Abstract

In the 2000s and 2010s, there is an influential phenomenon called “state advance and private retreat” in China’s SOE reforms in strategic industries related to the production and processing of petroleum, ferrous metals, tobacco and telecommunication. Although some indicators have shown SOEs’ decreasing proportions in these industries, considering SOEs’ paid-in capital and assets, the tide of state advance and private retreat does exist in the strategic industries.

There are four variables influencing state advance and private retreat. For interest groups, the government-SOE relationship cannot explain the existence of state advance and private retreat in the 2000s and 2010s since this relationship also existed before the 2000s. As SOEs’ strong representative in policy-making process, the SASAC has greatly contributed to SOEs’ march in the market after its establishment in 2003, while at the same time, private enterprises do not have enough access to policy making process. For political elites, differences between Jiang-Zhu leadership and Hu-Wen leadership are one of the causes. As for institutional factors, both the fiscal and financial systems have increased SOEs’ advantages in market competitions. For influential event, “Lang Whirlwind”, China’s accession to the WTO, and the 2008 financial crisis in the 2000s all greatly contributed to the emergence of state advance and private retreat.
Preface

This thesis is original, unpublished, independent work by the author, Hui Zhang.
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I owe special thanks to my dad, my mom and my best friends, who were in China, Canada, UK, US and Japan. Without their constant support and patience, it would be impossible for me to overcome all the difficulties I had in Canada; without their unconditional love, it would be impossible for me to make my dreams come true.
Dedication

To my parents
Introduction

Ever since the reform and opening up in 1978, China has experienced tremendous changes and unprecedented economic growth in global history (Lardy, 2014). In 1980, the World Bank classified China as one of 30 the most poorest countries in the world (Lardy, 2014), however, 30 years later since 2010, the Chinese economy has become the world’s second largest economy, with GDP growth rates averaging 10% for more than 30 years,¹ and people’s living standard has been greatly improved. By 2013, the World Bank considered China as a upper-middle-income country (Lardy, 2014). In November 2013, the Third Plenum of the 18th CCP Central Committee held in Beijing, which intended to draw another blueprint for China’s economic development, aimed at “comprehensively deepening reforms”, redefined the relationship between the state and the market, and confirmed the market’s decisive role in allocating resources.² With many guidelines for future economic growth, the Third Plenums set the tone for the coming round of economic reforms, including SOEs reforms, which holds the key to the redefinition of the government’s role in the market economy and the improvement of economic structure.

SOE reforms are not a new topic on China’s reform agenda. The first round of SOE reforms was a key part of China’s urban economic reforms in the late 1970s and 1980s, together with the implementation of the household contract responsibility system in rural areas. Although SOE reforms may have contributed a lot to China’s economic prosperity in the past, nowadays,

as some scholars argue, SOEs are still acting as a bottleneck in China’s economic and social transformations with entrenched problems, like low efficiency, large numbers of state subsides, monopolies and unfair distributions of dividends (Deng, 2010; Naughton, 2007; Sheng & Zhao, 2012; Yang, 2014a). Although reforming SOEs has always been a heated topic of debate of China’s reform agenda for more than 30 years, one thing worth our attention is that debates on SOE reforms gradually cooled down around 2004 and almost stopped in 2007 and SOE reforms almost stagnated (Fan & Hope, 2013; Yang, 2014a). What is more important, from 2004 to the present, especially after the 2008 financial crisis, SOEs have been more and more expansive in the economy, which many scholars believe would increase the state sector’s market power, strengthen the monopolistic position of SOEs, push the private sector \(^3\) to the brink, and finally weaken the decisive role of the market playing in efficient allocation of resources (Du, Liu & Zhou, 2014; Sheng & Zhao, 2012; Yang, 2014a). According to Rosalea Yao (2012), SOEs have been larger and stronger than before and have become more and more competitive, which has increased the competitions private enterprises have to face. This phenomenon is called “state advance and private retreat” (guojin min tui, in Chinese “国进民退”), which has repeatedly appeared in the press for a long time and has been considered a retreat of China’s economic reforms by many scholars (Du et al., 2014; Sheng & Zhao, 2012; Xu, 2009). Represented by Ma Jiantang, the head of the National Statistical Bureau, some government officials and scholars have been denying the existence and harm of state advance and private retreat (Hu, 2012; Lardy,

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\(^3\)“Private sector” and “private enterprises” in this thesis refer to the universe of household businesses, enterprises registered as private companies, and enterprises whose dominant shareholders are indigenously private. Therefore, enterprises whose dominant shareholders are the state, collective organizations, or foreign investors are not included in the concept of “private sector” and “private enterprises” here. For the “private economy” in this thesis, it means that the economy consists of private enterprises.
2012, 2014; Wei & Zhang, 2010). On the other hand, influential scholars, for example, James McGregor (2012), Rosalea Yao (2012), Zhang Shuguang (2009, 2010), Zhang Weiyong (2010), Sheng Hong and Zhao Nong (2012), and Yang Weidong (2013, 2014a, 2014b), have shown their evidence to prove the existence of state advance and private retreat and have seriously criticized it. Then, what has actually happened to China’s SOEs reforms in the 2000s and 2010s? Has the state really advanced in the economy? If so, what are the evidence and causes? This paper is going to answer these questions, considering the performance of SOE reforms in the past 15 years. After careful analyses of relevant data and cases, I hold that the phenomenon of state advance and private retreat does exist in strategically important industries in the 2000s and 2010s, though not in every industry. For the causes of this phenomenon, I argue that interest groups, political elites and influential events have played an essential role in the emergence of “state advance and private retreat”.

This thesis consists of five parts. Part I provides an overview of the SOE development in China. I consider the SOE reforms as evolving through four distinct stages. Part II intends to prove that the state has advanced and pushed the private sector to retreat. Part III presents the relationships between my dependent variable (the emergence of state advance and private retreat in strategically important industries proved in Part II) and four independent variables (interest groups, political elites, institutions, influential events) which have been widely considered by existing explanations of the emergence and deepening of China’s reform and opening up. Based on the analyses of Part III, Part IV makes several policy suggestions for the new round of SOE reforms. Part V is the concluding part.

The industries of great strategical importance usually refer to production of electric and heat power, petroleum and petrochemicals, telecommunications, coal, steel, civil aviation, information technology and waterway transport.
State-Owned Enterprises and SOE Reforms in China

According to the Organization for Economic Co-operation and Development (OECD), state-owned enterprise usually refers to “business entities established by central and local governments, and whose supervisory officials are from the government” (OECD, 2009, p. 5), which only includes wholly invested by the state. This kind of state-owned SOEs is usually known as enterprises owned by “the whole people” (quanmin suoyouzhi qiye, in Chinese “全民所有制企业”) (Lardy, 2014). There is another kind of SOEs, called state-controlled shareholding enterprises (guoyou konggu qiye, in Chinese “国有控股企业”), whose major shareholders are the state (Lardy, 2014; OECD, 2009; Yang, 2014a). Both state joint ownership enterprises (enterprises jointly owned SOEs) and joint state-collective ownership enterprises (enterprises jointly owned by SOEs and collectively owned enterprises) are included into state-controlled shareholding enterprises (also called state-holding enterprises) (Lardy, 2014). This paper considers both enterprises wholly invested by the state and state-controlled shareholding enterprises as state-owned enterprises (SOEs).

Considering their functions, products and investors, SOEs can be classified into different types. In terms of the managers of state-owned assets, there are two kinds of SOEs, central SOEs and local SOEs. Assets of the former ones are managed by the central government or its adjunct institutions, like the central State-owned Assets Supervision and Administration Commission of the State Council (the central SASAC) \(^5\), Ministry of Finance, and Ministry of Commerce (Fan & Hope, 2013; Lardy, 2014; OECD, 2009). For example, PetroChina, Sinopec Group, State

\(^5\) For the complete list of SOEs supervised by the central SASAC, see [www.sasac.gov.cn/n1180/n1226/n2425/index.html](http://www.sasac.gov.cn/n1180/n1226/n2425/index.html), accessed May 26, 2015.
Grid, and China Mobile are all central SOEs which are managed by the central SASAC. As for state-owned financial institutions, they are under the supervision of special authorities, namely the CBRC (short for China Banking Regulatory Commission), the CSRC (short for China Securities Regulatory Commission), and the CIRC (short for China Insurance Regulatory Commission) (OECD, 2009). In addition, for other central SOEs, their supervisory authorities are individual departments of the central government, like Ministry of Commerce and Ministry of Science and Technology (OECD, 2009). Assets of local SOEs are under the control of local governments or their adjunct institutions, like provincial-level SASACs or municipal governments (Fan & Hope, 2013; Lardy, 2014). Take Shandong Iron and Steel Group Co. Ltd (supervised by the SASAC of Shandong Provinicial Government), Shanxi Coal Transportation and Sales Group Co. Ltd (supervised by the SASAC of Shanxi Provinicial Government), and Inner Mongolia Power Group Co. Ltd (supervised by the SASAC of Inner Mongolia Autonomous Regional Government) as examples. From the perspective of their functions, SOEs can be classified into three types: SOEs for policy purpose, SOEs with specific functions, and general commercial SOEs (Huang & Yu, 2014; Yang, 2010). SOEs for policy purpose are established to facilitate the implementation of public policies and to deal with possible market failures. China Reform Holdings Corporation Ltd.⁶ is a good example, which was established to help the State-owned Assets Supervision and Administration Commission (the SASAC) improve its management of central SOEs and state-owned assets. SOEs with special functions aim to

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⁶ China Reform Holdings Corporation Ltd. was established on December 22, 2010. It is under the control of the central SASAC and it is positioned as a platform to cooperate with the SASAC in improving central SOEs’ investment structure and the management of state-owned assets, especially focusing on the restructuring of central SOEs, the improvement of SOEs’ competitive ability, and auxiliary investment to new emerging industries and industries related to the economic lifeline. China Reform Holdings Corporation Ltd. home page [http://www.crhc.cn/n1441300/n1441419/index.html](http://www.crhc.cn/n1441300/n1441419/index.html)
strengthen the socialist economic system and ensure the economic security. This kind of SOEs includes PetroChina, Sinopec, CNOOC, State Grid, China Eastern Airlines, and China Southern Airlines, and so on. General commercial SOEs are the ones in competitive areas (Huang & Yu, 2014). SOEs can also be sorted by the degrees of their monopoly (see Table 1).

