On Ownership, Competition, Management and Labour:
A Chinese Perspective

所有權、競爭、管理和勞工的研究：
以中國的轉型為個案分析

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Abstract

The bulk of the literature on transition economies such as the Eastern and Central European and Asian economies has explored transformation mechanisms from different perspectives and aspects. The study aims to answer two questions. Question one concerns the role of ownership, competition and management in the process of public enterprise transformation. Question two asks how public enterprise transformation interacts with the labour system and the relation to social safety nets. To address this question, the study investigates the impacts of enterprise transformation on labour by interviewing affected employees. This paper is particularly devoted to an examination of existing literature on the Chinese transition case. The second section briefly outlines the debate over China's reform path - whether it is radical or gradual, and a general review of literature on transition economies. Then it examines the three groups of arguments over the transformation mechanisms. The fourth section looks at literature concerned with the interaction between the transformation and labour. The final section provides a conclusion.

Keywords: Ownership, Competition, Management, Labour

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針對轉型經濟體的研究，已有相當多的研究成果，例如：中歐、東歐和亞洲國家等，其各自從不同的觀點，來探尋其間的轉換機制。本文旨在回答二個問題：問題一係指所有權、競爭和管理在公營事業轉型過程的角色；問題二則是關注在公營事業轉型過程是如何與勞工系統以及社會安全網絡互動。本文特別以中國大陸的轉型為主要探討個案，先針對其在轉型經濟上的相關文獻進行探求；第二部分則是簡述中國大陸的改革路徑之爭，其是否為激進或是漸進呢？之後，則分就所有權、競爭和管理的主張，來論述轉換機制；然後，在來分析這三個面向與勞工議題上的關係，最後則是提出本文針對發展中國家轉型過程中的研究建議和結論。

關鍵詞：所有權、競爭、管理、勞工
1. Introduction

The bulk of the literature on transition economies such as the Eastern and Central European and Asian economies has explored transformation mechanisms from different perspectives and aspects. By and large, views have circled around the notions of radical privatization and gradual reform. The former is concerned with the change of ownership from public to private, and the latter is about the introduction of competition and the improvement of management which includes regulation, institutions and enterprise management. There is a divergence of views on economic transformation between the earlier studies Kornai (1990) and Sachs and Woo (1994) and recent evidence demonstrated in the studies of Kolodko (1999), Carlin et al (2000), Sachs et al (2000a and 2000b) and Estrin (2002). There are also striking differences described in the literature which looks at transformation between the Eastern and Central European countries (typically Russia) and China (such as the contrasting evidence demonstrated by Naughton, 1994, 1995; Rawski, 1994; Nolan, 1995; Walder 1996; and Bevan et al, 2001).

This paper is particularly devoted to an examination of existing literature on the Chinese transition case. The second section briefly outlines the debate over China’s reform path - whether it is radical or gradual, and a general review of literature on transition economies. Then it examines the three groups of arguments over the transformation mechanisms. The fourth section looks at literature concerned with the interaction between the transformation and labour. The final section provides a conclusion.

2. The Chinese reform path - gradual or radical

The literature on China’s overall reform generates a debate over China’s reform path - gradual or radical. A large body of the literature acknowledges that Chinese economic reform has taken a gradual path. The main features of such a reform path are seen to be gradual, incremental, experimental and evolutionary (Zhang, 1992; Macmillan & Naughton, 1993; Fan, 1996; Walder, 1996). Specifically, there is no rapid leap to free prices, cutting of state subsidies, trade liberalization or sweeping privatization of state enterprises. All these characteristics are seen in striking contrast with the ‘big bang’ path which is characterized by the rapid release of price controls and state subsidies, restrictions of foreign competition and investment, and the rapid and massive privatization of public enterprises (Walder, 1996). As Naughton (1995) indicates, the gradualist path allows a transition economy to grow out of a planned economy by the steady introduction of competition and market mechanisms and slowly altering the old

1 In this paper state-owned enterprise, SOEs and public enterprises, PEs are the same and exchangeable terminology.
planning system and mechanisms throughout the economy, while avoiding the hardships of rapid privatization. Fan (1996) notes that China’s gradual and incremental path of reform starts outside the existing system which has been known to be difficult to reform, by creating a new system while letting the old system continue for some time. Eventually the old system is compelled to reform and therefore achieve a relatively smooth transition of the economy. The basic method used in China’s gradual incremental reform is the ‘dual-track approach’. Through the ‘dual-track approach’ to reform, it is intended that nobody should be made worse off; instead, most people are to benefit from the reform and in turn support reform (although they may not support every single reform measure).

