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Lessons of China' Transition from a Planned Economy to a Market Economy

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INTRODUCTION

One of the most important events in the modern economic history is the socialist countries' transition from the Soviet-type planned economy to a market economy starting in the last two decades of the 20th Century. China's experience of transition has produced many interesting contrasts to the experiences of transition in Eastern Europe and Former Soviet Union (EEFSU). When the transition started in EEFSU, most economists in the West favoured a big bang approach, which included stabilization, price liberalization, and privatization. They considered these three reforms to be the necessary for a successful transition to a market economy and attempted to complete all these reforms simultaneously or in a short sequence (Blanchard et al 1991, Gomulka 1989, Kahn and Richardson 1991, Lipton and Sachs 1990). The big bang approach in essence is a version of the Washington Consensus, which is based on the basic principles of neoclassical economics for a well-functioning market economy and was recommended by the IMF/World Bank for market-oriented reforms in the developing countries. The proponents of big bang approach expected the transition in EEFSU to have a "J-curve" effect on economic growth; that is, they expected the GDP in a country that implemented the big bang approach to decline initially and to be followed by a strong recovery in a short period of time. Most countries in EEFSU followed this approach. The big bang approach, nevertheless, has resulted in an unexpected sharp and prolonged decline in GDP with extraordinarily high inflation rates and serious deterioration of other social indicators (World Bank 1996; 2002).

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