What are the characteristics of SOEs? The answer lies in the differences between SOEs and private enterprises. First, the only goal of private enterprises is to maximize their profits within the law. But for SOEs, they are not only enterprises chasing profits but more importantly the government’s macroeconomic tools that should shoulder more social responsibilities than private enterprises (Gu & Hu, 2014; Huang & Yu, 2014; Wang & Meng, 2012; Yang, 2010). Hence, since the government’s economic goals change in different stages, SOEs’ main tasks are not fixed (Yang, 2014a). Second, private enterprises’ investors are individuals and private organizations, but SOEs are wholly or mainly invested by the state. Third, the CCP and the government has the power to dismiss and appoint executives of SOEs. The top three executives (party secretary, chief executive officer, and chairman of the board) of 53 most important SOEs are appointed by the Organization Department of the CCP, and SOE executives below the vice ministerial level are appointed by the SASAC. Besides, and it can also evaluate executives’ performance (Fan & Hope, 2013; Jung, 2008, 2011; Lardy, 2014). Executives in private enterprises are appointed by shareholders or the board of directors (Heng, 2011; Lardy, 2014; Oi & Han, 2011; Yang, 2014a, 2014b).

The history of SOEs in contemporary China dates back to the “Three Great Socialist Reforms” in the 1950s, which were in fact a process of socialization and nationalization (Lardy, 2014). Theses three reforms were socialist reforms of agriculture, handicraft industry, and capitalist industry and commerce.
2014; Sheng & Zhao, 2012). After the “Three Great Socialist Reforms” were finished in the mid-1950s, China established a highly centralized and planned economic system, under which SOEs were like government departments. At that time, both SOEs’ daily operation and their personnel appointments and removals largely relied on administrative orders and

Table 1  SOEs’ Degrees of Monopoly in Different Industries

<table>
<thead>
<tr>
<th>Type of Monopoly</th>
<th>Industries</th>
</tr>
</thead>
<tbody>
<tr>
<td>Industries of natural monopoly</td>
<td>Production and supply of electric power and heat power, telecommunication, railway transportation, air transportation, post industry, production and supply of water, production and supply of gas</td>
</tr>
<tr>
<td>Industries of administrative monopoly</td>
<td>Manufacture of tobacco, mining and washing of coal, extraction of petroleum and natural gas, processing of petroleum, coking, processing of nuclear fuel, banking industry</td>
</tr>
<tr>
<td>Industries of economic monopoly</td>
<td>Manufacture of beverages, manufacture of rubber, mining and processing of non-ferrous metals, manufacture of chemical fibres</td>
</tr>
<tr>
<td>Competitive industries</td>
<td>Manufacture of transport equipment</td>
</tr>
</tbody>
</table>


instructions from the government (Sheng & Zhao, 2012). The State Planning Commission set output targets for the production of goods and the State Price Commission set the prices of almost all the goods produced (Lardy, 2014). Thus, before the reform and opening up in the end of 1978, it was the state, SOEs and collectively owned enterprises that played an essential and pervasive role in the economy, while private economic activity and the market were severely constrained (Chiu & Lewis, 2006; Lardy, 2014; Yueh, 2013). This situation gradually changed after Deng Xiaoping’s reform and opening up in 1978 (Fan & Hope, 2013; Haggard & Huang, 2008; Yueh, 2013). Though economists have different criteria to divide the long series of SOE
reforms, the trajectory of SOE reforms is fixed, which generally consists of four main stages with a few milestones. The first stage is from 1978 to 1992, marked by the decision “providing SOEs with greater autonomy” in the Third Plenum of the 11th CCP Central Committee, aiming at economic decentralization and interest concession by allowing SOEs to retain part of their profits, instead of turning over all their profits to the Ministry of Finance (Huang & Yu, 2014; Lardy, 2014; Naughton, 2007; Naughton, 2008; Sheng & Zhao, 2012). During the first stage in the 1980s, the government began to liberalize retail prices through the so-called “dual-track pricing system”8 to replace the pricing system that the state set prices for almost all the products (Chiu & Lewis, 2006; Lardy, 2014; Naughton, 2007; Yueh, 2013). At the same time, the fiscal policy changed. China embraced fiscal federalism by decentralizing fiscal power to local governments, in order to encourage local officials to promote the development of local economy (Ong, 2011). The remittance of profit SOEs needed to turn over to the state was replaced by a profit tax, which is the so-called “tax for profit” reform (Chiu & Lewis, 2006; Naughton, 2007; Yueh, 2013). As for the financial policy, in 1985, the banking system was reformed to have commercial banking services. In the mid-1980s, commercial banking functions of the People’s Bank of China (PBOC) were separated into four state-owned commercial banks with different focuses, which were Bank of China (BOC), Industrial and Commercial Bank of China (ICBC), Agricultural Bank of China (ABC) and China Construction Bank (CCB), while the PBOC became the manager of these commercial banks (Chiu & Lewis, 2006; Yueh, 2010). In the meanwhile, bank loans replaced grants and subsidies SOEs used to get from the government.

8 The “dual-track pricing system” was adopted by the Third Plenum of the 12th CCP Central Committee, which was an coexistence of a traditional plan and a market channel for the allocation of goods. The dual-track pricing system gave SOEs the autonomy to sell above quota output at market prices and retain the profits, while the output within the quota was sold at the prices set by the state.
directly and gradually banks were able to make investment decisions according to the market situation, instead of just obeying administrative orders before (Yueh, 2013). Many scholars, like Barry Naughton (2007), Huang Yasheng (2008) and Linda Yueh (2013), have confirmed the achievements of this first stage of China’s reforms because the competition generated by the reforms at the first stage eroded SOEs’ high profit margins and improved the efficiency of the economy. The second stage of the SOE reforms is from the Third Plenum of 14th CCP Central Committee in 1993 to 2003, focusing on market-supporting institutions, especially the establishment of modern corporate governance system and the restructuring of SOEs into limited liability enterprises (youxian zeren gongsi, in Chinese “有限责任公司”) (Chiu & Lewis, 2006; Fan & Hope, 2013; Lardy, 2014; Yueh, 2013). The 15th CCP Central Committee in 1997 made a breakthrough on the statuses of state ownership and private ownership. Private ownership was regarded as “an important component of the socialist economy”, while state ownership was no longer “a principal component of the economy” but “a pillar of the economy” (Chiu & Lewis, 2006, p. 48) The well-known SOE policy “grasp the big, let the small go” (zhua da fang xiao, in Chinese “抓大放小”) was endorsed by the 15th CCP Central Committee in 1997, which enabled large SOEs to get strong support from the state and allowed small and medium SOEs to go private through employee buyout, open sales, leasing, joint ventures, mergers and bankruptcy (Chen, 2006; Chiu & Lewis, 2006; Fan & Hope, 2013; Naughton, 2007; Yueh, 2013; Zeng & Tsai, 2011). The fiscal system was reformed in 1994, from fiscal federalism to fiscal centralization, and in this way, the fiscal support from local government to local SOEs was largely weakened (Naughton, 2007, 2008; Yueh, 2013), while at the same time, the shareholding system for restructuring SOEs widened the financial sources for SOEs (Chiu & Lewis, 2006).
During this period, Zhu Rongji’s SOE reform is considered of great importance by many scholars, like Chen (2006), Steinfeld (1998), Naughton (2007), Tiberghien (1998) and Joo-Youn Jung (2011), for finally pushing forward China’s SOE reforms with a shrinking state sector and casting off many social and policy burdens from SOEs. However, during this period, due to SOE restructuring and the lack of a good social security system, many SOE works had to face unpaid back wages and pensions and laid-off workers did not have enough compensation, which caused many social problems (Chen, 2006; Naughton, 2008; Yueh, 2013). In terms of the entire second stage, although privatization (siyouhua, in Chinese “私有化”) was used to deal with small and medium SOEs, it was never officially made into a national policy and there has been no legislation to dictate the process of privatization yet (Chen, 2006; Naughton, 2007; Oi, 2005). The expressions usually used to replace the word “privatization” were “ownership transformation” (suoyouzhi gaizao, in Chinese “所有制改造”), “ownership by people” (minyinghua, in Chinese “民营化”), “restructuring” (gaizhi, in Chinese “改制”), or “transformation of ownership to a joint-stock system” (gufenzhi gaizao, in Chinese “股份制改造”) (Chen, 2006; Zeng & Tsai, 2011). Yueh (2013) clearly points out that “the period of the mid- to late 1990s was characterized by the historical downsizing of SOEs… the large SOEs were consolidated and transformed into shareholding companies” (p. 307). The third stage is from 2004 to 2013, a phase of “state advance and private retreat”. Many scholars have tried to deny the existence of this phenomenon, using various indicators to show that private sector’s proportions of the national economy have been always rising, while state-owned economy’s

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9 Privatization here includes both one-step and multi-step SOE restructuring to transfer SOEs’ ownership directly from the state to private hands.
proportions have been shrinking (Hu, 2012; Lardy, 2012, 2014; Wei & Zhang, 2010). However, according to Naughton and Tsai (in-press), since the mid-2000s, China’s economy has stabilized in a model that most of the economic sectors continue the process of marketization and globalization, while industries of strategical importance are still firmly dominant by SOEs. Interestingly, even the 2011 annual report to the US Congress by the US-China Economic and Security Review Commission (the USCC) has noticed the existence of state advance and private retreat. the USCC (2011) argues that the government’s control over economy has decreased and the market is playing a more important role in resource allocation. I will prove the existence of state advance and private retreat and relevant fiscal and financial reforms in Part III and Part IV.

The fourth stage (2014-present) is marked by a new round of SOE reforms intended to ensure the market’s decisive role in allocating resources, which I will show together with my understandings of the Third Plenum of the 18 CCP Central Committee in Part V.10

SOEs have been playing an important role in China’s economic growth. A significant proportion of China’s overseas investment comes from SOEs, especially large central SOEs (Fan & Hope, 2013). Substantively, by the end of 2013, there were close to 220,508 SOEs and central SOEs alone respectively represented 61.5% and 64.4% of all the corporate income taxes turned over in China in 2012 and 2013.11 The data of OECD (2009) show that in 2007, SOEs owned 83.1% of the total capitalization in the stock market and by the end of 2006, central SOEs were in control of more than half of the total assets of all SOEs and their profits reached 64% of SOEs’

10 These four stages are classified based on articles by Huang and Yu (2014), Sheng and Zhao (2013), Tiberghien (1998), Yang (2010) and Yuan and Shao (2010).