However, the gradual path has been criticized by advocates of the radical approach. Fan (1996) and Wu et al (1996) point out that the weakness of the gradualism reform path lies in the accompanying corruption (rent-seeking), contradictions and costs of the long-term coexistence of old and emerging new systems, excessive government intervention and disparity and inequality of income distribution. In addition, criticisms of gradual reform also come from those who see China’s reform path as an integration of both gradual and radical reforms, partial (or limited) and full-scale reforms combined in the reform process (Li, 1996). Li argues that any single term such as ‘gradualism’ would be too simplistic and incomplete to describe the wide and complex reforms in China. On the other hand, Sachs and Woo (1994) argue that China’s reform has taken a ‘radical’ path. In the rural sector, reform through the household contract responsibility system is a kind of reform with ‘big bang’ style and the creation of the non-state sector moves China’s economy toward privatization. Wu et al (1996) warn that the concept of ‘gradualism’ cannot fully describe China’s reform and that the gradualist strategy does not best serve China’s transition due to its weakness. Wu urges the integration of overall advancement and breakthroughs in important areas. A third claim is that China’s reform path is an integration of a gradual and radical approach - a dual-track approach - in the overall reform process. Fan (1996) and Lau et al (2000) summarize that the ‘dual-track’ approach is the main basic strategy of China’s transition and will remain the key method for reform in the foreseeable future. In summary, the major body of literature on China’s transformation from a planned to a market economy reflects a basic consensus that the gradualist style of reform undertaken over the last two decades is likely to produce more sustainable and more effective change in the long run. But it needs to be integrated with more comprehensive measures as necessary in the process of reform so as to minimize the costs of reform. Nolan (1995) and Nolan and Wang (1999) indicate that China may eventually move towards a form of a private ownership economy, but for almost two decades it was possible to obtain sustained improvements in economic performance in all sectors based on a form of mainly public ownership of assets without mass privatization.
3. Research Methodology

The study aims to answer two questions. Question one concerns the role of ownership, competition and management in the process of public enterprise transformation. Question two asks how public enterprise transformation interacts with the labour system and the relation to social safety nets. To address this question, the study investigates the impacts of enterprise transformation on labour by interviewing affected employees. Thus the study explores the Chinese public enterprise reform from 1978 to 2000. It focuses on reforms related to ownership change, competition and the management of SOEs, and also examine the interaction between enterprise transformation and labour.

In order to increase the validity of the findings, the structured questionnaire survey was supplemented with in-depth interviewing, and existing statistical and governmental records. The in-depth interview included 11 semi-strucutred questiones, gathering information on case companies’ brief history, organisational structure, major reform measures, operation and labour issues. Due to financial and personnel resources, the study was restricted to a manageable sample of cases studies by only including 18 cases. The case studies rely on in-depth evidence that is evaluated on the basis of analytical generalisation.

Several factors influenced the selection of the sample. The cases were chosen according to the following characteristics: size (large, medium, and small SOEs), and relatively focused on the adoption of one of the three main reform mechanisms – the creation of competition, ownership transfer or management reform. Reform mechanisms employed have generally been grouped according to one of three kinds of representative mechanisms. Some, however, have been reformed through a mix of all three mechanisms. SOEs used in this case study are selected according to the philosophy that the higher the variance of cases, the more representative the study will be of the process of SOE transformation. In total, 108 copies of the questionnaire were given out to 12 case enterprises and 105 copies were completed and returned. All the employees answered the questionnaires had worked in the target company for over five years. This length of working time was anticipated to ensure that all the respondents had personally experienced the reform and had a good knowledge of the reforms in the period examined.

