) control purchases of basic consumer goods and light industrial goods from outside the area; the passage reads as if these were controls against *new* trade flows possibly occurring in response to the new right for enterprises to freely sell above-plan output.

For the next eight years, neither the SC nor any of its departments appears to have seen a need for significant action. Only in 1990 did the SC issue a second circular, now on breaking interregional blockades (SC, 10 Nov. 1990).² The circular holds local leaders responsible for blockades, and involves the Supervision Ministry. It sends a one-time signal from the center; the matter subsequently vanished from the center's agenda.

In detail, the 1990 circular, first, announced that all purchases and sales related to the mandatory plan must be fulfilled; once enterprises have completed their obligations under the

¹ The two circulars of 1982 and 1990 and the 2001 regulation, as well as a follow-up circular of the State Administration of Industry and Commerce in 1990, are provided (in Chinese) in a separate appendix on State Council regulations. Another piece of evidence that the center fully understands the importance of a domestic free trade area for the economy (or economic growth), if any further evidence were needed, would be the "Grand International Circulation" policy of the second half of the late 1980s that focused on using regional comparative advantages within China in an international context.

² The Chinese term for "interregional," *diqujian*, is not limited to inter-provincial but equally covers inter-municipal/ prefectural and inter-county, etc.

plan, they have the right to sell their additional output anywhere in the country, subject to the relevant government policies and regulations. Second, all current trade checkpoints must be rectified. Those that need to be retained must be approved by the provincial-level government. In the case of some minority areas, the State Planning Commission (SPC) can approve short-term controls for imports if the local supply is sufficient and meets quality standards, but imports of same-quality goods must be allowed at least up to a certain share of local sales. Third, differential tax rates (or tax exemptions) based on product origin are not allowed. Fourth, banks may not differentiate in their lending behavior and their interest rates between commercial institutions that sell local vs. imported products. Fifth, the price bureaus are to supervise the commercial activities of enterprises and to strictly implement price regulations; the prices of imported products may not be manipulated without authorization. Sixth, all local and all ministerial regulations which contradict the spirit of this circular are to be cancelled without exception.³

If blockades continue after promulgation of this circular, the relevant leaders will be held responsible. Provinces and ministries are to immediately upon receipt of the circular pass it on to the local levels. They are also to implement a one-time inspection and to report on the implementation of this circular to the SC by 25 December 1990. Implementation of this circular is to be supervised by the Supervision Ministry and its local counterparts.⁴

A follow-up circular by the State Administration for Industry and Commerce (SAIC), issued on 3 Dec. 1990, provides further details on the manning of checkpoints and the long-distance transport of agricultural goods (and inspections for fake goods, sold illegally under another company's brand name).

The tone of the SC circular, and the extent to which it requests action and assigns supervision authority and responsibility for implementation, match that of other central documents at the time, such as, for example, the macroeconomic control measures of 1988-1990 (which suffer from a similar local free-rider problem as open markets and which were successful in the end).⁵ The power to approve checkpoints is located at a very high level, the provincial level, and exceptions to open markets need to be approved at the central level, by the State Planning Commission. This allows clear assignment of responsibility to provincial leaders and central ministers, all appointed under the central nomenklatura. Localities are not given any leeway to decide on how, and to what extent, to implement the center's instructions. The SC never issued any follow-up circular. Either local governments obeyed its original circular, or the SC perceived whatever trade barriers continued to exist as having little or no substantial impact on economic growth.

³ In between the lines, the circular reveals just how little of a market economy China was by 1990, with the mandatory production plan still occupying center stage, unspecified government policies and regulations "legally" restricting free trade, and the local tax authority and banking system operating along geographic lines.

⁴ The Supervision Ministry is not a light-weight institution. While it may not have as much clout as the CCP Disciplinary Commission, it comes an immediate second. It is likely to be more effective than the SPC would have been as supervising institution, and the SPC itself is not exactly light-weight.

⁵ The center, in order to lower the economy-wide inflation rate, asked for a reduction in investment; some localities initially disobeyed. See Carsten Holz (1999) for a detailed analysis of the central-local interactions.

For the next eleven years, the topic of local trade barriers vanished from the center's agenda. The term "interregional blockades" (*diqu fengsuo*) appears in numerous circulars but usually only as one item in some longer list of undesirables, never as a key issue. The standard phrase is "ministerial and sectoral monopolies, and interregional blockades."

When the issue resurfaces, on 21 April 2001, it is in form of a long-term SC regulatory framework, a "stipulation" (*guiding*) that must have been developed over some period of time, possibly years. It could probably have been issued at any point of time, except that in 2001 the overarching issue of the malfunctioning of the "market order" provided an opportune moment.⁶

The stipulation spells out in eight points what is prohibited and what is not. This is followed by eleven articles listing in great detail which institution is to revoke (*chexiao*) what kinds of barriers.