11 Data come from the database named Annual Data from National Data of National Bureau of Statistics, with the indicators “Number of Corporate Enterprises by the Status of Holdings”, “Corporate Income Tax (100 million yuan)” and “Central Government Revenue, Corporate Income Tax (100 million yuan)”. Retrieved May 26, 2015, from http://data.stats.gov.cn/english/easyquery.htm?cn=C01
total profits (see Table 2). According to Li Rongrong (2008), the former director of the SASAC, 82% of the assets owned by central SOEs were concentrated in industries related to petroleum, petrifaction, electricity, telecommunication, transportation, mining and state security. Therefore, even after SOE reforms for a long time, state ownership is still playing an essential role in China’s economy (Li & Putterman, 2008).

Though China’s SOE reforms have been implemented for more than three decades, they are far from being over. According to Huang and Yu (2014) and Naughton (2007), there are still five areas worth our attention: establishing modern corporate and shareholding systems, restructuring SOEs in monopolistic sectors, strategically adjusting the state sector, supervising SOEs’ operations, and managing state-owned assets.

<table>
<thead>
<tr>
<th>Year</th>
<th>Number</th>
<th>Asset</th>
<th>Revenue</th>
<th>Total Profits</th>
</tr>
</thead>
<tbody>
<tr>
<td>1997</td>
<td>9.9</td>
<td>38.9</td>
<td>n.a.</td>
<td>n.a.</td>
</tr>
<tr>
<td>2000</td>
<td>7.9</td>
<td>42.1</td>
<td>n.a.</td>
<td>n.a.</td>
</tr>
<tr>
<td>2003</td>
<td>13.0</td>
<td>49.2</td>
<td>n.a.</td>
<td>n.a.</td>
</tr>
<tr>
<td>2006</td>
<td>18.1</td>
<td>51.7</td>
<td>51.2</td>
<td>64.0</td>
</tr>
</tbody>
</table>

*Note. Adapted from “State Owned Enterprises in China: Reviewing the Evidence,” by OECD, 2009, p.9.*
State Advance and Private Retreat

Since 2004, there have been heated debates on whether the phenomenon of state advance and private retreat (guo jin min tui) really exists. Ma Jiantang, the director of the National Bureau of Statistics, demonstrates that instead of advancing, the state sector keeps retreating from many areas, and uses economic data from 2005 to 2008 as his evidence (Ma, 2013; Wang & Zhang, 2010; Yang, 2014a). On November 22, 2009, Ma Jiantang presented a set of data about SOEs and state-holding enterprises at the China Economist Tribune in Renmin University of China. Based on his statistical data, Ma Jiantang claimed that China did not have the trend of state advance and private retreat, as compared to 2005, all the indicators showed that the proportion of SOEs in the economy was shrinking (see Table 3). Represented by Ma Jiantang, some scholars, like Hu (2012), Liu and Wang (2010), Wei and Zhang (2010), and Zhou (2010) also strongly dispute against the existence of state advance and private retreat. Hu Angang (2012), an influential economist of Tsinghua University, also deems that “China has faced state advance and private retreat” is a false proposition, as the number of SOEs, SOEs’ output value, the number of SOEs’ employees and the proportion of SOEs’ profits in total corporate profits are all decreasing, while all the indicators show an increase of the private sector. Wei and Zhang (2010) also make a comparison between SOEs and private enterprises, using the data of the Second National Economic Census. In their article, the data show that from 2004 to 2008, the number of SOEs reduced to 143,000 by 20%, while the number of private enterprises increased 1,614,000 to 3,596,000 by 81.4%. According to The First Communique of Main Data in the Third National Economic Census, by the end of 2013, 113,000 SOEs were only 1.4% of all enterprises in China.
According to the *China Statistical Yearbook (2012)*, the number of SOEs decreased from 39.2% of all enterprises in 1998 to 5.2% in 2011 and at the same time, SOEs’ proportion of industrial output decreased from 49.6% in 1998 to 26.2% in 2011. In their book *China’s State-Owned Enterprises: Nature, Performance and Reform*, Sheng and Zhao (2012) also admit that on the whole, SOEs’ proportion of the gross industrial output value has decreased year by year since 1999, as Figure 1 shows. Furthermore, for recent cases that SOEs merge private enterprises, Wei and Zhang (2010) consider them as individual cases instead of a trend. One of the reasons why Wei and Zhang (2010) deny the existence of state advance and private retreat is that the concept of “state advance and private retreat” has never been mentioned in the central government’s documents. Therefore, these scholars argue that the statistical data do not substantiate the general existence of state advance and private retreat, and it is in fact the private sector that is advancing instead of the state sector. According to them, SOEs have been retreating and making more room for the private economy, instead of squeezing the private economy’s living space. Some scholars, like Zheng and Zeng (2011), even take the debates on state advance and private retreat as an opportunity to criticize privatization and economic reforms. Nicholas Lardy (2014) also strongly demonstrates that the decade of Hu-Wen Administration (2003-2013) did not increase the role of SOEs in the market since generally the proportion of SOEs’ output in the economy was decreasing and the profit margins of SOEs and non-SOEs were virtually indistinguishable. Thus, Lardy (2014) thinks that SOEs did not gain more market power in the Hu-Wen era than before.

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Table 3 Comparison between SOEs and Private Enterprises

<table>
<thead>
<tr>
<th></th>
<th>Number</th>
<th>Industrial output</th>
<th>Profits</th>
<th>Assets</th>
<th>Number of employees</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>SOEs’ proportions</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>among all enterprises</strong></td>
<td>2005</td>
<td>10.11%</td>
<td>32.80%</td>
<td>44.04%</td>
<td>48.05%</td>
</tr>
<tr>
<td></td>
<td>2008</td>
<td>5.00%</td>
<td>28.34%</td>
<td>29.66%</td>
<td>43.75%</td>
</tr>
<tr>
<td><strong>Private enterprises’ proportions among all enterprises</strong></td>
<td>2005</td>
<td>89.89%</td>
<td>66.72%</td>
<td>55.96%</td>
<td>51.95%</td>
</tr>
<tr>
<td></td>
<td>2008</td>
<td>95.00%</td>
<td>71.66%</td>
<td>70.34%</td>
<td>56.25%</td>
</tr>
</tbody>
</table>


Figure 1 Proportion of the gross industrial output value of SOEs


The first report that mentioned the exact concept of “state advance and private retreat” is an article named “Reorganizing the market caused state advance and private retreat” (*Chongzu shichang yanyi guojinmintui*, in Chinese “重组市场演绎国进民退”), which was published by
Based on the evidence above, it seems that SOEs have not advanced since 2004. However, after further analysis, I find that those scholars’ evidence above is not convincing due to the lack of accurate indicators. For instance, although the proportions of SOEs’ number and assets to the number and assets of all enterprises are declining, it does not mean that SOEs are less powerful than before. There could be fewer small SOEs and more large and medium ones. It could also mean that the assets and capital of SOEs are concentrated in particular sectors in order to apply absolute control to these sectors. For example, in 2009, Shandong Iron and Steel Group, which is the largest company solely invested by the state within Shandong Province and also a large loss-making SOE, swallowed up a promising profit-making private company, Rizhao Steel, by purchasing 67% of Rizhao Steel’s shares with a low price (Sheng & Zhao, 2012). In 2008, Shandong Iron and Steel Group was formed by combing several steel SOEs in Shandong Province, including Laigang Group, Jigang Group and their subsidiaries, which means a decline of the steel SOEs’ number in Shandong Province, which means a decrease of the total number of steel SOEs. But after taking over Rizhao Steel, Shandong Iron and Steel Group became the third largest steel enterprise in China, controlling the steel production in Shandong Province (Sohu Net, 2009; Xinhua Net, 2009). This case is in fact a sign of state advance and private retreat in mining and processing of ferrous metal ores, which we can see from both Figure 4 and Figure 5. As for the decreasing proportions of SOEs’ industrial output and profits to all enterprises, despite the state’s retreat, it could be caused by SOEs’ low efficiency and other entrenched problems, instead of their retreat or the private sector's advance. Thus, the indicators above cannot really prove that the state has not advanced. According to Xu (2009) and Yuan and Shao (2010), though the number of SOEs are decreasing, the total amount
of their business is increasing and the private sector is losing access to important and profitable industries; consequently, private enterprises are less and less capable to compete with SOEs in those areas and the entry barriers become higher and higher. My paper employs two indicators of input instead of output to assess the changes of SOEs’ market power. The reason why I use indicators of input is that during the process of production, there are too many factors that can affect SOEs’ output, including industrial output, turnover, profits and taxes, which cannot show SOEs’ actual market power. On the contrary, SOEs’ input, such as capital, assets and shares, can provide accurate information on the scope and degree of SOEs’ influence. Figure 2 illustrates the average assets per firm in different economic sectors, from which we can tell that in terms of assets, SOEs have greater and greater advantages over domestic private and foreign enterprises. Meanwhile, Figure 3 shows an obvious decrease of SOEs’ efficiency in allocating resources.

Figure 2  By average total assets per firm in the different sectors

The first indicator in this paper is the proportion of SOEs’ paid-in capital in the total paid-in capital of all enterprises, which indicates the market power of SOEs and state-owned capital. Figure 4 elaborates the changes of SOEs’ proportion of paid-in capital among all enterprises in several industrial sectors which are of great significance. For manufacture of tobacco, SOEs’ proportion rose from 96.93% in 2002 to 99.04% in 2012, indicating that during those ten years, although SOEs in manufacture of tobacco had had absolute control over the entire industry, the degree of SOEs’ monopoly was rising continuously. As for the extraction of petroleum and natural gas, the trend of state advance and private retreat is also very obvious. From 2004, the proportion of SOEs began to rise from 95.37% to 99.01% in 2012, even more than their proportion in 2000, which was 98.53%. This means that after reforming SOEs for more than ten years, the degree of SOEs’ monopoly was rising continuously.

Figure 3 Resource allocation for the surviving firms in different sectors


13 The lines in figure represent resource allocative efficiency of surviving SOEs, private, privatized and nationalized firms in China.
years, the degree of SOEs’ monopoly is even higher than before. The same thing also happens to production and supply of electric power and heat power, in which area SOEs’ proportion grew from 83.90% in 2000 to 88.63% in 2011. For processing of petroleum, coking and processing of nuclear fuel, there was a clear trend of the state's retreat before 2004, and the proportion of SOEs declined from 88.2% in 2000 to 73.07% in 2004. Nevertheless, the number of SOEs’ proportion went back to 80.06% in 2008. Though the number dropped to 71.18% in 2009, but then there was a continuous increase from 71.18% in 2009 to 72.67% in 2012. For production and processing of ferrous metal ores, though the overall trend of SOEs’ proportion is declining, but there did exist a rebound from 41.55% in 2009 to 56.21% in 2011, implying that in two years, SOEs’ market power in the industry of production and processing of ferrous metal ores increased.