Data analysis is conducted according to the framework provided by the economic and managerial theories reviewed in the literature: the three-dimensional transition mechanism, competition, ownership and management. Theories of the firm are closely referred to and the interaction between the transformation and labour is examined, particularly in relation to employment and social safety nets.

The questionnaire presented to each of the case enterprises, the closely related interviews carried out with the enterprise manager, and the questionnaire about employee welfare, were
processed and analysed. The findings are used to interpret the variables relating to the creation of competition, ownership change, and management reform. The target SOE's performance is measured against four enterprise indicators, namely profitability, labour productivity, wages and welfare. Discussion is based on the practice of public enterprise transition practice in China, the framework provided by relevant theories, such as property rights theory, principal-agent theory, and new institutional theory. The outcomes from case studies of SOEs are also incorporated into the analysis.

4. A comparison of transition between China and other transition economies

Although the economic systems under centrally-planned economies share considerable convergence between China and other transition economies, their reform in the last two decades for the common goal of improved efficiency diverged explicitly. As Cook and Nixson (1995) have noted, in other previously centrally-planned economies such as those of Eastern Europe, political change generally preceded economic change. China has progressively and intensively undertaken economic reforms since 1978, but with comparatively little political change. China has shown a contrasting difference in the transformation process, despite it takes some note of the essential feature of transition in terms of the main focus of employing transition mechanisms.

The existing literature has shown that China’s reform has been a great success without following the dominant transition orthodoxy (Byrd, 1991; Mcmillan & Naughton, 1993; Naughton, 1995; Nolan, 1995; Walder, 1996; Stiglitz, 1999; Qian, 2000; Xu, 2000). Since China's economy followed a Soviet model of planning before the reforms initiated in the late 1970s, like other ex-socialist economies, most aspects of supply and distribution were subject to compulsory allocation (Ellman, 1989; Nolan, 1995). Both capital and human resources were relatively immobile and the industrial sector was predominantly state-owned. The policy principles for transforming Chinese state enterprises were first embodied in the contract responsibility system (CRS) before the early 1990s, where state ownership remained and then in the modern enterprise system (MES) until the current stage, where property rights are required to be clarified (partial privatization has been officially permitted ever since) and management improvement is required too. The CRS principles are mainly about the expansion of management autonomy and the retention of profits with continuing state ownership (Child, 1994, 1996; OECF, 1998; Hassard et al, 1999). Since the early 1990s China’s SOE transformation has mainly followed the principles of the MES which consist of four key elements: clarification of property rights, clear definition of rights and responsibilities, separation between government and enterprise management, and scientific management. The MES clearly highlights ownership
restructuring and management reform. As OECF (1998) and Hassard et al (1999) note, the MES embraces reform which adopts new enterprise management mechanisms; reconstruction which consists of technical transformation and improvement, and restructuring which involves the reorganization and ownership divestiture of property rights and assets. However, Hassard et al (1999) also caution that the MES is still not able to touch all ‘forbidden areas’ of reform. Some problems, for instance surplus workers and management appointments, seem to remain unsolved in the near future due to great political sensitivity (Hassard et al, 1999; Zhang, 1999).

The Eastern and Central European (‘ECE’) transition economies have emphasized deregulation and privatization during transition. Kornai (1990) asserts that it is a vain hope to expect that the state unit will behave as if it were privately owned and will spontaneously act as if it were a market-oriented agent and that ‘state ownership permanently recreates bureaucracy’ (p.58). Sachs and Woo (1994) attribute the immediate different results of the Eastern European countries (‘EEC’) and the Former Soviet Union (‘FSU’) with a worsened economy and China with an improved economy, to different initial conditions. They believe that ‘shock therapy’ transition would help the EEC and FSU states to achieve better economies, and that China would face the trap of property rights, as it avoids the privatization of state-owned enterprises. Under the ‘shock therapy’ approach, public enterprises have been encouraged to undertake schemes of rapid and mass privatization which ranged from self-privatization in Hungary and Poland, to mass privatization programmes in the former Czechoslovakia, and Russia’s voucher scheme and direct sale (Sachs, 1993; Cook & Nixson, 1995; Nolan, 1995; Ellman & Kontorovich, 1998). However, these views face challenges from recent evidence from a number of transition countries.