The SC departments in charge of the economy and trade (presumably the SETC), of industrial and commercial administration (presumably the SAIC), and of quality supervision, are free to, at any time, examine possible digressions at the provincial level. Any work unit or individual can lodge complaints with any of these three government departments at the provincial or central level. They are guaranteed anonymity and promised rewards for valid complaints; any later revenge by the local government is to be penalized with demotion if not the dismissal of the local cadre. The regulation lists specific response times to complaints and also penalties (demotion, dismissal) for cadres who are responsible for barriers to interregional trade. This SC regulation is taken up at the local and at the central ministerial level, mostly as part of the campaign for rectifying and standardizing the order of the market economy.

Of the three regulations, only that of 1990 appears to address an issue of some current importance, which was either quickly resolved or not regarded as important later. The 1982 regulation seems to promote a reduction in *existing* trade barriers more than prohibiting the establishment of new trade barriers. None of the three regulations are linked, i.e., the 1990 regulation does not mention that of 1982, and the 2001 regulatory framework does not refer back to 1982 or 1990, suggesting that the 1982 and 1990 regulations are isolated events, and even the regulatory framework of 2001 does not happen as part of a two-decade campaign against local protectionism.

In AY's view, "the central regime railed, in a number of circulars, against interprovincial trade wars" (p. 1103). He refers to a Chinese source (Chen Yongjun, 1994) as noting "circulars and directives against interregional trade barriers ... issued by the State Council, Party Congress, People's Congresses, etc. in 1980, 1981, 1982, 1984, 1985, 1987, 1988, 1989, and 1990" (p. 1103, note 17). Following up on the details in Chen Yongjun, only the 1982 and 1990 SC regulations directly address interregional trade barriers. The evidence for all other years consists of some marginal mentioning, on the order of half to one sentence, in otherwise lengthy

⁶ A SC regulation of 27 April 2001 on rectifying and standardizing the market order addresses a wide range of issues from brand name imitations to excessive administrative procedures; trade barriers appear in a standard phrase referring to "breaking local blockades and sectoral monopolies." China Infobank carries regulations only of Guangdong and of Hebei Province that directly address barriers to interregional trade.

regulations on other topics, or in the annual (particularly lengthy) government work reports. The 1990 SC circular would not seem to justify a portrayal of *prolonged* central regime *railings* against *inter-provincial* trade wars.

The possibility exists that central regulations on barriers to interregional trade were issued throughout the 1980s and 1990s but were never made public. Since trade barriers are a highly public issue, this is unlikely. Two regulations by the SAIC in 1992 and 1998 listed hundreds of its old regulations that were either to be scrapped or to be retained. The SAIC follow-up regulation on the SC circular (SAIC, 3 Dec. 1990) was retained in both instances; neither the 1992 nor the 1998 SAIC lists contained any further regulations related to barriers to interregional trade.

Mentioning of local protectionism in the law/regulation and news database China Infobank

A keyword search of the laws and regulations database in China Infobank (<http://www.chinainfobank.com>) for the term “market blockade” (*shichang fengsuo*), the topic of the 1990 SC circular, in the period 1 Jan. 1978 (1985) through 28 May 2004 yielded 30 (28) hits, and for the term “interregional blockade” (*diqu fengsuo*) 243 (236) hits. Central Party institutions issued not a single document on “interregional blockade,” but the term appears in a peripheral role in 7 of their 741 (672) documents covered in China Infobank for this period; the SC mentions it in 34 (31) documents out of its 3701 (2984), of which only the three discussed here actually focus on this topic.

Slightly more than trivial coverage is provided in two other regulations. The Competition Law of 1993 (NPC 2 Sept. 1993), as one item in a long list, prohibits barriers to interregional trade; the reference to trade into and out of a “locality” (*bendi*) leaves no doubt that all administrative levels, including all sub-provincial levels, are addressed. In 1997, a State Economic and Trade Commission (SETC) circular on “market circulation” (*shichang liutong*) carries a standard admonition, taking up only about 1% of the circular, to keep markets open (SETC, 25 June 1997, Art. 9).

A keyword search of the *news* database in China Infobank for the term “market blockade” in the period 1 Jan. 1978 (1985) through 27 May 2004 yielded 112 (112) hits, and for the term “interregional blockades” 1122 (1111) hits. In the vast majority of these news articles the targeted term appears in the standard one phrase against interregional blockades and sectoral monopolies used by policy makers. A very few address centrally imposed or approved barriers to interregional trade, the key example being the car industry, or their removal.

The local protectionism concept appears strongly associated with road blocks. But a SC circular of 5 July 1985 specifically prohibiting the “chaotic” establishment of road blocks makes no mentioning at all of local protectionism. Road blocks appear to have been established at that time by various local institutions to raise funds for their institution (with no thought to protecting local enterprises against outside competition).

Provincial regulations

One would normally also expect follow-up provincial instructions adapting the central instructions to local conditions. But the database on rules and regulations in *China Infobank* carries no provincial counter-parts to the 1982 or 1990 SC circulars. While it is possible that *China Infobank* in 1990 did not provide the wide coverage of provincial rules and regulations that it does today, it could also be the case that the SC circular is simply passed on by provincial governments without modification, in particular because the SC circular does not leave room for local modification.