Figure 4 Proportion of SOEs’ paid-in capital to all enterprises’ paid-in capital

Note: Made by the author with data from the database “National Data”.

19
Table 4  SOEs’ Share of Stock Market Capitalization

<table>
<thead>
<tr>
<th>Year</th>
<th>Volume of market capitalisation (100 million yuan)</th>
<th>SOEs’ share (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Overall market</td>
<td>SOEs</td>
</tr>
<tr>
<td>1995</td>
<td>3,867 (311)</td>
<td>2,826 (211)</td>
</tr>
<tr>
<td>1999</td>
<td>27,974 (923)</td>
<td>19,421 (626)</td>
</tr>
<tr>
<td>2003</td>
<td>45,255 (1,266)</td>
<td>37,108 (928)</td>
</tr>
<tr>
<td>2007</td>
<td>400,409 (1,516)</td>
<td>332,769 (936)</td>
</tr>
</tbody>
</table>

Note. Adapted from “State Owned Enterprises in China: Reviewing the Evidence,” by OECD, 2009, p. 17

by 35.3%. The case that Shandong Iron and Steel Group merged Rizhao Steel can be a good example of the state’s advance at that time. Table 4 shows that SOEs with a state share of more than 10% expanded largely in market capitalization of the Chinese stock market in the 2000s, which exactly indicates the trend of SOEs’ expansion in the stock market (OECD, 2009).

The second indicator is the proportion of SOEs’ assets in the total assets of all enterprises (see Figure 5), which has almost the same results with Figure 4. In terms of assets, the proportion of SOEs in manufacture of tobacco rose from 98.16% in 2000 to 99.30% in 2011, which is coherent with the result in Figure 4. For the assets of SOEs in the industry of production and supply of electric power and heat power, as a result of state advance, SOEs’ proportion grew year by year, from 87.27% in 2005 to 90.65% in 2011. In the production and supply of water, due to former SOE reforms, there did exist a retreat of state before 2007 from 90.30% in 2000 to 75.60% in 2007. Nonetheless, the proportion of SOEs gradually grew back to 80.78% in 2012. For the industry of mining and processing of ferrous metal ores, the turning point was 2009, which is the same with the outcome of Figure 4. The proportion of SOEs in this area increased from
30.91% in 2009 to 48.19% in 2010, and then reached 49.97% in 2011. Through their analysis of the report *Market Competition Status of the Chinese Economy Evaluation and Policy Suggestions*, written by the Unirule Institute of Economics, Sheng and Zhao (2012) point out that in some particular industries, the situation of monopoly was much worse in 2007 than in 2002, and those industries were the ones with high proportions of SOEs, like tobacco products and processing of petroleum, coking and nuclear fuel, which perfectly matches the information from Figure 4 and Figure 5. Besides, central SOEs have expended rapidly and their proportion of assets to the total assets of all SOEs increased from 38.3% in 1998 to 54.1% in 2007, and in 2007, the proportion of central SOEs’ profits was 61.5% of the total profits of all SOEs, while they only accounted for 0.2% of all SOEs (Deng, 2010).
In financial and banking sectors, According to Yao Yang, the government has recently increased its control over the economy in recent years (The Economist, 2011). According to Yang (2013), central SOEs only account for 18% of all the enterprises in the stock market, however, the available capital they have is 48% the total capital in the stock market, and their assets are 76% of the total assets of all enterprises. Moreover, if we take local SOEs and state-holding enterprises into consideration, the assets of the state sector are 55% of the total assets of listed companies, and the proportion of the state sector’s available capital reaches 77%.

As for civil aviation, after the industry became open to private capital in 2005, 12 private airlines were gradually formed (Lardy, 2014). However, since 2008, the newborn private airlines have been affected by state advance and private retreats In 2008, Da Tian W. Group, a logistics company on the State Council’s list of enterprises that should be greatly supported, absorbed the first private airline company Okay Airways through buying 100% of its shares. In the same year, another private airline, Kunpeng Airlines, became a subsidiary of Shenzhen Airlines. In 2009, Sichuan Airlines, one of the major state-owned airlines in China, took over United Eagle Airlines by buying 76.2% of its shares (Liu, 2009). East Star Airlines, a promising airline which already made profits of 1.09 million in its first month, was pushed to go bankrupt by the municipal government of Wuhan and Air China together in 2009 (Cui, 2009a, 2009b).

Another evidence of state’s advance is that SOEs are becoming prevalent in real estate and there are some SOEs whose major business is not even relevant to real estate (Deng, 2010). According to He (2010), more than 70% of central SOEs (94 out of 127) stepped into real estate. In 2009, more than 60% of the “Kings of Land” were either large SOEs or their subsidiaries (Deng, 2010; He, 2010; Ma, 2013; Xu, 2009; Wang & Zhang, 2010). Due to the public’s
negative reaction, many SOEs claimed to step out of real estate, and 82% of those central SOEs who had real estate business gave up their business of real estate, which seems very good. However, the rest of 16 central SOEs in fact controlled 85% of the central SOEs’ total investment, 86% of the central SOEs’ sales revenues and 94% of the total profits, which is apparently “disguised advance under cover” (He, 2010, p. 12). In the report *US-China Economic Relations in the Next Ten Years*, Fan and Hope (2013) also point out that “there have been many subsidiaries of SOEs involved in real estate business that have bid very aggressively for land in public auctions in recent years, benefitting from the abundant low-cost capital and bank loans they could get” (p. 4).

To sum up, although some indicators show that the proportion of the state sector in the economy is declining, based on the robust evidence, the state has been tightening its control over industries referred to as “backbones”, “key areas” and “strategically important fields”, including industries related to petroleum, ferrous metals, tobacco and telecommunications (Deng, 2010; Sheng & Zhao, 2012; The Economist, 2011; Wang, 2011). Therefore, the phenomenon of state advance and private retreat does exist in particular areas, though not in all economic sectors.
Causes of State Advance and Private Retreat

China has undertaken several rounds of economic reforms for almost four decades and SOEs have always been an objective to reform. Ironically, in the third stage of SOE reforms from 2004 to 2013, SOEs’ strong march in the market is regarded as an obvious retreat of China’s economic reforms (Du et al., 2014; Sheng & Zhao, 2012; Xu, 2009). Du (2010) demonstrates that instead of starting in 2009, the trend of state advance and private retreat already began in 2004, and both the re-nationalization of private petroleum companies in Shanxi (in Chinese “陕西”) in 2005 and the restructuring of coal mining enterprises in Shanxi (in Chinese “山西”) in 2010 are typical cases of the state’s advance (Fan & Hope, 2013). One of the most influential economists in China, Zhang Weiying, thinks that the proportion of the state sector in the entire economy is too high, and the peak of state advance and private retreat was in 2009 (Qian, 2010). The analysis in Part II also proves it. What, then, causes the state’s advance and the private sector’s retreat? My next section addresses this question. I consider four variables, interest groups, political elites, institutions, and influential events.

Interest Groups

The government

In China, the government always plays an essential role in the economic development (Huang, 2003, 2008; Naughton, 2007, 2008). The government is not only a planner, monitor, and coordinator of the national economy, but also a executor and player (Jung, 2011). Since the government is a policy-making body, not surprisingly, interest groups never stop influencing the government in order to lobby through policies and regulations that can maximize their benefits.
(Deng & Yu, 2008; Kennedy, 2005, 2007). In the market, the government acts as both the main investor of SOEs and an rule-maker. Due to the close relationship with SOEs, when the government is making polices, it is more inclined to prioritize SOEs’ interests and benefits first. If SOEs are in control of most of the industries and sectors in a country, the government can be relatively fair when it is making policies. However, if SOEs concentrate in several particular industries and sectors, the government’s incentive to protect their interests can be very obvious (Deng & Yu, 2008). Before the reform and opening up, there was no preferential treatment toward SOEs due to the absence of private sector and the government did not need to take the nature of enterprises into consideration when it was making policies. Thus, there was only preferential policies among different industries. After the reform and opening up, China falls into the latter category and the government is more likely to give SOEs preferential treatment since SOEs are more and more concentrated in some particular industries, especially the profitable ones (Deng, 2010). However, the analysis of Deng and Yu (2008) and Deng (2010) could not fully explain the reasons why the state began to advance after 2004 because according to them, the government’s preferential treatment toward SOEs always exist after the private sector appeared. Then why did the government’s support become very obvious after 2004 instead of before 2004? Apparently, there were other factors intensifying this relationship between the government and SOEs and changing the direction of SOE reforms.

**The SASAC and SOEs**

The State-owned Assets Supervision and Administration Commission (the SASAC) is the agency overseeing state-owned assets after 2003. In 2004, provincial SASACs were established (Sheng & Zhao, 2012). The establishment of SASAC changed the direction of SOE reforms at
that time (Cao, 2011; Huang & Yu, 2014; Yang, 2014a). SOEs in China are well-known for their political influence and they have been even more influential than before, after the establishment of the central SASAC in 2003 (He, 2011; McGregor, 2012). Before 2003, the supra agency of SOEs was the State Economic and Trade Commission (SETC), in charge of SOEs, industrial policy-making, sectoral planning and macroeconomic coordination among other economic departments (Jung, 2011). The SETC played an essential role in Zhu Rongji’s economic and SOE reforms. After Zhu Rongji fell out of power, the SETC was immediately dismantled and transferred its function of SOE management to a new successor, the SASAC, in order to reduce the state’s control over the economy (Jung, 2008; Yueh, 2013). The SETC’s other economic function were transferred to other agencies, like the State Development Planning Commission and the Ministry of Foreign Trade and Economic Cooperation (Jung, 2011).