Carlin et al (2000) reveal their findings, based on the results of a cross-country survey of 3,300 firms across 25 transition countries, that the nature of competition in the product market has important effects on the performance of firms; there is no statistically significant relation between privatization and performance. Their report finds that state-owned firms and privatized firms that had formerly been owned by the state show no significant differences in sales or productivity growth. This is supported by Estrin’s (2002) evidence from an across country study of Central and Eastern Europe. It asserts that although the transition countries began with very different initial conditions and have employed a variety of policies with respect to privatization, price and trade liberalization and competition, transition policies underlying enterprise restructuring must be regarded as complements, not substitutes. Privatization alone will not be enough; effective corporate governance and hard budget constraints will also be necessary for enterprise transformation.

Sachs et al (2000a), based on empirical evidence across 24 transition countries, warn that the transition process is a transformation of not only markets but also the government. The
objective of the government is an important determinant of privatization gains. Sachs et al (2000b) reveal that post-privatization experiences has not always found improved performance. The immediate economic effectiveness and social acceptability of privatization depend on the existence of the institutional underpinnings of capitalism. Where these underpinnings are absent, even if the government is willing and able to construct and enforce, it is better to delay privatization until the right conditions are in place.

Sachs et al (2000b) come to a further conclusion that privatization involving a change-of-title alone is not enough to generate improvements in economic performance, and that privatization policies must be tailored to the (cluster-specific) level of complementary reforms in place. In turn, the complementary institutional reform does not guarantee improved efficiency unless a minimum level of privatization has already been attained. The idea of ‘one size policy (privatization) fits all’ does not apply to transition economies. This view is backed up by Kolodko’s (1999) study on ‘ten years of post-socialist transition’, arguing that it is naive to assume that a market economy can be introduced by ‘shock therapy’. A market economy requires adequate market-supporting institutions and appropriate behaviour, both of which can be introduced only gradually because they require new organizations, new laws and behavioural changes in various economic entities. McNally and Lee (1998) and Shieh (1999) cast criticisms over too close government-enterprise relationship. However, radical political power change preceding economic reform may not necessarily lead to smooth transition. Such reform in Eastern European and the FSU countries was generally viewed as a failure. Taking the Russian example, the removal of the Party from economic management appears to have been the single most important blow to the economy. The Party’s withdrawal from the economy caused an institutional vacuum which resulted in serious disorganization and loss of control of the economy (Ellman and Kontorovich 1998). Cook and Nixson (1995) confirm that if the corresponding authority to operate it effectively has not been provided, there is a danger of institutions being set up but operating in a vacuum which is often the case in a transition economy.

5. Main arguments about the transformation mechanisms in the Chinese case

Within the broad literature on transition economies there are various ways of describing the reforms which range from partial or comprehension reform to gradualist or shock therapy reform. Cook and Nixson (1995) and Jeffries (2001) provide an overview of this. Different from the radical style of reform which is often characterized with radical political change preceding economic change, China chose a gradual style reform by focusing on economic change with substantial continuity in its political system (only a few other Asian transition economies take
note of the Chinese path, such as Vietnam (Nixson, 1995).

It is widely acknowledged that the Chinese style reform gained phenomenal success in sustainable high growth for more than 20 years. China’s rapid economic progress has aroused considerable interest worldwide as an economic model of gradualism (Jeffries, 2001).

The arguments about the mechanisms for China’s state enterprise transformation and its reform path remain an open debate. Their ideas and advocates are generally reflected in three groups of academics. One group refers to those who hold viewpoints from the perspective of centrally-planned and transition economies (e.g. Barry Naughton, Peter Nolan and Thomas Rawski). Another group refers to the Chinese economists being deeply exposed to Western economic and management literature, which include those who studied in American and British universities (Lin Yifu as a competition-solution representative was once a doctoral student at Chicago University and Zhang Weiying as a ownership-solution representative studied for a PhD at Oxford University; both now work in China). A third group refers to the Chinese specialists who worked in the centrally-planned system and experienced transition by directly participating in the design and implementation of policy and reform schemes (e.g. Wu Jinglian and Li Yining). Similar to the international debates as discussed, the arguments about Chinese public enterprise transformation also remain on-going around the mechanisms of ownership-solution, competition-solution, and management-solution. This is accompanied by an emerging body of literature. The ideas of this literature can be grouped into three which, by and large, reflect the main arguments about ownership change, competition and management reform.