Internal (and non-exhaustive) compendia of documents issued by the Xi'an municipal government and its departments show that the Shaanxi provincial government issued a decision on problems in "enlivening the circulation system" sometime prior to 19 Sept. 1991 (with no other protectionism-related document in 1990 or 1991 in these compendia). On 19 Sept. 1991, the Xi'an municipal government issued its own circular on implementing the provincial decision. Of its 40 numbered paragraphs, two refer to road blocks and interregional blockades.

All road blocks must be disbanded. Those that need to be retained require provincial government approval and must be publicized. Economic losses caused in the future by illegal road blocks must be compensated.

The state-owned commercial system is allowed to expand into townships for the purchase and sale of goods, and the supply and marketing cooperatives (which are rural, collective institutions) can establish an urban network. The commercial system is free to procure the best and cheapest products. Other localities (*waidi*) that establish an outlet in Xi'an for the sale of famous, high-quality, and special local products (*ming, you, techanpin*) should receive support, and intentional blockades (*renwei fengsuo*) are not allowed.

This text appears to refer more to intra-municipal trade than to trade with other municipalities or provinces. There is no reference to other provinces. Even the last issue, of other localities selling in Xi'an, simply refers to non-Xi'an entities.

One may also want to not lose track of the historical perspective. It would appear that Xi'an is actually moving away from an even more constrained, earlier trading system where a monolithic local state-owned commercial system served urban households, and a cooperative local rural commercial system served rural households, and each had its established long-term suppliers with little or no purchases from "outside" its own system. Non-members of Xi'an municipality, in terms of selling directly in Xi'an, appear to earlier not figure in at all.

For about five years in approximately the second half of the 1990s I subscribed to *Shaanxi xinxiobao*, a thin, first weekly then bi-weekly economics newspaper of Shaanxi Province, and clipped articles of interest. My filing system, on local protectionism, contains three clippings of 1997 and 1998. First, petroleum end products are not allowed to be exported outside the province as long as the provincial distribution plan quota is not met (30 Jan. 1997). Second, provincial administrative organs and facilities, as well as mass organizations, are to meet their demand for products to the largest extent possible with locally produced products; imports from other

provinces require approval by the local finance bureau (the fiscal authority at the level at which the purchasing unit is located) (13 August 1998). Third, enterprises in Shaanxi province are requested to meet their needs for inputs and producer goods with locally produced products as long as price, quality, and transportation and sales services are the same as for products produced in other provinces; the purchase of a locally produced car is encouraged with a 40% reduction in the car purchase fee and a 50% reduction in the first year's road maintenance fee (but no reduction in national and provincial taxes and fees (*shuifei*)) (24 September 1998).

The first article appears to reflect an attempt to adhere to remnants of the planning system rather than the imposition of new trade barriers. The second article covers the purchasing behavior of state or quasi-state organs; the 2002 Government Procurement Law (NPC, 29 June 2002) has presumably put an end to such local preferences. The law does not even address local protectionism directly. It prohibits any limitations on free access for all suppliers to government purchases in whatever geographic area or industrial sector (Art. 5).⁷ The third article reflects first of all a "buy local" campaign, of no obviously binding character. The car industry is given special treatment. The provincial government, probably the owner, could apparently not resist the temptation to slash its fees for the purchase of provincially produced vehicles at a time when the economy was experiencing slower-than-usual growth. Not knowing what the level of these fees was, one guess would be on the order of 100 or 200 yuan RMB, which would be equivalent to perhaps 0.1% of the purchasing cost of a car. In other words, the exhortations to buy locally produced cars may have had little more than symbolic value.

Overall, the impression I obtain is one of a gradual move away from the traditional planning system (with near-perfect trade barriers), much more than the imposition of new trade barriers. A mentality of localism is definitely entrenched (and probably more traditional than new). New trade barriers may be imposed at some points of time, for some products, in some localities, but when that happens, it perhaps happens to a degree that has little impact on actual trade.

Pre-reform period trade barriers

Beyond the literature covered in the paper, Audrey Donnithorne (1972) provides concrete details of local trade barriers. Reporting on Tsunhua county in 1970, she writes that the county authorities were "in the position of a monopolist, able to give priority to local goods and keep out competing products, thus assuring a protected market for local commodities at local prices" (p. 616) and that, in general, "prices of most light industrial goods have been controlled by local authorities" and "often *hsien* [counties] are likely to get lower prices for goods sold outside the *hsien* [county] than they can charge in their protected home markets" (p. 616). She recalls an event where,

when the mayor of Shanghai asked Chiang Hua, first secretary of the Chekiang Party Committee for specified quantities of certain commodities, Chiang Hua is reported to have replied that "Chekiang is not a colony of Shanghai." In 1962, a year of grave food shortages in many parts of China, "when some fraternal provinces asked Chekiang for certain amounts

⁷ At the national vs. international level, it says that demand should be met with products and services produced in China (Art. 10).

of supplementary food items, he turned down the request, saying, ‘I have pigs to feed.’” (pp. 616f.)

She summarizes “the picture given” in Chinese reports as “of a large number of highly protectionist states” (p. 611) with the local “promotion of light industry for the deliberate purpose of generating profits to be used for the development of other sectors of the economy” (p. 617). It would seem hard for such local protectionism to increase yet further in the course of the reform period.

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