Compared to the SETC, the SASAC has strengthened the power and influence of SOEs from two main perspectives. First, the SASAC is more concentrated on SOEs and state-owned assets. The SETC had to coordinate among different economic goals and tasks as mentioned before, but the only objective of the SASAC is SOEs. The initial intention to establish the SASAC was to separate SOEs and state-owned capital from the government’s control and reduce the state’s direct control over SOEs, and thus, the role of the SASAC should be an “investor”, instead of “manager”; nonetheless, after the SASAC replaced multiple departments supervising SOEs, which were inefficient and overstaffed, it successfully avoided administrative interventions on SOEs from other departments and agencies, increased its impacts on SOEs and has become a strong representative of SOEs, responsible for SOE restructuring, asset evaluation, performance assessment, management and supervision of state-owned asset (Huang & Yu, 2014;
Sheng & Zhao, 2012; Wang, Guthrie & Xiao, 2011). For example, before 2003, it was the Ministry of Finance that has the power to register and approve equity transactions, however, this power was transferred to the SASAC, meaning that the SASAC became not only the investor but also the manager of SOEs (Fan & Hope, 2013; Jung, 2008, 2011). Therefore, gradually, the SASAC has positioned itself as the representative of SOEs and an owner of state-owned assets, and has regarded maintaining and increasing the state-owned capital’s value (bao zhi zeng zhi, in Chinese “保值增值”) as its only goal so as to increase its own status in the administrative system (Cao, 2011; Jung, 2008, 2011; Sheng & Zhao, 2012; Yang, 2014b). The vice director of the SASAC, Huang (2013) admits that the goal of the SASAC during the twelfth “five-year plan” (from 2011 to 2015) is still to strengthen SOEs and turned them into the world’s first-class enterprises and enterprise groups with great competitive abilities. Hence, the establishment of the SASAC turned the direction of SOE reform to the maintenance and appreciation of state-owned assets and capital. After the establishment of the SASAC, SOEs supervised by the SASAC enjoyed a dramatic growth in their profits with more administrative and financial protections than before (Lardy, 2014). Since the SASAC is directly subordinate to the State Council, SOEs’ economic strength has gradually increased and SOEs have been transformed into “national champion” through the management of the SASAC (Jung, 2011; McGregor, 2012; Naughton, 2005; Sheng & Zhao, 2012; Yueh, 2013).

The SASAC has been vilified by scholars, like Sheng and Zhao (2012), Yang (2014a), Chiu and Lewis (2006), and Wang, Guthrie and Xiao (2011), and Yueh (2013), for changing the position of SOEs. According to the Decision of the Central Committee of Chinese Communist Party concerning Several Major Issues in the Reform and Development of State-Owned
Enterprises, passed by the Fourth Plenum of the 15th CCP Central Committee in September in
1999, the state-owned economy should be in control of industries related to national security,
national monopoly and backbone industries (Sheng & Zhao, 2012). However, in its Notice of the
General Office of the State Council on Forwarding the Guiding Opinions of the SASAC about
Promoting the Adjustment of State-Owned Capital and the Reorganization of State-owned
Enterprises in 2006, the SASAC claimed that the industries where SOEs should dominate are
those related to “national security, major infrastructures and important mineral resources,
industries that supply major products and services to the public, and pillar industries and the
major backbone enterprises in high and new technology sectors” (Sheng & Zhao, 2012, p. 155),
and the SASAC also called to accelerate the SOEs’ corporatization and to prevent state assets
from further losing in the process of restructuring and reorganization (Lardy, 2014). By
expanding the scope in which SOEs should play a dominant role, the SASAC blatantly increases
the degree of SOEs’ monopoly in the economy (Wang, Guthrie and Xiao, 2011; Yang, 2014a).

Second, after the establishment of the SASAC, most of the dividends from SOEs
supervised by the SASAC are not handled to the Ministry of Finance, but go into the State
Capital Management Budget, which is managed by the SASAC and the dividends are used for re-
investment into SOEs under the control of the SASAC (Lardy, 2014; Wong & Bird, 2008), which
makes it easier for SOEs to get the funds they need than private enterprises. Although the
number of SOEs has declined, the left SOEs have grown even larger through mergers,
reorganization and restructuring (Naughton, 2007; Lardy, 2014). For example, the total profits of
the two largest SOEs, China Mobile and Sinopec, were more than the total profits of China’s 500
largest private enterprises in 2009 (Lardy, 2014). Under the leadership of the SASAC, from 2005
to 2012, SOEs gradually adopted shareholding (restructuring) system and went into the stock market successfully, which further promoted the listing of large scale and top-ranking SOEs (Heng, 2011; OECD, 2009). According to McGregor (2012), the SASAC contributed greatly to SOEs’ return to prominence in Hu-Wen era, which have served as “guarantors of Party Supremacy” (p. 13).

Since the establishment of the SASAC, SOEs have been a strong competitor in the market (see the number of SOEs in the Fortune 500 list). There were only six central SOEs in 2002, but 16 central SOEs in 2007, and 92 SOEs in 2014 (Li, 2008; Sina Net, 2014). Though the number of SOEs supervised by the SASAC has decreased, their proportion of assets has increased to more than half the total amount of all SOEs. Therefore, the establishment of the SASAC has increased the state’s control over SOEs and directly raised SOEs status in policy-making process.

**Private Enterprises**

Compared to SOEs, private enterprises lack a strong and influential representative like the SASAC arguing for their interests in the process of policy making (Kennedy, 2009). In his book *The Business of Lobbying in China*, after comparing China’s formal and informal lobbying groups, Scott Kennedy (2009) comes to conclusion that though the government has encouraged industry associations to develop, the CCP and the government are not willing to permit social participation into policy making. “The state wants to appear as consultative but not pluralistic” (Kennedy, 2009, p. 196). Therefore, most of the industry associations have been intervened by the state through occupying the leadership of the associations and providing outlays to the
associations, which has caused industry associations to be weak. This is one of the reasons why private enterprises’ voice is still limited in policy-making process.

Second, industry associations industries with a high proportion of SOEs are less intensive to lobby for their benefits since SOEs are supervised by the state (Kennedy, 2005, 2009). This is why industries having a large share of SOEs, like steel industry and petroleum industry, always have a weak association, which will further prevent private enterprises in those industries from lobbying for their interest.

Third, even to some extent, a few industry associations are working to get benefited by policies, enterprises’ influence on policies greatly depend on their size (Kennedy, 2005, 2009). Largest SOEs always have the most regular interaction with the government in many ways (Kennedy, 2005). However, as compared to large SOEs in the industries having “state advance and private retreat” in Part II, private enterprises do not have advantage in the policy-marking process. This could be one of the causes that the state sector began to advance in 2004 after the establishment of the SASAC in 2003.

**Political Elites**

In China, the directions and focuses of SOE reforms are not fixed, but have been largely influenced by political elites’ ideas and the transition of leadership. Lardy (2014) points out that while SOE reforms in the Jiang-Zhu era were far-reaching, the Hu-Wen government slowed down SOE reforms. To explain the emergence of state advance and private retreat, let us consider the ideas and behaviour of political elites.

After Jiang Zemin became the top person in China’s hierarchical system, he did not immediately gain absolute power (Naughton, 2008). To consolidate his power, Jiang chose to
strengthen his coalition by supporting the reformist Zhu Rongji, who also had the background of Shanghai, against Li Peng, who was more conservative (Naughton, 2008). “In this way, Jiang Zemin retained for himself the final say on the most important issues while giving Zhu Rongji significant leeway” (Naughton, 2008, p. 115). Therefore, Zhu Rongji had the opportunity to push forward his economic reforms. Zhu Rongji was a politician with a self-confident, decisive personality and often made quick and strong decisions (Naughton, 2007, 2008). Under great pressure from groups with vested interest, Zhu strongly promoted SOE reforms by pursuing relevant policies, such as the end of the dual-track pricing system, fiscal recentralization and layoffs of redundant workers, which brought price stability and the downsizing of SOEs and also caused broad protests by the laid-off workers (Chen, 2006; Naughton, 2007; Tiberghien, 1998).

According to Steinfeld (1998), SOEs had never truly been forced to face hard budgets and bankruptcy before Zhu Rongji’s SOE reform.

Hu Jintao succeeded to Jiang Zemin and became the president in 2003, and Wen Jiabao became the successor of Zhu Rongji, as the premier. Hu also gave Wen significant leeway, however “in terms of personalities, these two individuals [Hu and Wen] could hardly have been more different than Jiang Zemin and Zhu Rongji” (Naughton, 2008, p. 115). In contrast, “under Wen [Jiabao], the style of policy-making has changed rather dramatically, becoming more consultative and deliberative than Zhu Rongji” (Naughton, 2007, p. 108). The differences of leaders’ personality can have impacts on their political behaviours. Therefore, the differences between Zhu Rongji and Wen Jiabao could have influence on their policies, including their attitudes towards SOE reforms.
In addition to politician’s personality, political elite’s solution to problems could also be influential to SOE reforms. Reforms in the 1980s did not produce “losers”, because the economic reforms in both rural and urban areas did not have negative consequences for major interest groups; however, Zhu Rongji’s reforms created a large number of “losers”, especially the former SOE workers laid off by downsizing SOEs and taking away the “iron rice bowl” (Chen, 2006; Naughton, 2007, 2008; Oi & Han, 2011). The number of layoffs is shocking. In 1993, there were still 76 million SOE workers; however, after the 10-year SOE reform by Zhu Rongji, there were only 28 million SOE workers by 2004 (Naughton, 2008). More than 30 million SOE workers lost their jobs (xiagang, in Chinese “下岗”) or forced to retire early, and 18 million SOE workers were working in enterprises which were not SOEs any more through the process of SOE restructuring (Naughton, 2008). Due to the lack of a good social security system, the contradiction between laid-off workers and the government was increasingly acute (Naughton, 2007). To ease the social contradictions and maintain their legitimacy and power, Hu-Wen government decided to comfort regions and individuals left behind by the economic reforms in the 1990s and used “‘harmonious society” as their slogan to show their efforts on promoting social equality, instead of continuing pushing forward Zhu Rongji’s strong SOE reforms. Therefore, the Hu-Wen Government’s gentle solution to social contradictions generated at Zhu’s era could be one of the reasons why Zhu’s strong SOE reform did not proceed. In the absence of external pressure, the state sector began to expand in the economy, which can explain the state sector’s advance Under Hu-Wen administration.
Institutions