Group one - the ownership-solution group whose viewpoints can be seen in Wu et al (1996); Zhang (1997, 1999) and World Bank (1995, 1996, 1997) - advocates that China’s SOE reform should focus on the problems of property rights and change of state ownership. This group argues that reform without clarified property rights means the CRS can neither promote efficient resource allocation nor avoid government intervention. Another group – the competition-solution group (Nolan & Wang 1998) consider that the introduction of competition is more important than a change in ownership. A third group refers to the management - solution group. The core advocates of this group argue that the state ownership of SOEs does not have to shift into private ownership, although some ownership adjustment may be helpful in some cases. The reform priority should be in the improvement of management and the creation of more effective institution. As Nolan notes, economics has limitations in guiding economic transition and cannot be relied upon to solve all the problems in public enterprises. Rather, political economy needs to be considered (Shirk, 1993). Zheng and Zhang (1986) argue that SOEs’ reform should further improve the Contract Responsibility System (CRS) for even greater autonomy. They claim that the problems of the SOE sector were mainly due to insufficient autonomy in decision-making. They sought to solve the autonomy issue through further expansion of enterprise
autonomy while maintaining state ownership. There are some recent empirical cases studies that focus on management, organisation and institutions such as Zhang (2000), China Reform and Development Report Expert Group (1999) and Hassard et al (2002). But this group seems to have been relatively less vocal than the other two groups due to limited studies and evidence so far. But management is highlighted as an essential component in the MES which is employed as a policy guide for the further SOE transformation. More details about the debates among these three groups are given below.

5.1 Ownership-solution group

This group claims that an unclear definition of ownership is the source for the SOEs’ inefficiency. The representatives of the group include Yining Li (1986, 1987) and Weiying Zhang (1997, 1999). The common points of view on the state enterprises among these Chinese economists are the unclear definition of the SOEs’ property rights and the bureaucratic asset management system which weaken the monitoring capability of the state as the representative of the owner (the whole people). The state, as the owner representative of the SOEs, has failed to supervise management in the SOEs effectively. As a result, the insufficient monitoring has allowed managers to pursue their private interests at the expense of the profit of the enterprise. In order to solve the efficiency problem, privatization or property rights adjustment was suggested by World Bank (1997); Li (1986, 1987) and Zhang (1997, 1999). These writers note that as the SOEs belong to ‘the whole people’, the state acts as the SOE owner on behalf of the whole people. The state, as the owner-representative of the SOE, cannot supervise management in the SOEs sufficiently because of the high costs of checking under the imperfect market system. Thus under state ownership, the owner can hardly make the enterprise manager work towards the maximization of the owner’s interests. Managers of the SOEs are therefore able to operate their enterprises according to their own interests without being checked by the owners. Thus enterprise management without owner supervision inevitably gives rise to inefficiency.

Li (1986, 1987) strongly advocates the establishment of a shareholding system to transform the SOEs. In such a shareholding system, the state is a shareholder, the state assets are turned into state shares and state asset operating companies are set up to enforce the functions of the state shareholders. However, the shareholding advocates faced criticisms from Zhang (1999) in relation to three concerns. As Zhang warns, the shareholding advocates cannot address the issues of the mechanism of managerial appointments, value-adding of state assets, and separating government and enterprise operations. Zhang (1999) therefore suggests changing the state assets into creditor rights in order to really clarify property rights and separate government and enterprise operation. To clarify property rights in corporate governance and establish effective incentive and control mechanisms, Zhang suggests that privatization is the only way out for
China’s state-owned enterprises. Empirically, Zhang (2000) and the Expert Group of China Reform and Development Report (1999) have described a number of case companies which have gone through ownership restructuring, mainly in the 1990s. Their empirical evidence has demonstrated the benefits and restraints of ownership change. With respect to China’s ‘grasping the large and letting go the small SOEs’, Wu (1999) has warned that the Chinese authorities should not be attempting to forcibly weld sampans together to form an aircraft carrier. He indicates that enterprises are subject to ‘forced marriages’ or ‘high-speed fattening’ where entire industries are merged into a few large firms or one or two big enterprise groups (Economic Daily (Jingji Ribao) February 12, 1998 P. 5).

5. 2 Competition-solution group

Lin (1997) and Lin et al (1998) assert that the real causes of the SOEs’ problems do not lie in the ambiguous definition of ownership but in the lack of a fully competitive external environment. They point out that the separation and conflict between owners and managers has existed ever since the appearance of modern corporations and that the ownership structure is not the focal point in the SOE efficiency problem. The introduction of the shareholding system would not improve the SOEs’ efficiency without the existence of a fair and competitive market. Thoburn (1997) and Nolan and Wang (1998) show that privatization is not necessarily required for the improvement of enterprise performance in the Chinese cases of SOE reform. According to Lin et al (1997), changing the SOEs’ ownership to private ownership is neither a sufficient nor a necessary condition for an enterprise to be efficient. But the most essential condition for reforming the SOEs is to eliminate the policy-determined burdens from SOEs in order to foster competition, and therefore the vicious cycle from policy-determined burdens to information asymmetry to soft budget constraints can be stopped. The SOEs can therefore be put into competition with private firms on a level playing field. After the stripping of policy-induced burdens, the SOEs can determine whether or not to change ownership. Lin et al also employ the cases of ownership change in the UK coal mining industry, Korean, Indian and some Latin American countries to justify their view. Lin et al (1997) maintain that in perfectly competitive markets, there would be little difference between the performance of public and private firms. This is further strengthened by Lin et al (1998), who assert that if competition is sufficient to equalize public and private performance, then there is little need to consider the nature of ownership. In other words, privatization or ownership change does not necessarily solve the problem of soft budget constraints. Moreover, the competition-solution group points out that in many cases in transition economies, after radical privatization, the severity of soft budget constraints was no better than it was before privatization. Similarly, Nolan and Wang show that from the experience of Hungary, Poland and Russia, there is no satisfactory way to privatize
large SOEs. Regarding the reform of the large state enterprise sector, they further stress that ‘the main goals of reform become autonomy and competition rather than privatization’ (Nolan and Wang 1999: 180). In all, this group claims that creating a competitive and functional market environment is more important than shifting the ownership from state to private hands in the improvement of SOE performance.

5. 3 Management-solution group

Realising the limitations of the ownership-solution advocates in the Chinese context, the management-solution group stresses the importance of institutional change at the state macro-management level and management reform at the enterprise level. Wu et al (1993) and Wu (1999) argue that a market system can be established on the basis of a pluralized property system with the presence of dominant public ownership. The market economy is composed of firms which are responsible for profits and losses, the competitive market system and market-suitable macro-management and government regulations.

A growing body of scholarship examines the emergence of China’s new economic institutions, such as Guthrie (1999); Li et al (1999); Oi and Walder (1999); Qian (1999) and Hassard et al (2002). This literature on market-supporting institutions stresses the role of institutions in the legal structure, property rights, enterprise system, market system, labour issues and state law / governance from the view of economic analysis, and advocates the improvement of state macro-management. Qian (1999) summarizes four aspects of transitional institutions as the institutional foundations of China’s market transition. That is, regional decentralization of the government, encouragement of entry and expansion of non-state firms (local government and private firms), financial dualism in government revenue and the lending side of the financial system, and market liberalization through the dual-track approach (the plan track and market track coexisted until the plan track was phased out sometime later). Qian (1999) noted that each of the four pillars of institutional change contributed to China’s transformation success since they changed the functioning of the government, firms, the financial system and market to unleash the forces of positive incentives, hard budget constraints and competition. Hassard et al (2002) particularly examined the effects of political-institution on issues concerned with Chinese SOEs’ surplus workers. In general, there is a lack of market-supporting institutions and the ad hoc enterprise reform often appears to be chaotic. Different localities and industries adopt different institutions and regulations.