Fiscal institution

Theoretically, SOEs are publicly declared to belong to the whole nation; thus, “the whole people” of China are entitled to the SOEs dividends: public products and services funded by the SOEs. However, from the fiscal and tax reform in 1994 to 2007, SOEs did no longer need to turn over profits to the state. After distributing dividends among their shareholders, about 90% of their profits were left to SOEs themselves (Deng, 2010; He, 2011; Yuan & Shao, 2014). Therefore, the percentage of profits SOEs turn did not match the ownership (Zhou, 2014). Even after the budget system of state-owned capital was put into effect in 2007, SOEs in manufacture of tobacco, production and processing of petroleum, production of electric power, telecommunication and mining and washing of coal, only need to turn over 10% of their profits after tax to the Ministry of Finance. As for SOEs in production of steel, transportation, electronic industry, trade and construction, the proportion of profits after tax they need to turn over is only 5%, while SOEs in other countries should turn over 20% to 50% of their profits (He, 2011; Yuan & Shao, 2010; Zhao, 2013). For example, in 2008, the undistributed profits only in PetroChina, Sinopec, Baogang, China Mobile, China Unicom and ICBC reached 1046.26 billion yuan (Yuan & Shao, 2010). Most of the profits left to SOEs have been used for new investments, leading to the increase of SOEs’ market power in both monopolistic and competitive areas, and the salaries, bonus, and welfare of SOEs’ employee have been greatly improved, which has widened the income gap between employees, especially executives, in SOEs and private enterprises (He, 2011; Yuan & Shao, 2010; Zhou, 2014). Besides, the tax institutions also give preference to SOEs (Deng, 2010; Jiang, 2010). In December 1993, the State Council passed the Decision of
the State Council on Implementing the Tax Division Management System, which said that “[as] a transitional measure, most of the old wholly state-owned enterprises registered before 1999 may withhold their after-tax profits according to specific circumstances. Meanwhile, the income taxes paid by low-profit enterprises will not be withdrawn from the treasury” (Sheng & Zhao, 2012, p. 20). Table 5 elaborates the ratio of taxes enterprises actually paid to their sales revenues. From Table 5 we can see that in the 2000s, the ratio of SOEs’ taxes to sales revenues was continuously decreasing while the ratio of private enterprises is increasing. Therefore, the large number of profits SOEs have saved from the fiscal and tax institutions can be one of the reasons why SOEs have great numbers of available cash flows and why they are very capable to buy shares from private enterprises (Deng, 2010; Yuan & Shao, 2010). However, this could only

Table 5  Taxes to Sales Revenue Ratio of SOEs and Private Enterprises

<table>
<thead>
<tr>
<th>Year</th>
<th>SOEs</th>
<th>Private enterprises</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Total Taxes</td>
<td>Sales revenue</td>
</tr>
<tr>
<td>2001</td>
<td>5367.42</td>
<td>76355.5</td>
</tr>
<tr>
<td>2002</td>
<td>5359.20</td>
<td>85326.0</td>
</tr>
<tr>
<td>2003</td>
<td>5890.92</td>
<td>100160.9</td>
</tr>
<tr>
<td>2004</td>
<td>6851.93</td>
<td>120772</td>
</tr>
<tr>
<td>2005</td>
<td>7528.99</td>
<td>140726.6</td>
</tr>
<tr>
<td>2006</td>
<td>8195.07</td>
<td>162390.3</td>
</tr>
<tr>
<td>2007</td>
<td>9615.79</td>
<td>195030.8</td>
</tr>
</tbody>
</table>

Note. Unit: 0.1 billion yuan. Adapted from “A Critique of ‘The State-Owned Enterprise Advances While the Privately-Owned Enterprise is Lagged Behind’,” by S. Jiang, 2010, Academic Journal of Anhui University (Philosophy and Social Sciences), 5, p. 126.
partly explain the state’s advance after 2004 because the support of fiscal institution to SOEs has existed for a long time and did not just start from the beginning of the 2000s.

**Financial institution**

According to Allen, Jun Qian and Meijun Qian (2008), there are four main financial sources for enterprises in China, which are bank loans, enterprises’ self-fund-raising, the state budget, and foreign direct invest, and the first two are considered as the most important sources.

For bank loans, one of the biggest advantages SOEs have over private enterprise is that compared to private enterprises, it’s easier for them to get loans from banks. There are two reasons. First, the Chinese financial system is dominated by a large banking sector predominantly owned by the state, and due to the special relationship between the state and SOEs, state-owned commercial banks are inclined to advance loans to SOEs instead of private enterprises. (Ayyagari, Demirgüç-Kunt & Maksimovic, 2008; Lardy, 2014; Naughton, 2007). Second, SOEs have more credits than enterprises, since the government and fiscal revenues are their “guarantors” (Cao, 2011; Deng, 2010; Li, 2013; Ma, 2013). SOEs are less risky than private enterprises, banks are more likely to advance loans to SOEs at lower interest rates (Chiu & Lewis, 2006; Fan & Hope, 2013; Garnaut, Song, Yao & Wang, 2001; Huang, 2003).

The state’s control over the banking system is reflected not only in the high share of state ownership in banks, but also by the fact that senior executives in banks are often former officials from the People’s Bank of China (China’s central bank) and the China Banking Regulatory Commission and they also can work for these two institutions after their jobs in banks. (Ayyagari, Demirgüç-Kunt & Maksimovic, 2008; Lardy, 2014; Naughton, 2007). Linda Yueh (2010, 2013) also mentions that though China’s banking system has been reformed since the
1980s, by 2009, the banking sector was still dominant by the state since about 60% of the credits were issued by state-owned commercial banks and China’s state-owned commercial banks are among the largest banks in the world.

In their paper *Formal versus Informal Finance: Evidence from China*, after analyzing 2,400 Chinese firms, Ayyagari, Demirgüç-Kunt and Maksimovic (2008) argue that in China, only a small portion of private enterprises can benefit from the formal finance system, while a large number of fundings and loans goes into SOEs, despite their efficiency and profitability. This lending bias is also emphasized by Brandt, Rawski and Sutton (2008) and Chiu and Lewis (2006). According to the Brandt, Hsieh and Zhu (2008), small and medium enterprises only receive 3% of bank loans which is far from what they need, while most of them are private enterprises and they contribute to more than half of the GDP every year. Therefore, the proportion of the loans and funds SOEs are getting is more than their contribution to the economy, and thus, compared to private enterprises, SOEs are more capital intensive (Brandt, Hsieh & Zhu, 2008; Chiu & Lewis, 2006; Fan & Hope, 2013; Moody & Hu, 2013).

Furthermore, Ayyagari et al. (2008) find that firms getting support from formal bank finance grow faster than those financed by informal bank finance, which implies that the gap between the growth rates of the state and private sectors can be wider and wider. Fan and Hope (2013) argue that if the formal finance could help private enterprises with more financial support, China’s economy would be more efficient. Besides, McGregor (2012), and David Pilling (2013) also agree that China’s banks, especially the ones owned by the state, is in fact preventing SOEs from shrinking by investing massive loans and funds to SOEs while ignoring the needs of private enterprises.
However, the 2008 financial crisis made it a cause of state advance and private retreat. Owe to the 2008 financial crisis, many enterprises experienced decreasing profits, losses or even bankrupts. In face of the crisis, to avoid bad debts and financial risks, banks were more inclined to make advance to SOEs instead of private enterprises than before, which made the unfair allocation of loans and credits even worse (Fan & Hope, 2013; Li, 2013). Resulting from the lack of loans and capital in the financial crisis, private enterprises did not have a fair chance to compete with SOEs and lots of them went bankrupt, which led to the appearance of state advance and private retreat (Bai, Lu & Tao, 2006; Cao, 2011; Deng, 2010). As a result, the financial bias to private enterprises is one of the main factors widening the development gap between the state and private sectors, and finally pushed the tide of state advance and private retreat.

For self-fund-raising, SOEs still have advantages over private enterprises. As mentioned above, after the establishment of the SASAC in 2003, most the dividends that SOE should turn over to Ministry of Finance go into the State Capital Management Budget managed by the SASAC and are used for re-investment into SOEs under the control of the SASAC (Lardy, 2014; Wong & Bird, 2008). Besides, according to Li Yining (2013), some SOEs even have their own subsidiaries specializing in raising capital from the state and banks (Li, 2013). So far, the financial institution cannot explain the state’s advance after 2004 because this unfair allocation of financial resources also existed before.

Financial bias against private enterprises has existed for a long time. This bias was unable to fully explain the emergence of state advance and private retreat. However, the negative effects
were worsened by the 2008 financial crisis, which could be one of the causes of the state advance and private retreat.

**Influential Events**

**Accession to the WTO**

China’s accession to the World Trade Organization (WTO) was a clear signal that the Chinese economy would compete with other economies on the international stage and it was also a significant turning point of China’s SOE reforms (Branstetter & Lardy, 2008; Jung, 2011). To join the WTO, China had to cut tariffs and reduce import barriers. Due to that, Chinese enterprises were faced with much fiercer international competition than before (Branstetter & Lardy, 2008). In previous stages, SOE reforms focused on “decentralizing powers and giving up profits” (1978-1986), “separating control from ownership” (1987-1992) and “establishing a modern enterprise system” (1993-1999) (Sheng & Zhao, 2012). However, to prepare for its accession to the WTO, China replaced its previous goal of reforming SOEs with a new one: building the world’s first-class enterprises and enterprise groups to deal with the competition in the international market (Huang & Yu, 2014; Lin, 2000). To protect the economic lifeline and main economic stability after entering the WTO, in 1999, the Fourth Plenum of the 15th CCP Central Committee decided to “grasp the big and let the small go” (zhua da fang xiao, in Chinese “抓大放小”) ((Chen, 2006; Chiu & Lewis, 2006; Fan & Hope, 2013; Naughton, 2007; Yueh, 2013; Zeng & Tsai, 2011). “Grasp the large” means that a small number of large enterprises will be strengthened and their competitive ability will be increased with the support from the government. (Deng, 2010; Deng & Yu, 2008; Heng, 2011; Li & Liu, 2014). Besides, to meet the needs of the WTO, both the Fourth Plenum of the 15th CCP Central Committee in 1999 and the
Third Plenum of the 16th CCP Central Committee in 2003 stressed the development of mixed ownership economy. As a result, many of the large enterprises became joint stock enterprises or limited liability enterprises (Lardy, 2014), which has given SOEs more opportunities to control social capital. This is because in terms of available capital, SOEs have much more political and financial advantages over private enterprises in investment, as mentioned above (Li & Liu, 2014). Moreover, these SOEs can often be found in the “strategically important” industries, such as petroleum, metallurgy, electricity, military industry, and telecommunications (Li & Putterman, 2008). “Let the small go” means that while promoting the development of large and important SOEs, the government gives a freer rein to small and medium SOEs through restructuring, combination, merger and mixed ownership (Chen, 2006; Chiu & Lewis, 2006; Fan & Hope, 2013; Naughton, 2007; Yueh, 2013; Zeng & Tsai, 2011). As a consequence, the number of SOEs greatly decreased from 442,000 in 1996 to 370,000 in 2003. However, with great support from the government, many SOEs, especially large and central SOEs became extremely giant (the so-called “national champion” by McGregor, 2012) and turned into the so-called “backbones” of the economy, which with no doubt contributed to the state’s advance.

In addition, Yueh (2013) points out that China’s “going out” policy enacted in 2000 has similar impacts on state advance and private retreat. The “going out” policy was aimed to turn China’s enterprises into global players (Yueh, 2013), which, cooperating with the accession to the WTO, gave large SOEs to become larger.