It is also noted in the literature that institutions are often required to be built from scratch I the transition to the market, and they cannot be simply imitated from the Western-style ones. Some transitional institutions may be more effective and applicable for the transition situation (Qian, 1999). It has been warned that there is incompatibility between Western-style market-
supporting institutions and China’s requirement for institutions, such as the incompatibility between Corporation Law and the communist constitutional rules (Yang, 1998) and the inconsistency between state monopoly in the telecommunications sector and the Anti-Unfair Competition Law (Mueller, 1998). The institution-emphasizing literature argues that successful economic development needs not only markets, but also market-supporting institutions including constitutional order and the rule of law, which protect individual rights and provide effective checks and balances of government power.

As regards government intervention, Ma (1997) has documented a legacy of the planned economy which is excessive government intervention, which often makes the SOEs both political and economic entities with conflicting economic objectives and social responsibilities. Zhang (2000) and the Report of China Reform and Development (1999) give many examples of government intervention in the firms as well as the adverse affects of such intervention. In one sense SOE reform in China is essentially the separation of government and enterprise operations; in a deeper sense, that is the separation of ownership (state as owner) and operation. However, a considerable literature has described how one thorny problem of the SOEs is extensive administrative interventions in their internal affairs (Wu, 1999; Zhang, 2000; Shirk, 1993). These problems include interference in personnel appointments in terms of manager selection and senior promotions. According to the situation of 762 listed enterprises in 1998, it is estimated that over 90 per cent of shareholding companies (formerly state-owned) have the same person as board director and general manager (Liu & Gao, 1999).

Given the above situation, there are several consequences unfavourable for SOE transformation into economic entities. First, SOE managers do not have a free rein to manage the enterprise by looking only at the market, but have to consider the preferences of their senior supervisors. Second, government interference involves wage-setting characterized by nationally unified grades and managerial appointments; worse still, such intervention often has no regard for the ‘rule of law’. Third, the SOEs’ major investment decisions need the approval of higher authorities. According to OECD (1998), three quarters of the enterprises have not obtained the right to make decisions on large investments. Similarly, three quarters of the SOEs have not obtained the right to purchase and dispose of assets.

Xu’s (2000) empirical studies of 500 Chinese SOEs confirms the importance of competition, control rights and managerial and internal incentives. Cheng (2000) examines the importance of management, the problems facing Chinese firms and measures suggested for enterprise management. Zhang’s (2000) 36 case studies reflect various issues including the problems and importance of enterprise management. Wei (2001) has documented that the management systems of the firm should be regarded as an important part of the firm’s system, and that those who only emphasize the importance of property rights and corporate governance in the economics circle
have ignored the importance of management institutions in the firm. Wei also points out that using the theory of separation of ownership and control rights to explain the problems of the firm is outdated and misleading. As Wei notes, the updated theory guiding corporate governance is about the definition of the relationship between monetary capital and human resource capital rather than the definition of the relationship between owner and manager. It is mainly about establishing mechanisms for incentives and the control of human capital.

Lin et al (1997) argue that because information asymmetry maintains the state enterprises in an advantaged position of bargaining with the state for subsidies, even when they make losses, a crucial task of SOE reform is to develop proper macro- and micro-management structures.

Similarly, Nolan and Wang (1999: p.191) echo the point; as ownership reform went deeper in the larger SOEs, they evolved progressively from state-administered plants towards pluralized institutional ownership and de facto management control. From the corporate governance perspective, He (1999) compares three different models – the private shareholder-oriented model, the manager-oriented model and the legal person shareholder-oriented model, and concluded that in the Chinese case, institutional legal person-shareholder-oriented corporate governance should be fostered and used to replace the previous version of manager-oriented administrative intervention.