“Lang Whirlwind”

According to Yang (2010), the “Lang Whirlwind” was one of the main factors ending the SOE reform of property right and causing the state’s advance. From 2004, economists,
represented by Lang Xianping\textsuperscript{14}, began to question and criticize the SOE reform of property right, and pointed out that state-owned assets were eroded and pocketed by SOE executives and private entrepreneurs through the reform. Lang (2006) holds a rather negative attitude towards the reform of SOE property right and uses Management Buyout (MBO) as an example to explain how SOE executives and private entrepreneurs plunder state-owned assets by pricing the assets at much less than their own values in property right transactions. In his article, Lang (2006) puts labels on MBO, which is a flagrant abuse of state-owned property right, and draws an analogy between China’s SOE reform and Russia’s privatization. In fact, Lang (2004) deems that property right transaction should be paused due to the lack of relevant laws and MBO should be banned. Lang’s statements and remarks were like a whirlwind, sweeping across the entire country overnight. Although it was MBO that Lang (2006) sharply criticized, his arguments did provoke the wrath of the public and then caused a great panic in the government. Gu Chujun, the founder and former CEO of Gelin Ker Holding, was criticized by Lang for plundering state-owned assets while acquiring Hisense Kelon, Meiling Electrical Appliance, Yaxing Bus and ST Xiang Bearing. As an outcome of the Lang-Gu dispute, Gu was sentenced to 12 years in prison for usurping state-owned assets. Under this circumstance, in 2009, the SASAC reacted severely to this phenomenon with new strict regulations on the privatization of SOEs, in order to protect state-owned assets and capital, which slowed down the process of SOE reforms. For example, the central SASAC passed document like *Opinions on Regulating Listed Enterprises’ State Shareholders’ Behaviours* and *Opinions on Strengthening supervision on local state-owned*

\textsuperscript{14} Lang Xianping (Larry Hsien Ping Lang) is a well-known Hong-Kong based economist, commentator, author and TV host in China. Lang has become a famous and controversial figure in China in recent years due to his altitude towards the SOE reform of property right.
assets in September 2009, with stick items and sharp words inside. To avoid political risks, local governments also slowed down the pace of their SOE reforms (Yang, 2014a). The SASAC also claimed to strengthen the state-owned economy’s control over the national economy.

In the 2000s, with more and more criticisms to SOEs’ denationalization and the market economy, the government began to strengthen its support to the state sector (Li & Liu, 2014; Yang, 2013). For instance, in 2005, National Development and Reform Commission announced a new policy on the development of the steel industry, which greatly raised the threshold that the production of enterprises producing plain carbon steel must exceed 5 million tons per years, and the production of special steel companies must be more than 0.5 million tons per year. As a result, a large number of medium and small steel companies were closed and most of them were private enterprises (Deng, 2010; Yang, 2014a). In this way, the monopolist position of SOEs in iron and steel industry was strengthened. The case that Shanxi provincial government promoted the integration of coal resources is another example (Deng, 2010; Fan & Hope, 2013; Jiang, 2010; Ma, 2013; Sheng & Zhao, 2012; Yang, 2010). In 2009, the Shanxi provincial government issued a new policy, *The Plan of Shanxi Province for the Restructuring and Revitalization of the Coal Industry*, which withdrew the mining right from small coal enterprises. This is because according to the policy, small mines whose production capacity is below 0.3 million tones per year should be shut down. State-owned mines or state-holding mines used this policy as an opportunity to integrate coal resources within Shanxi Province and merged a lot of small mines. As one of the biggest state-owned coal mining enterprises, Lu’an Group participated in the restructuring and integration in 13 counties and six cities and involved in 3.02 billion tons of coal resources (Sheng & Zhao, 2012). After the consolidation, four extremely large state-owned coal
mining enterprises formed and the number of coal mines in Shanxi Province reduced to 1,057 from about 2,600 and the number of coal business companies even dropped from 2,200 to 130 (Deng, 2010; Sheng & Zhao, 2012; Yang, 2010, 2014a). In 2005, Shanxi Province reformed its coal mining industry and attracted a large number of private investors. For the capital in coal mining industry in Shanxi, from 2005 to 2006, the capital from Shuitou County of Wenzhou invested in Shanxi was more than 30 billion and the total investment from Wenzhou was more than 50 billion. However, to protect and support the development of seven SOEs in coal mining, after The Plan of Shanxi Province for the Restructuring and Revitalization of the Coal Industry, there were only two ways for private capital, either totally retreating or participating with no right to hold the majority of the shares (Jiang, 2010). Thus, the government has played a significant role in hindering the development of private sector by setting entry barriers and unfair competition (Ma, 2013). Besides, in order to ensure the economic stability, the government give most of the transfer payments and government purchase to SOEs or state-owned economy (Cao, 2011).

Since the 2008 financial crisis, there have been more and more attacks towards the market and free competition. Some scholars even appeal for more interferences from the state to the economy (Wang & Jin, 2010; Zhang, 2010). Therefore, the superstition on the state, the government and the authoritarian system has been the theoretical and ideological foundation of the state’s advance in the economy. One of the most important economists in China, Li Yining (2000) directly points out that the ideas “the larger proportion of state ownership, the better” and “reducing state-owned shares is weakening the state economy” are wrong.
Therefore, gradually, SOEs were not an objective of reforms any more, but the objective to be strengthened (He, 2011; Yang, 2014b).

**The 2008 financial crisis**

The 2008 financial crisis is a contingent event that made the trend of state advance and private retreat inevitable. The government led by Hu and Wen carried out two projects, the “Four Trillion Project” (*si wan yi ji hua*, in Chinese “四万亿计划”) and the “Revitalization Project of Ten Industries” (*shi da chanye zhenxing guihua*, in Chinese “十大大产业振兴计划”) to deal with the crisis, both of which intended to stimulate the economy by investment (Xu, 2009; Yang, 2014a).

In the end of 2008, the central government gradually invested 4 trillion yuan into different industries to deal with the financial crisis, which is the so-called “Four Trillion Project”. Nevertheless, most of these funds were spent on the construction of infrastructures, such as highways, railways, airports (Deng, 2010; Fan & Hope, 2013; Lardy, 2012; Xing, 2009; Xu, 2009; Yu, 2012). From Figure 6, we can tell that about 86% of the stimulus package went to transportation and power infrastructure, earthquake construction, rural infrastructure and the construction of public housing. These industries were largely monopolized by SOEs. Hence, though the four trillion yuan was invested into the economy, in fact, most of the four trillion went into the pocket of SOEs, which greatly increased their available capital and helped them get larger market shares, while private enterprises were in great need of financial support (Bremer, 2010; Deng, 2010; Fan & Hope, 2013; Piling, 2009; Xu, 2009; Yang, 2014a; Yu, 2012). For medium and small enterprises, it was rather difficult for them to get the investment and most of
them were private enterprises (Xu, 2009). In this circumstance, it was not difficult for SOEs to nationalize formerly private enterprises (Lardy, 2012).

Figure 6 Areas of spending in China’s four trillion stimulus package (%)

![Areas of spending in China’s four trillion stimulus package](image)


Since the principle of the government was to use investment to promote economic development, banks were pushed by the government to increase loans and credits to enterprises (Fan & Hope, 2013; Xu, 2009). To avoid nonperforming loans, banks often chose to advance money to large SOEs instead of private enterprises, which worsened the unfair allocation of financial resources as I mentioned above (Bai et al., 2006; Deng, 2010; Xu, 2009).

Besides the Four Trillion Project, National Development and Reform Commission and Ministry of Industry and Information Technology together issued another investment program, called “Revitalization Project of Ten Industries”, which stressed great importance of the industries of steel, auto, petroleum, textile, non-ferrous metal, equipment production and
information technology, light industry and logistics industry. This project had the same effect with the Four Trillion Project (Fan & Hope, 2013). Both of them inclined to increase the degree of industrial integration and support largest enterprises and enterprise groups in those areas of strategical significance, and most of those enterprises were either central or local SOEs (Xu, 2009).

Besides, the 2008 financial crisis has shown the market failure and retaken the state back onto the stage (Naughton, 2011). To deal with the 2008 financial crisis and maintain the stability of the capital market, one of the other, the United States, the United Kingdom, Germany and other western countries began to subsidize domestic financial and industrial enterprises and promote nationalization in particular industries (Wei & Zhang, 2010; Yang, 2013, 2014b). For instance, in the United States, on September 7, 2008, the federal government announced to directly take over two financial institutions raising money for real estate investment, the Fannie Mae and Freddie Mac, and then the Federal Reserve got 79.9% of the American International Group’s shares by lending 58 billion dollars to the AIG (Wei & Zhang, 2010). Similar cases also appeared in other countries. In the name of saving the market economy, the Chinese government raised a tide of re-nationalization, and SOEs seized this opportunity to march massively in economic sectors (Yang, 2013).

In addition to the measures above, in December 2008, the State Council announced the Opinions concerning How Finance Promotes the Economic Development and Opinions on Facilitating Circulation and Increasing Consumption, in which the central government clearly committed to facilitate the formation of several large enterprises and enterprise groups with great competitive ability, which means SOEs and state-owned enterprise groups (Li & Liu, 2014). The
government intended to maintain the competitiveness of its economy in international
competitions during the financial crisis. This kind of polices and regulations was very common to
see during the Hu-Wen Administration after 2008.

Before the 2008 financial crisis, the development of both foreign-invested companies and
private enterprises were protected and encouraged by local governments. Nonetheless, from
2008, SOEs’ investment began to increase dramatically. In 2007, the increase rate of SOEs’
investment was 16.7%, but in 2009 it became 37.8%. Meanwhile, the increase rate of private
enterprises reduced to 35% from 47.4% (Deng, 2010). This is because the local governments
were prone to cooperate with SOEs. One reason is that most of the key investment programs
were under the control of SOEs. The other reason is that SOEs had richer capital than private
investors due to their financial relationship with the government (Cao, 2011; Deng, 2010; Ma,
2013). Thus, through cooperation with large SOEs, local governments could not only get enough
investment, but could prevent their local small SOEs from being shut down (Deng, 2010).

Therefore, the 2008 financial crisis has changed the trajectory of China’s SOE reforms
and has strengthened the momentum of state advance and private retreat through the
government’s measures.

In addition to the above-mentioned causes, there are also some other indirect causes of
the state’s advance, for instance, the lack of motivation to reform SOEs. According to Jung
(2011), SOEs in China finally started the long-delayed restructuring from the middle of the
1990s. Compared to the 1990s when SOEs were facing entrenched problems, like inefficient low
efficiency, high debt ratio, poor management quality, poor product quality and redundant
personnel (Oi, 2011), pressures for SOEs to reform in the 2000s and 2010s were greatly
alleviated since those problems were greatly solved by Zhu Rongji’s SOE reform in the 1990s (Deng, 2010; Huang & Yu, 2014). Zhu Rongji’s SOE reform was economic and removed a lot of policy burdens from SOEs’ shoulders, which indeed improved their efficiency and competitive ability in the market and helped them become profit-seeking market players (Deng, 2010; Yang, 2014a). According to Lardy (2014), since the second half of the 1990s, the proportion of lose-making SOEs among all SOEs has been declining and the amount of their losses has been smaller and smaller. After 2003, SOEs experienced a rapid growth of profits, benefiting from the 10-year reform of property right since 1993 and the situation of their operation was greatly improved. Therefore, the government lacks the sense of urgency to continue reforming SOEs (Yang, 2010; 2014a).
Policy Suggestions

The phenomenon of “state advance and private retreat” has enhanced SOEs’ market power, which to some extent has contributed to China’s increased role in the international market. However, it has brought various negative impacts on China’s economic development. First of all, it has hindered the development of China’s private economy, since SOEs have been supported by the government’s policies and have got many advantages over private enterprises in getting loans, administrative subsidies, and access to the market. For example, although SOEs are in control of upstream industries, such as the production and processing of ferrous metals, petroleum and gas, they can still influence downstream private enterprises by controlling the prices of raw materials and fuels (Deng, 2010; Yuan & Shao, 2010). Second, it has worsened the unbalanced industrial structure. This is because the industries under the control of state-owned capital will develop faster, while most of them are facing the problem of overcapacity (Chai, 2015; Deng, 2010; Wang & Jin, 2010; Yuan & Shao, 2010). Third, the tide of state advance and private retreat has increased credit risks of the financial system. Though banks’ initial intention of advancing money to SOEs is to avoid bad debts, however, in many cases, it is SOEs that cannot repay the loans and banks cannot take their assets as repayment, which results in large debts (Cao, 2011; Deng, 2010). Fourth, the tide of state advance and private retreat has hindered the transformation of our economic structure because “state advance and private retreat” also means “rich state and poor public” (guo fu min pin), which with no doubt has a negative effect on the increase of domestic demands and hamper the process of economic reforms (Chen, 2008; Deng, 2010; Yuan & Shao, 2010). Fifth, “private advance and private retreat” has widened the income gap between people in monopolistic areas and people in competitive areas,
which will also reduce the employment since the living space of private economy is being squeezed by the state economy (Deng, 2010; Wang & Jin, 2010; Yuan & Shao, 2010). What is more, Cali argues that since the salaries and welfare are so different in SOEs and private enterprises, there has been the hierarchy of workers (Oi, 2011). Last but not least, SOEs’ monopoly also leads to serious corruption (Chai, 2015; Zhang, 2013). In addition, from the perspective of private entrepreneurs, to some extent, the state’s advance has reduced private entrepreneurs’ confidence in the future of the investment environment, which will cause more negative influence China’s economy than we have ever thought (Zhang, 2013).

According to Lardy (2014), China’s current Xi-Li government has no intention to follow Hu-Wen government’s strategy of relying on SOEs to promote economic development. Instead, Xi-Li government has performed to liberalize the market in resource allocation and reduce the government’s control over the economy, which will downsize SOEs’ influence on the economy (Lardy, 2014). Besides, Lardy (2014) also argues that the development of China’s economy in the future will be market driven, not state driven. Based on the analysis in the former parts, I have three policy suggestions for the coming round of reforms.

First of all, we need to give up the old thought that SOEs are a symbol of socialism. As a matter of fact, SOEs existed in feudal society and also exist in capitalist countries (Yang, 2010). SOEs are not the economic base of a socialist country, either. If so, why the socialist China could be founded with almost no SOEs in 1949 (Yang, 2010)? Why did the socialist countries in east Europe finally collapse in the end of 1980s while SOEs were still the absolute majority in their economies (Soviet Union, Bulgaria, Romania, the German Democratic Republic) (Yang, 2014a)? In fact, during the WWII in Germany the state was in control of the entire economy and after the
WWII, Japan had the same situation (Yang, 2010). Therefore, it is inappropriate for new leftists to impede further SOE reforms in the name of maintaining the basis of China’s socialism (Du, 2010; He, 2011). Besides, we also need to give up the idea that key economic areas should be dominated by the state economy (Wang & Jin, 2010). This reform of theories and ideas should be the first step in the new round of SOE reforms and further economic reforms.

Second, we need to deepen the administrative, fiscal and financial reforms together. The administrative reform should abolish more administrative examinations and approvals in order to untie the market and the private economy. Therefore, the government must stop protecting SOEs in competitive areas, in order to promote the development of the market and private enterprises, and make the best of SOEs’ profits to improve the public’s welfare. Both the SASAC and SOEs should not continue considering “maintaining and appreciating the value of state-owned assets” and “expanding and strengthening SOEs” as their goals (He, 2011; Huang & Yu, 2014; Yang, 2014b). In the meanwhile, the government should also push forward the fiscal reform, through which the government should raise the proportion of SOEs’ profits turned over to the state, and the government should use the money to improve the supply of public goods and services, including education, healthcare and environmental protection. Through the financial reform, the financial system should give up the bias it has for private enterprises. Besides, the restructuring of SOEs should be continued. In areas of natural monopoly, it is the quantity and quality of public products and public services that SOEs should focus on. Compared to gaining profits through monopoly, public welfare should be ensured first (Fan & Hope, 2013; Huang & Yu, 2014; Yang, 2013, 2014a; Yuan & Shao, 2010; Zhang, 2014). As for areas of administrative monopoly, like banking industry, they should be open to private capital and there should not be
forbidden areas that only allow the access of SOEs (Cao, 2011; Fan & Hope, 2013; Yang, 2013, 2014a; Zhang, 2014). For state-owned capital, it should aim at the investment in high technology, instead of monopolizing industries with great profits with the excuse of maintaining the economic stability.

Third, political reform also should be taken at the same time as the core of the new round of reforms, since the most essential way to change the trend of state advance and private retreat is to reform the government. This is because in China, it is the government that creates both the economic and industrial structures. Whether SOE reforms can succeed or not does not rely on whether SOEs can make money or not, neither depends on how much SOEs can make, but relies on whether the public’s welfare can be maximized. If the government continues being the major beneficiary and does not respect the market’s decisive role in the economy, not only SOEs reforms, but also other reforms cannot be successful. Since nowadays, the middle class has become aware of their rights and political influence, if the government’s power cannot be constrained, gradually social constructions will be fiercer and fiercer, which will lead to reforms from bottom to top.
Conclusion

SOE reforms have been a hot topic ever since the reform and opening up in 1978. In the 2000s and 2010s, there is an influential phenomenon called “state advance and private retreat” in particular economic sectors with strategically importance. These industries are mainly related to the production and processing of petroleum, ferrous metals, tobacco and telecommunications. Through the number of SOEs, employees working in SOEs, the proportion of SOEs’ output to the total output of all enterprises, and other indicators have been decreasing in these industries, however, considering the degree of SOEs’ monopoly and the controlling capacity of state-owned capital, the tide of state advance and private retreat does exist in strategic industries. There are many factors leading to the state’s advance and private sectors’ retreat during this period, including interest groups, political elites, institutions, and influential events. In terms of interest group, the relationship between the government and SOEs cannot explain the state sector’s advance since the government’s preferential treatment toward SOEs also existed before the 2000s. As SOEs’ strong representative in policy-making process, the SASAC has contributed to the state sector’s march after its establishment in 2003. Steered by the SASAC, SOEs’ market power has been greatly enhanced. As compared to SOEs, private enterprises do not have enough access to policy making process. In terms of political elite, first, Zhu Rongji had a strong and decisive personality. With the support from Jiang Zemin, Zhu strongly pushed forward the SOE reform, though there were many “reform losers”. Second, social contradictions were generated during Zhu’s strong SOE reforms, especially the contradictory between the government and the laid-off SOE workers. To deal with the contradictions, maintain legitimacy and get support coalition, the Hu-Wen government turned their attention to social equality and stability, which
slowed down the speed of the SOE reform. As for institutional factors, the fiscal and tax system facilitate the accumulation of SOEs’ profits; the financial system gives SOEs more accesses to loans and credits. These systems increase SOEs’ available capital in market competitions, which is a great advantage over private enterprises and make the state sector capable to advance.

Table 6 Variables to Explain “State Advance and Private Retreat”

<table>
<thead>
<tr>
<th>Variable</th>
<th>Result</th>
<th>Explanation</th>
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<tr>
<td>Interest groups</td>
<td>not explain</td>
<td>the relationship between the govt and SOEs</td>
</tr>
<tr>
<td></td>
<td>explain</td>
<td>the SASAC and SOEs V.S. private enterprises</td>
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<tr>
<td>Political elites</td>
<td>explain</td>
<td>transition from Jiang-Zhu Government to Hu-Wen Government</td>
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<tr>
<td>Institutions</td>
<td>partly explain</td>
<td>fiscal system</td>
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<td></td>
<td>partly explain</td>
<td>financial system</td>
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<td>Influential events</td>
<td>explain</td>
<td>“Lang Whirlwind”</td>
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<td></td>
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<td>the 2008 financial crisis</td>
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In terms of influential event, there were three important academic and economic events that contributed greatly to the state advance and private retreat. They are “Lang Whirlwind”, China’s accession to the WTO, and the 2008 financial crisis. Lang Xianping,, sharply criticized the denationalization of SOEs and state-owned assets during former SOE reforms and caused great panic among officials and the public. To maintain the state’s control over the economy and avoid political risks, government officials prefer to promote the development of the state economy. As for influential event, both China’s entry to the WTO and the 2008 financial crisis,
especially the measures taken to deal with the financial crisis, are attributed to the state’s advance. Given that, many countries used the tool of nationalization to deal with the 2008 financial crisis, the Hu-Wen Administration use the opportunity to promote re-nationalization, which resulted in the trend of state advance and private retreat. Therefore, I demonstrate that interest groups, political elites, ideology and influential events together contributed to the phenomenon of state advance and private retreat.

To restart the economic reforms, theoretical changes are needed and the goal of future SOE reforms should be clear. Moreover, we need to promote both political and administrative reforms, in order to ensure the market’s decisive role in resource allocation and restrain the government’s power in competitive areas. In addition, as Li Yining (2000) says, we should always have the sense of crisis, and should not avoid reforms until crises come.

China’s SOE reforms have been a process of “crossing the river by feeling the stones with your feet”, and technically, there is not a clear blueprint before the SOE reforms each time. SOEs did make a contribution to China’s economic development in history, however, we should never let SOEs capable to kidnap the government and the economy.
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