Hassard et al (1999) indicate that the current problems of SOE management rest on administrative intervention in personnel appointment and dismissal, which often results in the general manager and the director of the firm’s board being the same person, the mixing up of roles of each entity in corporate organizations, and the informal role of the Party’s organizations in the operation of the SOEs. As for the external conditions for establishing effective corporate governance, missing in the SOEs are a developed stock market and banking system, and an institutionally-strong legal framework. OECF (1998), Zheng and Wang (2000), CEF and CESS (2001) and CESS (2000) constitute a comprehensive summary of the arguments which cover current problems and the causes of the SOEs’ management problems, mainly including inadequate incentives and insufficient personnel autonomy. A CEF and CESS (2001) survey of 1,075 SOEs demonstrated that the majority of SOE managers were appointed by the relevant government authorities. It showed that 73.47 per cent of the SOE managers were appointed by relevant government authorities, and only 20.14 per cent were appointed by the board of directors of the SOEs. Such an appointing mechanism is viewed to be inappropriate. As regarding incentives, CESS (2000) revealed that pay incentives for the Chinese SOE managers were not as good as those for the managers of other types of ownership companies. The lack of adequate incentives and absence of proper control for SOE managers is seen to be a major source of SOEs’ problems. At the state level, the reform of macro-management is required. As Shirk (1993), Qian (1999) and Song (2000) note, this reform includes the establishment or perfection
of institutions, managerial structures and the transformation of government functions to serve the goal of overall reform.

6. The interaction between the enterprise transformation and labour

There is relatively little research looking into the impacts of China’s SOE reform on labour and employment. Yet it is evident that China’s SOE transition has resulted in dramatic downsizing. A large number of surplus workers have been, and are to be, made redundant while there is a serious lack of a social safety net (Hassard et al., 1999, 2002; Wu, 1999; Ding et al., 2000; Cook, Fabella & Lee, 2007; Cook, Kirkpatrick, Minogue & Parker, 2003; Robison, 2007; Reinert, 2007). The literature indicates that economic transition, including enterprise transformation, generates a range of impacts on labour and employment, and labour gives various effects on the transition.

On the one hand, the transformation of SOEs brings an end to lifetime employment, and substitutes it with contract employment (Ding et al., 2000), consequently changing the nature, contents and forms of the employment-related welfare system. It also places enormous pressure on social stability and social protection due to rapid job reductions for the purpose of reducing the high proportion of surplus labour in the SOEs (Wu, 1999; Ding et al., 2000). The immediate impact on layoffs and unemployment resulting from SOE reform comes to the centre of attention in China, as it generates forceful resistance to transition and causes social instability (Ding et al., 2000; Hassard et al., 2002). Due to the fear of such labour impacts, while there was a lack of well-established social security in China, the fundamental transformation of the SOEs was delayed and the SOEs were made to cushion the social unrest until the second half of the 1990s (Wu, 1999). The impacts on labour issues of the transformation reach the main areas of lifelong employment, managerial appointment, labour mobility, redundancy, incentives and welfare. It is claimed that the state enterprise transformation has generated such heavy impacts on SOE workers that the issues of surplus workers and social security are a ‘hard core’ of further Chinese economic transition.

7. Conclusion

The literature on China’s SOE transformation implies that China has so far avoided large-scale sweeping privatization and mainly resorted to the gradual evolution of reforms and the creation of competition and management reform. China employs its own theoretical framework for economic transformation which is different from most of the conventional transition
principles. Its policies on ownership divestiture is mainly centred on the clarification of property rights which began to be implemented on a large scale, not at the initial transition stage but during the second half of the 1990s. The management reforms at the macro and enterprise levels, and the introduction of competition have played important roles in the transition, especially before the 1990s, which is reflected in encouraging the growth of the non-state sector to produce competitive pressure on the state sector (Lin et al, 1997; Qian, 1999).

In the case of Chinese public enterprise transformation, debates remain over which matters most, ownership change, competition or management reform. The debates have not to date provided conclusive evidence on whether competition or ownership matters most in the achievement of smooth and effective economic transition. The importance of management is recognized, but is relatively less addressed.

As regards the interactions between the transformation and labour in the Chinese case, the literature notes that the transformation brings in changes to employment relationships and the related welfare structure. It also stresses that the surplus labour of the SOEs is a ‘hard core’ concerning for state enterprise transformation.

Reference


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